Hon Simon Watts, Minister of Revenue

Information Release

Budget 2026

September 2026

List of documents included in this proactive release

#	Reference	Type	Title	Date
Budget 2026 documents				
Taxation (Budget Measures) Bill (No 3)				
1	IR2026/143	Policy report	Draft Cabinet paper – Taxation (Budget Measures) Bill (No 3): Approval for introduction	01/05/2026
2	LEG-26-SUB-0094	Cabinet paper	Taxation (Budget Measures) Bill (No 3): Approval for Introduction	14/05/2026
3	LEG-26-MIN-0094	Cabinet minute	Taxation (Budget Measures) Bill (No 3): Approval for Introduction	21/05/2026
4	CAB-26-MIN-0178	Cabinet minute	Minute of Decision – Report of the Cabinet Legislation Committee: Period Ended 22 May 2026	25/05/2026
5	BN2026/172	Briefing note	Budget Bill: Summary of Committee of the whole House	04/06/2026
Budget 2026 reporting				
6	IR2026/081	Policy report	Budget 2026: Regulatory impact statements for the Revenue portfolio	19/03/2026
2026 Budget Economic and Fiscal Update				
7	IR2025/372	Finance report	2025 October Baseline Update submission for Vote Revenue	16/10/2025
8	IR2025/408	Finance report	2025 Half Year Economic and Fiscal Update for nondepartmental expenditure appropriations	21/11/2025
9	IR2025/457	Finance report	Approach to Budget 2026 and the 2026 Performance Plan	27/11/2025
10	IR2025/458	Finance report	Budget 2026 initiative submission for the Revenue portfolio	10/12/2025
11	IR2026/007	Finance report	2026 March Baseline Update submission for Vote Revenue	12/02/2026
12	IR2026/032	Finance report	2026 Preliminary Budget Economic and Fiscal Update for the Research and Development Tax Incentive appropriation	16/02/2026

#	Reference	Type	Title	Date
13	IR2025/504	Finance report	Vote Revenue Ministerial Certification of Contingent Liabilities and Contingent Assets as at 31 December 2025	19/02/2026
14	IR2026/024	Finance report	2026 Preliminary Budget Economic and Fiscal Update for non-departmental expenditure appropriations	19/02/2026
15	IR2026/027	Finance report	Output performance measures and targets for the 2026–27 financial year	25/02/2026
16	IR2026/070	Finance report	Vote Revenue: 2026 Budget Economic and Fiscal Update for the Research and Development Tax Incentive appropriation	16/04/2026
17	IR2026/077	Finance report	Vote Revenue: 2026 Budget Economic and Fiscal Update for non-departmental expenditure appropriations	20/04/2026
18	IR2026/139	Finance report	Budget 2026 Estimates for Vote Revenue – Vote Minister sign-off	01/05/2026
19	IR2026/154	Finance report	Vote Revenue: 2026 June Technical Adjustment Request	26/05/2026
Charities and not-for-profit changes (including donation tax credit change)				
20	IR2024/110	Policy report	Charities and not-for-profits overview	20/03/2024
21	IR2024/161	Policy report	Volunteers and honoraria: advice and response to the Minister for the Community and Voluntary Sector	10/04/2024
22	IR2024/237	Policy report	Tax policy options for the not-for-profit sector	17/07/2024
23	IR2024/238	Policy report	The income tax treatment of not-for-profit member transactions and options for simplification	17/07/2024
24	IR2024/199, T2024/2396	Policy report	Charity business income tax exemption	30/08/2024
25	BN2024/387, CVS20244176	Briefing note	Overview of ‘charitable purpose’ under the Charities Act 2005	20/09/2024
26	IR2024/359	Policy report	Donation tax concession caps	20/09/2024
27	IR2024/360	Policy report	Donor-controlled charities	20/09/2024
28	IR2024/454	Policy report	Charities and not-for-profits: Proposed 2025 public consultation	05/12/2024
29	BN2024/504	Briefing note	Charities and not-for-profits consultation: Scope and timing changes	11/12/2024

#	Reference	Type	Title	Date
30	IR2024/482, T2024/3292	Policy report	Reducing expenditure on donation tax concessions	11/12/2024
31	BN2025/032	Briefing note	Summary of the "charity business income tax exemption" issue	31/01/2025
32	BN2025/042	Briefing note	Taxation and the not-for-profit sector: Updated officials' issues paper and timeline	07/02/2025
33	BN2025/047	Briefing note	Revenue impact of charity business income and other not-for-profit income tax exemption proposals	10/02/2025
34	BN2025/044	Briefing note	Reducing expenditure on donation tax credits - follow up advice	11/02/2025
35	IR2025/079, T2025/635	Policy report	Reducing expenditure on donation tax credit – further advice on options	13/03/2025
36	BN2025/135	Briefing note	Taxation of not-for-profits: Possible in-principle decisions	21/03/2025
37	BN2025/149	Briefing note	Reducing expenditure on donation tax credits – impact if school activity donations are treated differently	28/03/2025
38	BN2025/155	Briefing note	Reducing expenditure on donation tax credits – delivery of an option to retain current donation tax credit entitlements for school donations	31/03/2025
39	IR2025/146	Policy report	Taxation and the not-for-profit sector – submission summary and next steps	04/04/2025
40	IR2025/169	Policy report	Charities and NFPs tax issues announcements	17/04/2025
41	BN2025/213	Briefing note	Not-for-profits: Inland Revenue advice to submitters and stakeholders	06/05/2025
42	IR2025/257	Policy report	Taxation and the not-for-profit sector: Recommendations from officials	28/08/2025
43	IR2025/258	Policy report	Taxation and the not-for-profit sector: Supplementary Report	28/08/2025
44	BN2025/385	Briefing note	Taxation and the not-for-profit sector: Draft media statement, Q&A and proactive release	16/10/2025
45	BN2025/411	Briefing note	Taxation and the not-for-profit sector: Timelines and consultation	16/10/2025
46	BN2025/443	Briefing note	Not-for-profits: Inland Revenue advice to the sector during targeted consultation	30/10/2025
47	BN2026/060	Briefing note	Taxation and the not-for-profit sector: Virtual meetings with submitters	25/02/2026

#	Reference	Type	Title	Date
48	IR2026/083	Policy report	Taxation and the not-for-profit sector: Interim update and possible lines of communication	13/03/2026
49	BN2026/119	Briefing note	Taxation and not-for-profit sector draft Regulatory Impact Statements	09/04/2026
Non-resident contractors' tax exemption for aircraft asset leasing				
50	IR2025/364	Policy report	Non-resident contractors' tax: asset leasing	24/09/2025
51	IR2026/001	Policy report	Non-resident contractors' tax: Budget 2026 policy options for aircraft asset leasing	28/01/2026
Company loans to shareholders				
52	IR2024/383, T2024/2730	Policy report	Integrity measures (making imputation work)	09/10/2024
53	IR2024/423, T2024/3336	Policy report	Advice on integrity measures	11/12/2024
54	IR2025/165	Policy report	Loans to shareholders – case studies and data from company liquidations	14/05/2025
55	BN2025/378	Briefing note	Timeframes and smoothing options for company loans to shareholders	09/09/2025
56	BN2025/406	Briefing note	Taxation of loans made by companies to shareholders - revised Cabinet paper and issues paper	06/10/2025
57	BN2025/425	Briefing note	Shareholder loans - information for joint Ministers' meeting on 23 October	21/10/2025
58	IR2025/440	Policy report	Shareholder loans design features	06/11/2025
59	CBC-25-SUB-0064	Cabinet minute	Consulting on the taxation of loans made by companies to shareholders – Release of consultation paper	24/11/2025
60	CBC-25-MIN-0064	Cabinet minute	Taxation of Loans Made by Companies to Shareholders: Release of Consultation Paper	24/11/2025
61	CAB-25-MIN-0428	Cabinet minute	Report of the Cabinet Business Committee: Period Ended 28 November 2025	28/11/2025
62	BN2026/055	Briefing note	Shareholder loans – consultation feedback and next steps	19/02/2026
Working for Families: Family scheme income and residence requirements				
63	IR2025/379, T2025/2673, REP/25/10/818	Policy report	Working for Families: Changes to residency requirements, information sharing and definition of income	29/10/2025

#	Reference	Type	Title	Date
64	BN2026/121	Briefing note	BUDGET SENSITIVE: Fiscal implications in Working for Families report IR2026/090	09/04/2026
65	IR2026/090	Policy report	Working for Families: Design decisions to simplifying the definition of family scheme income and residence requirements	09/04/2026
66	BN2026/128	Briefing note	BUDGET SENSITIVE: Policy Decisions in Working for Families report IR2026/090	15/04/2026
67	BN2026/148	Briefing note	Budget Bill - Family scheme income legislative flexibility	08/05/2026
Foreign Investment Fund changes				
68	IR2025/161	Policy report	Timeframes for further FIF changes and migrant related reforms – Phase One and Two	08/04/2025
69	IR2025/345	Policy report	Reducing tax barriers to retaining and attracting highly skilled people: phase two	21/08/2025
70	IR2025/405	Policy report	Reducing tax barriers to retaining and attracting people with skills and capital: policy decisions	19/11/2025
71	BN2026/067	Briefing note	Going for Growth Ministers' meeting 11 March	26/02/2026
Changes to financial arrangements rules to support migrants				
72	IR2025/431	Policy report	Financial arrangements rules – options to support new migrants	11/11/2025
73	IR2026/053	Policy report	Financial arrangements rules – decisions on migrant-specific proposals following consultation	31/03/2026
Non-resident contractors' tax modernisation				
74	IR2026/026	Policy report	Targeted consultation outcomes on proposals to modernise and simplify non-resident contractors' tax	09/03/2026
75	BN2026/122	Briefing note	Information on non-resident contractors' tax for the joint Ministers meeting on 20 April	15/04/2026
Research and Development Tax Incentive changes				
76	IR2025/376, REQ-0019154	Policy report	Options for enhancing the Research and Development Tax Incentive	06/11/2025
77	BN2025/452	Briefing note	RDTI: Information further to 6 November 2025 report	20/11/2025
78	BN2025/482	Briefing note	RDTI Ministers' Meeting	01/12/2025
79	IR2025/491, REQ-0024980	Policy report	RDTI – Options to progress	10/12/2025

#	Reference	Type	Title	Date
80	IR2026/040, REQ-0027276	Policy report	RDTI options for Budget 2026	18/02/2026
81	BN2026/073	Briefing note	RDTI and internal software	05/03/2026
Fringe benefit tax changes				
82	IR2025/220	Policy report	Fringe benefit tax review update	27/05/2025
83	IR2026/069	Policy report	Fringe benefit tax review – options to progress	05/03/2026
Changes to thin capitalisation rules for foreign-owned banking groups				
84	IR2025/100	Policy report	Determining Funding Costs of Permanent Establishments of Foreign Banks	09/04/2025
85	IR2025/331	Policy report	Determining Funding Costs of Branches of Foreign Banks	31/07/2025
86	BN2025/347	Briefing note	Communications Plan for Consultation on Determining Funding Costs of Permanent Establishments of Foreign Banks	03/09/2025
87	IR2025/464	Policy report	Determining Funding Costs of Branches of Foreign Banks	27/11/2025
88	IR2025/493	Policy report	Approval to consult on changes to taxation rules for foreign-owned New Zealand banking groups	12/12/2025
89	IR2026/066	Policy report	Changes to tax rules for foreign-owned New Zealand banking groups	13/03/2026

#	Reference	Type	Title	Date
Considered but discontinued projects				
Investment Boost				
90	IR2025/348, HUD2025-007930	Policy report	Extending Investment Boost to certain residential buildings	11/09/2025
91	IR2025/468, HUD2025-008735	Policy report	Extending Investment Boost to build-to-rent developments	10/12/2025
Software subsidy for small businesses				
92	IR2025/475	Policy report	Software subsidy for small businesses	10/12/2025

Information withheld

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).

Where this is the case, the relevant sections of the Act that would apply are identified.

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

Sections of the Act under which information was withheld:

6(a) to prevent prejudice to the security or defence of New Zealand or the international relations of the Government

6(c) to prevent prejudice to the maintenance of the law, including the prevention, investigation, and detection of offences, and the right to a fair trial

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

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

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

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

9(2)(h) to maintain legal professional privilege

Where a document included in this information release attached a draft version of a later published document (such as a regulatory impact statement) the draft document has been withheld under section 9(2)(g)(i). The final published documents are available on Inland Revenue or the Treasury's website (as applicable).

Information publicly available

The following links are to previous information releases and may be linked to the advice being published as part of this release:

Regulatory Impact Statements for items included in the Taxation (Budget Measures) Bill (No 3):
Taxation (Budget Measures) Bill (No 3) – Regulatory impact statements

Information relating to charities and not-for-profit changes:
Taxation and the not-for-profit sector – information release

Information relating to the increase in the in-work tax credit: Increase to the in-work tax credit – Information release

Some information relating to Budget 2026 has previously been released under the OIA:
26OIA1922 response
26OIA1795 response
26OIA1293 response
26OIA1191 response

Information relating to Revenue initiatives considered for Budget 2026 has also been released by the Treasury:
http://www.treasury.govt.nz/publications/budgets/budget-2026

Availability

This proactive release is available on Inland Revenue's Tax Policy website here: Publications.

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Tax policy report

Inland Revenue
Te Tari Taake

Draft Cabinet paper – Taxation (Budget Measures) Bill (No 3): Approval for introduction

Date	1 May 2026	**Priority**	High
Security level	Budget sensitive	**Report number**	IR2026/143
Bill name	Taxation (Budget Measures) Bill (No 3)		

Action sought		**Deadline**
Minister of Finance	**Authorise** lodgement of the finalised Cabinet paper	14 May 2026
Minister of Revenue	**Agree** to begin ministerial consultation from 7 May **Authorise** lodgement of the finalised Cabinet paper	7 May 2026 14 May 2026

Purpose
This report asks you to approve and lodge the attached Cabinet Legislation Committee paper (LEG paper) with the Cabinet Office by 10am Thursday 14 May 2026 for consideration at the Cabinet Legislation Committee meeting on Thursday 21 May 2026.

Contact for phone discussion, if required			
Name	**Position**	**Phone number**	**First contact**
Maraina Hak	Policy Director	s 9(2)(a)	✓
Ella Yeatman	Policy Advisor		☐

Draft Cabinet paper – Taxation (Budget Measures) Bill (No 3): Approval for introduction

Summary

1 This report asks you authorise lodgement of the attached Cabinet Legislation Committee paper (LEG paper) with the Cabinet Office by 10am Thursday 14 May 2026 for consideration at the Cabinet Legislation Committee meeting on Thursday 21 May 2026. Ministerial consultation will need to be undertaken before lodgement, but after 7 May 2026, once Cabinet has considered the Budget Cabinet paper.

2 The LEG paper seeks approval to introduce a Bill on 28 May 2026. The Bill will contain tax measures that Cabinet will consider as part of Budget 2026.

Policy items approved by Cabinet

3 The Bill will give effect to the tax measures Cabinet considers as part of the Budget 2026 package on 7 May 2026 that are agreed to progress as part of Budget day legislation, including:

- A permanent exemption from non-resident contractors' tax for the leasing of aircraft and parts,
- A donation tax credit threshold of $100,000 (a maximum tax credit entitlement of $33,333.33),
- Changes to tax a shareholder on an outstanding loan six months after the company is removed from the Companies Register, and
- Several changes to the Working for Families scheme, including
  - Removing low-risk adjustments from the family scheme income definition, and increasing the "other payments" adjustments de minimis to $8,000 for family scheme income, and
  - Simplifying the residence requirements by requiring both the principal caregiver and a dependent child to be physically present and ordinarily resident in New Zealand with a six-week overseas travel exemption before payments stop.

New Zealand Bill of Rights Act 1990

4 The Ministry of Justice will undertake the required Bill of Rights Act vetting. Although not expected, we will advise if any issues arise from this process.

Proactive release

5 We propose to proactively release the Cabinet paper, Cabinet minutes and key advice papers with appropriate redactions at the same time as all other Budget 2026 material is released.

Consultation

6 The Treasury was informed of the contents of this report and the LEG paper.

Next steps

7 Subject to your agreement, the attached draft LEG paper should be circulated for ministerial consultation after Cabinet has considered the Budget Cabinet paper on 7 May 2026.

8 Following this consultation, the LEG paper should be finalised and lodged with the Cabinet Office before 10am on Thursday 14 May 2026 for the Cabinet Legislation Committee meeting on 21 May 2026.

9 The Bill, departmental disclosure statement and final regulatory impact statements need to be lodged alongside the LEG paper. These will be provided to your office prior to lodgement. You have already received the draft regulatory impact statements for the Revenue portfolio.

10 We will also work with your office to ensure the appropriate publicity for the introduction of the Bill, as part of Budget 2026 announcements.

Recommendations

We recommend that you:

1 **Agree** to refer the draft Cabinet Legislation Committee paper for Ministerial consultation.

Agreed/Not Agreed

Minister of Revenue

2 **Authorise**, subject to ministerial consultation, lodgement of the finalised Cabinet paper with the Cabinet Office before 10am on Thursday 14 May 2026 for consideration by the Cabinet Legislation Committee on Thursday 21 May 2026.

Authorised/Not authorised	Authorised/Not authorised
Minister of Finance	*Minister of Revenue*

s 9(2)(a)

Maraina Hak

Policy Director

Policy | Inland Revenue

1 May 2026

Hon Nicola Willis	Hon Simon Watts
Minister of Finance	**Minister of Revenue**
/ /2026	/ /2026

Budget Sensitive

Office of the Minister of Finance

Office of the Minister of Revenue

Cabinet Legislation Committee

TAXATION (BUDGET MEASURES) BILL (NO 3): APPROVAL FOR INTRODUCTION

Proposal

1 This paper seeks the Cabinet Legislation Committee's agreement to introduce the Taxation (Budget Measures) Bill (No 3) under urgency on 28 May 2026. This Bill introduces amendments to the:

1.1 Income Tax Act 2007;

1.2 Tax Administration Act 1994;

1.3 Student Loan Scheme Act 2011.

2 The Taxation (Budget Measures) Bill (No 3) holds a category 3 priority on the 2026 Legislative Programme (must be passed before the 2026 General Election).

Policy

3 The Bill will implement the policy items listed below. A Bill is necessary as amendments to existing legislation are required to implement the proposed policy changes.

4 The Bill will give effect to the following tax measures that Cabinet agreed to be delivered as part of Budget 2026 on 7 May 2026:

4.1 Non-resident contractors' tax - exemption for aircraft asset leasing;

4.2 Introducing a ceiling on donation tax credit entitlements;

4.3 Company loans to shareholders;

4.4 Working for Families – residency requirements and family scheme income.

5 The Bill contains detailed design features to give effect to Cabinet's decisions. Minor and technical changes may still be required prior to introduction on Budget Day to ensure the policies operate as intended.

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Non-resident contractors' tax - exemption for aircraft asset leasing

6 This Bill introduces a permanent exemption from non-resident contractors' tax for the dry leasing of aircraft and parts. This change will apply from 1 April 2026.

7 In many cases, the non-resident contractors' tax currently charged on aircraft leasing is much greater than the potential tax liability of the non-resident lessor, and this is typically passed on as an additional cost to the New Zealand lessee. This presents a barrier to the leasing of these capital assets by New Zealand businesses.

Introducing a ceiling on donation tax credit entitlements

8 This Bill introduces a donation tax credit threshold of $100,000 (a maximum tax credit entitlement of $33,333.33). Current settings allow donation tax credits at a rate of 33⅓% up to the taxpayer's taxable income.

9 This change continues to support charitable giving across a broad donor base, whilst managing the Government's expenditure on the donation tax credit scheme. This change will apply to gifts of money made on and after 1 April 2027.

Company loans to shareholders

10 This Bill also introduces changes to tax a shareholder on an outstanding loan six months after the lending company is removed from the register of companies. This strengthens existing rules that tax loans when they are forgiven, by providing a clear and certain timing rule that will support tax compliance and improve Inland Revenue's ability to collect tax.

11 These changes will apply from 4 December 2025 (the release date of the officials' issues paper).

Working for Families – residency requirements and family scheme income

12 This Bill gives effect to several changes to the Working for Families scheme as follows:

12.1 simplifying the residence requirements by requiring both the principal caregiver and a dependent child to be physically present and ordinarily resident in New Zealand,

12.2 providing a six-week overseas travel exemption before payments stop, as well as exemptions for longer periods of absence for specified reasons,

12.3 removing low-risk adjustments from the family scheme income definition,

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12.4 increasing the “other payments” adjustment de minimis to $8,000 for family scheme income, and

12.5 introducing an empowering provision for certain family scheme income adjustments to be applied by Order in Council.

13 The empowering provision for family scheme income adjustments is narrower than the wording agreed by Cabinet, in response to feedback from PCO. Further changes to the empowering provision are being considered for a future legislative vehicle.

14 Changes to these settings will reduce complexity for customers when applying for Working for Families, and potential future debt. These changes will apply from 1 April 2027.

Impact analysis

15 Regulatory impact statements were prepared for the following policy items in the Bill and are submitted with this paper:

15.1 Introducing a ceiling on donation tax credit entitlements;

15.2 Company loans to shareholders;

15.3 Working for Families – residency requirements and family scheme income.

16 The Ministry for Regulation has granted a regulatory impact analysis exemption to the following proposal, on the basis that its impacts are, or are likely to be, limited/minor and easy to assess;

16.1 Non-resident contractors' tax - exemption for aircraft asset leasing.

Compliance

17 This Bill complies with:

17.1 the principles of the Treaty of Waitangi;

17.2 advice from the Treaty Provisions Officials Group on any Treaty of Waitangi provisions (include a summary of any concerns raised);

17.3 the rights and freedoms contained in the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993;

17.4 the disclosure statement requirements;

17.5 the principles and guidelines set out in the Privacy Act 2020;

17.6 relevant international standards and obligations;

17.7 the Legislation Guidelines (2021 edition), which are maintained by the Legislation Design and Advisory Committee.

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Consultation

18 Consultation on the proposals in this Bill has been undertaken, as outlined below (subject to Budget sensitivity).

Relevant Government Departments or Other Public Bodies

19 In developing the proposals set out in the Bill, Inland Revenue consulted with the Treasury, the Ministry of Social Development, the Department of Internal Affairs, the Ministry for Culture and Heritage, New Zealand Customs Service, and the Ministry of Business, Innovation and Employment.

Relevant private sector organisations and public consultation processes

20 The Government released a discussion document in May 2025 on a set of proposals for improving Working for Families, including the family scheme income adjustments and residence requirement proposals. Stakeholders frequently expressed their concerns of complexity within the scheme, impact on customers in debt, stress and difficulty managing their entitlement. While detailed comments were limited, feedback on both proposals supported simplification. Broader themes from feedback (both written submissions and stakeholder workshops) were considered alongside customer insights. Together these have influenced the problem definition and detailed design of the proposals.

21 Inland Revenue released an officials' issues paper in December 2025 on proposals to improve the way new loans by companies to shareholders are taxed. This included the proposal to tax a shareholder on an outstanding loan after the company is removed from the register of companies. Stakeholders were generally supportive of this proposal.

22 Inland Revenue undertook targeted consultation with stakeholders on options for non-resident contractors' tax changes for the airline industry, including the option for an exemption. Stakeholders agree with the merits of an exemption for non-resident contractors' tax for aircraft asset leasing.

The Government Caucus and Other Parties Represented in Parliament

23 The coalition Government caucuses represented in Parliament have been consulted on the initiatives included in the Bill to ensure they are aligned with the coalition agreements.

Binding on the Crown

24 The Bill amends the Acts listed in paragraph 1 and, where those Acts bind the Crown either in whole or in part, this Bill does not change that position.

Creating new agencies or amending law relating to existing agencies.

25 This legislation will not create a new agency.

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26 This legislation will not amend the existing coverage of the Ombudsman Act 1975, the Official Information Act 1982, or the Local Government Official Information and Meetings Act 1987.

Allocation of decision-making powers

27 The Bill does not involve the allocation of decision-making powers between the executive, the courts, and tribunals.

Associated regulations

28 No regulations are required to bring the proposed Bill into force.

Other instruments

29 The Bill proposes a new Order in Council mechanism to apply certain income adjusting types within the definition of family scheme income that is contained within the Income Tax Act 2007.

Definition of Minister/department

30 The Bill does not contain a definition of Minister, department, or chief executive.

Commencement of legislation

31 Each provision of the Bill comes into force on the date specified in the Bill for that provision.

Parliamentary stages

32 The Bill should be introduced on 28 May 2026 and passed as soon as possible under urgency.

Communications

33 The Minister of Finance will announce the Budget 2026 proposals contained in this Bill on Budget Day. Budget documents and other material to support this announcement are currently being prepared.

34 Inland Revenue will prepare a commentary on the Bill that will be published at the same time the Bill is introduced to the House. Inland Revenue will also include details of the new legislation in the Act Commentary after the Bill is enacted.

Proactive Release

35 We propose to proactively release this Cabinet paper, associated minutes, and key advice papers with appropriate redactions alongside all other Budget 2026 material.

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Recommendations

We recommend that the Committee:

1 note that the Taxation (Budget Measures) Bill (No 3) holds a category 3 priority on the 2026 Legislation Programme (must be passed before the 2026 General Election);

2 note that the Bill will make amendments to the:

2.1 Income Tax Act 2007;

2.2 Tax Administration Act 1994;

2.3 Student Loan Scheme Act 2011;

3 approve the Taxation (Budget Measures) Bill (No 3) for introduction on Budget Day, subject to the final approval of the Government caucus and sufficient support in the House of Representatives;

4 agree that minor and technical changes to give effect to proposals agreed to by Cabinet and contained in the Bill can be made prior to introduction on Budget Day;

5 note the Minister of Finance and the Leader of the House have been delegated authority by Cabinet to decide which legislation will progress under urgency on Budget Day.

Authorised for lodgement

Hon Nicola Willis

Minister of Finance

Hon Simon Watts

Minister of Revenue

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Cabinet Legislation Committee

Minute of Decision

This document contains information for the New Zealand Cabinet. It must be treated in confidence and handled in accordance with any security classification, or other endorsement. The information can only be released, including under the Official Information Act 1982, by persons with the appropriate authority.

Taxation (Budget Measures) Bill (No 3): Approval for Introduction

Portfolios **Finance / Revenue**

On 21 May 2026, the Cabinet Legislation Committee:

1 **noted** that the Taxation (Budget Measures) Bill (No 3) (the Bill) holds a category 3 priority on the 2026 Legislation Programme (a priority to be passed before the 2026 General Election);

2 **noted** that the Bill will amend the:

2.1 Income Tax Act 2007;

2.2 Tax Administration Act 1994;

2.3 Student Loan Scheme Act 2011;

3 **approved** the Taxation (Budget Measures) Bill (No 3) [IRD 28643/3.0] for introduction;

4 **agreed** that minor and technical changes to give effect to proposals agreed by Cabinet and contained in the Bill can be made prior to introduction;

5 **noted** that the Minister of Finance and the Leader of the House will confirm the legislation to progress under urgency on Budget Day.

Sam Moffett
Committee Secretary

Present:
Rt Hon Winston Peters
Hon Paul Goldsmith
Hon Louise Upston (Chair)
Hon Penny Simmonds
Hon Brooke van Velden
Hon Casey Costello
Hon Nicola Grigg
Hon James Meager
Hon Scott Simpson
Hon Cameron Brewer
Hon Andrew Hoggard
Stuart Smith MP
Jamie Arbuckle MP

Officials present from:
Office of the Minister of Commerce and Consumer Affairs
Officials Committee for LEG

CAB-26-MIN-0178

Cabinet

Minute of Decision

This document contains information for the New Zealand Cabinet. It must be treated in confidence and handled in accordance with any security classification, or other endorsement. The information can only be released, including under the Official Information Act 1982, by persons with the appropriate authority.

Report of the Cabinet Legislation Committee: Period Ended 22 May 2026

On 25 May 2026, Cabinet made the following decisions on the work of the Cabinet Legislation Committee for the period ended 22 May 2026:

Not in scope

LEG-26-MIN-0094	**Taxation (Budget Measures) Bill (No 3): Approval for Introduction** Portfolios: Finance / Revenue	CONFIRMED

Not in scope

Not in scope

Rachel Hayward
Secretary of the Cabinet

Briefing note

Inland Revenue
Te Tari Taake

Reference	BN2026/172
Date	4/06/2026
To	Revenue Advisor, Minister of Revenue – Angela Graham Private Secretary, Minister of Revenue – Melissa Zhen
From	Ella Yeatman
Subject	**Budget Bill: Summary of Committee of the whole House**

Purpose

1 This briefing note provides you with information about the passage of the Taxation (Budget Measures) Bill (No 3). The Bill was introduced on 28 May 2026 and progressed Committee of the whole House stage that evening and the following morning. Royal assent is expected in the following days.

2 This briefing note summarises the Committee of the whole House stage, specifically issues raised by members. It also notes the key messages that we advised the Minister for responding to members' questions.

3 Opposition parties supported the Bill through all readings, and members generally supported the individual measures in the Bill. Of most concern was the impact of the donation tax credit cap on philanthropic giving.

Changes to donation tax credit

4 The questions relating to the donation tax credit changes included:

- How this cap may have an impact on charitable giving. We advised this does not target the amount that can be donated, only the amount of gifts qualifying for the tax credit. We advised (consistent with the regulatory impact statement) that evidence is inconclusive on whether a reduction in donation tax credit entitlements would produce a behavioural response by donors.
- How this cap may have an impact on sectors supported by charitable giving.
- Whether there may be a change in donation behaviour between the Bill being introduced and the change coming into effect. We advised we may expect donors to bring their donation forward and the revenue estimates reflect this.
- Why this change was chosen to respond to integrity concerns. We advised this change was a simpler response compared to changing the donor-controlled charities rules.
- Whether there would be scope to look at the rules concerning deductions for companies who donate. We advised most donations come from individuals.
- Whether Inland Revenue will monitor substitution donations. We advised Inland Revenue will be monitoring splitting donations and donations through companies.
- Why this change was legislated now but comes into effect 1 April 2027. We advised this gives taxpayers certainty on their entitlements so they can plan their response.

Non-resident contractors' tax exemption for aircraft asset leasing

5 The questions relating to the non-resident contractors' tax exemption for aircraft asset leasing included:

- Whether other options were considered to resolve the tax barrier for the industry.
- How the problem definition was established and if consultation was undertaken.
- Whether this change could lead to subsequent exemptions for other industries. We advised that other industries have not been considered for the current proposal but could be considered in future.
- How this change would apply to aircraft lessors based in countries that are eligible for relief under their double tax agreement. We advised that this change would simply extend that relief to all lessors in all countries.
- Why this change is retrospective. We advised this change is retrospective to provide taxpayers with certainty.

Company loans to shareholders

6 The questions relating to the company loans to shareholders change included:

- Why the change applies from 4 December 2025. We advised this is tied to the release date of the officials' issues paper and mitigates the risk of structuring opportunities.
- Why six months was the chosen timeframe. We advised this time frame allows companies that are inadvertently removed from the register to be reinstated.
- How the change interacts with the financial arrangements rules We advised that the new rule applies to all shareholder loans irrespective of size.
- Why option 6 (improving record keeping) was not included in this Bill. We advised this does not require legislative change.
- How Inland Revenue will communicate this change with companies that have already been removed from the register.

Working for Families: family scheme income and residence requirements

7 The questions relating to the Working for Families changes included:

- Why these changes need to be legislated now but come into effect 1 April 2027. We advised this allows Inland Revenue enough time to establish system changes and enables notices of entitlement can go to customers before the next tax year begins.
- Whether income types that are being removed from family scheme income would become income exempt. We advised this is not the case.
- What the impact of the removal of overseas pensions and salaries, and income equalisations from family scheme income will be.
- Why an Order in Council is required for these changes. We advised this mechanism will allow changes to be made quickly if an integrity risk were to arise.
- Whether the Order in Council mechanism is a Henry VIII clause.
- Whether there are any fairness concerns by removing some types of income. We advised income types that are being removed have a low risk of abuse or structuring.
- What consultation has taken place.
- Why 42-days was chosen as the time frame. We advised this is to align with the summer school holidays.

Ella Yeatman
Policy advisor
s 9(2)(a)

Tax policy report

Inland Revenue
Te Tari Taake

Budget 2026: Regulatory impact statements for the Revenue portfolio

Date	19 March 2026	**Priority**	High
Security level	Budget sensitive	**Report number**	IR2026/081

Action sought		**Deadline**
Minister of Finance	**Note** the contents of this report **Refer** the regulatory impact statements to the Minister for Regulation	24 March 2026
Minister of Revenue	**Note** the contents of this report **Refer** the regulatory impact statements to the Minister for Regulation	24 March 2026

Purpose

This report:

- Attaches draft regulatory impact statements for the Budget 2026 initiatives in the Revenue portfolio; and
- Provides a short summary of key points raised in the draft regulatory impact statement for each initiative.

Contact for phone discussion, if required

Name	**Position**	**Phone number**	**First contact**
Maraina Hak	Policy Director	s 9(2)(a)	✓
Ella Yeatman	Policy Advisor		☐

Budget 2026: Regulatory impact statements for the Revenue portfolio

Impact analysis for Budget 2026 proposals

1 Policies that are progressed as part of Budget 2026 would deliver regulatory change. This means that the regulatory impact analysis (RIA) requirements apply, which generally involve providing a Regulatory Impact Statement (RIS). RISs provide a summary of analysis and advice provided to Ministers throughout the policy process, and that can include an assessment of Treaty of Waitangi implications. RISs are also rated for quality, which includes an assessment of the entire policymaking process.[1]

2 Budget 2026 guidance states that a RIS (at least in draft form) is to be provided to the portfolio Minister, Minister of Finance and Minister for Regulation to inform Budget Ministers' decisions. The attached RISs are all in draft form, meaning they have not yet been through the formal RIA quality assurance process.

3 RISs are required to compare the preferred option of the responsible Minister(s) with the range of feasible options, including officials' recommendation, against the stated policy objectives. Ministers have not yet taken decisions on some proposals, in which case we do not yet know Ministers' preferred option. When Ministers' preferred option is not reflected in the draft RIS, this will be updated in the final RIS that accompanies the relevant Cabinet paper.

4 A list of draft RISs that are attached to this report is contained in Appendix 1. RIS summaries are contained in Appendix 2.

Proposals without RISs attached

5 The Ministry for Regulation has granted exemptions from the RIA requirements to the following proposals (on the basis that impacts are, or are likely to be, limited/minor and easy to assess) that are progressing as potential Budget 2026 initiatives:

- modernise non-resident contractor tax proposal
- reduce non-resident contractor tax for asset leasing in the airline industry proposal, and
- s 9(2)(f)(iv)

6 The RIA requirements apply to the discussion document on the proposed information sharing agreement between Inland Revenue and the New Zealand Customs Service for Working for Families. However, no separate RIS is required at this stage of the process because the discussion document itself is assessed against the quality assurance criteria.

7 We will report to you on the charities and not-for-profits proposals on 26 March. RISs for these proposals will be provided to you at a later date subject to your direction on these proposals (we will work with your offices on appropriate timing):

- tax policy settings for the donation tax credit
- donor-controlled charities
- tax policy settings for taxable not-for-profits, and
- s 9(2)(f)(iv)

8 RISs for the following proposals will be provided by the Ministry of Social Development to Ministers on 1 April:

- welfare reform: Working for Families tax credits
- Working for Families: residence requirements, and

[1] Quality Assurance of Regulatory Impact Statements Guidance Note (August 2025)

- Working for Families: family scheme income.

9 s 9(2)(g)(i)

10 Based on feedback from the Joint Ministers' meeting on 16 March, the following initiatives are no longer being progressed for Budget 2026 and so no RIS is being provided for:

- s 9(2)(f)(iv)
- s 9(2)(f)(iv)
- Research and Development Tax Incentive: in-year payments.

Consultation

11 The Treasury was consulted during the preparation of this report and provided comments on specific draft RISs.

12 The Ministry of Business, Innovation and Employment was consulted on the Research and Development Tax Incentive RISs.

13 Further inter-agency consultation will be undertaken on some proposals to inform the final RISs. More broadly, other agencies have been consulted as part of policy development on some proposals.

Next steps

14 The draft RISs should be referred to the Minister for Regulation as required by Budget 2026 guidance. The draft RISs will be made available to inform Budget Ministers' decisions.

15 Final RISs will be provided when the Cabinet Legislation Committee considers legislative approval of each proposal, whether that is as part of Budget night legislation or as part of the next annual rates taxation Bill to be introduced later this year.

Recommendations

We recommend that you:

1	**Note** that for Budget initiatives in the Revenue portfolio, draft regulatory impact statements (RISs) are required to be provided to the Minister of Finance, Minister for Regulation, and the Minister of Revenue in advance of decisions by Budget Ministers.

2	**Refer** the attached draft RISs to the Minister for Regulation.	
	Referred/not referred	Referred/not referred
	Minister of Finance	*Minister of Revenue*

s 9(2)(a)

Maraina Hak
Policy Director
Policy | Inland Revenue
19 March 2026

Hon Nicola Willis
Minister of Finance
/ /2026

Hon Simon Watts
Minister of Revenue
/ /2026

Appendix 1 – Draft RISs for Budget 2026 proposals

The following draft RISs are attached to this report:

- Foreign investment funds: phase two
- Foreign investment funds: lifting de minimis threshold
- Financial arrangement rules amendments to support new migrants*****
- Changes to thin capitalisation rules for foreign-owned New Zealand banking groups*****
- Improving taxation of loans made by companies to shareholders
- Simplifying motor vehicle fringe benefit tax rules*****
- Research and Development Tax Incentive: mining exclusions
- Research and Development Tax Incentive: Commissioner's discretionary powers
- Research and Development Tax Incentive: internal software.

***** Starred initiatives have been recommended by officials to be added to the Tax Policy Scorecard. If Joint Ministers agree to add these to the Scorecard, they would no longer be Budget 2026 proposals.

Appendix 2 – RIS summaries for Budget 2026 proposals

RIS summaries begin from the next page.

Improving taxation of loans made by companies to shareholders

Problem definition

Companies controlled by a few shareholders often lend money to those shareholders, which can create tax integrity issues if loans are not repaid or taxed appropriately. The current rules tax these loans as dividends if the loan is forgiven or if the interest rate charged is below a prescribed rate.

Under the status quo, some shareholder loan balances can grow to an unmanageable level that does not match the shareholder's financial resources to repay the loan. This means tax is not collected, particularly if the lending company is wound up. While current rules can tax a shareholder loan on forgiveness, this taxing point is often uncertain and may be many years after the company has ceased, at which stage it is impractical to collect tax on the loan.

A secondary problem is there can be inadequate record keeping to support tax compliance (on both shareholder loans and calculating amounts that are treated as taxable dividends) when a company ceases.

Options and recommendation

The options in the RIS are not mutually exclusive, meaning a combination of options may be most effective.

1. Status quo.
2. Time limit for repaying new company loans to shareholders.
3. Targeted intervention for loans at risk of not being repaid.
4. Require loans to be documented with commercial terms.
5. Tax a shareholder on an outstanding loan six months after company is removed from the Companies Register **(Ministers' and officials' preferred option)**.
6. Improve record keeping for company cessation **(Ministers' and officials' preferred option)**.

Officials recommend option 5 and option 6 because they will improve tax collection, integrity and equity and help companies maintain the relevant information to support compliance.

Limitations

Data

- Shareholder loans are under-reported and people make mistakes when they do report them. The data is generally unreliable at an individual company level but is more meaningful at an aggregate level.

Risks

Consultation

- Public and targeted consultation has been used to refine the problem definition and proposed options.
- There was general support from stakeholders for taxing shareholder loans on removal of a company from the Companies Register and for improved record keeping (the recommended options 5 and 6).
- Most submitters opposed the proposed time-limit rule (option 2) because they considered it would be significant overreach, which would unduly impact ordinary practices and compliant shareholders.

Fiscal impact and outcomes

- Option 5 is currently estimated to raise approximately $38 million per annum ($146 million over the forecast period).
- The impact of the proposed changes will be monitored through data on outstanding shareholder loan balance trends particularly for companies that are removed from the Companies Register, and any improved record-keeping requirements that are introduced.

Inland Revenue report: 2025 October Baseline Update submission for Vote Revenue

Date:	16 October 2025	**Priority:**	Medium
Security level:	In confidence	**Report no:**	IR2025/372

Action sought

	Action sought	Deadline
Minister of Revenue	**Note** and **agree** to recommendations; and **Sign** and **forward** the attached submission and Attachment 1 to the Minister of Finance by **1:00pm Thursday, 23 October 2025**	1:00pm 23 October 2025

Contact for telephone discussion (if required)

Name	Position	Telephone
Nick Bradley	Enterprise Leader Finance Services (Chief Financial Officer)	s 9(2)(a)
Darren Cheevers	Domain Lead Finance Services	
Rachel Parker	Domain Lead Finance Services	

16 October 2025

Minister of Revenue

2025 October Baseline Update submission for Vote Revenue

Purpose

1. This report seeks your approval of the attached 2025 October Baseline Update (OBU) submission to the Minister of Finance for Vote Revenue.

Background

2. The October Baseline Update is a technical update of baselines for matters that do not raise significant policy issues or curtail new funding and therefore do not require Cabinet approval. All the proposed changes being requested in this report are limited to technical, non-discretionary matters and can be made by joint Ministers – the appropriation Minister and the Minister of Finance.

3. The Treasury administers the baseline process. This includes providing agencies with letter templates and setting the timeframes and due dates. The attached draft letter from you to the Minister of Finance follows the Treasury template.

4. Forecast changes to non-departmental appropriations and tax forecasts will be included in our 2025 Half-Year Economic and Fiscal Update (HYEFU) submission. These forecasts will be based on the Treasury macroeconomic forecasts of 28 October 2025. Our HYEFU 2025 submission is due to the Treasury on 7 November 2025. We will send you a report seeking joint approval for any forecast changes to appropriations shortly after the 2025 HYEFU submission.

5. Any decisions made by Cabinet or joint Ministers between 16 October 2025 and the 2025 HYEFU submission will also be captured in our 2025 HYEFU report.

6. The final OBU submission for Vote Revenue is due to the Minister of Finance by 1pm, Thursday 23 October 2025.

7. A copy of the proposed letter from you to the Minister of Finance for this baseline update is attached.

Overview of this baseline update submission

8. The following departmental matters are included in this submission:

   - a forecast adjustment to the departmental Capital Expenditure Permanent Legislative Authority appropriation
   - the departmental baseline roll out to 2029/30, and
   - a previous in-principle expense transfer request that is not required.

9. The following non-departmental matters are included in this submission:
    - the establishment of two new non-departmental other expenses annual appropriations:
        - Payments to Settle Residual Claims, and
        - Ex Gratia Payments
    - the non-departmental baseline roll out to 2029/30
    - approval of core data changes to a title and scope for two non-departmental appropriations, and
    - confirmation of three in-principle expense transfers from 2024/25 to 2025/26:
        - $39,000 for COVID-19 Resurgence Support Payment
        - $54,000 for COVID-19 Support Payment, and
        - $9,000 for Cost of Living payment.
10. Cabinet and joint Ministers' decisions made since Budget 2025 and up to 16 October 2025 and that impact Vote Revenue non-departmental appropriations have been included in this report for your information. There are no Cabinet or joint Ministers' decisions since Budget 2025 that impact departmental appropriations.

Details of proposed changes – departmental matters

Forecast change for planned departmental capital expenditure

11. Inland Revenue's departmental annual capital expenditure can be reduced for 2025/26 as our long-term asset management plans and required capital for Government initiatives have now been confirmed.

	$ million – increase / (decrease)				
Inland Revenue Department - Capital Expenditure PLA	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
BEFU 2025	47.700	42.900	40.400	40.000	40.000
OBU 2025	32.000	42.900	40.400	40.000	40.000
Forecast change - inc/(dec)	(15.700)	-	-	-	-

12. The forecast reduction of $15.700 million in 2025/26 in capital expenditure is included for your noting.

Other departmental matters

Baseline roll out to 2029/30 for departmental appropriations

13. As part of each October Baseline Update, departments are required to roll out their baseline by an additional year. This roll out preserves a five-year planning horizon within the Treasury Crown Financial Information System.

14. The baseline changes sought in this letter have been incorporated into the forecast financial statements, together with the adjustments necessary to accurately reflect estimated operating expenditure, cash flows and capital injections.

	$ million – increase / (decrease)				
	2025/26	2026/27	2027/28	2028/29	2029/30
Baseline (BEFU2025)	787.630	773.102	785.111	800.911	788.411
OBU 2025 – no changes	-	-	-	-	-
Baseline (after OBU 2025)	787.630	773.102	785.111	800.911	788.411

15. The rolled-out baseline of $788.411 million in 2029/30 is $12.500 million lower than the prior year. This reduction reflects a previous funding increase for depreciation expenditure in 2028/29 that reverses in 2029/30. There are no changes in the baseline over this 5-year period from the 2025 October Baseline Update.

Departmental in-principle expense transfer not required

16. As part of the 2025 March Baseline Update 2025 (IR2025/012 refers) you agreed to an in-principle expense transfer (IPET) of up to $3.000 million from 2024/25 to 2025/26 for the deferred cost for the implementation of international initiatives. As part of the October Baseline Update the final amount of IPETs are required to be confirmed after the year-end audit.

17. Our audited 2024/25 financial statements were signed on 30 September 2025. We can now advise that this funding transfer from 2024/25 to 2025/26 is no longer required. Greater certainty about the application dates and implementation cost means we can self-fund these initiatives from our 2025/26 baseline without the need for a funding transfer.

Details of proposed changes – non-departmental matters

A new Payments to Settle Residual Claims appropriation

18. We administer several closed payment schemes where a liability may remain for Inland Revenue to make a payment under the scheme. These closed schemes include the Cost of Living payment, COVID-19 Resurgence Support Payment, and COVID-19 Support payment.

19. Despite these schemes now being closed, customers s 9(2)(g)(i) . The value and level of disputed payment is expected to be very low, but we require an appropriation for the legal authority to make such payments. Retaining a separate appropriation with a nominal balance for each of these schemes creates additional administration for the Treasury and ourselves. We are therefore seeking a new combined appropriation to cover the rare instances where payments are made under these circumstances which are outside of the control of the Department.

20. We propose creating a new non-departmental other expenses appropriation for Payments to Settle Residual Claims, as follows:

Vote	Appropriation Minister	Title	Type	Scope
Revenue	Minister of Revenue	Payments to Settle Residual Claims	Non-departmental Other Expenses	This appropriation is limited to payments made to eligible recipients to settle residual claims for products Inland Revenue has previously administered.

21. If you jointly agree to establish this new appropriation, IR will seek a fiscally neutral transfer from the Cost of Living, the COVID-19 Resurgence Support Payment, and COVID-19 Support payment appropriations through the 2026 March Baseline Update submission. In the unlikely event that any material new funding requirement arises in the future, we will seek funding decisions from joint Ministers at the time.

22. We propose exempting this new appropriation from end-of-year performance reporting as the amount of the appropriation is less than $5 million (s15D(2)(b)(iii) of the Public Finance Act 1989).

23. We seek your agreement to submit this request for a new non-departmental Payments to Settle Residual Claims appropriation and request a performance reporting exemption.

A new Ex Gratia Payments other expenses annual appropriation

24. Occasionally we make ex gratia payments to customers. These are voluntary and not required by law but are given as a gesture of goodwill or reflecting a moral responsibility.

25. An ex gratia payment is a last resort action. IR have broad provisions in legislation, for example the care and management provisions in s6 and s6A of the Tax Administration Act 1994, that we apply before we consider an ex gratia payment.

26. The number and value of these payments is relatively small (c$20,000 a year), with the exception of a few large ex gratia payments made in the past, for example a $7.200 million payment was made in 2020/21 to compensate KiwiSaver members who were adversely impacted by a system migration delay.

27. Historically, we have funded all ex gratia payments from a departmental 'output expense' appropriation. However, under the Public Finance Act 1989 definitions for appropriation types, we have agreed with the Treasury and Audit NZ that ex gratia payments of this nature should more correctly be classified as a non-departmental 'other expense' appropriation.

28. The creation of a new ex gratia appropriation would not change the delegation levels set by Cabinet for these payments (CO(18)2 refers[1]). We would also continue to make ex gratia payments to staff or ex staff through our departmental output appropriations.

[1] Cabinet Office Circular, CO (18)2, Proposals with Financial Implications and Financial Authorities, 30 July 2018

29. We propose creating a new non-departmental appropriation for ex gratia payments to customers, as follows:

Vote	Appropriation Minister	Title	Type	Scope
Revenue	Minister of Revenue	Ex Gratia Payments	Non-departmental Other Expenses	This appropriation is limited to ex gratia payments in relation to Vote Revenue non-departmental activities.

30. If you jointly agree to establish this new appropriation, we would initially fund this appropriation through a fiscally neutral transfer of $0.050 million per annum from our departmental appropriations through our 2026 March Baseline Update submission. We would discuss with you funding sources on the rare occasions we need to exceed $0.050 million a year.

31. We propose exempting this new appropriation from end-of-year performance reporting as performance information is unlikely to be informative because we would not disclose individual ex gratia payments from a privacy or integrity of the tax system perspective (s15D(b)(ii) of the Public Finance Act 1989).

32. We seek your agreement to submit this request for a new non-departmental ex gratia appropriation and request a performance reporting exemption.

Baseline roll out to 2029/30 for non-departmental appropriations

33. The roll out of the non-departmental 2029/30 financial year for OBU includes any policy decisions or changes in funding profiles applicable to 2029/30 and not previously included in 2028/29. No forecasting adjustments which are not already accounted for in previous baseline updates are included in the roll out of 2029/30 within this submission.

Details of proposed changes – non-departmental in-principle expense transfers

34. As part of the 2025 June technical adjustment process, joint Ministers approved in-principle expense transfers (IPET) and early confirmation of up to $104,000 for three appropriations where the original claim period had passed but residual claims are still being settled (IR2025/252 refers).

35. Our audited 2024/25 financial statements were signed on 30 September 2025. Based on a confirmed non-departmental underspend of $102,000 in relation to these three appropriations, we are now confirming in-principle expense transfers of $102,000 from 2024/25 to 2025/26. The table below shows these amounts by appropriation:

	$million			
Vote Revenue	2024/25 Actual	2024/25 Budget	2024/25 Underspend	2025/26 IPET
Non-Departmental Other Expenses:				
COVID-19 Resurgence Support Payment	0.001	0.040	0.039	0.039
COVID-19 Support Payment	0.026	0.080	0.054	0.054
Cost of Living payment	0.001	0.010	0.009	0.009
Total Other Expenses	0.028	0.130	0.102	0.102

Other matters

Cabinet decisions

36. We have included the following Cabinet decisions which were approved between 14 April 2025 (BEFU 2025) and 16 October 2025 in this baseline update and which impact tax revenue.

	$ million – increase / (decrease)					
Vote Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	Reference
Crown Revenue and Receipts: Tax Revenue						
Other Persons	(0.228)	(0.397)	(0.412)	(0.428)	(0.428)	Measures for Inclusion in the Taxation (Annual Rates for 2025-26) Bill CAB-25 MIN-0224 EXP-25-MIN-0052
	0.050	0.200	0.200	0.200	-	Further Measures for Inclusion in the Taxation (Annual Rates for 2025-26) Bill CAB-25-MIN-0255
	(0.030)	(0.030)	(0.030)	(0.030)	(0.030)	Income Tax (Deemed Rate of Return on Attributing Interests in Foreign Investment Funds, 2024–25 Income Year) Order 2025 CAB-25-MIN-0240 LEG-25-SUB-0130
Fringe Benefit Tax	(1.870)	(1.870)	(1.870)	(1.870)	(1.870)	Income tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations (No 2) 2025 CAB-25-MIN-0240 LEG-25-MIN-0131
Company Income Tax	0.520	0.520	0.520	0.520	0.520	
GST	(0.900)	(3.700)	(3.700)	(3.700)	(3.700)	GST and Unincorporated Joint Ventures CAB-25-MIN-0263 EXP-25-MIN-0065
Total Operating	2.458	5.277	5.292	5.308	5.508	

37. There was only one Cabinet decision which was approved between 14 April 2025 (BEFU 2025) and 16 October 2025 and which impacts Vote Revenue non-departmental appropriations:

	$ million – increase / (decrease)					
Vote Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	Reference
Benefits or Related Expenses: FamilyBoost Tax Credit PLA	(25.000)	1.000	1.000	-	-	Ensuring FamilyBoost Reaches More Families CAB-25-MIN-0217
Total Operating	(25.000)	1.000	1.000	-	-	

Joint Ministers approvals

38. This submission includes the following decisions approved by joint Ministers between 14 April 2025 (BEFU 2025) and 16 October 2025 and that impact tax revenue:

	$ million – increase / (decrease)					
Vote Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	Reference
Crown Revenue and Receipts: Tax Revenue						
Other Persons	-	(0.200)	(0.200)	(0.200)	(0.200)	Fiscal remedial measures for inclusion in the Taxation (Annual Rates for 2025-26, FBT Simplification, and Remedial Measures) Bill (IR2025/191)
	-	(0.047)	(0.351)	(0.983)	(0.983)	Foreign Investment Fund – Phase One technical decisions (IR2025/233)
Fringe Benefit Tax	0.200	0.200	0.200	0.200	0.200	Fiscal remedial measures for inclusion in the Taxation (Annual Rates for 2025-26, FBT Simplification, and Remedial Measures) Bill (IR2025/191)
GST	(0.200)	-	-	-	-	Fiscal remedial measures for inclusion in the Taxation (Annual Rates for 2025-26, FBT Simplification, and Remedial Measures) Bill (IR2025/191)

	$ million – increase / (decrease)					
Vote Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	Reference
Withholding Taxes	-	-	(0.592)	(1.551)	(1.489)	s 6(c)
Total Operating	-	0.047	0.943	2.534	2.472	

39. There were no decisions approved by joint Ministers between 14 April 2025 (BEFU 2025) and 16 October 2025 that impact Vote Revenue non-departmental appropriations.

Core data changes

40. We have reviewed our non-departmental appropriation titles and scope statements to ensure they accurately reflect our services and expenditures. We have identified the following two changes resulting from this review. We seek your agreement for the following core data title and scope statement changes that do not financially impact the appropriations. The proposed changes are shown below in italics:

	Current	Proposed
Non-Departmental Other Expenses: Impairment of debt relating to the SBCS Reason for change: To ensure the appropriation name is consistent with other impairment appropriations.		
Title	Impairment of debt relating to the SBCS	Impairment of *D*ebt *R*elating to the SBCS

We confirm that no expenditure has been incurred against this appropriation between 1 July 2025 and the time of this request, and as such we request the change to the appropriation above be effective immediately.

	Current	Proposed
Non-Departmental Other Expenses: Impairment of Debt and Debt Write-Offs Reason for change: Explicit exclusion of the impairment of the Small Business Cashflow Scheme as this has a separate appropriation.		
Scope statement	This appropriation is limited to write-offs and remissions for Crown debt administered by Inland Revenue, excluding child support and student loans, and to the impairment of this debt.	This appropriation is limited to write-offs and remissions for Crown debt administered by Inland Revenue, excluding child support, *the Small Business Cashflow Scheme* and student loans, and to the impairment of this debt.

We confirm that expenditure has been incurred against this appropriation between 1 July 2025 and the time of this request, and therefore we request the change to the appropriation above be effective from 1 July 2026.

Treasury CFISnet Table 2 items

41. We have attached a Treasury CFISnet table, referred to by Treasury as 'Table 2', that sets out all of the changes for Vote Revenue departmental (Vote 19).

42. We have also attached a Table 2 that sets out all of the changes from cabinet and joint Ministers' decisions for Vote Revenue non-departmental (Vote 20). Forecast changes for Vote 20 will be included in the 2025 HYEFU report.

Consultation with the Treasury

43. We have consulted on the 2025 October Baseline Update submission with the Treasury.

Recommendations

44. It is recommended that you:

a. **Sign and forward** the attached OBU 2025 letter and Attachment to the Minister of Finance by 1pm Thursday 23 October 2025.

Signed and forwarded

Nick Bradley
Enterprise Leader Finance Services (Chief Financial Officer)
16 October 2025

Hon Simon Watts
Minister of Revenue
/ /2025

Attachments:

a) 2025 October Baseline Update submission to the Minister of Finance for Vote Revenue
b) Attachment - Table 2 Baseline changes report, 2025/26 OBU (HYEFU) Vote 19 – Inland Revenue departmental.
c) Attachment - Table 2 Baseline changes report, 2025/26 OBU (HYEFU) Vote 20 – Inland Revenue non-departmental.

Hon Simon Watts

Minister of Climate Change
Minister for Energy
Minister of Local Government
Minister of Revenue

16 October 2025

Hon Nicola Willis
Minister of Finance
Parliament Buildings
WELLINGTON

2025 October Baseline Update Submission for Vote Revenue

1. Introduction

This report covers those items affecting the baseline for Vote Revenue for the 2025 October Baseline Update.

I confirm that none of the changes contained in this update require Cabinet decisions at this time.

The Table 2 for departmental and the Table 2 for non-departmental referred to below are attached to this letter.

The proposed changes to the baseline are set out below.

2. Departmental matters

2.1 Forecast adjustments for planned departmental capital expenditure

Inland Revenue (IR)'s departmental annual capital expenditure can be reduced for 2025/26 as their long-term asset management plans and required capital for Government initiatives have now been confirmed.

	$ million – increase / (decrease)				
Inland Revenue Department - Capital Expenditure PLA	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
BEFU 2025	47.700	42.900	40.400	40.000	40.000
OBU 2025	32.000	42.900	40.400	40.000	40.000
Forecast change - inc/(dec)	(15.700)	-	-	-	-

The forecast reduction of $15.700 million in 2025/26 in capital expenditure is included for your noting.

3. Other departmental matters

3.1 Baseline roll out to 2029/30 for departmental appropriations

As part of each October Baseline Update, departments are required to roll out their operating baseline by an additional year. This roll out preserves a five-year planning horizon within the Treasury Crown Financial Information System.

The baseline changes sought in this letter have been incorporated into the forecast financial statements, together with the adjustments necessary to accurately reflect estimated operating expenditure, cash flows and capital injections.

	$ million – increase / (decrease)				
	2025/26	2026/27	2027/28	2028/29	2029/30
Baseline (BEFU2025)	787.630	773.102	785.111	800.911	788.411
OBU 2025 – no changes	-	-	-	-	-
Baseline (after OBU 2025)	787.630	773.102	785.111	800.911	788.411

The rolled-out baseline of $788.411 million in 2029/30 is $12.500 million lower than the prior year. This reduction reflects a previous funding increase for depreciation expenditure in 2028/29 that reverses in 2029/30. There are no changes in the baseline over this 5-year period from the 2025 October Baseline Update.

3.2 Departmental in-principle expense transfer not required

As part of the 2025 March Baseline Update 2025 (IR2025/012 refers) you agreed to an in-principle expense transfer (IPET) of up to $3.000 million from 2024/25 to 2025/26 for the deferred cost for the implementation of international initiatives. As part of the October Baseline Update the final amount of IPETs are required to be confirmed after the year-end audit.

IR's audited 2024/25 financial statements were signed on 30 September 2025. I can now advise that this funding transfer from 2024/25 to 2025/26 is no longer required. Greater certainty about the application dates and implementation cost means IR can self-fund these initiatives from their 2025/26 baseline without the need for a funding transfer.

4. Establishment of two new non-departmental appropriations

4.1 A new Payments to Settle Residual Claims appropriation

IR administers several closed payment schemes where a liability may remain for IR to make a payment under the scheme. These closed schemes include the Cost of Living payment, COVID-19 Resurgence Support Payment, and COVID-19 Support payment.

Despite these schemes now being closed, s 9(2)(g)(i) . The value and level of disputed payment is expected to be very low, but IR requires an appropriation for the legal authority to make these payments. Retaining an appropriation with a nominal balance for each of these schemes creates additional administration for the Treasury and IR. IR is therefore seeking a new appropriation to cover the rare instances where payments are made under these circumstances which are outside of the control of the department.

I recommend that you agree to establish the following appropriation:

Vote	Appropriation Minister	Title	Type	Scope
Revenue	Minister of Revenue	Payments to Settle Residual Claims	Non-departmental Other Expenses	This appropriation is limited to payments made to eligible recipients to settle residual claims for products Inland Revenue has previously administered.

If you agree to establish this new appropriation, IR will seek a fiscally neutral transfer from the Cost of Living, the COVID-19 Resurgence Support Payment, and COVID-19 Support payment appropriations through the 2026 March Baseline Update submission. In the unlikely event that any material new funding requirement arises in the future, IR will seek funding decisions from joint Ministers at the time.

IR proposes exempting this new appropriation from end-of-year performance reporting as the amount of the appropriation is less than $5 million (s15D(2)(b)(iii) of the Public Finance Act 1989).

I seek your agreement to establish a new non-departmental Payments to Settle Residual Claims appropriation and request a performance reporting exemption.

4.2 A new Ex Gratia Payments other expenses annual appropriation

Occasionally IR makes ex gratia payments to customers. These are voluntary and not required by law but are given as a gesture of goodwill or moral responsibility.

An ex gratia payment is a last resort action. IR have broad provisions in legislation, for example the care and management provisions in s6 and s6A of the Tax Administration Act 1994, that IR applies before they consider an ex-gratia payment.

The number and value of these payments is relatively small (c$20,000 a year), with the exception of a few large ex gratia payments made in the past, for example a $7.200 million payment was made in 2020/21 to compensate KiwiSaver members who were adversely impacted by a system migration delay.

Historically, IR has funded all ex gratia payments from a departmental 'output expense' appropriation. However, under the Public Finance Act 1989 definitions for appropriation types, IR has agreed with the Treasury and Audit NZ that ex gratia payments of this nature should more correctly be classified as a non-departmental 'other expense' appropriation.

The creation of a new ex gratia appropriation would not change the delegation levels set by Cabinet for these payments (CO(18)2 refers[2]). IR would also continue to make ex gratia payments to staff or ex staff through their departmental output appropriations.

I recommend that you agree to establish the following appropriation:

Vote	Appropriation Minister	Title	Type	Scope
Revenue	Minister of Revenue	Ex Gratia Payments	Non-departmental Other Expenses	This appropriation is limited to ex gratia payments in relation to Vote Revenue non-departmental activities.

If you agree to establish this new appropriation IR would initially fund it through a fiscally neutral transfer of $0.050 million per annum from their departmental appropriations through the 2026 March Baseline Update submission. IR would discuss with joint Ministers the funding sources on the rare occasions IR needs to exceed $0.050 million a year.

IR proposes exempting this new appropriation from end-of-year performance reporting as performance information is unlikely to be informative because they would not disclose individual ex gratia payments from a privacy or integrity of the tax system perspective (s15D(b)(ii) of the Public Finance Act 1989).

I seek your agreement to establish a new non-departmental Ex Gratia Payments appropriation and request a performance reporting exemption.

[2] Cabinet Office Circular, CO (18)2, Proposals with Financial Implications and Financial Authorities, 30 July 2018

5. Other non-departmental matters

5.1 Baseline roll out to 2029/30 for non-departmental appropriations

The roll out of the non-departmental 2029/30 financial year for OBU includes any policy decisions or changes in funding profiles applicable to 2029/30 and not previously included in 2028/29. No forecasting adjustments which are not already accounted for in previous baseline updates are included in the roll out of 2029/30 within this submission.

5.2 Non-departmental in-principle expense transfers

As part of the 2025 June technical adjustment process, you approved in-principle expense transfers and early confirmation of up to $104,000 for three appropriations where the original claim period had passed but residual claims are still being received (IR2025/252 refers).

IR's audited 2024/25 financial statements were signed on 30 September 2025. Based on a confirmed non-departmental underspend of $102,000 in relation to these three appropriations, I recommend that you agree to the $102,000 in-principle expense transfer from 2024/25 to 2025/26. The table below shows these amounts by appropriation.

	$million			
Vote Revenue	2024/25 Actual	2024/25 Budget	2024/25 Underspend	2025/26 IPET
Non-Departmental Other Expenses:				
COVID-19 Resurgence Support Payment	0.001	0.040	0.039	0.039
COVID-19 Support Payment	0.026	0.080	0.054	0.054
Cost of Living payment	0.001	0.010	0.009	0.009
Total Other Expenses	0.028	0.130	0.102	0.102

5.3 Cabinet decisions

IR has included the following Cabinet decisions which were approved between 14 April 2025 (BEFU 2025) and 16 October 2025 in this baseline update and which impact tax revenue.

	$ million – increase / (decrease)					
Vote Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	Reference
Crown Revenue and Receipts: Tax Revenue						
Other Persons	(0.228)	(0.397)	(0.412)	(0.428)	(0.428)	Measures for Inclusion in the Taxation (Annual Rates for 2025-26) Bill CAB-25 MIN-0224 EXP-25-MIN-0052
	0.050	0.200	0.200	0.200	-	Further Measures for Inclusion in the Taxation (Annual Rates for 2025-26) Bill CAB-25-MIN-0255
	(0.030)	(0.030)	(0.030)	(0.030)	(0.030)	Income Tax (Deemed Rate of Return on Attributing Interests in Foreign Investment Funds, 2024–25 Income Year) Order 2025 CAB-25-MIN-0240 LEG-25-SUB-0130
Fringe Benefit Tax	(1.870)	(1.870)	(1.870)	(1.870)	(1.870)	Income tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations (No 2) 2025 CAB-25-MIN-0240 LEG-25-MIN-0131
Company Income Tax	0.520	0.520	0.520	0.520	0.520	
GST	(0.900)	(3.700)	(3.700)	(3.700)	(3.700)	GST and Unincorporated Joint Ventures CAB-25-MIN-0263 EXP-25-MIN-0065
Total Operating	2.458	5.277	5.292	5.308	5.508	

There was one Cabinet decision which was approved between 14 April 2025 (BEFU 2025) and 16 October 2025 and which impacts Vote Revenue non-departmental appropriations.

	$ million – increase / (decrease)					
Vote Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	Reference
Benefits or Related Expenses: FamilyBoost Tax Credit PLA	(25.000)	1.000	1.000	-	-	Ensuring FamilyBoost Reaches More Families CAB-25-MIN-0217
Total Operating	(25.000)	1.000	1.000	-	-	

5.4 Joint Ministers approvals

This submission includes the following decisions we jointly approved between 14 April 2025 (BEFU 2025) and 16 October 2025 and that impact tax revenue.

	$ million – increase / (decrease)					
Vote Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	Reference
Crown Revenue and Receipts: Tax Revenue						
Other Persons	-	(0.200)	(0.200)	(0.200)	(0.200)	Fiscal remedial measures for inclusion in the Taxation (Annual Rates for 2025-26, FBT Simplification, and Remedial Measures) Bill (IR2025/191)
	-	(0.047)	(0.351)	(0.983)	(0.983)	Foreign Investment Fund – Phase One technical decisions (IR2025/233)
Fringe Benefit Tax	0.200	0.200	0.200	0.200	0.200	Fiscal remedial measures for inclusion in the Taxation (Annual Rates for 2025-26, FBT Simplification, and Remedial Measures) Bill (IR2025/191)
GST	(0.200)	-	-	-	-	Fiscal remedial measures for inclusion in the Taxation (Annual Rates for 2025-26, FBT Simplification, and Remedial Measures) Bill (IR2025/191)
Withholding Taxes	-	-	(0.592)	(1.551)	(1.489)	s 6(c)
Total Operating	-	0.047	0.943	2.534	2.472	

5.5 Core data changes

IR has reviewed their non-departmental appropriation titles and scope statements to ensure they accurately reflect their services and expenditures. They have identified the following two changes resulting from this review.

I recommend that you approve the following core data title and scope statement changes that do not financially impact the appropriations. The proposed changes are shown below in italics:

	Current	Proposed
Non-Departmental Other Expenses: Impairment of debt relating to the SBCS Reason for change: To ensure the appropriation name is consistent with other impairment appropriations.		
Title	Impairment of debt relating to the SBCS	Impairment of *D*ebt *R*elating to the SBCS

IR has confirmed that no expenditure has been incurred against this appropriation between 1 July 2025 and the time of this request, and as such I recommend that the change to the appropriation above be effective immediately.

	Current	Proposed
Non-Departmental Other Expenses: Impairment of Debt and Debt Write-Offs Reason for change: Explicit exclusion of the impairment of the Small Business Cashflow Scheme as this has a separate appropriation.		
Scope statement	This appropriation is limited to write-offs and remissions for Crown debt administered by Inland Revenue, excluding child support and student loans, and to the impairment of this debt.	This appropriation is limited to write-offs and remissions for Crown debt administered by Inland Revenue, excluding child support, *the Small Business Cashflow Scheme* and student loans, and to the impairment of this debt.

IR has confirmed that expenditure has been incurred against this appropriation between 1 July 2025 and the time of this request, and therefore I recommend that the change to the appropriation above be effective from 1 July 2026.

6. Treasury CFISnet Table 2 items

I have attached two Treasury CFISnet tables, referred to by Treasury as 'Table 2', that sets out all of the changes for Vote Revenue departmental (Vote 19) and non-departmental (Vote 20).

Forecast changes for Vote 20 will be included in the 2025 HYEFU report.

7. Other Cabinet decisions

IR has assured me that all Cabinet decisions relating to this Vote for departmental and non-departmental, made after the Budget Update have been included in this update and are listed in detail in the Table 2s attached to this letter.

8. Consultation with the Treasury

Inland Revenue has consulted on the 2025 October Baseline Update submission with the Treasury.

9. Recommendations

I recommend that you:

1. **agree** the changes to those baselines for the appropriations within Vote Revenue that require Joint Ministers' approval as set out in Table 2 for Vote 19 and Table 2 for Vote 20.

2. **agree** that the proposed changes for 2024/25, covered by recommendation one above, be included in the 2025/26 Supplementary Estimates and that, in the interim, the increases be met from Imprest Supply.

3. **note** that Table 2 for Vote 019 (Vote Revenue departmental) and Table 2 for Vote 020 (Vote Revenue non-departmental) include for completeness changes to baselines for the appropriation on Vote Revenue that have been approved by Cabinet or joint Ministers since the previous update (BEFU 2025) or do not require such approval.

4. **approve** the following core data change to the title of the following appropriation (capitalisation) with the changes shown in italics:

	Current	Proposed
Non-Departmental Other Expenses: Impairment of debt relating to the SBCS Reason for change: To ensure the appropriation name is consistent with other impairment appropriations.		
Title	Impairment of debt relating to the SBCS	Impairment of *D*ebt *R*elating to the SBCS

5. **approve** the following core data change to scope of the following appropriation with the changes shown in italics:

	Current	Proposed
Non-Departmental Other Expenses: Impairment of Debt and Debt Write-Offs Reason for change: Explicit exclusion of the impairment of the Small Business Cashflow Scheme as this has a separate appropriation.		
Scope statement	This appropriation is limited to write-offs and remissions for Crown debt administered by Inland Revenue, excluding child support and student loans, and to the impairment of this debt.	This appropriation is limited to write-offs and remissions for Crown debt administered by Inland Revenue, excluding child support, *the Small Business Cashflow Scheme* and student loans, and to the impairment of this debt.

6. **agree** to establish the following appropriation:

Vote	Appropriation Minister	Title	Type	Scope
Revenue	Minister of Revenue	Payments to Settle Residual Claims	Non-departmental Other Expenses	This appropriation is limited to payments made to eligible recipients to settle residual claims for products Inland Revenue has previously administered.

7. **approve** an exemption for the new appropriation in recommendation 6 from end-of-year performance reporting as the amount of the appropriation is less than $5 million (s15D(2)(b)(iii) of the Public Finance Act 1989).

8. **agree** to establish the following appropriation:

Vote	Appropriation Minister	Title	Type	Scope
Revenue	Minister of Revenue	Ex Gratia Payments	Non-departmental Other Expenses	This appropriation is limited to ex gratia payments in relation to Vote Revenue non-departmental activities.

9. **approve** an exemption for the new appropriation in recommendation 8 above from end-of-year performance reporting as performance information is unlikely to be informative because they would not disclose individual ex gratia payments from a privacy or integrity of the tax system perspective (s15D(b)(ii) of the Public Finance Act 1989).

10. **agree** to the in-principle expense transfer from 2024/25 to 2025/26 outlined in this letter.

Hon Simon Watts
Minister of Revenue

Table 2: Baseline Changes Report, 2025/26 OBU (HYEFU), Vote 19 - 0: IRD Department - Revenue. Data has not been validated

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Departmental Capital Expenditure								
Inland Revenue Department - Capital Expenditure (PLA)								
Dept Other Appropriation								
Capital forecast adjustment	Fcst Adj	(15,700)	-	-	-	-	CO(18)2	On going
Total changes - Departmental Capital Expenditure		**(15,700)**	**-**	**-**	**-**	**-**		
Multi-Category Expenses and Capital Expenditure								
Services for Customers (MCA)								
Departmental Output Expenses								
Services to manage debt and unfiled returns								
Dept Annual Appropriation								
One-off depreciation transferred to 2028/29 in OBU 2021/22 and to 2029/30 in MBU 2022/23	Tech Adj	-	-	-	-	2,137	CO(18)2	On going
Revenue Crown								
One-off depreciation transferred to 2028/29 in OBU 2021/22 and to 2029/30 in MBU 2022/23	Tech Adj	-	-	-	-	2,137	CO(18)2	On going
Services to Ministers and to assist and inform customers to get it right from the start								
Dept Annual Appropriation								
One-off depreciation transferred to 2028/29 in OBU 2021/22 and to 2029/30 in MBU 2022/23	Tech Adj	-	-	-	-	(3,683)	CO(18)2	On going
Revenue Crown								
One-off depreciation transferred to 2028/29 in OBU 2021/22 and to 2029/30 in MBU 2022/23	Tech Adj	-	-	-	-	(3,683)	CO(18)2	On going
Services to process obligations and entitlements								
Dept Annual Appropriation								
One-off depreciation transferred to 2028/29 in OBU 2021/22 and to 2029/30 in MBU 2022/23	Tech Adj	-	-	-	-	(13,375)	CO(18)2	On going
Revenue Crown								
One-off depreciation transferred to 2028/29 in OBU 2021/22 and to 2029/30 in MBU 2022/23	Tech Adj	-	-	-	-	(13,375)	CO(18)2	On going
Services to protect the integrity of the tax system and functions the Commissioner administers								
Dept Annual Appropriation								
One-off depreciation transferred to 2028/29 in OBU 2021/22 and to 2029/30 in MBU 2022/23	Tech Adj	-	-	-	-	2,421	CO(18)2	On going
Revenue Crown								

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
One-off depreciation transferred to 2028/29 in OBU 2021/22 and to 2029/30 in MBU 2022/23	Tech Adj	-	-	-	-	2,421	CO(18)2	On going
Total changes - Multi-Category Expenses and Capital Expenditure		**-**	**-**	**-**	**-**	**(12,500)**		
Total changes - Output revenue (Crown +Dept+Other)		**-**	**-**	**-**	**-**	**(12,500)**		

Classification Key

Short Name	Description	Reference
Cabinet	Cabinet policy decision	Approvals are sought in cabinet papers (refer to cabinet manual), with authority given via a cabinet minute. The authority for change should reference both supporting documents.
ECT	Expense and Capital Transfer	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding within an appropriation across financial years.
ECT ip	Expense and Capital Transfer in-principle	Defined in (Cabinet Office Circular). The portion of an ECT that can't be accurately quantified so the transfer amount has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Fcst Adj	Forecast Adjustments	Defined in (Cabinet Office Circular). Adjustments to the forecast expenditure of PLAs or where there is a pre-determined cost calcultion, or Crown Revenue.
FLoS	Front-Loading of Spending	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Bringing forward expenditure to create lasting cost savings.
FNA	Fiscally Neutral Adjustment	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding between appropriations within a financial year.
RoU	Retention of Underspends	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring underspends to the next financial year.
RoU 50%	Retention of Underspends @ 50%	Defined in CO Circular. Portion of an ROU can't accurately quantify so the transfer amount of 50% of an underspend has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Tech Adj	Technical adjustment	Defined in (Cabinet Office Circular). Technical accounting adjustments with no cash impact to the Crown, MYA spending profile changes, non-controversial appropriation title or scope changes.
SuppsJune	Offset MYA June vs Supps Difference	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the difference between the Supps Forecast and June Actual.
BudgetOY4	Offset MYA Budget OY4 Rollover	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the rollover of Budget OY4 into OBU OY4.
Return Sav	Return of savings to the Crown	Returning savings to the Crown is always encouraged. Departments can achieve this by constantly looking for efficiency gains through improvements in processes and technology.
Crwn Liab	Recognition of Existing Crown liability	Crown liabilities need to be recognised as soon as possible. These affect Non-Departmental Appropriations.
Other	Other changes outside the above criteria	There should be very few changes outside the above criteria, so if there are any they require extra scrutiny.

Table 2: Baseline Changes Report, 2025/26 OBU (HYEFU), Vote 20 - 0: IRD Crown - Revenue (IRD-Crown). Data has not been validated

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Benefits or Related Expenses								
FamilyBoost Tax Credit (PLA)								
Non-Dept Other Appropriation								
Ensuring FamilyBoost Reaches More Families	Cabinet	(25,000)	1,000	1,000	-	-	CAB-25-MIN-0217	On going
Total changes - Benefits or Related Expenses		**(25,000)**	**1,000**	**1,000**	**-**	**-**		
Non-Departmental Other Expenses								
Cost of Living payment								
Non-Dept Annual Appropriation								
JPECT IPET COVID-19 payments and COL payments	ECT ip	9	-	-	-	-	CO (18) 2	On going
COVID-19 Resurgence Support Payment								
Non-Dept Annual Appropriation								
JPECT IPET COVID-19 payments and COL payments	ECT ip	39	-	-	-	-	CO (18) 2	On going
COVID-19 Support Payment								
Non-Dept Annual Appropriation								
JPECT IPET COVID-19 payments and COL payments	ECT ip	54	-	-	-	-	CO (18) 2	On going
Final-year Fees Free Payments								
Non-Dept Annual Appropriation								
Rollout: Delivering Quality and Timely Primary Care: Next Steps and Implementation	Cabinet	-	-	-	-	(4)	CAB-25-Min-0045	On going
Initial Fair Value Write-Down Relating to Student Loans								
Non-Dept Annual Appropriation								
Rollout: Delivering Quality and Timely Primary Care: Next Steps and Implementation	Cabinet	-	-	-	-	144	CAB-25-Min-0045	On going
Rollout: Disregarding EFTS for students receiving partial tuition fee refunds as a result of Covid-19	Cabinet	-	-	-	-	(185)	CAB-20-MIN-0164	2029/30
Rollout: Final-year Fees Free - Impacts Related to Student Loans	Cabinet	-	-	-	-	(2,000)	CAB-24-MIN-0148.69	On going
Rollout: Increasing Medical School Enrolments for the 2024 Intake	Cabinet	-	-	-	-	67	CAB-23-MIN-0207.01	On going
Rollout: Increasing Student Loan Scheme Overseas Interest Formula - Impacts Related to Student Loans	Cabinet	-	-	-	-	27	CAB-24-MIN-0148.69	On going
Rollout: Increasing Tuition Fees - Impacts Related to Student Loans	Cabinet	-	-	-	-	580	CAB-24-MIN-0148.69	On going
Rollout: Training 25 More Doctors – Impact on Student Loans	Cabinet	-	-	-	-	97	CAB-24-MIN-0148.69	On going

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Rollout: Training Incentive Allowance – Supporting Eligible Ministry of Social Development Clients to Study	Cabinet	-	-	-	-	70	Decision 11 April 2023	On going
Rollout: Waiving Student Support Residency Rules for Families of Those Directly Affected by the Chch Mosques Attack	Cabinet	-	-	-	-	1	CAB-22-MIN-0498, SWC-22-MIN-0191	2029/30
Total changes - Non-Departmental Other Expenses		**102**	**-**	**-**	**-**	**(1,203)**		
Tax Revenue								
Companies								
Non-Dept Revenue								
Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations (No 2) 2025	Cabinet	520	520	520	520	520	CAB-25-MIN-0240, LEG-25-MIN-0131	On going
Fringe Benefit Tax								
Non-Dept Revenue								
Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations (No 2) 2025	Cabinet	(1,870)	(1,870)	(1,870)	(1,870)	(1,870)	CAB-25-MIN-0240, LEG-25-MIN-0131	On going
Tax treatment of open loop cards provided to employees	Other	200	200	200	200	200	IR2025/191 Approved by JM CO (18) 2	On going
Goods and Services Tax (IRD)								
Non-Dept Revenue								
GST and Unincorporated Joint Ventures	Cabinet	(900)	(3,700)	(3,700)	(3,700)	(3,700)	CAB-25-MIN-0263, EXP-25-MIN-0065	On going
GST secondhand goods interaction with adjustment rules	Other	(200)	-	-	-	-	IR2025/191 Approved by JM CO (18) 2	On going
Other Persons								
Non-Dept Revenue								
Charities recommended for overseas donee status	Cabinet	(178)	(197)	(212)	(228)	(228)	CAB-25-MIN-0224, EXP-25-MIN-0052	On going
Donation tax credit clawback for refunded donations	Other	100	200	200	200	200	IR2025/191 Approved by JM CO (18) 2	On going
Exclude payments made to trustee of deceased estate from definition of pension	Other	(50)	(200)	(200)	(200)	(200)	IR2025/191 Approved by JM CO (18) 2	On going
Financial arrangements thresholds	Other	(50)	(200)	(200)	(200)	(200)	IR2025/191 Approved by JM CO (18) 2	On going
Foreign Investment Fund - Phase One technical decisions	Other	-	(47)	(351)	(983)	(983)	IR2025/233 Approved by JM CO (18) 2	On going
Income derived from residential sale of excess electricity	Cabinet	50	200	200	200	-	CAB-25-MIN-0255	2029/30
Income Tax (Deemed Rate of Return on Attributing Interests in Foreign Investment Funds, 2024–25 Income Year) Order 2025	Cabinet	(30)	(30)	(30)	(30)	(30)	CAB-25-MIN-0240, LEG-25-SUB-0130	On going
Tax treatment of digital nomads and other visitors	Cabinet	(50)	(200)	(200)	(200)	(200)	CAB-25-MIN-0224, EXP-25-MIN-0052	On going
Withholding Taxes								
Non-Dept Revenue								

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
s 6(c)								
Total changes - Tax Revenue		**(2,458)**	**(5,324)**	**(6,235)**	**(7,842)**	**(7,980)**		
Non-Tax Revenue								
Interest on Impaired Student Loans								
Non-Dept Revenue								
Rollout: Delivering Quality and Timely Primary Care: Next Steps and Implementation	Cabinet	-	-	-	-	58	CAB-25-Min-0045	On going
Total changes - Non-Tax Revenue		**-**	**-**	**-**	**-**	**58**		

Classification Key

Short Name	Description	Reference
Cabinet	Cabinet policy decision	Approvals are sought in cabinet papers (refer to cabinet manual), with authority given via a cabinet minute. The authority for change should reference both supporting documents.
ECT	Expense and Capital Transfer	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding within an appropriation across financial years.
ECT ip	Expense and Capital Transfer in-principle	Defined in (Cabinet Office Circular). The portion of an ECT that can't be accurately quantified so the transfer amount has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Fcst Adj	Forecast Adjustments	Defined in (Cabinet Office Circular). Adjustments to the forecast expenditure of PLAs or where there is a pre-determined cost calcultion, or Crown Revenue.
FLoS	Front-Loading of Spending	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Bringing forward expenditure to create lasting cost savings.
FNA	Fiscally Neutral Adjustment	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding between appropriations within a financial year.
RoU	Retention of Underspends	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring underspends to the next financial year.
RoU 50%	Retention of Underspends @ 50%	Defined in CO Circular. Portion of an ROU can't accurately quantify so the transfer amount of 50% of an underspend has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Tech Adj	Technical adjustment	Defined in (Cabinet Office Circular). Technical accounting adjustments with no cash impact to the Crown, MYA spending profile changes, non-controversial appropriation title or scope changes.
SuppsJune	Offset MYA June vs Supps Difference	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the difference between the Supps Forecast and June Actual.
BudgetOY4	Offset MYA Budget OY4 Rollover	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the rollover of Budget OY4 into OBU OY4.
Return Sav	Return of savings to the Crown	Returning savings to the Crown is always encouraged. Departments can achieve this by constantly looking for efficiency gains through improvements in processes and technology.
Crwn Liab	Recognition of Existing Crown liability	Crown liabilities need to be recognised as soon as possible. These affect Non-Departmental Appropriations.
Other	Other changes outside the above criteria	There should be very few changes outside the above criteria, so if there are any they require extra scrutiny.

Inland Revenue
Te Tari Taake

Vote Revenue: 2025 Half Year Economic and Fiscal Update for non-departmental expenditure appropriations

Date:	21 November 2025	**Priority:**	High
Security level:	In Confidence (Budget Sensitive)	**Report no:**	IR2025/408

Action sought

	Action sought	**Deadline**
Minister of Finance	**Approve** recommendations	28 November 2025
Minister of Revenue	**Approve** recommendations **Refer** report to the Minister of Finance	21 November 2025

Contact for telephone discussion (if required)

Name	**Position**	
Nick Bradley	Enterprise Leader Finance Services (Chief Financial Officer)	s 9(2)(a)
Rachel Parker	Domain Lead Finance Services	
Sandra Watson	Manager Forecasting	

Inland Revenue
Te Tari Taake

21 November 2025

Minister of Finance
Minister of Revenue

Vote Revenue: 2025 Half Year Economic and Fiscal Update for non-departmental expenditure appropriations

Executive summary

1. Inland Revenue Te Tari Taake submitted forecasts for non-departmental appropriations to the Treasury for the 2025 Half Year Economic and Fiscal Update (HYEFU 2025) on 7 November 2025. The forecasts in this report incorporate actual results to September 2025 and are based on the Treasury's updated macroeconomic forecasts of 28 October 2025. These forecasts include Cabinet and joint Minister's decisions that impact Vote Revenue up to 7 November 2025.

2. This report seeks your joint approval for the forecast changes to appropriations that are reflected in HYEFU 2025, and which are not established under a permanent legislative authority (PLA). Forecast changes to appropriations which are established under a PLA do not require approval[1] but are also provided for your information. A full list of the appropriations is provided in Appendix A.

3. We incorporated a roll out to include the 2029/30 financial year, for which the 2025 Budget Economic and Fiscal Update (BEFU 2025) had an implied repeat of 2028/29 with no explicit growth assumptions, in the October Baseline Update (OBU 2025) [IR 2025/372 refers]. Where the structure of this HYEFU report requires a comparison to BEFU 2025, that comparison is shown in italics for 2029/30, as part of the revision will reflect the inclusion of growth.

4. We have consulted on this submission with the Treasury and included their comments in the body of this report.

5. The major forecast changes since BEFU 2025 for appropriations requiring joint Ministers' approval (not including PLAs) are:

    - The Impairment of Debt and Debt Write-Offs appropriation has increased by $851.3 million across the forecast period, reflecting:

[1] As per the Public Finance Act, section 65ZH.

- There is a $551.3 million increase in forecast across the forecast period, resulting from a delay in the expected economic recovery, with a flow on impact into the outyears. The 2025/26 and 2026/27 forecasts remain broadly in line with BEFU 2025, with forecasts for outyears 2027/28 to 2029/30 increasing from circa $1.2 billion to circa $1.4 billion each year. Economic recovery is slower than was expected at BEFU 2025 and the forecast reflects the lag between economic recovery and reductions to debt levels. In addition to existing compliance initiatives, strategic options are currently being investigated to further curtail debt growth, and in turn reduce impairment growth. Any updates to forecast will be reflected in the next forecasting period.

- A buffer of $300 million has been included for 2025/26 to help manage the appropriation due to the volatility involved with impairment. This brings the total appropriation for 2025/26 to $1,850 million.

- The forecast for the Initial Fair Value Write-Down Relating to Student Loans appropriation has increased by $1,259.2 million over the forecast period due to;

  - an increase of $650 million following agreement of the accounting treatment for final-year fees free with the Treasury. This now recognises the expected expense of amounts to be 'offset' against the student loan as a forgiveness of the loan at the point of lending (rather than as a separate expense against the Final-year Fees Free Payments appropriation as the application for the fees-free payment is approved). This is a change to how funding was originally allocated and is partially offset by a decrease of $544.5 million in the Final-year Fees Free Payments appropriation,

  - an uplift in forecast new lending of just over $1,141 million, reflecting greater numbers of students borrowing. This has increased the initial fair value write-down by just over $421 million, and

  - an increase of $188 million from changes to the initial fair value write-down rate due to discount rate changes and other forecast cashflow changes which impact the expected initial fair value write-down.

- The forecast for the Final-year Fees Free Payments appropriation has decreased by just under $534 million due to the accounting change above, offset by a small increase in expected cash payments.

- As a result of the accounting change relating to final-year fees free, there is a one-off impairment expense of $30 million in 2025/26. This reflects a correction to the projected cashflows at 30 June 2025 for the small number of borrowers who took out loans in 2024/25 and are expected to be eligible for final-year fees free payments. As this expenditure has already been incurred, there is a breach of appropriations until this expenditure is approved. We will separately seek retrospective approval through the Appropriation (2025/26 confirmation and validation) Bill.

6. For PLA appropriations, the major forecast changes since BEFU 2025 are:

    - Family tax credit (FTC) increases by $75 million in 2025/26 and $153 million in 2026/27, largely due to earlier Consumer Price Index (CPI) indexation than assumed at BEFU 2025 (now 5.27% from 1 April 2026, rather than 6.84% from 1 April 2027). The 2027/28 year is $23 million less than forecasted at BEFU 2025 because the indexation was at a lower rate than previously assumed. A further indexation is now expected to occur in April 2029, consequently the 2028/29 year and 2029/30 year have been revised up by $54 million and $197 million respectively.

    - The KiwiSaver: Employee and Employer Contributions appropriation has increased by $1,860 million over the forecast period, due to a stronger nominal wage growth than what was assumed in BEFU 2025. $1,280 million of this increase is in 2029/30 and reflects the fact that the roll over from 2028/29 excluded growth. This does not affect the operating balance, as this is a pass-through transaction.

7. Further details of all forecast changes, including the major forecast changes above, are contained within the body of this report. Appendix B sets out all forecast changes for Vote Revenue Crown (non-departmental) in a tabulated format. This table includes tax forecasts prepared by the Treasury.

8. We included a table of Ministerial and Cabinet decisions made between BEFU 2025 and 16 October 2025 in OBU 2025 which was submitted on 23 October 2025 [IR2025/372 refers]. There have been no Ministerial and Cabinet decisions made since 16 October 2025 which impact on appropriations.

9. The Science, Innovation and Technology: R&D Tax Incentive appropriation is managed under Vote Revenue using forecasts developed by the Ministry of Business, Innovation and Employment (MBIE). We are separately seeking approval from the Minister of Finance and the Minister of Science, Innovation and Technology for forecast changes to this appropriation [IR2025/401 refers].

Recommended action

10. We recommend that you:

(a) **note** the HYEFU 2025 forecasts in this report incorporate actual results to September 2025, are based on the Treasury's macroeconomic forecasts of 28 October 2025, and were submitted to the Treasury on 7 November 2025.

Noted Noted

(b) **approve** the following forecast changes to appropriations for non-departmental benefits or related expenses that are not established under a PLA, with a corresponding impact on the operating balance and net core Crown debt:

	$ million – increase / (decrease)					
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total Forecast Period**
Non-Departmental Benefits or Related expenses:						
KiwiSaver: Tax Credit, Contribution and Residual Entitlement	14.800	12.600	15.700	20.400	*42.400*	105.900
Paid Parental Leave Payments	(5.000)	(5.000)	(5.000)	(5.000)	*35.000*	15.000
Total Operating	**9.800**	**7.600**	**10.700**	**15.400**	***77.400***	**120.900**

Approved/Not approved Approved/Not approved

(c) **approve** the following forecast changes in appropriations for non-departmental other expenses that are not established under a PLA, with a corresponding impact on the operating balance and net core Crown debt:

	$ million – increase / (decrease)					
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total Forecast Period**
Non-Departmental Other Expenses:						
Initial Fair Value Write-Down Relating to Student Loans	146.000	220.000	273.000	291.000	*329.199*	1,259.199
Impairment of Debt and Debt Write-Offs	330.000	5.000	202.100	172.100	*142.100*	851.300
Final-year Fees Free Payments	(35.000)	(66.000)	(114.000)	(163.000)	*(155.996)*	(533.996)
Impairment of Debt Relating to Student Loans	30.000	-	-	-	-	30.000
Total Operating	**471.000**	**159.000**	**361.100**	**300.100**	***315.303***	**1,606.503**

Approved/Not approved Approved/Not approved

(d) **note** the following forecast changes to non-departmental benefits or related expenses, non-departmental borrowing expenses, and non-departmental other expenses that are established under a PLA:

	$ million – increase / (decrease)					
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total Forecast Period**
Non-Departmental Benefits or Related Expenses - PLA:						
Best Start Tax Credit	-	2.000	(20.000)	(12.000)	*(3.000)*	(33.000)
Child Support Payments	(7.000)	(10.000)	(18.000)	(22.000)	*(16.000)*	(73.000)
Family Tax Credit	75.000	153.000	(23.000)	54.000	*197.000*	456.000
In-Work Tax Credit	(15.000)	(5.000)	(33.000)	(23.000)	*(16.000)*	(92.000)
Minimum Family Tax Credit	0.400	0.400	0.400	0.200	-	1.400
Total change – inc/(dec)	**53.400**	**140.400**	**(93.600)**	**(2.800)**	***162.000***	**259.400**
Non-Departmental Borrowing Expenses – PLA:						
Environmental Restoration Account Interest	(0.100)	(0.100)	(0.100)	(0.100)	*(0.100)*	(0.500)
Total change – inc/(dec)	**(0.100)**	**(0.100)**	**(0.100)**	**(0.100)**	***(0.100)***	**(0.500)**
Non-Departmental Other Expenses - PLA:						
KiwiSaver: Employee and Employer Contributions*	100.000	130.000	160.000	190.000	*1,280.000*	1,860.000
Total change – inc/(dec)	**100.000**	**130.000**	**160.000**	**190.000**	**1,280.000**	**1,860.000**
Total Operating*	**53.300**	**140.300**	**(93.700)**	**(2.900)**	***161.900***	**258.900**

* The KiwiSaver: Employee and Employer Contributions appropriation does not affect the operating balance as it is a pass-through transaction.

Noted Noted

(e) **note** that the Science, Innovation and Technology: R&D Tax Incentive appropriation is managed under Vote Revenue using forecasts developed by MBIE and that we are separately seeking approval from the Minister of Finance and the Minister of Science, Innovation and Technology for changes to this appropriation [IR2025/401 refers].

Noted Noted

(f) **agree** that all proposed changes to appropriations for 2025/26, covered by the recommendations above, be included in the 2025/26 Supplementary Estimates and that, in the interim, the increases be met from Imprest Supply.

Agreed/Not agreed

Agreed/Not agreed

(g) **note** that the Table 2[2] Baseline Changes Report (attached – Appendix B) for Vote 20 sets out the forecast changes for Vote Revenue Crown (non-departmental) for the 2025 Half Year Economic and Fiscal Update.

Noted

Noted

s 9(2)(a)

Nick Bradley
Enterprise Leader Finance Services - Chief Financial Officer
21 / 11 / 2025

Hon Nicola Willis
Minister of Finance
___/___/2025

Hon Simon Watts
Minister of Revenue
___/___/2025

[2] This is a technical report from Treasury's CFISnet system which sets out the quantum and authority for each change.

Background

11. Inland Revenue manages a number of non-tax items which require appropriations to cover the expenditure. Authority to spend is needed for appropriations established without a PLA. A full list of the non-departmental expenditure appropriations is attached in Appendix A.

12. We update the forecasts for these appropriations during the year to feed into the Government Budget and/or half year economic and fiscal updates. With each revision to forecasts we need joint Minister authority to change the forecast for appropriations without a PLA. If the changes are jointly approved, they will be included in the 2025/26 Supplementary Estimates and in the interim, the increases will be met from Imprest Supply.

13. Inland Revenue submitted forecasts for non-departmental appropriations for the Half Year Economic and Fiscal Update 2025 (HYEFU 2025) to the Treasury on 7 November 2025. These forecasts are based on the Treasury's HYEFU 2025 macroeconomic forecasts of 28 October 2025, and they incorporate actual results to September 2025. The forecasts include all Cabinet and joint Minister decisions that impact Vote Revenue made up to 7 November 2025.

14. This report seeks your joint approval for forecast changes to appropriations that are not established under a PLA. Forecast changes to appropriations established under PLA do not require approval and are also provided for your information. The body of the report briefly explains, at a high level, the main drivers of each change.

15. Forecasts are compared to amounts appropriated at the Budget Economic and Fiscal Update 2025 (BEFU 2025). At BEFU 2025 the 2029/30 fiscal year was outside of the forecast period and was indicated as a rollover of the 2028/29 expenditures, with no explicit growth. 2029/30 was included in the forecast period as part of the October Baseline Update 2025 (OBU 2025). Comparatives to BEFU 2025 for the 2029/30 fiscal year in this report are shown in italic in the tables as these new figures now reflect growth assumptions.

16. Appendix B sets out the forecast changes for Vote Revenue Crown (non-departmental) in a tabulated format. This table includes tax forecasts prepared by the Treasury.

Non-departmental benefits or related expense appropriations

17. The following table sets out the forecast changes for non-departmental benefits or related expenses that are not established under a PLA.

	$ million				
Non-departmental benefits or related expenses	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
KiwiSaver: interest					
BEFU 2025	4.000	4.000	4.000	4.000	*4.000*
HYEFU 2025	4.000	4.000	4.000	4.000	4.000
Forecast change - inc/(dec)	-	-	-	-	-
KiwiSaver: Tax Credit, Contribution and Residual Entitlement					
BEFU 2025	541.000	561.000	584.000	609.000	*609.000*
HYEFU 2025	555.800	573.600	599.700	629.400	651.400
Forecast change - inc/(dec)	14.800	12.600	15.700	20.400	*42.400*
Paid Parental Leave Payments					
BEFU 2025	745.000	775.000	810.000	850.000	*850.000*
HYEFU 2025	740.000	770.000	805.000	845.000	885.000
Forecast change - inc/(dec)	(5.000)	(5.000)	(5.000)	(5.000)	*35.000*
Total forecast change – inc/(dec)	**9.800**	**7.600**	**10.700**	**15.400**	***77.400***

18. The KiwiSaver: Interest appropriation has not changed. There is ongoing growth in contributions handled by Inland Revenue, which means there will be growth in amounts held and exposed to interest payable, but this is offset by declining interest rates.

19. The KiwiSaver: Tax Credit, Contribution and Residual Entitlement appropriation covers government contributions to KiwiSaver schemes. The appropriation has been revised up since BEFU 2025 to reflect a stronger outlook for growth in nominal wages, which increases contributions and hence the likelihood that entitlements reach the cap. There is also a stronger outlook for the size of the labour force, which flows to an increase in contributing membership.

20. The downwards revision in the Paid Parental Leave Payments appropriation reflects slightly weaker outturns since Budget 2025 (the year to June 2025 was $11 million below the BEFU 2025 forecast), which carries through into the outyears.

Non-departmental other expenses

21. The following table sets out the forecast changes and Cabinet and joint Minister approvals for non-departmental other expenses that are not established under a PLA. The forecast changes require your joint approval.

	$ million				
Non-departmental other expenses	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
COVID-19 Resurgence Support Payment					
BEFU 2025	-	-	-	-	-
HYEFU 2025	0.039	-	-	-	-
Joint Minister approval OBU 2025 – inc/(dec)	0.039	-	-	-	-
COVID-19 Support Payment					
BEFU 2025	-	-	-	-	-
HYEFU 2025	0.054	-	-	-	-
Joint Minister approval OBU 2025 – inc/(dec)	0.054	-	-	-	-
Cost of Living payment					
BEFU 2025	-	-	-	-	-
HYEFU 2025	0.009	-	-	-	-
Joint Minister approval OBU 2025 – inc/(dec)	0.009	-	-	-	-
Initial Fair Value Write-Down Relating to Student Loans					
BEFU 2025	636.000	628.000	627.000	653.000	*653.000*
HYEFU 2025	782.000	848.000	900.000	944.000	981.000
Forecast change – inc/(dec)	146.000	220.000	273.000	291.000	*329.199*
Cabinet decisions – inc/(dec)	-	-	-	-	*(1.199)*
Final-year Fees Free Payments					
BEFU 2025	55.000	100.000	163.000	223.000	*223.000*
HYEFU 2025	20.000	34.000	49.000	60.000	67.000
Forecast change – inc/(dec)	(35.000)	(66.000)	(114.000)	(163.000)	*(155.996)*
Cabinet decisions – inc/(dec)	-	-	-	-	*(0.004)*
Impairment of Debt Relating to Student Loans					
BEFU 2025	-	-	-	-	-
HYEFU 2025	30.000	-	-	-	-
Forecast change – inc/(dec)	30.000	-	-	-	-
Impairment of Debt and Debt Write-Offs					
BEFU 2025	1,520.000	1,425.000	1,237.900	1,237.900	*1,237.900*
HYEFU 2025	1,850.000	1,430.000	1,440.000	1,410.000	1,380.000
Forecast change – inc/(dec)	330.000	5.000	202.100	172.100	*142.100*
Total forecast change – inc/(dec)	**471.000**	**159.000**	**361.100**	**300.100**	***315.303***
Total Cabinet decisions – inc/(dec)	**-**	**-**	**-**	**-**	***(1.203)***
Total joint Minister approval OBU 2025 – inc/(dec)	**0.102**	**-**	**-**	**-**	**-**

22. At OBU 2025, you jointly approved a fiscally neutral expense transfer of $102,000 from 2024/25 to 2025/26 for three non-departmental appropriations (COVID-19 Resurgence Support Payment, COVID-19 Support Payment and the Cost of Living payment). This funding provides for the settlement of residual claims after the original claim period has passed.

Final-year fees free

23. We have worked with the Treasury to finalise the accounting treatment of the Budget 2024 final-year fees free policy. Previously all the funding for final-year fees free payments was allocated to the Final-years Fees Free Payments appropriation in the year the application for the final-year fees free payment was expected to be approved, with no differentiation of treatment between cash payments to recipients and amounts offset against student loans. Additionally, for the purpose of setting the initial fair value write-down rate for new lending, the amount expected to be offset against the student loan was assumed to be a cash inflow when the application was approved. We have now confirmed that the amounts expected to be offset against student loans are effectively grants which forgive the student loan for accounting purposes. As a result, the amount of the final-year student loan expected to be forgiven when study is completed is now required to be written-off when the borrowing occurs. This effectively brings forward the expense and treats it as an initial fair value write-down of the student loan rather than as a final year fees free repayment.

24. The Initial Fair Value Write-Down Relating to Student Loans appropriation has increased by $1,258 million over the forecast period. This increase relates to;

- a $650 million increase from the change to the accounting treatment explained in the paragraph above – this is partially offset by the $544.5 million decrease in the Final-year Fees Free Payments appropriation explained in paragraph 25 below. The net difference of $105.5 million represents the earlier recognition of cost under the new treatment,

- a $421 million increase in forecast write-down on new lending over the forecast period. Lending is forecast to increase by $1,141 million over the period due to a 20% increase in the number of student loan applications compared to the same time last year. The increase in the number of students is due to weaker labour market conditions, which have made it more difficult for people to find and retain work,

- a $188 million increase from changes to the initial fair value write-down rate due to discount rate changes and other forecast cashflow changes which impact the expected initial fair value write-down. This type of adjustment is expected every forecasting round, and is dependent on movements in discount rates and experience/forecasts for the student loan scheme, and

- the rollover of several Budget 24 and 2025 initiatives totalling ($1) million which had different approved appropriations for 2029/30 than 2028/29. This is shown as cabinet decisions in the table above.

25. The decrease in the Final-year Fees Free Payments appropriation of $534 million largely reflects the change in treatment of the final year fees free expense as noted in paragraph 23 ($544.5 million). This appropriation now only reflects amounts expected to be paid in cash to eligible students on approval of their application for the payment (i.e. to those with no Student Loan). There has been a small offsetting increase in the forecast cash payment of $10.5 million over the forecast period. There is also a small decrease to the appropriation from the Budget 2025 Delivery Quality and Timely Primary Health Care initiative to increase and retain doctors in primary care, which approved the 2029/30 appropriation for final-year fees free to be $0.004 million lower than the 2028/29 amount rolled over from BEFU 2025.

26. As a result of the accounting change in paragraph 23 above, there is a one-off impairment of $30 million in 2025/26 which reflects a correction to the projected cashflows at 30 June 2025 for the small number of borrowers who took out loans in 2024/25 and are expected to be eligible for final-year fees free. As this expenditure has already been incurred, there is a breach of appropriations until it is approved. We will separately seek retrospective approval through the Appropriation (2025/26 confirmation and validation) Bill.

Impairment of Debt and Debt Write-Offs

27. The Impairment of Debt and Debt Write-Offs appropriation is dependent on the level and quality of the debt book. The most significant drivers of impairment are the amount of new debt added in any year, as well as the amount of repayments and write-off of older debt compared with the expectations of these movements in previous valuations.

28. The level of overdue debt is impacted by the size and buoyancy of the economy, customer behaviour and Inland Revenue compliance effort. It is compounded by increasing penalties and interest as the core debt grows.

29. Whilst the economy is indicating a softening of inflationary impacts, we know that any inflation impacts the level of debt more than it impacts revenue, as it also impacts on our customer's ability to pay as the time value of money decreases.

30. Inland Revenue is investing heavily in increased compliance activities to reduce debt. This includes increasing the number of people working on debt through the Budget 2024 and 2025 compliance initiatives, as well as internal reprioritisation, and using our tools differently to ensure we maximise the return on debt. These efforts are increasing repayments on overdue debt and reducing the debt balance from what it would otherwise have been. The returned agreed from the Budget 2024 and 2025 compliance initiatives will reduce tax debt by $1.1 billion from what it would otherwise have been over the forecast period.

31. Between July and September 2025, we collected $1.1 billion overdue tax from debt activity. This is above the minimum target from the Budget 2024 and 2025 compliance initiatives but 8% ($100 million) down on the same period for the previous year, due to more timely processing of tax-pooling transfers this period (several large tax-pooling transfers were processed late between July – Sept 2024, inflating cash receipts).

32. Despite our efforts, overdue tax debt continues to rise and was just over $9.5 billion at 30 September 2025. This is an increase of over $200 million from June 2025. The increase in the first quarter of the year is largely related to GST and income tax.

33. We are forecasting that overdue debt will reach $10.5 billion by the end of the current financial year and increase by between $700 million and $800 million each year over the remainder of the forecast period. The forecast assumes inflation will continue to trend down, and our increased compliance effort will continue to slow the growth of debt from what it would otherwise have been. The debt forecast reflects the expected reduction in debt from the Budget 2024 and Budget 2025 compliance initiatives and current operational activity but does not yet assume any reductions from other initiatives which are currently being worked on, as the impact on debt has not yet been quantified.

34. Our definitions for overdue debt changed in 2025 from when we began action to collect it or it remained unpaid 25-days after the due date, to one-day after the due date. The change in definition has resulted in higher reported overdue debt balances, and it also introduces greater volatility in the debt balance at month-end depending on when payment due dates fall. Whilst this change increases the nominal size of the debt book, the "very new" debt is more valuable, and has a lower associated impairment.

35. Based on the current debt forecast, we are forecasting the impairment of debt and debt write-off expense to increase by $551.3 million across the forecasting period, reflecting a delay in the expected economic recovery, and the flow on impact into the outyears.

36. The impairment forecast is prepared on the basis that whilst new debt growth is slowing, there is a lag between economic recovery and reduction in debt levels. In the meantime, existing debt continues to attract more penalties and interest as it ages. These penalties and interest are added to old debt and will continue to incur significant additional impairment.

37. We believe the impairment cost has peaked and with the slowing of the debt growth, will continue to fall over the next two years. However, we no longer consider it will settle at the levels previously forecast for 2027/28 and outyears. The $551.3 million increase in forecast brings the appropriation in outyears to approximately $1.4 billion per annum which is consistent with the amount already approved for 2026/27.

38. A buffer of $300 million has been added to the forecast for 2025/26, to help manage the appropriation due to the volatility involved with impairment. This brings the total appropriation for 2025/26 to $1,850 million. The actual expenditure for 2024/25 was $1,872 million. Previously we have only included a buffer for the current year as part of BEFU (Supplementary Estimates). Given the current focus on impairment, and the magnitude of the appropriation, we consider it prudent to signal the need for the buffer through HYEFU this year. The buffer does not impact on budget allowances. We will add buffers to outyears as appropriate in future exercises.

39. In addition to the existing compliance initiatives and internal reprioritisation of resources to debt work, strategic options are currently being investigated and developed to further curtail debt growth, which in turn, may reduce impairment growth. This includes, for example, wider credit reporting of customers with debt and s 9(2)(f)(iv) [IR 2025/398

refers]. Any updates to the debt forecast and consequential impact on the impairment appropriation from these will be reflected in the next forecasting update.

40. The final expense for 2025/26 will not be confirmed until August 2026 after completion of the final valuation for the year.

41. We have discussed and agreed the above approach with The Treasury.

Non-departmental benefits or related expenses - PLA

42. The following table sets out the forecast changes and Cabinet decisions for non-departmental benefits or related expenses which are established under a PLA.

	$ million				
Non-departmental benefits or related expenses - PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Best Start Tax Credit *					
BEFU 2025	326.000	285.000	292.000	281.000	*281.000*
HYEFU 2025	326.000	287.000	272.000	269.000	278.000
Forecast change - inc/(dec)	-	2.000	(20.000)	(12.000)	*(3.000)*
Child Support Payments					
BEFU 2025	442.000	451.000	460.000	469.000	*469.000*
HYEFU 2025	435.000	441.000	442.000	447.000	453.000
Forecast change - inc/(dec)	(7.000)	(10.000)	(18.000)	(22.000)	*(16.000)*
FamilyBoost Tax Credit					
BEFU 2025	171.000	167.000	165.000	163.000	*163.000*
HYEFU 2025	146.000	168.000	166.000	163.000	163.000
Cabinet decisions - inc/(dec)	(25.000)	1.000	1.000	-	-
Family Tax Credit *					
BEFU 2025	2,374.000	2,446.000	2,601.000	2,541.000	*2,541.000*
HYEFU 2025	2,449.000	2,599.000	2,578.000	2,595.000	2,738.000
Forecast change - inc/(dec)	75.000	153.000	(23.000)	54.000	*197.000*
In-Work Tax Credit *					
BEFU 2025	588.000	596.000	615.000	593.000	*593.000*
HYEFU 2025	573.000	591.000	582.000	570.000	577.000
Forecast change - inc/(dec)	(15.000)	(5.000)	(33.000)	(23.000)	*(16.000)*
Minimum Family Tax Credit *					
BEFU 2025	7.900	7.500	7.000	7.000	*7.000*
HYEFU 2025	8.300	7.900	7.400	7.200	7.000
Forecast change - inc/(dec)	0.400	0.400	0.400	0.200	-
Total forecast change – inc/(dec)	**53.400**	**140.400**	**(93.600)**	**(2.800)**	***162.000***
Total Cabinet decisions – inc/(dec)	**(25.000)**	**1.000**	**1.000**	**-**	**-**

* Working for Families Tax Credits

43. The forecasts for Best Start payments to families have been reduced by $33 million over the forecast period. The forecast for 2025/26 remains unchanged from BEFU 2025. From 2026/27, Best Start payments continue to fall year-on-year, driven by the full-year impact of income testing and ongoing income-related abatement, which outweighs the CPI

adjustment. A further CPI indexation of 6.71% is expected on 1 April 2029, offsetting some of the impacts of abatement in 2029/30.

44. The forecasts for child support payments to custodial parents have been reduced by between $7 million to $22 million per annum across the forecast period. This reflects a continued decline in the number of child support arrangements managed by Inland Revenue, following a policy change in 2023/24 that had the effect of reducing the demand for Inland Revenue's involvement for welfare recipients. The slight year on year increase in the forecast reflects modest expected income growth.

45. The forecast for FamilyBoost tax credit has decreased by $23 million over the forecast period, reflecting the net impact of policy changes introduced on 1 July 2025. These changes increased the maximum rebate (from 25% to 40%), increased the quarterly income cap (from $975 to $1,560), and reduced the abatement rate (from 9% to 7%). Expenditure rises in 2026/27 as these changes phase in. From 2027/28, spending is expected to gradually decline as rising family incomes reduce entitlements, although this is partially offset by increasing Early Childhood Education fees.

46. The forecast for family tax credit (FTC) has increased by $456 million over the forecast period. This reflects CPI indexation occurring on 1 April 2026 rather than 1 April 2027 and at a lower rate (5.27% compared with 6.84% at BEFU 2025) as a result of the recent CPI quarterly release and changes to CPI forecasts. There has also been an increase in the number of recipients of upfront payments in the first three months of 2025/26 which is expected to continue for the remainder of the year. The 2027/28 year is $23 million less than forecasted at BEFU 2025 because the indexation was at a lower rate than previously assumed. A further CPI indexation of 6.71% is now expected to occur on 1 April 2029 resulting in higher expenditure in 2028/29 and 2029/30 than forecast at BEFU 2025.

47. The forecast for in-work tax credit (IWTC) has decreased by $92 million over the forecast period. Stronger wage growth in the 2025 and 2026 tax years relative to BEFU 2025 is contributing to lower IWTC payments in the first 3 months of the year. Softer payments of IWTC are expected to continue over the remainder of the financial year. Other factors including weaker employment relative to BEFU 2025 may also be contributing to lower IWTC payments. Weaker IWTC payments in the first part of the year are partially offset by the earlier CPI indexation change to FTC. IWTC abates after FTC and an increase in the FTC entitlement will result in abatement of IWTC occurring at a later point for working families. These changes are expected to flow through to outyears.

48. The forecast for minimum family tax credit (MFTC) has increased by $1.4 million over the forecast period. MFTC spending declines over time as family incomes grow, reducing the need for top-ups to the guaranteed income level. The increase is a flow on from the slightly higher payments in 2024/25.

Non-departmental borrowing expenses - PLA

49. The following table sets out the forecasts for non-departmental borrowing expenses that are established under a PLA.

	$ million				
Non-departmental borrowing expenses - PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Environmental Restoration Account Interest					
BEFU 2025	4.200	4.200	4.200	4.200	*4.200*
HYEFU 2025	4.100	4.100	4.100	4.100	4.100
Forecast change - inc/(dec)	(0.100)	(0.100)	(0.100)	(0.100)	*(0.100)*
Income Equalisation Interest					
BEFU 2025	7.000	6.000	6.000	6.000	*6.000*
HYEFU 2025	7.000	6.000	6.000	6.000	6.000
Forecast change - inc/(dec)	-	-	-	-	-
Total forecast change - inc/(dec)	**(0.100)**	**(0.100)**	**(0.100)**	**(0.100)**	***(0.100)***

50. The environmental restoration account and income equalisation account allow for timing changes for tax on qualifying income or expenditure and usage of both accounts is demand-driven.

51. For the Environmental Restoration Account Interest appropriation, the 2024/25 fiscal year was slightly below the BEFU 2025 forecast and this result has been carried through to forecasts for subsequent years.

52. The main income equalisation account allows qualifying taxpayers from the primary sector to smooth their taxable income across years. The forecast for the Income Equalisation Interest appropriation has been left unchanged, with the forecast profile for interest continuing to reflect a softly declining scheme balance.

Non-departmental other expenses

53. The following table sets out the forecasts for non-departmental other expenses that are established under a PLA.

	$ million				
Non-departmental other expenses - PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
KiwiSaver: Employee and Employer contributions					
BEFU 2025	10,670.000	12,230.000	12,920.000	14,000.000	*14,000.000*
HYEFU 2025	10,770.000	12,360.000	13,080.000	14,190.000	15,280.000
Total forecast change – inc/(dec)	**100.000**	**130.000**	**160.000**	**190.000**	***1,280.000***

54. KiwiSaver employee and employer contributions to scheme providers have increased by $1,860 million over the forecast period. This reflects the increase in KiwiSaver contributions in recent months which have been above BEFU 2025 and an increase to nominal wage growth. $1,280 million of this increase is in 2029/30 and reflects the fact that the roll over from 2028/29 excluded growth. KiwiSaver employee and employer contributions are a pass-through transaction and do not impact the operating balance.

Research and Development (R&D) Tax Incentive

55. Science, Innovation and Technology: R&D Tax Incentive appropriation is managed under Vote Revenue using forecasts developed by the Ministry of Business, Innovation and Employment (MBIE). We are separately seeking approval from the Minister of Finance and the Minister of Science, Innovation and Technology [IR2025/401 refers] for forecast changes relating to this appropriation. The following changes are included for your information.

	$ million				
Vote Revenue **Minister of Science, Innovation and Technology**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Other Expenses Science, Innovation and Technology: R&D Tax Incentive					
BEFU 2025	650.742	731.000	784.000	839.000	*839.000*
HYEFU 2025	630.742	713.000	765.000	820.000	876.000
Forecast change – inc/(dec)	**(20.000)**	**(18.000)**	**(19.000)**	**(19.000)**	***37.000***

- The decreases forecasts for 2025/26 to 2028/29 are primarily driven by a decrease in the baseline estimate of R&D, which is drawn from the latest R&D Survey estimate. The estimate of the RDTI-eligible R&D expenditure derived from the 2024 R&D Survey results is approximately 2-3% lower than the amount previously forecasted based on the 2023 R&D Survey results used in BEFU 2025. This decrease was also partly driven by changes in forecast Nominal Gross Domestic Product (GDP) in the relevant years.
- The increase of $37 million in 2029/30 is driven by updating the roll forward of the 2028/29 appropriation of $839 million with MBIE's RDTI latest forecast for that year ($876 million).

Consultation

56. The Treasury has been consulted on the contents of this report and notes the significant increase in the Impairment of Debt and Debt Write-Offs across the forecast period ($851.3 million). This consists of a forecast increase of $551.3 million across the forecast period. It also includes a buffer of $300 million for 2025/26 which brings the total appropriation for 2025/26 to $1,850 million. Officials have previously reported to you on this increase and have reported to you recently on policy options to reduce tax debt [IR 2025/398 refers].

    The Treasury also notes a significant increase in the Fair Value Write-Down Relating to Student Loans across the forecast period ($1,258 million). This figure is not a net-expenditure increase, as a proportion of this is offset by a decrease in the Final-Year Fees Free appropriation, relating to the change in accounting treatment for Final-Year Fees Free. As the remainder is mainly driven by the level of borrowing and the write-down rate, so mainly outside of Inland Revenue's control, there are limited mitigation options.

Appendix A

The forecasts cover the following non-departmental expenditure appropriations (with an asterisk identifying expenditure items that are established under a PLA):

Benefits or related expenses:

- Best Start Tax Credit*
- Child Support Payments*
- FamilyBoost Tax Credit *
- Family Tax Credit*
- In-Work Tax Credit*
- KiwiSaver: Interest
- KiwiSaver: Tax Credit, Contribution and Residual Entitlement
- Minimum Family Tax Credit*
- Paid Parental Leave Payments

Borrowing expenses:

- Environmental Restoration Account Interest*
- Income Equalisation Interest*

Other expenses:

- Cost of Living payment
- COVID-19 Resurgence Support Payment
- COVID-19 Support Payment
- Final-year Fees Free Payments
- Initial Fair Value Write-Down Relating to Student Loans
- Impairment of Debt and Debt Write-offs
- KiwiSaver: Employee and Employer Contributions*
- Science, Innovation and Technology: R&D Tax Incentive
- Impairment of Debt and Debt Write-Offs Relating to Child Support
- Impairment of Debt Relating to Student Loans
- Impairment of debt relating to the SBCS

There are two appropriations which currently have a nil balance and forecast for the five-year period. These appropriations will be reviewed ahead of the 2026 Budget Economic and Fiscal Update (BEFU 2026) after an interim valuation of the associated asset has been completed. These appropriations include:

Other expenses:

- Impairment of Debt and Debt Write-Offs Relating to Child Support
- Impairment of debt relating to the SBCS

Appendix B – Table 2 report for Vote Revenue non-departmental appropriations

The attached Table 2 Baseline Changes Report sets out the forecast changes for Vote Revenue Crown (non-departmental) since BEFU 2025 in a tabulated format. The table includes tax forecasts prepared by the Treasury.

The Table 2 Baseline Changes Report attached is for:

- HYEFU 2025 - final forecasts.

Table 2: Baseline Changes Report, 2025/26 OBU (HYEFU), Vote 20 - 0: IRD Crown - Revenue (IRD-Crown).

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Benefits or Related Expenses								
Best Start Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Best Start Tax Credit	Fcst Adj	-	2,000	(20,000)	(12,000)	(3,000)	CO (18) 2	On going
Child Support Payments (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Child Support Payments	Fcst Adj	(7,000)	(10,000)	(18,000)	(22,000)	(16,000)	CO (18) 2	On going
Family Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Family Tax Credit	Fcst Adj	75,000	153,000	(23,000)	54,000	197,000	CO (18) 2	On going
FamilyBoost Tax Credit (PLA)								
Non-Dept Other Appropriation								
Ensuring FamilyBoost Reaches More Families	Cabinet	(25,000)	1,000	1,000	-	-	CAB-25-MIN-0217	On going
In-Work Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting In-Work Tax Credit	Fcst Adj	(15,000)	(5,000)	(33,000)	(23,000)	(16,000)	CO (18) 2	On going
KiwiSaver: Tax Credit, Contribution and Residual Entitlement								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting KiwiSaver: Tax Credit, Contribution and Residual Entitlement	Fcst Adj	14,800	12,600	15,700	20,400	42,400	CO (18) 2	On going
Minimum Family Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Minimum Family Tax Credit	Fcst Adj	400	400	400	200	-	CO (18) 2	On going
Paid Parental Leave Payments								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting Paid Parental Leave Payments	Fcst Adj	(5,000)	(5,000)	(5,000)	(5,000)	35,000	CO (18) 2	On going
Total changes - Benefits or Related Expenses		**38,200**	**149,000**	**(81,900)**	**12,600**	**239,400**		
Non-Departmental Borrowing Expenses								
Environmental Restoration Account Interest (PLA)								

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Environmental Restoration Account Interest	Fcst Adj	(100)	(100)	(100)	(100)	(100)	CO (18) 2	On going
Total changes - Non-Departmental Borrowing Expenses		**(100)**	**(100)**	**(100)**	**(100)**	**(100)**		
Non-Departmental Other Expenses								
Cost of Living payment								
Non-Dept Annual Appropriation								
JPECT IPET COVID-19 payments and COL payments	ECT ip	9	-	-	-	-	CO (18) 2	On going
COVID-19 Resurgence Support Payment								
Non-Dept Annual Appropriation								
JPECT IPET COVID-19 payments and COL payments	ECT ip	39	-	-	-	-	CO (18) 2	On going
COVID-19 Support Payment								
Non-Dept Annual Appropriation								
JPECT IPET COVID-19 payments and COL payments	ECT ip	54	-	-	-	-	CO (18) 2	On going
Final-year Fees Free Payments								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting Final-year Fees Free Payments	Fcst Adj	(35,000)	(66,000)	(114,000)	(163,000)	(155,996)	CO (18) 2	On going
Rollout: Delivering Quality and Timely Primary Care: Next Steps and Implementation	Cabinet	-	-	-	-	(4)	CAB-25-Min-0045	On going
Impairment of Debt and Debt Write-Offs								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting Impairment of Debt and Debt Write-Offs	Fcst Adj	330,000	5,000	202,100	172,100	142,100	CO (18) 2	On going
Impairment of Debt Relating to Student Loans								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting Impairment of Debt Relating to Student Loans	Fcst Adj	30,000	-	-	-	-	CO (18) 2	On going
Initial Fair Value Write-Down Relating to Student Loans								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting Initial Fair Value Write-Down Relating to Student Loans	Fcst Adj	146,000	220,000	273,000	291,000	329,199	CO (18) 2	On going
Rollout: Delivering Quality and Timely Primary Care: Next Steps and Implementation	Cabinet	-	-	-	-	144	CAB-25-Min-0045	On going
Rollout: Disregarding EFTS for students receiving partial tuition fee refunds as a result of Covid-19	Cabinet	-	-	-	-	(185)	CAB-20-MIN-0164	2029/30
Rollout: Final-year Fees Free - Impacts Related to Student Loans	Cabinet	-	-	-	-	(2,000)	CAB-24-MIN-0148.69	On going
Rollout: Increasing Medical School Enrolments for the 2024 Intake	Cabinet	-	-	-	-	67	CAB-23-MIN-0207.01	On going

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Rollout: Increasing Student Loan Scheme Overseas Interest Formula - Impacts Related to Student Loans	Cabinet	-	-	-	-	27	CAB-24-MIN-0148.69	On going
Rollout: Increasing Tuition Fees - Impacts Related to Student Loans	Cabinet	-	-	-	-	580	CAB-24-MIN-0148.69	On going
Rollout: Training 25 More Doctors – Impact on Student Loans	Cabinet	-	-	-	-	97	CAB-24-MIN-0148.69	On going
Rollout: Training Incentive Allowance – Supporting Eligible Ministry of Social Development Clients to Study	Cabinet	-	-	-	-	70	Decision 11 April 2023	On going
Rollout: Waiving Student Support Residency Rules for Families of Those Directly Affected by the Chch Mosques Attack	Cabinet	-	-	-	-	1	CAB-22-MIN-0498, SWC-22-MIN-0191	2029/30
KiwiSaver: Employee and Employer Contributions (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting KiwiSaver: Employee and Employer Contributions	Fcst Adj	100,000	130,000	160,000	190,000	1,280,000	CO (18) 2	On going
Science, Innovation and Technology: R&D Tax Incentive								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting Science, Innovation and Technology: R&D Tax Incentive	Fcst Adj	(20,000)	(18,000)	(19,000)	(19,000)	37,000	CO (18) 2	On going
Total changes - Non-Departmental Other Expenses		**551,102**	**271,000**	**502,100**	**471,100**	**1,631,100**		
Tax Revenue								
Companies								
Non-Dept Revenue								
Cumulative forecasting changes impacting Companies	Fcst Adj	(500,520)	(726,520)	292,480	197,480	1,699,480	CO (18) 2	On going
Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations (No 2) 2025	Cabinet	520	520	520	520	520	CAB-25-MIN-0240, LEG-25-MIN-0131	On going
Fringe Benefit Tax								
Non-Dept Revenue								
Cumulative forecasting changes impacting Fringe Benefit Tax	Fcst Adj	25,670	31,670	29,670	40,670	87,670	CO (18) 2	On going
Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations (No 2) 2025	Cabinet	(1,870)	(1,870)	(1,870)	(1,870)	(1,870)	CAB-25-MIN-0240, LEG-25-MIN-0131	On going
Tax treatment of open loop cards provided to employees	Other	200	200	200	200	200	IR2025/191 Approved by JM CO (18) 2	On going
Gaming Duties								
Non-Dept Revenue								
Cumulative forecasting changes impacting Gaming Duties	Fcst Adj	5,000	4,000	1,000	6,000	23,000	CO (18) 2	On going
Online Casino Gambling Bill: Community Returns	Cabinet	-	8,000	16,000	16,000	16,000	CAB-25-MIN-0382	On going
Goods and Services Tax (IRD)								
Non-Dept Revenue								

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Cumulative forecasting changes impacting Goods and Services Tax	Fcst Adj	398,100	613,700	721,700	895,700	2,354,700	CO (18) 2	On going
GST and Unincorporated Joint Ventures	Cabinet	(900)	(3,700)	(3,700)	(3,700)	(3,700)	CAB-25-MIN-0263, EXP-25-MIN-0065	On going
GST secondhand goods interaction with adjustment rules	Other	(200)	-	-	-	-	IR2025/191 Approved by JM CO (18) 2	On going
Other Indirect Taxes								
Non-Dept Revenue								
Cumulative forecasting changes impacting Other Indirect Taxes	Fcst Adj	23,000	17,000	15,000	16,000	23,000	CO (18) 2	On going
Other Persons								
Non-Dept Revenue								
Charities recommended for overseas donee status	Cabinet	(178)	(197)	(212)	(228)	(228)	CAB-25-MIN-0224, EXP-25-MIN-0052	On going
Cumulative forecasting changes impacting Other Persons	Fcst Adj	(359,792)	398,474	414,793	477,441	1,108,641	CO (18) 2	On going
Donation tax credit clawback for refunded donations	Other	100	200	200	200	200	IR2025/191 Approved by JM CO (18) 2	On going
Exclude payments made to trustee of deceased estate from definition of pension	Other	(50)	(200)	(200)	(200)	(200)	IR2025/191 Approved by JM CO (18) 2	On going
Financial arrangements thresholds	Other	(50)	(200)	(200)	(200)	(200)	IR2025/191 Approved by JM CO (18) 2	On going
Foreign Investment Fund - Phase One technical decisions	Other	-	(47)	(351)	(983)	(983)	IR2025/233 Approved by JM CO (18) 2	On going
Income derived from residential sale of excess electricity	Cabinet	50	200	200	200	-	CAB-25-MIN-0255	2029/30
Income Tax (Deemed Rate of Return on Attributing Interests in Foreign Investment Funds, 2024–25 Income Year) Order 2025	Cabinet	(30)	(30)	(30)	(30)	(30)	CAB-25-MIN-0240, LEG-25-SUB-0130	On going
Tax treatment of digital nomads and other visitors	Cabinet	(50)	(200)	(200)	(200)	(200)	CAB-25-MIN-0224, EXP-25-MIN-0052	On going
Source Deductions								
Non-Dept Revenue								
Cumulative forecasting changes impacting Source Deductions	Fcst Adj	(688,000)	(1,014,000)	(1,409,000)	(1,530,000)	1,625,000	CO (18) 2	On going
Withholding Taxes								
Non-Dept Revenue								
s 6(a)								
Cumulative forecasting changes impacting Withholding Taxes	Fcst Adj	(246,800)	(236,800)	(318,208)	2,751	368,689	CO (18) 2	On going
s 6(c)								
Total changes - Tax Revenue		**(1,346,000)**	**(910,000)**	**(243,000)**	**114,000**	**7,298,000**		
Non-Tax Revenue								
Child Support Collections								

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Non-Dept Revenue								
Cumulative forecasting changes impacting Child Support Collections	Fcst Adj	6,000	5,000	5,000	4,000	4,000	CO (18) 2	On going
Interest on Impaired Student Loans								
Non-Dept Revenue								
Cumulative forecasting changes impacting Interest on Impaired Student Loans	Fcst Adj	(81,000)	(87,000)	(66,000)	(51,000)	(21,058)	CO (18) 2	On going
Rollout: Delivering Quality and Timely Primary Care: Next Steps and Implementation	Cabinet	-	-	-	-	58	CAB-25-Min-0045	On going
Other non-tax revenue								
Non-Dept Revenue								
Cumulative forecasting changes impacting Other Non-Tax Revenue	Fcst Adj	(11,000)	-	-	-	-	CO (18) 2	On going
Small Business Cashflow Scheme interest unwind								
Non-Dept Revenue								
Cumulative forecasting changes impacting SBC interest unwind	Fcst Adj	1,208	592	323	102	31	CO (18) 2	On going
Unclaimed Monies								
Non-Dept Revenue								
Cumulative forecasting changes impacting Unclaimed Monies	Fcst Adj	28,000	-	-	-	-	CO (18) 2	On going
Working for Families Tax Credit Interest and Penalties								
Non-Dept Revenue								
Cumulative forecasting changes impacting WfFTC Interest & Penalties	Fcst Adj	(2,000)	(2,000)	(3,000)	(4,000)	(1,000)	CO (18) 2	On going
Total changes - Non-Tax Revenue		**(58,792)**	**(83,408)**	**(63,677)**	**(50,898)**	**(17,969)**		
Capital Receipts								
Income Equalisation Reserve Account								
Non-Dept Revenue								
Cumulative forecasting changes impacting Income Equalisation Reserve Account	Fcst Adj	(20,000)	(30,000)	(20,000)	(20,000)	(20,000)	CO (18) 2	On going
Small Business Cashflow Scheme receipts								
Non-Dept Revenue								
Cumulative forecasting changes impacting SBC Scheme Receipts	Fcst Adj	14,100	2,200	-	20	(400)	CO (18) 2	On going
Student Loans - Receipts								
Non-Dept Revenue								
Cumulative forecasting changes impacting Student Loan - Receipts	Fcst Adj	3,000	17,000	35,000	41,000	95,000	CO (18) 2	On going
Total changes - Capital Receipts		**(2,900)**	**(10,800)**	**15,000**	**21,020**	**74,600**		

Classification Key

Short Name	Description	Reference
Cabinet	Cabinet policy decision	Approvals are sought in cabinet papers (refer to cabinet manual), with authority given via a cabinet minute. The authority for change should reference both supporting documents.
ECT	Expense and Capital Transfer	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding within an appropriation across financial years.
ECT ip	Expense and Capital Transfer in-principle	Defined in (Cabinet Office Circular). The portion of an ECT that can't be accurately quantified so the transfer amount has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Fcst Adj	Forecast Adjustments	Defined in (Cabinet Office Circular). Adjustments to the forecast expenditure of PLAs or where there is a pre-determined cost calcultion, or Crown Revenue.
FLoS	Front-Loading of Spending	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Bringing forward expenditure to create lasting cost savings.
FNA	Fiscally Neutral Adjustment	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding between appropriations within a financial year.
RoU	Retention of Underspends	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring underspends to the next financial year.
RoU 50%	Retention of Underspends @ 50%	Defined in CO Circular. Portion of an ROU can't accurately quantify so the transfer amount of 50% of an underspend has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Tech Adj	Technical adjustment	Defined in (Cabinet Office Circular). Technical accounting adjustments with no cash impact to the Crown, MYA spending profile changes, non-controversial appropriation title or scope changes.
SuppsJune	Offset MYA June vs Supps Difference	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the difference between the Supps Forecast and June Actual.
BudgetOY4	Offset MYA Budget OY4 Rollover	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the rollover of Budget OY4 into OBU OY4.
Return Sav	Return of savings to the Crown	Returning savings to the Crown is always encouraged. Departments can achieve this by constantly looking for efficiency gains through improvements in processes and technology.
Crwn Liab	Recognition of Existing Crown liability	Crown liabilities need to be recognised as soon as possible. These affect Non-Departmental Appropriations.
Other	Other changes outside the above criteria	There should be very few changes outside the above criteria, so if there are any they require extra scrutiny.

Inland Revenue
Te Tari Taake

Inland Revenue report: Approach to Budget 2026 and the 2026 Performance Plan

Date:	27 November 2025	**Priority:**	Medium
Security level:	Budget Sensitive	**Report number:**	IR2025/457

Action sought

	Action sought	Deadline
Minister of Revenue	**Note** the contents of this report	8 December 2025

Contact for telephone discussion (if required)

Name	Position	Telephone
Nick Bradley	Enterprise Leader Finance Services – Chief Financial Officer	s 9(2)(a)
Darren Cheevers	Domain Lead Finance Services	

27 November 2025

Minister of Revenue

Approach to Budget 2026 and the 2026 Performance Plan

Summary

1. This report:

   - outlines our proposed approach to Budget 2026 for your feedback
   - provides an initial list of potential Budget 2026 initiatives for submission to the Treasury on 19 December 2025 for you to note (Appendix 1), and
   - describes the process for developing the second Inland Revenue Performance Plan.

2. A range of potential policy and Budget initiatives are under active consideration for Vote Revenue, including initiatives being led by other portfolios. Initial estimates suggest that, if these initiatives proceed, they could generate s 9(2)(f)(iv)

3. Our preliminary assessment indicates that departmental operating costs associated with these potential initiatives are likely to require between s 9(2)(f)(iv) of operating expenditure and between s 9(2)(f)(iv) of capital expenditure over the forecast period. The final costs will be contingent on policy and design decisions.

4. Our proposed approach for Budget 2026, set out in more detail in this report, is to:

   a) extend our commitment to managing departmental cost pressures to include the new Budget 2026 2% saving target, s 9(2)(f)(iv), noting that this will be challenging and will involve forgoing other opportunities

   b) seek departmental funding for costs beyond this s 9(2)(f)(iv) commitment, for example those costs required to implement and deliver Budget 2026 initiatives, recognising departmental savings in Budget 2024 included approximately s 9(2)(f)(iv) of change capacity

   c) set out reprioritisation options for any cost pressures above our commitment of s 9(2)(f)(iv) per annum should funding not be provided, noting that options will have impacts on revenue, debt and/or contracted performance, and

   d) identify potential 'invest to save' opportunities that could be explored.

[1] The forecast period is the current financial year plus four outyears being 2025/26 to 2029/30.

Background and Government priorities for Budget 2026

5. The Budget 2026 process has formally begun with the issue of Budget 2026 invitation letters from the Minister of Finance to Ministers and Chief Executives[2].

6. These letters note that Budget 2026 is taking place in a tight fiscal environment and global uncertainty and therefore maintaining fiscal discipline is crucial.

7. Cabinet has agreed that Budget 2026 will progress the Government's overarching goals in the following way:

   - most agencies and Ministers will need to manage cost pressures and other commitments within existing baselines
   - there will be limited funding for new initiatives and cost pressures, with a focus on meeting outstanding coalition commitments, and
   - sufficient savings will need to be identified to fund the above priorities within or below the net $2.4 billion operating allowance.

8. The invitation letter for the Revenue portfolio includes the following key points:

   - we are required to deliver a further 2% ($15.8m) ongoing baseline reduction, in addition to meeting all cost pressures
   - we are required to provide advice on options for s 9(2)(f)(iv) [redacted]
   - we are not invited to submit any cost pressure bids
   - we are not invited to submit any spending initiatives other than those related to the Tax and Social Policy Work Programme (TSPWP), and
   - included within the scope of TSPWP initiatives are savings workstreams for shareholder loans, charities and bank related policies.

9. An accompanying report provides more information on the TSPWP and outlines the process for how items could be invited into the Budget submission process, should you wish to progress non-work programme items into Budget 2026 (IR2025/476 refers).

10. The next step in the Budget process is the submission of proposed policy and savings initiatives to the Minister of Finance and Treasury on Friday 19 December 2025. These initiatives will form the basis for discussion with Budget Ministers and the development of the Budget package to be approved by Cabinet.

11. Throughout the Budget process we will work with you and Treasury officials to confirm and refine the initiatives that will be included in the Budget package.

Our proposed approach to Budget 2026

12. We have developed a proposed approach to Budget 2026, based on the guidance from the Minister of Finance, Government Priorities, potential Budget initiatives, and our strategic intentions. We seek your feedback and endorsement to this approach.

13. We continue to deliver a comprehensive work programme, with many current Government initiatives being self-funded. This approach reflects our strong commitment

[2] Budget 2026 invitation letter from the Minister of Finance to the Minister of Revenue and copied to the Commissioner of Inland Revenue, 4 November 2025.

to fiscal discipline and efficient resource management. Our work programme also encompasses critical enhancements to compliance activities, technology, and process improvements - initiatives that drive departmental savings while improving outcomes for the Government. These projects span multiple years and fully utilise current resourcing, which limits our capacity to fund additional initiatives arising from Budget 2026 and the TSPWP.

a) We will extend our commitment to managing departmental cost pressures and savings within our baseline up to s 9(2)(f)(iv) *per annum, noting that this will be challenging and will involve forgoing other opportunities*

14. We will continue our 2025 Performance Plan commitment to maintain the $29.6 million of annual savings from Budget 2024 and manage compounding cost pressures of up to a further $16 million (2%) per annum. This includes $10 million for remuneration[3] and $6 million for inflationary cost pressures across office accommodation leases and technology contracts.

15. In addition, we will manage emerging cost pressures, estimated at s 6(c) per annum. This includes cost pressures from open banking, digital, and artificial intelligence. Some of this expenditure creates benefits to the Crown and/or our customers but no cost saving to the department, whilst other elements of this expenditure will deliver departmental savings in outyears, but not in initial years.

16. We will also commit to delivering the new Budget 2026 saving target for Vote Revenue of 2% ($15.8 million) per annum, through further efficiencies and savings.

17. Delivering this combined annual saving of s 9(2)(f)(iv) will be challenging and difficult decisions will be required. We will achieve this through a singular focus on fiscal discipline and value for money. s 9(2)(f)(iv)

18. Our intention is that through careful planning we can deliver a s 9(2)(f) saving. However, as seen in recent years, economic uncertainty creates challenges for tax administrations, and we can't be certain on the level of efficiencies we can continue to generate each year.

19. We have been successful at putting in place mechanisms to deliver savings, meet customer growth, manage inflationary cost pressures (e.g. managing our leased office accommodation portfolio) and invest in areas that will deliver productivity efficiencies (for example a frontline integrated operational planning solution and artificial intelligence driven phone call summarisation). We have also achieved savings through focused change processes, particularly across back-office functions.

20. In delivering savings, we will aim to minimise the impact on revenue, debt and contracted performance. However, achieving these savings will inevitably require forgoing certain opportunities. While further analysis is needed, these forgone opportunities are likely to arise from an inability or reduced ability to:

s 9(2)(f)(iv)

[3] This amount aligns with the 2% cap advised by the Minister of Finance in Budget 2025.

b) Seek departmental funding to implement and deliver Budget 2026 initiatives,

21. We have identified the potential Budget initiatives that will impact Vote Revenue departmental and/or non-departmental appropriations[4]. This includes initiatives led by the Revenue portfolio and initiatives being led by other portfolios.

22. The potential initiatives include those that previously would have been funded from the Tax Policy Scorecard but will instead proceed through the Budget process, due to the low balance in the scorecard.

23. Most Budget initiatives are in development with options analysis and consultation still to occur. For some initiatives we will need to submit placeholder templates with indicative departmental and non-departmental fiscals for the 19 December 2025 submission date to the Treasury.

24. A list of currently known initiatives that impact Vote Revenue is provided in Appendix 1. We will seek your endorsement to submit a final list of Budget initiatives in a subsequent report to you on 12 December 2025.

25. Overall, the proposed initiatives will s 9(2)(f)(iv)

26. The successful delivery of Budget initiatives will require departmental implementation (build) and ongoing delivery (run) expenditure. Expenditure will include system changes, process changes, engagement with customers and compliance activities. Our early assessment of proposed initiatives is a requirement for an estimated s 9(2)(f)(iv) over the forecast period. Policy and design decisions will determine the final cost.

27. In Budget 2024 we committed to, and are delivering, administration savings of $29.6 million per annum. This saving included a $15 million reduction in our change capacity based on an expected lower level of future tax and social policy change. In our advice to the Budget 2024 Assurance Panel and yourself it was noted that we would have a reduced ability to self-fund any new tax and social policy initiatives and it could take longer to scale up to deliver new initiatives (IR2024/022 refers[5]). We advised that we may be unable to deliver new initiatives without a corresponding increase in funding. The level of proposed Budget 2026 and TSPWP initiatives exceeds the level of change envisaged in 2024.

28. We consider that additional funding for the relatively low departmental costs to successfully implement and deliver significant revenue and savings to the Crown is important and required.

c) Provide reprioritisation options for cost pressures arising from potential budget initiatives above s 9(2)(f)(iv) *.*

29. The Treasury guidance indicates that we need to advise reprioritisation options if we were not successful in securing departmental funding to implement and deliver Budget 2026 initiatives.

30. Reprioritisation options would be required as we will be unable to successfully deliver Budget initiatives in addition to s 9(2)(f)(iv) without impacting revenue, debt or performance.

31. As advised last year our reprioritisation approach is to protect higher value interventions and services to ensure we deliver our statutory requirement of the highest net revenue over time within available resources. This approach includes

[4] Non-departmental appropriations include expenditure on s 9(2)(f)(iv) and the impairment of debt and debt write-offs.
[5] IR2024/022, Budget 2024 - Savings options and Assurance Panel, 29 January 2024.

protecting the investment and reprioritisation of resources into compliance and debt. Preserving our core activities will be our focus, with secondary unfunded activities needing to be scaled back (for example s 9(2)(f)(iv)).

32. We have previously advised on reprioritisation options, noting s 9(2)(f)(iv)

- In our 2025 Performance Plan we noted a $204 million per annum negative impact on the Crown's operating balance (i.e. a decrease in tax revenue and an increase in debt impairment) would occur with the cessation of $26.5 million of Budget 2022 time-limited funding to manage the impacts of COVID-19. This impact was avoided through the continuation of this funding in Budget 2025. s 9(2)(f)(iv)
- We also noted in our 2025 Performance Plan that any reductions in our funding reduces our ability to respond to population growth, net businesses growth (i.e. opening and closing), and customers in financial difficulties.
- s 9(2)(f)(iv)

33. s 6(c)

34.

35. The departmental cost to implement and deliver initiatives is dependent on policy and design decisions. We will work with you during the Budget process to identify cost effective options for each initiative. This may require choices between a simple delivery option versus a more complex and/or automated option.

d) There are some 'invest to save' opportunities that could be explored.

36. Many of the potential Budget initiatives can be defined as 'invest to save' opportunities where a relatively small departmental investment will deliver significant savings, benefits, or revenue to the Crown.

37. The investment in compliance activities from Budget 2024 and Budget 2025 plus internal reprioritisation of resources is an example of an 'invest to save' initiative that is delivering for the Crown.

38. In our business segments we have ramped up our resources in compliance activities considerably in response to the last two years of investment through the Budget process. We are also continuing to enhance and innovate in our audits and debt

s 6(c)

management, and we are actively developing ways to further enhance our technology to improve compliance outcomes. At this juncture, our focus needs to be on embedding this investment to realise the significant return on investment expectations.

39. s 9(2)(f)(iv)

40.

Performance Plan

41. The Minister of Finance has formally commissioned the second year of Performance Plans (TC2025/18 refers[9]).

42. The submission date for plans has not been set but is likely to be in June 2026 (after Budget Day). Final plans will be provided to the Cabinet Expenditure and Regulatory Review Committee (EXP).

43. Plans continue to be a critical tool to ensure fiscal sustainability and drive value from public spending over the medium-term within existing baselines.

44. The priorities for this year's plans are:

    - a sharp uplift in how departments demonstrate the value and impact that spending delivers, and
    - a continued focus on fiscal discipline to achieve the Government's fiscal strategy while delivering value for New Zealanders.

45. We will engage with you next year to discuss and develop the second plan in parallel to the Budget process. Our work will include refining key impact areas, enhancing the intervention logic, and strengthening the linkages to value and performance.

46. In the Budget 2026 invitation letter the Minister of Finance indicated that she was considering inviting further baseline reductions in outyears. This consideration has not come through in the Performance Plan guidance material but may come later. Any further outyear baseline reduction requests would negatively impact revenue, debt and/or contracted performance.

[8] s 9(2)(f)(iv)

[9] Performance Plans – Formal Commissioning, Treasury Circular, TC2025/18, 14 November 2025.

Next steps

47. If you have any feedback on our proposed approach, these can be discussed on Tuesday 2 December at your regular officials' meeting, as the Budget 2026 process is on the agenda for discussion. On Friday 12 December 2025 we will report to you on our progress and provide a templated report for you to sign and forward to the Minister of Finance by 1pm on Friday 19 December.

48. The report to the Minister of Finance will confirm the list of initiatives for Inland Revenue that covers all proposals for the Revenue portfolio. A draft of the initiatives is provided in Appendix 1.

Recommended action

49. We recommend that you:

(a) **Note** this report and provide any feedback on our proposed approach for Budget 2026, as set out in paragraph 4.

Noted

(b) **Note** that on Friday 12 December 2025 we will report to you on our progress and provide a templated report for you to sign and forward to the Minister of Finance by 1pm on Friday 19 December

Noted

s 9(2)(a)

Nick Bradley
Enterprise Leader Finance Services
Chief Financial Officer

Hon Simon Watts
Minister of Revenue
/ /2025

Appendix 1 – Potential initiatives and indicative fiscals

The following table provides a first draft of the potential initiatives to be submitted to the Minister of Finance for consideration as part of the Budget 2026 package. Placeholder initiatives will be submitted where decisions and options are still being considered by Ministers. Each initiative include includes potential revenue, non-departmental and/or departmental fiscal impacts. Initiatives and fiscals are subject to upcoming policy and design decisions.

Initiative type[1]	Portfolio / lead agency	Initiative/proposal	Potential options	Indicative impact over forecast period in $million Impact on Crown operating balance or net assets			
				Dept. operating Inc / (dec)	Dept. capital Inc/(dec)	Tax revenue (Inc)/dec	Non-dept operating Inc/(dec)
Saving	Revenue	TSPWP - bank tax	s 9(2)(g)(i)				
Saving	Revenue	TSPWP - charities and not-for-profits	s 9(2)(f)(iv)				
Saving	Revenue	TSPWP - shareholder loans	1	5 - 10		(640)	
New spending	Revenue	TSPWP - Foreign Investment Funds phase 2	1	1		54	
New spending	Revenue	TSPWP small-to-medium sized initiatives[3]	1 -15	1 - 2	0 - 1	150	
s 9(2)(f)(iv)							
Saving	Social Dev. & Emp. (MSD)	Wider welfare reform – IR options[2]	s 9(2)(f)(iv)				
s 9(2)(f)(iv)							
Neutral	Internal Affairs (DIA)	Offshore gambling duty rate increase - to fund community initiatives[4]	1	1	0 - 1	(56)	56 [4]
New spending	Housing (HUD)	Investment Boost extensions (Housing)	1	1	0 - 1	77	
Estimated total potential range				s 9(2)(f)(iv)			
Saving	Revenue	Baseline reduction for Vote Revenue (2%)	1	(64)			

1. Indicates the primary initiative type where there are multiple initiatives and or options.
2. Some of these initiatives/options will form part of the wider Budget 2026 welfare reform package. The lead Ministers are the Minister of Finance and the Minister of Social Development and Employment.
3. Includes initiatives to attract and retain capital and talent, support small business, simplify and uphold the integrity of the tax system, and improve social policy.
4. s 9(2)(f)(iv)
5.

Estimated fiscal impact - increase or decrease:	Small	Medium	Large

Inland Revenue
Te Tari Taake

Inland Revenue report: Budget 2026 initiative submission for the Revenue portfolio

Date:	10 December 2025	**Priority:**	Medium
Security level:	Budget Sensitive	**Report number:**	IR2025/458

Action sought

	Action sought	**Deadline**
Minister of Revenue	**Note** the recommendations in this report. **Sign and refer** the attached letter to the Minister of Finance.	1pm on Friday 19 December 2025

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**
Darren Cheevers	Enterprise Leader Finance Services – Acting	s 9(2)(a)
Sandra Simon	Accountant, Finance Services	

10 December 2025

Minister of Revenue

Budget 2026 initiative submission for the Revenue portfolio

Summary

1. The next step in the Budget 2026 process is for all proposed Budget 2026 initiatives to be submitted to the Treasury by Friday, 19 December 2025. This submission must be accompanied by a letter from the relevant portfolio Minister to the Minister of Finance, confirming the list of initiatives being submitted.

2. This report:

   - provides an updated list of proposed Budget 2026 initiatives being led through your Revenue portfolio, to be considered for inclusion in the Budget 2026 package
   - requests that you sign and refer the attached templated letter to the Minister of Finance to submit these proposed initiatives, and
   - provides a list of proposed Budget 2026 initiatives being led by other portfolio Ministers that impact Vote Revenue.

3. This report follows on from our earlier report that outlined our approach to Budget 2026 and provided an initial list of proposed Budget 2026 initiatives (IR2025/457 refers[1]).

4. On Friday 19 December 2025 we will submit to Treasury via their CFISnet system the templates for each proposed initiative being led through the Revenue portfolio. We are also contributing to initiatives being led by other portfolio Ministers that have impacts for Vote Revenue.

5. Proposed initiatives will be assessed by Treasury in January, considered by Budget Ministers from February, with final Cabinet decisions expected in April.

6. At this stage of the Budget process, most of the Revenue portfolio initiatives require further policy and design decisions. As agreed with the Treasury, we will submit placeholder templates that reflect the current options being considered.

7. We will continue providing separate reports for all initiatives under consideration as part of Budget 2026. Throughout the process, we will work with the Treasury to ensure initiatives are updated in their CFISnet system.

8. The proposed initiatives reflect the reports that we have provided to you to date. We will adjust the titles and the content of initiatives as further decisions are made. We will advise your office if there are any material changes to the initiatives we propose submitting.

9. Each initiative will include estimates of the non-departmental fiscals and departmental implementation and delivery costs. Initial estimates suggest that if all

[1] Approach to Budget 2026 and the 2026 Performance Plan, IR2025/457, 27 November 2025.

the Revenue portfolio initiatives proceed, overall, they could generate a net positive impact to the Crown of s 9(2)(f)(iv) [2] across the forecast period[3].

Initiatives to be submitted on 19 December 2025

Initiatives being led by the Revenue portfolio

10. The following table sets out the proposed Budget 2026 initiatives being led through the Revenue portfolio that we intend to submit to the Treasury on 19 December 2025.

11. As requested by the Treasury, we will submit placeholders where policy and design decisions are pending. During the next phase of the Budget process, we will work with yourself and the Treasury to finalise the initiatives that will proceed into the Budget 2026 package.

Lead Portfolio	Initiative Type	Initiative Title and Notes
Revenue	Other Savings Initiatives	Bank tax (two initiatives): • an Australian style bank tax or prudential levy • foreign owned New Zealand banking group tax rule changes
Revenue	Other Savings Initiatives	Charities and not-for-profits (5 options): • donor controlled charities • member transactions and descriptions • donation tax credit ceiling • tax exemptions • simplification for donors and volunteers
Revenue	Other Savings Initiatives	Shareholder loans
Revenue	New Spending	Foreign investment funds rules reform
Revenue	New Spending	Tax and Social Policy Work Programme initiatives This placeholder initiative includes the small-to-medium sized TSPWP initiatives being progressed through Budget 2026. As the Budget proceeds some of these initiatives may become standalone initiatives.
Revenue	Other Savings Initiatives	Welfare reform – Working for Families s 9(2)(f)(iv) Working for Families Revenue portfolio initiatives as part of the welfare reform package for Budget 2026. Initiatives will be updated as policy options are agreed.
Revenue	Baseline reduction	Baseline reduction for Inland Revenue Sets out the impacts of the requested $15.8 million (2%) per annum baseline reduction for Vote Revenue.

[2] Tax and Social Policy Work Programme – Dashboard update – 27 November 2025.
[3] The forecast period is the current financial year plus four outyears being 2025/26 to 2029/30.

Lead Portfolio	Initiative Type	Initiative Title and Notes
Revenue	Other Savings Initiatives	Additional compliance activities - s 9(2)(f)(iv) An invest to save proposal to reduce impairment expenditure by $45 million per annum with an investment of $15 million per annum (a 3:1 return). IR2025/457 provides further detail.
s 9(2)(f)(iv)		

12. The initiatives potentially covered under the Tax and Social Policy Work Programme placeholder initiative include:

- Simplify fringe benefit tax
- Review the impact of the financial arrangement rules on new migrants
- Thin capitalisation for infrastructure (a potential saving from the Budget 2025 tagged contingency)
- Modernise non-resident contractors' withholding tax (NRCT)
- Reduce NRCT for asset leasing in the airline industry
- s 9(2)(f)(iv)
- Continue double tax agreement negotiations
- Progress wider Inland Revenue compliance work and reduce tax debt
- Clarify the income tax treatment of software development expenditure
- Review software expenditure by businesses on software-as-a-service customisation and configuration
- Improve FamilyBoost, including investigating a possible direct data feed with ECEs, and
- Progress the remedial work programme.

13. Other Revenue portfolio led initiatives outside of the Tax and Social Policy Work Programme would require approval from the Minister of Finance to be invited into the Budget 2026 process. This would include initiatives such as the potential business software subsidy for micro and small businesses (IR2025/475 refers).

Initiatives being led by other portfolios

14. We are contributing to the following potential initiatives being led by other Portfolio ministers. The relevant lead agencies will submit these initiatives to the Treasury.

Lead Portfolio	Initiative Type	Initiative Title and Notes
Housing	New Spending	Investment Boost extension to build to rent
s 9(2)(f)(iv)		
Social Dev. & Employment	Other Savings Initiatives	Welfare reform package Other welfare reform package initiatives being developed under the Social Development & Employment portfolio that indirectly impact Vote Revenue appropriations.
s 9(2)(f)(iv)		
Universities	Other Savings Initiatives	Student loans - increased tuition fees

Other initiatives

15. There are other initiatives being considered prior to Budget 2026 or are in the early stages of consideration. We will keep a watching brief on these initiatives, and we will advise you if any of these initiatives will proceed through Budget 2026.

Lead Portfolio	Initiative Type	Initiative Title
s 9(2)(f)(iv)		
Revenue; Science, Innovation & Technology	TBC	Targeting and reducing the cost of the Research and Development Tax Incentive while reducing compliance burden for small business. Potential departmental implementation costs.

Detailed information on initiatives

16. Detailed information for each policy initiative is contained in policy reports we have provided and will continue to provide in coming months. We will update the initiatives in the Treasury CFISnet system as decisions are made.

17. Detailed information for the departmental specific initiatives was provided in our previous report (IR2025/457 refers).

Recommended action

18. We recommend that you:

(a) **Note** the initiatives we intend to submit to the Treasury via the CFISnet system by 1pm on Friday 19 December 2025.

Noted

(b) **Note** that we will advise you if there are any material changes to the initiatives we submit.

Noted

(c) **Sign and refer** the attached letter to the Minister of Finance by 1pm on Friday 19 December 2025.

Signed and referred.

s 9(2)(a)

Darren Cheevers
Acting Enterprise Leader Finance Services

Hon Simon Watts
Minister of Revenue
/ /2025

Hon Simon Watts

Minister of Climate Change
Minister for Energy
Minister of Local Government
Minister of Revenue

19 December 2025

Hon Nicola Willis
Minister of Finance
Parliament Buildings
Wellington

Dear Nicola

I am confirming that I, as the Minister of Revenue, have submitted the initiatives for Inland Revenue, which covers all proposals for the Revenue Portfolio.

Spending Initiatives

ID	Initiative Type	Initiative Title
17152	New Spending	Foreign investment funds rules reform
17148	New Spending	Tax and Social Policy Work Programme initiatives

I have also submitted the following saving initiatives as detailed below.

Baseline Reduction

ID	Initiative Title	Total Operating ($million)
17146	Baseline reduction for Inland Revenue	15.800
Total Baseline Reduction submitted		15.800
Baseline Reduction Target identified in invitation letter		15.800

Other Savings Initiatives

ID	Initiative Type	Initiative Title
17147	Other Savings Initiatives	Additional compliance activities - s 9(2)(f)(iv)
s 9(2)(f)(iv)		
17149	Other Savings Initiatives	Australian style bank tax or prudential levy
17187	Other Savings Initiatives	Foreign owned New Zealand banking group tax rule changes
17150	Other Savings Initiatives	Charities and not-for-profits
17151	Other Savings Initiatives	Shareholder loans
s 9(2)(f)(iv)		

ID	Initiative Type	Initiative Title
s 9(2)(f)(iv)		

Yours sincerely

Hon Simon Watts
Minister of Revenue

BUDGET SENSITIVE

Inland Revenue
Te Tari Taake

Inland Revenue report: 2026 March Baseline Update submission for Vote Revenue

Date:	12 February 2026	**Priority:**	Medium
Security level:	Budget Sensitive	**Report no:**	IR2026/007

Action sought

	Action sought	Deadline
Minister of Revenue	**Agree** to recommendations, and **sign** and **forward** the attached submission to the Minister of Finance.	1.00pm Thursday, 19 February 2026

Contact for telephone discussion (if required)

Name	Position	
Nick Bradley	Chief Financial Officer	s 9(2)(a)
Darren Cheevers	Domain Lead, Finance Services	
Rachel Parker	Domain Lead, Finance Services	

Inland Revenue
Te Tari Taake

12 February 2026

Minister of Revenue

2026 March Baseline Update submission for Vote Revenue

Purpose

1. This report seeks your approval of the attached Vote Revenue 2026 March Baseline Update (MBU) submission letter to the Minister of Finance.

Background

2. The MBU is a technical update of baselines for matters that do not raise significant policy issues and therefore do not require Cabinet approval. All of the proposed changes in this report can be made by joint Ministers – the Vote Minister and the Minister of Finance.

3. The Treasury administers the MBU process. This includes providing agencies with letter templates and setting the due dates. The attached draft letter from you to the Minister of Finance follows the Treasury template.

4. Our MBU submission includes changes to Vote Revenue departmental appropriations (Vote 19)[1] and preliminary changes to Vote Revenue non-departmental appropriations (Vote 20)[2].

5. Further changes to Vote Revenue non-departmental appropriations and tax forecasts (Vote 20) will be submitted to you separately on 19 February as part of the 2026 Preliminary Budget Economic and Fiscal Update (BEFU). These changes will reflect the latest Treasury macroeconomic forecasts.

Overview

6. We request your approval to submit to the Minister of Finance the following proposed Vote Revenue baseline changes for 2025/26 and outyears:

   - technical adjustments within our *Services for customers* multi-category appropriation

   - a fiscally neutral adjustment of $0.050 million a year to fund the new non-departmental *Ex Gratia Payments* appropriation.

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[1] Vote Revenue departmental (Vote 19) includes appropriations to operate the department and deliver outputs and outcomes.

[2] Vote Revenue non-departmental (Vote 20) includes tax revenue and appropriations for expenditure administered by Inland Revenue such as Working for Families Tax Credits, FamilyBoost payments and the KiwiSaver Tax Credit.

- fiscally neutral adjustments of $0.102 million in 2025/26 to fund the new non-departmental *Payments to Settle Residual Claims* appropriation.

- the disestablishment of non-departmental appropriations for the *Cost of Living payment*, the *COVID-19 Resurgence Support Payment*, and the *COVID 19 Support Payment* following the fiscally neutral adjustment above.

- an in-principle expense transfer of up to $0.102 million from 2025/26 to 2026/27, within the *Payments to Settle Residual Claims* appropriation, with early confirmation requested.

- a scope change for the non-departmental *Final-year Fees Free Payments* appropriation.

7. In this report we also provide an update on our departmental funding position and a forecast change for departmental capital expenditure, for you to note.

8. The MBU submission letter for Vote Revenue is due to the Minister of Finance by 1.00pm Thursday 19 February 2026. A proposed letter from you to the Minister of Finance is attached.

Our departmental financial position and funding transfers

9. Our departmental operating budget for the 2025/26 financial year is $787.6 million. This budget reflects $29.6 million in savings from Budget 2024 and includes $64 million in additional compliance funding from Budget 2024 and Budget 2025.

10. For Budget 2026, Budget Ministers have agreed to a departmental baseline reduction of 2% for most agencies, equating to $15.8 million per annum for Vote Revenue. In response, and alongside our ongoing commitment to managing remuneration and inflationary cost pressures, we will deliver further efficiencies across areas such as back-office functions, technology and depreciation savings.

11. In the current year the efficiencies we are achieving may result in an underspend of between $5 million (0.6%) to possibly $15 million (1.3%).

12. Achieving ongoing efficiencies is a core part of our strategy, and we manage spending and savings commitments on a multi-year basis. However, the annualised structure of appropriations constrains our ability to do so. As a result, we have relied on funding transfers in previous years to support service delivery and manage cost pressures across years.

13. We recognise the importance of prudent management of the Government's accounts and, accordingly, are not proposing the transfer of any underspend in this baseline update. Instead, any underspend arising in 2025/26 will be returned to the Crown.

14. We are mindful that decisions on a number of potential Budget 2026 initiatives affecting Vote Revenue are still to be made. The policy, design and funding decisions for these initiatives will have implications for next year and outyears budgets. We will report back to you during the Budget process if a funding transfer from 2025/26 is required to manage any resulting funding constraints.

Details of proposed changes requiring joint Minister approval

Technical adjustments within our *Services for customers* appropriation

15. Our *Services for customers* multi-category appropriation is our primary departmental operating appropriation, with a 2025/26 budget of $786.166 million. This appropriation has five interrelated categories (refer table in paragraph 18). These categories are fully costed[3].

16. Under a multi-category appropriation, individual categories may be over- or underspent provided the total appropriation amount is not exceeded. We are, however, seeking your approval for fiscally neutral adjustments between categories to ensure our forecasts reflect the latest allocations of resources.

17. Each year, the mix of expenditure across these categories will change in response to customer demand, area of focus, work reprioritisation, internal savings, and the impact of new Government initiatives.

18. The following table sets out the proposed fiscally neutral adjustments (FNA).

	$ million – increase / (decrease)			
	2024/25 Actual	2025/26 Budget	Proposed FNA	2025/26 Revised Budget
Services for customers (MCA):				
Policy advice	13.348	13.997	-	13.997
Services to manage debt and unfiled returns	107.788	116.099	31.000	147.099
Services to Ministers and to assist and inform customers to get it right from the start	319.966	320.095	(10.000)	310.095
Services to process obligations and entitlements	187.317	184.602	(6.000)	178.602
Services to protect the integrity of the tax system and functions the Commissioner administers	122.604	151.373	(15.000)	136.373
Total operating	751.023	786.166	-	786.166

19. The mix of expenditure across the five categories was set last April as part of Budget 2025. Since then, we have reprioritised further staff and expenditure towards managing overdue debt, resulting in a $31.000 million increase to this category. The increase in the debt category results in a corresponding decrease in three other categories. The decreases in the other three categories reflect savings in back-off expenditure (i.e. overheads) and do not impact front-line activities or performance in these areas.

20. The following table shows the proposed fiscally neutral technical adjustments across the forecast period. We have not proposed outyear adjustments as this will be subject to Budget 2026 outcomes and updated work prioritisation plans.

21. We seek your approval to submit these fiscally neutral adjustments in this baseline update.

[3] A fully costed category includes direct costs (for example salaries) and indirect costs (for example accommodation and technology costs).

	$ million – increase / (decrease)				
Proposed fiscally neutral adjustments	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
Services for customers (MCA):					
Services to manage debt and unfiled returns	31.000	-	-	-	-
Services to Ministers and to assist and inform customers to get it right from the start	(10.000)	-	-	-	-
Services to process obligations and entitlements	(6.000)	-	-	-	-
Services to protect the integrity of the tax system and functions the Commissioner administers	(15.000)	-	-	-	-
Total operating	-	-	-	-	-

A fiscally neutral adjustment to fund the new non-departmental *Ex Gratia Payments* appropriation

22. As part of our 2025 October Baseline Update submission, you jointly approved the creation of a new non-departmental appropriation for ex gratia payments to customers (IR2025/372 refers). In that submission, we advised that following your approval, the appropriation would initially be funded through a transfer of $0.050 million per annum from Vote Revenue's departmental multi-category appropriation – *Services for customers*. We now seek your approval to submit the following fiscally neutral adjustment as part of this baseline update.

	$ million – increase / (decrease)				
Vote Revenue Minister of Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
Multi-category expenses and capital expenditure Services for customers (MCA):					
Services to Ministers and to assist and inform customers to get it right from the start	(0.050)	(0.050)	(0.050)	(0.050)	(0.050)
Non-departmental other expenses:					
Ex Gratia Payments	0.050	0.050	0.050	0.050	0.050
Total operating	-	-	-	-	-

A fiscally neutral adjustment to fund the new non-departmental *Payments to Settle Residual Claims* appropriation

23. As part of the 2025 October Baseline Update submission, you jointly approved the creation of a new non-departmental appropriation for payments to settle residual claims (IR2025/372 refers). In that submission, we advised that following your approval to establish this appropriation, it would be funded through a transfer of $0.102 million in 2025/26 from the *Cost of Living* payment, *COVID-19 Resurgence Support Payment*, and *COVID 19 Support Payment* non-departmental appropriations. We now seek your approval to transfer the remaining funds in each of these appropriations to the new *Payments to Settle Residual Claims* appropriation. We also seek your agreement to disestablish the *Cost of Living* payment, *COVID-19 Resurgence Support Payment* and the *COVID-19 Support Payment* appropriations following the transfer of these funds. We confirm that no expenditure has been incurred against these appropriations in 2025/26.

	$ million – increase / (decrease)				
Vote Revenue Minister of Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
Non-departmental Other Expenses:					
COVID-19 Resurgence Support Payment	(0.039)	-	-	-	-
COVID-19 Support Payment	(0.054)	-	-	-	-
Cost of Living payment	(0.009)	-	-	-	-
Payments to Settle Residual Claims	0.102	-	-	-	-
Total operating	**-**	-	-	-	-

An in-principle expense transfer for the non-departmental *Payments to Settle Residual Claims* appropriation

24. The timing of potential payments arising from settling residual claims is uncertain. We therefore seek your approval to submit an in-principle expense transfer of up to $0.102 million in operating funding from 2025/26 to fund payments that may be required in 2026/27. Early confirmation of these transfers is requested to enable us to draw down on the funds from 1 July 2026, should they be required. This avoids the risk of unappropriated expenditure if a claim is received, as there is no funding allocated for these appropriations in 2026/27.

	$ million – increase / (decrease)				
Vote Revenue Minister of Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
Non-departmental Other Expenses Payments to Settle Residual Claims	(0.102)	0.102	-	-	-
Total operating	(0.102)	0.102	-	-	-

A scope change for the non-departmental *Final-year Fees Free Payments* appropriation

25. As part of our 2025 Half Year Economic and Fiscal update submission, we advised you of an accounting change relating to final-year Fees Free payments. This removed the costs (and funding) relating to final-year Fees Free entitlements offset against a student loan from this appropriation (IR2025/408 refers). We now seek your joint approval to amend the scope statement for the associated appropriation to better reflect this accounting treatment by removing the reference to loan offsets, as follows:

Appropriation title	Existing scope statement	Amended scope statement
Final-year Fees Free Payments	This appropriation is limited to final-year Fees Free payments and loan offsets made to eligible recipients.	This appropriation is limited to final-year Fees Free payments made to eligible recipients.

26. We confirm that expenditure has been incurred against this appropriation between 1 July 2025 and the time of this request, and therefore we request the change to the scope for this appropriation be effective from 1 July 2026.

Details of proposed changes for noting

A forecast change for departmental capital expenditure

27. Our annual departmental capital expenditure is shaped by our asset management plans, capital injections and withdrawals, and the implementation timelines of policy initiatives.

28. We have updated our capital expenditure forecasts. This update will reduce forecast capital expenditure for three years and increase it from 2027/28. There are three primary drivers for this forecast change:

    - Over the next two years, one of our larger initiatives is the implementation of an integrated payroll system, which will be delivered as an as-a-service solution; as a result, the associated expenditure will be operating in nature rather than capital.

    - For our largest system asset (START) our medium-term focus (one to three years) is on maintenance and policy initiatives that adjust settings within this system. These types of initiatives are operating in nature rather than capital.

    - We have recently completed several upgrades to our leased accommodation. These upgrades support efficient space utilisation and enable rent savings. In the medium-term our capital expenditure relating to accommodation has reduced from that previously forecast.

29. We ask you to note that we are including the following capital expenditure changes in our baseline update.

	$ million – increase / (decrease)				
Inland Revenue Department - Capital Expenditure PLA[4]	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
HYEFU 2025	32.000	42.900	40.400	40.000	40.000
MBU 2026	27.000	25.000	30.000	50.000	45.000
Forecast change - inc/(dec)	(5.000)	(17.900)	(10.400)	10.000	5.000

Treasury CFISnet Table 2 items

30. We have attached a Treasury CFISnet table, referred to by Treasury as 'Table 2', which sets out all of the changes for Vote Revenue departmental (Vote 19).

31. Table 2 for Vote Revenue non-departmental (Vote 20) will be provided in our separate report requesting forecast changes to non-departmental appropriations which will be sent to you on 19 February.

Consultation with the Treasury

32. The Treasury was consulted on this report. The Treasury notes the proposed FNA would increase the funding for debt management and unfiled returns by $31 million in 2025/26 (compliant with CO(18)2). The Treasury supports the focus on debt management, as it is important for fiscal sustainability. However, a significant proportion of the redirected funding consists of reduced funding for the category that includes investigations and audits. Inland Revenue has indicated that this decrease has resulted from back-office

[4] Permanent Legislative Authority (PLA). Changes to a PLA do not require ministerial approval

efficiencies and does not impact front-line activities or performance. The Treasury supports this decrease in the relevant expenditure on this basis.

33. The Treasury notes that Inland Revenue received a significant amount of funding for compliance activities in Budget 2024 and Budget 2025. In light of the proposed transfer discussed above, the Treasury considers it will be even more important for Inland Revenue to effectively monitor and report against the marginality of this funding to demonstrate what rate of return is being achieved.

Recommendations

34. It is recommended that you:

Sign and forward the attached March Baseline Update letter to the Minister of Finance by 1pm Thursday, 19 February 2026

Signed and forwarded

s 9(2)(a)

Nick Bradley
Enterprise Leader Finance Services (Chief Financial Officer)
12 / 02 / 2026

Hon Simon Watts
Minister of Revenue
/ / 2026

Attachments:

a) 2026 March Baseline Update submission to the Minister of Finance for Vote Revenue
b) Table 2 Baseline changes report, 2025/26 MBU (BEFU) Vote 19 – Inland Revenue departmental

Hon Simon Watts

Minister of Climate Change
Minister for Energy
Minister of Local Government
Minister of Revenue

19 February 2026

Hon Nicola Willis
Minister of Finance
Parliament Buildings
WELLINGTON

2026 March Baseline Update submission for Vote Revenue

1. Introduction

This report covers those items affecting the baseline for Vote Revenue for the 2026 March Baseline Update.

I confirm that none of the changes contained in this update require Cabinet decisions at this time.

The proposed changes to the baseline are set out below.

2. Technical adjustments

2.1 Technical adjustments within our *Services for customers* appropriation

The *Services for customers* multi-category appropriation (MCA) is Inland Revenue's primary departmental operating appropriation, with a current 2025/26 budget of $786.166 million. This appropriation has five interrelated categories (refer following table). These categories are fully costed which means that they include direct costs (for example salaries) and indirect costs (for example accommodation and technology costs).

Under a multi-category appropriation, individual categories may be over- or underspent provided the total appropriation is not exceeded. Inland Revenue does, however, seek Joint Ministers approval for fiscally neutral adjustments between categories to ensure Inland Revenue's forecasts reflect the latest allocation of resources.

Each year, the mix of expenditure across these categories will change in response to customer demand, area of focus, work reprioritisation, internal savings, and the impact of new Government initiatives.

The following table sets out the proposed fiscally neutral adjustment (FNA).

	$ million – increase / (decrease)			
	2024/25 Actual	2025/26 Budget	Proposed FNA	2025/26 Revised Budget
Services for customers (MCA):				
Policy advice	13.348	13.997	-	13.997
Services to manage debt and unfiled returns	107.788	116.099	31.000	147.099
Services to Ministers and to assist and inform customers to get it right from the start	319.966	320.095	(10.000)	310.095
Services to process obligations and entitlements	187.317	184.602	(6.000)	178.602
Services to protect the integrity of the tax system and functions the Commissioner administers	122.604	151.373	(15.000)	136.373
Total operating	751.023	786.166	-	786.166

The mix of expenditure across the five categories was set last April as part Budget 2025. Since then, Inland Revenue has reprioritised further staff and expenditure towards managing overdue debt, resulting in a $31.000 million increase to this category. The increase in the debt category results in a corresponding decrease in three other categories. The decreases in the other three categories reflect savings in back-off expenditure (i.e. overheads) and do not impact front-line activities or performance in these areas.

The following table shows the proposed fiscally neutral technical adjustments across the forecast period. Inland Revenue has not proposed outyear adjustments as this will be subject to Budget 2026 outcomes and updated work prioritisation plans.

	$ million – increase / (decrease)				
Vote Revenue Minister of Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
Services for customers (MCA):					
Services to manage debt and unfiled returns	31.000	-	-	-	-
Services to Ministers and to assist and inform customers to get it right from the start	(10.000)	-	-	-	-
Services to process obligations and entitlements	(6.000)	-	-	-	-
Services to protect the integrity of the tax system and functions the Commissioner administers	(15.000)	-	-	-	-
Total operating	-	-	-	-	-

I recommend you approve these fiscally neutral adjustments.

3. Fiscally neutral adjustments

3.1 A fiscally neutral adjustment to fund the new non-departmental *Ex Gratia Payments* appropriation

As part of Inland Revenue's 2025 October Baseline Update submission, we jointly approved the creation of a new non-departmental appropriation for ex gratia payments to customers (IR2025/372 refers). In that submission, Inland Revenue advised that following our approval, the appropriation would initially be funded through a transfer of $0.050 million per annum from the departmental multi-category appropriation – *Services for customers*.

I recommend you approve the following fiscally neutral adjustment as part of this baseline update.

	$ million – increase / (decrease)				
Vote Revenue Minister of Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
Multi-category expenses and capital expenditure Services for customers (MCA): Services to Ministers and to assist and inform customers to get it right from the start	(0.050)	(0.050)	(0.050)	(0.050)	(0.050)
Non-departmental other expenses: Ex Gratia Payments	0.050	0.050	0.050	0.050	0.050
Total operating	-	-	-	-	-

3.2 A fiscally neutral adjustment to fund the new non-departmental Payments to Settle Residual claims appropriation

As part of Inland Revenue's 2025 October Baseline Update submission, we jointly approved the creation of a new non-departmental appropriation for *Payments to Settle Residual Claims* (IR2025/372 refers). In that submission, Inland Revenue advised that following our approval to establish this appropriation, it would be funded through a transfer of $0.102 million in 2025/26 from the *Cost of Living payment*, *COVID-19 Resurgence Support Payment*, and *COVID 19 Support Payment* non-departmental appropriations.

I recommend you approve the transfer of the remaining funds in each of these appropriations to the new *Payments to Settle Residual Claims* appropriation.

I also recommend you agree to disestablish the *Cost of Living* p*ayment*, *COVID-19 Resurgence Support Payment* and the *COVID-19 Support Payment* appropriations following the transfer of these funds.

	$ million – increase / (decrease)				
Vote Revenue Minister of Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
Non-departmental Other Expenses:					
COVID-19 Resurgence Support Payment	(0.039)	-	-	-	-
COVID-19 Support Payment	(0.054)	-	-	-	-
Cost of Living payment	(0.009)	-	-	-	-
Payments to Settle Residual Claims	0.102	-	-	-	-
Total operating	**-**	-	-	-	-

4. In-principle expense and capital transfer (IPECTs)

4.1 An in-principle expense transfer for the non-departmental Payments to Settle Residual Claims appropriation

The timing of potential payments arising from settling residual claims is uncertain. Inland Revenue is therefore seeking our approval to submit an in-principle expense transfer of up to $0.102 million in operating funding from 2025/26 to fund payments that may be required in 2026/27. Inland Revenue are also seeking early confirmation of these transfers to enable them to draw down on the funds from 1 July 2026, should they be required.

	$ million – increase / (decrease)				
Vote Revenue Minister of Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
Non-departmental Other Expenses Payments to Settle Residual Claims	(0.102)	0.102	-	-	-
Total operating	(0.102)	0.102	-	-	-

I recommend you approve an in-principle expense transfer of up to $0.102 million from 2025/26 to 2026/27 in the non-departmental *Payments to Settle Residual Claims* appropriation and provide early confirmation of the transfer.

5. Other Matters

5.1 A scope change for the non-departmental Final-year Fees Free Payments appropriation

As part of Inland Revenue's 2025 Half Year Economic and Fiscal update submission, they advised us of an accounting change relating to final-year Fees Free payments. This removed the costs (and funding) relating to final-year Fees Free entitlements offset against a student loan from this appropriation (IR2025/408 refers).

I recommend you approve the following change to the scope statement for the associated appropriation to better reflect this accounting treatment by removing the reference to loan offsets:

Appropriation title	Existing scope statement	Amended scope statement
Final-year Fees Free Payments	This appropriation is limited to final-year Fees Free payments and loan offsets made to eligible recipients.	This appropriation is limited to final-year Fees Free payments made to eligible recipients.

Inland Revenue confirms that expenditure has been incurred against this appropriation between 1 July 2025 and the time of this request, and therefore they request the change to the scope for this appropriation be effective from 1 July 2026.

5.2 A forecast change for departmental expenditure

Inland Revenue's annual departmental capital expenditure is shaped by their asset management plans, capital injections and withdrawals, and the implementation timelines of policy initiatives.

Inland Revenue have updated their capital expenditure forecasts. This update will reduce forecast capital expenditure for three years and increase it from 2027/28. There are three primary drivers for this forecast change:

- Over the next two years, one of Inland Revenue's larger initiatives is the implementation of an integrated payroll system, which will be delivered as an as-a-service solution; as a result, the associated expenditure will be operating in nature rather than capital.

- For Inland Revenue's largest system asset (START) their medium-term focus (one to three years) is on maintenance and policy initiatives that adjust settings within this system. These types of initiatives are operating in nature rather than capital.

- Inland Revenue have recently completed several upgrades to their leased accommodation. These upgrades support efficient space utilisation and enable rent savings. In the medium-term Inland Revenue's capital expenditure relating to accommodation has reduced from that previously forecast.

This forecast adjustment will be made to the *Capital expenditure* Permanent Legislative Authority (PLA) appropriation which does not require Joint Ministers approval.

	$ million – increase / (decrease)				
Inland Revenue Department - Capital Expenditure PLA	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears
HYEFU 2025	32.000	42.900	40.400	40.000	40.000
MBU 2026	27.000	25.000	30.000	50.000	45.000
Forecast change - inc/(dec)	(5.000)	(17.900)	(10.400)	10.000	5.000

5.3 Inland Revenue's financial position and funding transfers

Inland Revenue's departmental operating budget for the 2025/26 financial year is $787.6 million. This budget reflects $29.6 million in savings from Budget 2024 and includes $64 million in additional compliance funding from Budget 2024 and Budget 2025.

For Budget 2026, Budget Ministers have agreed to a departmental baseline reduction of 2% for most agencies, equating to $15.8 million per annum for Vote Revenue. In response, and alongside the department's ongoing commitment to managing remuneration and inflationary cost pressures, they will deliver further efficiencies across areas such as back-office functions, technology and depreciation savings.

In the current year the efficiencies Inland Revenue are achieving may result in an underspend of between $5 million (0.6%) to possibly $15 million (1.3%).

Achieving ongoing efficiencies is a core part of the department's strategy, and how they manage spending and savings commitments on a multi-year basis. However, the annualised structure of appropriations constrains their ability to do so. As a result, the department has relied on funding transfers in previous years to support service delivery and manage cost pressures across years.

Inland Revenue recognise the importance of prudent management of the Government's accounts and, accordingly, are not proposing the transfer of any underspend in this baseline update. Instead, any underspend arising in 2025/26 will be returned to the Crown.

The department is mindful that decisions on a number of potential Budget 2026 initiatives affecting Vote Revenue are still to be made. The policy, design and funding decisions for these initiatives will have implications for next year and outyears budgets. Inland Revenue

will report back to us during the Budget process if a funding transfer from 2025/26 is required to manage any resulting funding constraints.

6. Consultation with the Treasury

Inland Revenue has consulted on the 2026 March Baseline Update submission with the Treasury. The Treasury notes the proposed FNA would increase the funding for debt management and unfiled returns by $31 million in 2025/26 (compliant with CO(18)2). The Treasury supports the focus on debt management, as it is important for fiscal sustainability. However, a significant proportion of the redirected funding consists of reduced funding for the category that includes investigations and audits. Inland Revenue has indicated that this decrease has resulted from back-office efficiencies and does not impact front-line activities or performance. The Treasury supports this decrease in the relevant expenditure on this basis.

The Treasury notes that Inland Revenue received a significant amount of funding for compliance activities in Budget 2024 and Budget 2025. In light of the proposed transfer discussed above, the Treasury considers it will be even more important for Inland Revenue to effectively monitor and report against the marginality of this funding to demonstrate what rate of return is being achieved.

7. Recommendations

I recommend that you:

1. **agree** the changes to those baselines for the departmental appropriations within Vote Revenue that require Joint Ministers' approval as set out in Table 2 for Vote 19;

2. **note** that Table 2 for Vote 19 includes for completeness other changes to baselines for the appropriation on Vote Revenue that have been approved by Cabinet or Joint Ministers since the previous update or do not require such approval.

3. **approve** a fiscally neutral adjustment of $0.050 million per annum from Vote Revenue's departmental multi-category appropriation – *Services for customers* to the non-departmental *Ex Gratia Payments* appropriation.

4. **approve** a fiscally neutral adjustment of $0.102 million in 2025/26 from Vote Revenue's non-departmental *Cost of Living* payment, *COVID-19 Resurgence Support Payment*, and *COVID 19 Support Payment* appropriations to the *Payments to Settle Residual Claims* appropriation.

5. **agree** to the disestablishment of Vote Revenue's non-departmental appropriations for the *Cost of Living* payment, the *COVID-19 Resurgence Support Payment*, and the *COVID 19 Support Payment* following the transfer approved in recommendation 4 above.

6. **approve** an in-principle expense transfer of up to $0.102 million from 2025/26 to 2026/27 within Vote Revenue's non-departmental *Payments to Settle Residual Claims* appropriation and provide early confirmation of the transfer.

7. **approve** the following revised Vote Revenue non-departmental *Final-year Fees Free Payments* appropriation scope statement:

   - This appropriation is limited to final-year Fees Free payments made to eligible recipients.

8. **note** that Table 2 for Vote 20 will be included in the 2026 Preliminary Budget Economic and Fiscal Update (BEFU), which is a separate submission due to the Treasury on 16 February 2026, based on updated Treasury macroeconomic forecasts and interim valuations and that Inland Revenue will seek our joint approval for forecast changes to non-departmental appropriations in a separate report.

Hon Simon Watts
Minister of Revenue

Table 2: Baseline Changes Report, 2025/26 MBU, Vote 19 - 0: IRD Department - Revenue. Data has not been validated

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Departmental Capital Expenditure								
Inland Revenue Department - Capital Expenditure (PLA)								
Dept Other Appropriation								
Forecast change for departmental capital expenditure	Fcst Adj	(5,000)	(17,900)	(10,400)	10,000	5,000	CO(18)2	On going
Total changes - Departmental Capital Expenditure		**(5,000)**	**(17,900)**	**(10,400)**	**10,000**	**5,000**		
Multi-Category Expenses and Capital Expenditure								
Services for Customers (MCA)								
Departmental Output Expenses								
Services to manage debt and unfiled returns								
Dept Annual Appropriation								
Technical adjustments within the Services for customers appropriation	Tech Adj	31,000	-	-	-	-	CO(18)2	On going
Revenue Crown								
Technical adjustments within the Services for customers appropriation	Tech Adj	31,000	-	-	-	-	CO(18)2	On going
Services to Ministers and to assist and inform customers to get it right from the start								
Dept Annual Appropriation								
Fiscally neutral adjustment to fund the new non-departmental Ex Gratia Payments appropriation	FNA	(50)	(50)	(50)	(50)	(50)	CO(18)2 and IR2025/372	On going
Technical adjustments within the Services for customers appropriation	Tech Adj	(10,000)	-	-	-	-	CO(18)2	On going
Revenue Crown								
Fiscally neutral adjustment to fund the new non-departmental Ex Gratia Payments appropriation	FNA	(50)	(50)	(50)	(50)	(50)	CO(18)2 and IR2025/372	On going
Technical adjustments within the Services for customers appropriation	Tech Adj	(10,000)	-	-	-	-	CO(18)2	On going
Services to process obligations and entitlements								
Dept Annual Appropriation								
Technical adjustments within the Services for customers appropriation	Tech Adj	(6,000)	-	-	-	-	CO(18)2	On going
Revenue Crown								
Technical adjustments within the Services for customers appropriation	Tech Adj	(6,000)	-	-	-	-	CO(18)2	On going
Services to protect the integrity of the tax system and functions the Commissioner administers								

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Dept Annual Appropriation								
Technical adjustments within the Services for customers appropriation	Tech Adj	(15,000)	-	-	-	-	CO(18)2	On going
Revenue Crown								
Technical adjustments within the Services for customers appropriation	Tech Adj	(15,000)	-	-	-	-	CO(18)2	On going
Total changes - Multi-Category Expenses and Capital Expenditure		**(50)**	**(50)**	**(50)**	**(50)**	**(50)**		
Total changes - Output revenue (Crown +Dept+Other)		**(50)**	**(50)**	**(50)**	**(50)**	**(50)**		

Classification Key

Short Name	Description	Reference
Cabinet	Cabinet policy decision	Approvals are sought in cabinet papers (refer to cabinet manual), with authority given via a cabinet minute. The authority for change should reference both supporting documents.
ECT	Expense and Capital Transfer	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding within an appropriation across financial years.
ECT ip	Expense and Capital Transfer in-principle	Defined in (Cabinet Office Circular). The portion of an ECT that can't be accurately quantified so the transfer amount has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Fcst Adj	Forecast Adjustments	Defined in (Cabinet Office Circular). Adjustments to the forecast expenditure of PLAs or where there is a pre-determined cost calcultion, or Crown Revenue.
FLoS	Front-Loading of Spending	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Bringing forward expenditure to create lasting cost savings.
FNA	Fiscally Neutral Adjustment	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding between appropriations within a financial year.
RoU	Retention of Underspends	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring underspends to the next financial year.
RoU 50%	Retention of Underspends @ 50%	Defined in CO Circular. Portion of an ROU can't accurately quantify so the transfer amount of 50% of an underspend has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Tech Adj	Technical adjustment	Defined in (Cabinet Office Circular). Technical accounting adjustments with no cash impact to the Crown, MYA spending profile changes, non-controversial appropriation title or scope changes.
SuppsJune	Offset MYA June vs Supps Difference	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the difference between the Supps Forecast and June Actual.
BudgetOY4	Offset MYA Budget OY4 Rollover	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the rollover of Budget OY4 into OBU OY4.
Return Sav	Return of savings to the Crown	Returning savings to the Crown is always encouraged. Departments can achieve this by constantly looking for efficiency gains through improvements in processes and technology.
Crwn Liab	Recognition of Existing Crown liability	Crown liabilities need to be recognised as soon as possible. These affect Non-Departmental Appropriations.
Other	Other changes outside the above criteria	There should be very few changes outside the above criteria, so if there are any they require extra scrutiny.

[SENSITIVE]

Inland Revenue
Te Tari Taake

Vote Revenue: 2026 Preliminary Budget Economic and Fiscal Update for the Research and Development Tax Incentive appropriation

Date:	16 February 2026	**Priority:**	High
Security level:	In confidence (Budget Sensitive)	**Report no:**	IR2026/032

Action sought

	Action sought	Deadline
Minister of Finance	**Approve** recommendations	6 March 2026
Minister of Science, Innovation and Technology	**Approve** recommendations **Refer** report to the Minister of Finance	25 February 2026
Minister of Revenue	For your information	16 February 2026

Contact for telephone discussion (if required)

Name	Position	Telephone	
Nick Bradley	Enterprise Leader Finance Services (Chief Financial Officer)	s 9(2)(a)	
Rachel Parker	Domain Lead Finance Services		s 9(2)(a)

Inland Revenue
Te Tari Taake

16 February 2026

Minister of Finance
Minister of Science, Innovation and Technology

Vote Revenue: 2026 Preliminary Budget Economic and Fiscal Update for the Research and Development Tax Incentive appropriation

Executive Summary

1. This paper asks you to note the changes to the forecast costs of the Research and Development Tax Incentive (RDTI) and seeks your approval for the corresponding changes to the RDTI appropriation.
2. The RDTI appropriation is managed under Vote Revenue using forecasts developed by the Ministry of Business, Innovation and Employment (MBIE). The Minister of Science, Innovation and Technology is responsible for the appropriation.
3. Inland Revenue will submit an updated forecast for this appropriation to the Treasury on 16 February 2026 as part of the 2026 March Baseline Update submission (MBU 2026). This is a preliminary forecast which will be updated as part of the Budget Economic and Fiscal Update 2026 (BEFU 2026).
4. Forecast changes in this report are compared against the 2025 Half-year Economic and Fiscal Update (HYEFU 2025). They include all Cabinet and joint Minister decisions that impact the appropriation up to 16 February 2026.
5. The forecasts are based on MBIE's RDTI fiscal-cost forecast, which currently extends to 2029/30. MBIE's RDTI forecast is based on the Treasury's preliminary BEFU 2026 macroeconomic forecasts of nominal gross domestic product (GDP) as at 5 February 2026 and the 2024 R&D Survey results (released by Stats NZ on 23 April 2025).
6. MBIE's RDTI forecast relates to all RDTI-related expenditure. Cabinet agreed to decrease the forecast for the RDTI appropriation and approved a corresponding increase to expenditure in the in-year payments appropriation (DEV-22-MIN-0062 refers). This appropriation was not managed under Vote Revenue and hence was subtracted from the MBU 2026 forecast.
7. The in-year payments loans programme was discontinued in 2023/24, and the remaining funds transferred to the centre. However, the RDTI appropriation is still reduced by this amount until 2025/26 as the funds were transferred out of the RDTI appropriation at that time. The amounts are shown separately in the following table:

	$ million				
RDTI forecast – MBU 2026	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Out-years**
MBIE RDTI total fiscal-cost forecast	661.000	715.000	770.000	824.000	879.000
Less the in-year payment	(29.258)	-	-	-	-
RDTI within Vote Revenue	**631.742**	**715.000**	**770.000**	**824.000**	**879.000**

8. We are seeking your joint approval for the following forecast and appropriation changes within Vote Revenue since HYEFU 2025:

	$ million				
Vote Revenue **Minister of Science, Innovation and Technology**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Out-years**
Non-departmental Other Expenses: Science, Innovation and Technology: R&D Tax Incentive					
HYEFU 2025	630.742	713.000	765.000	820.000	876.000
MBU 2026	631.742	715.000	770.000	824.000	879.000
Forecast change – inc/(dec)	**1.000**	**2.000**	**5.000**	**4.000**	**3.000**

9. The increases in the MBU 2026 forecasts are entirely driven by an increase in Treasury's estimate of gross domestic product (GDP) for 2025/26.

10. The Treasury and Ministry of Business, Innovation and Employment have been consulted on this report.

Recommended action

13. It is recommended that you:

(a) **note** that the appropriations for 2025/26 to 2029/30 have increased as a result of the latest fiscal-cost forecasts from MBIE for RDTI-eligible expenditure, which are entirely driven by an increase in Treasury's estimate of gross domestic product (GDP) for 2025/26.

Noted Noted

(b) **approve** the following forecast changes to the Vote Revenue Science, Innovation and Technology: R&D Tax Incentive appropriation, with a corresponding impact on the operating balance:

	$ million – increase / (decrease)				
Vote Revenue **Minister of Science, Innovation and Technology**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Out-years**
Non-departmental Other Expenses: Science, Innovation and Technology: R&D Tax Incentive	1.000	2.000	5.000	4.000	3.000
Total Forecast change – inc/(dec)	**1.000**	**2.000**	**5.000**	**4.000**	**3.000**

Approved/Not approved Approved/Not approved

(c) **agree** that the proposed change to appropriations for 2025/26, as shown in recommendation (b) above, be included in the 2025/26 Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply.

Agreed/Not Agreed Agreed/Not Agreed

s 9(2)(a)

Nick Bradley
Enterprise Leader Finance Services - Chief Financial Officer
16/02/2026

Hon Nicola Willis
Minister of Finance

__/__/2026

Hon Dr Shane Reti
Minister of Science, Innovation and Technology

__/__/2026

Inland Revenue
Te Tari Taake

Inland Revenue report: Vote Revenue Ministerial Certification of Contingent Liabilities and Contingent Assets as at 31 December 2025

Date:	19 February 2026	**Priority:**	Medium
Security Level:	In confidence	**Report no:**	IR2025/504

Action sought

	Action sought	Deadline
Minister of Revenue	**Note** the contents of this report, and **Sign** and **return** the attached *Certification of Contingent Liabilities and Contingent Assets* (appendix 2) to Inland Revenue.	Wednesday, 25 February 2026

Contact for telephone discussion (if required)

Name	Position	Telephone	
Nick Bradley	Chief Financial Officer	s 9(2)(a)	
Darren Cheevers	Domain Lead Finance Services		
Rachel Parker	Domain Lead Finance Services	-	s 9(2)(a)

19 February 2026

Minister of Revenue

Vote Revenue Ministerial Certification of Contingent Liabilities and Contingent Assets as at 31 December 2025

Purpose

1. This report seeks your sign-off of the *Certification of Contingent Liabilities and Contingent Assets as at 31 December 2025* (certification) for Vote Revenue (refer Appendix 2).

2. We will submit the Certification and the attached *Register of Contingent Liabilities and Contingent Assets of Inland Revenue as at 31 December 2025* (register) to the Treasury on your behalf (refer Appendix 1).

Background

3. Vote Ministers are required to certify the balances of their departments' contingent liabilities and contingent assets every six months (ECC (91)M21/4 refers).

4. We are required to send the register and the signed certification to the Treasury. The register and the certification are based on templates from the Treasury.

5. We have a comprehensive internal review process to ensure all contingent liabilities and contingent assets are identified. We certify that the balances reported in the register are correct.

6. The changes in the balances of both departmental and non-departmental contingent assets and liabilities, from 30 June 2025, are set out in the following sections.

Contingent liabilities and contingent assets

Departmental contingent assets

7. As at 31 December 2025, Inland Revenue's departmental contingent assets totalled $798,000. This is a decrease of $204,000 compared to 30 June 2025.

Departmental contingent assets	30 Jun 2025	30 Jun 2025	Increase/ (Decrease)
Legal proceedings and disputes - taxpayer	$1,002,000	$798,000	$(204,000)

8. Departmental contingent assets represent our estimate of the court costs that we will recover if cases before the court (such as tax disputes) are decided in our favour. We distinguish departmental court costs from the tax revenue under dispute.

9. The decrease in departmental contingent assets is mainly due to cases having lower estimated court costs as at 31 December 2025 compared to 30 June 2025.

Departmental contingent liabilities

10. As at 31 December 2025 Inland Revenue's departmental contingent liabilities totalled $556,000. This is an increase of $228,000 compared to 30 June 2025.

Departmental contingent liabilities	30 Jun 2025	31 Dec 2025	Increase/ (Decrease)
Employee grievances	$90,000	$275,000	$185,000
Legal proceedings and disputes - taxpayer	$238,000	$186,000	$(52,000)
Other	-	$95,000	$95,000
Total	**$328,000**	**$556,000**	**$228,000**

11. 9(2)(a) [redacted]

12. The legal proceedings and disputes contingent liability represents our estimate of court costs associated with tax disputes and other tax litigation that we may be required to pay when cases before the court are decided against Inland Revenue. There is a decrease due to cases having lower estimated court costs as at 31 December 2025.

13. Other contingent liabilities as at 31 December 2025 represent a new claim from a s 9(2)(a) [redacted]

Non-departmental contingent assets

14. As at 31 December 2025, Inland Revenue's non-departmental contingent assets totalled $29,855,000 This is an increase of $10,536,000 compared to 30 June 2025.

Non-departmental contingent assets	30 Jun 2025	31 Dec 2025	Increase/ (Decrease)
Legal proceedings and disputes	$19,319,000	$29,855,000	$10,536,000

15. Non-departmental contingent assets arise as part of the tax disputes process. For example, when we advise a taxpayer of a proposed adjustment to their tax assessment, but we have not yet amended their assessment. We do not recognise additional tax revenue in these cases because we have not formally amended the assessment. Rather, we report the amount as a non-departmental contingent asset, estimated as the likely revenue we will collect based on experience of similar cases.

16. The total increase in non-departmental contingent assets of $10,536,000 compared to 30 June 2025 is mainly due to an increase in the total net tax value under dispute. This is driven by both existing disputes covering more financial periods and several new higher value cases.

Non-departmental contingent liabilities

17. As at 31 December 2025, Inland Revenue non-departmental contingent liabilities totalled $907,242,000. This is an increase of $42,760,000 compared to 30 June 2025.

Non-departmental contingent liabilities	30 Jun 2025	31 Dec 2025	Increase/ (Decrease)
Legal proceedings and disputes	$296,824,000	$312,284,000	$15,460,000
Unclaimed monies	$567,658,000	$594,958,000	$27,300,000
Total	**$864,482,000**	**$907,242,000**	**$42,760,000**

18. Legal proceedings and disputes arise when either Inland Revenue or a taxpayer disagrees with a proposed adjustment, the dispute process is fully exhausted, and the matter has proceeded to litigation. We issue an assessment at this point and recognise the revenue and a contingent liability for the full amount under dispute.

19. The amount of the contingent liabilities relating to legal proceedings and disputes increased by $15,460,000 in comparison to 30 June 2025. This reflects a small increase in both the amounts and the number of cases at litigation.

20. We administer unclaimed monies under the Unclaimed Money Act 1971. We use trends from previous years to estimate the value of unclaimed monies that will be paid out in the future. This estimate is recognised as a liability in our financial accounts, as it represents a probable outflow. The portion of unclaimed monies that is not expected to be claimed is reported as a contingent liability.

21. The amount of the contingent liabilities relating to unclaimed monies has increased by $27,300,000 from 30 June 2025. This increase largely reflects an increase of monies passed onto Inland Revenue but not expected to be paid out.

Recommendations

22. I recommend that you:

a) **Note** the contents of this report.

Noted

b) **Sign** the *Certification of Contingent Liabilities and Contingent Assets* (appendix 2).

c) **Return** the *Certification of Contingent Liabilities and Contingent Assets* to Inland Revenue by 5:00 pm, Wednesday 25 February 2026.

s 9(2)(a)

Nick Bradley
Chief Financial Officer
19 / 02 / 2026

Hon Simon Watts
Minister of Revenue
/ 02 / 2026

Appendix 1: Register

Register of Contingent Liabilities and Contingent Assets of Inland Revenue as at 31 December 2025

Departmental contingent assets	
Legal proceedings and disputes	$798,000
	$798,000
Departmental contingent liabilities	
Employee grievances	$275,000
Legal proceedings and disputes	$186,000
Other	$95,000
	$556,000
Non-departmental contingent assets	
Legal proceedings and disputes	$29,855,000
	$29,855,000
Non-departmental contingent liabilities	
Legal proceedings and disputes	$312,284,000
Unclaimed monies	$594,958,000
	$907,242,000

Appendix 2: Certification

Certification of Contingent Liabilities and Contingent Assets as at 31 December 2025.

In accordance with Cabinet Expenditure Control Committee minute ECC(91) M21/4 of 7 May 1991, I hereby certify that I am unaware of any contingent liability or asset that has been omitted from the Statement of Contingent Liabilities and Contingent Assets as reported in the register at 31 December 2025 prepared by Inland Revenue and reported in appendix 1.

Inland Revenue

……

Hon Simon Watts

Minister of Revenue

……

Date

Inland Revenue
Te Tari Taake

Vote Revenue: 2026 Preliminary Budget Economic and Fiscal Update for non-departmental expenditure appropriations

Date:	19 February 2026	**Priority:**	High
Security level:	In Confidence (Budget Sensitive)	**Report no:**	IR2026/024

Action sought

	Action sought	**Deadline**
Minister of Finance	**Approve** recommendations	2 March 2026
Minister of Revenue	**Approve** recommendations **Refer** report to the Minister of Finance	25 February 2026

Contact for telephone discussion (if required)

Name	**Position**	
Nick Bradley	Enterprise Leader Finance Services (Chief Financial Officer)	s 9(2)(a)
Rachel Parker	Domain Lead Finance Services	
Sandra Watson	Policy Lead Forecasting and Analysis	

Inland Revenue
Te Tari Taake

19 February 2026

Minister of Finance
Minister of Revenue

Vote Revenue: 2026 Preliminary Budget Economic and Fiscal Update for non-departmental expenditure appropriations

Executive summary

1. Inland Revenue Te Tari Taake submitted forecasts for non-departmental appropriations to the Treasury for the 2026 Preliminary Budget Economic and Fiscal Update (Preliminary BEFU 2026) on 16 February 2026. The forecasts in this report incorporate actual results to December 2025 and are based on the Treasury's updated macroeconomic forecasts of 5 February 2026. These forecasts include Cabinet and joint Minister's decisions that impact Vote Revenue up to 16 February 2026.

2. This report seeks your joint approval for the forecast changes to appropriations that are reflected in the Preliminary BEFU 2026, and which are not established under a permanent legislative authority (PLA). Forecast changes to appropriations which are established under a PLA do not require approval[1] but are also provided for your information. A full list of the appropriations is provided in Appendix A.

3. The preliminary forecasts are our 'best estimate' of the expected outturn as at 16 February 2026. Appropriations and forecasts will be updated again on 13 April as part of the final Budget Economic and Fiscal Update (BEFU), and we will seek your approval for any further changes to appropriations required as part of this update.

4. The major forecast changes across the forecast period since the Half Year Economic and Fiscal Update (HYEFU 2025) for appropriations requiring joint Ministers' approval (not including PLAs) are:

    - a $110 million increase in the forecast for the Paid Parental Leave Payments appropriation which reflects a stronger than-than-previously forecast outturn for 2025/26 to date. The increase includes a buffer of $25 million for appropriation management purposes. The higher base for 2025/26 flows into 2026/27 along with a slightly larger indexation adjustment than previously forecast. From 2027/28 onwards, stronger expected growth in weekly earnings drives increases in annual entitlement indexation across the forecast period.

[1] As per the Public Finance Act, section 65ZH.

- a $142 million increase in the forecast for the Initial Fair Value Write-Down Relating to Student Loans appropriation which reflects higher forecast new lending and an increase to the initial fair value write-down rate driven by discount rate changes and other forecast cashflow. The increase in 2025/26 also includes a buffer of $50 million for appropriation management purposes.

5. The forecast for the Impairment of Debt and Debt Write-offs appropriation has not changed since HYEFU 2025, with the exception of the Cabinet decision to reduce Use of Money interest rates. Where necessary this will be updated at BEFU when both the interim debt valuation as at 31 December 2025 and payments for the February due dates are available.

6. In this submission, we have included indicative buffers for 2025/26 for annual appropriations to help manage the risk of breaches of appropriation where the appropriation relates to impairment or volatile expenditure which is outside of Inland Revenue's control. These buffers are upper limits for appropriation management purposes and are not recorded against allowances.

7. For PLA appropriations, the major forecast changes across the forecast period since HYEFU 2025 are:

   - a $191 million decrease to the forecasts for child support payments to custodial parents, reflecting a continued fall in the number of cases managed by Inland Revenue.

   - a $400 million increase to the KiwiSaver: Employee and Employer Contributions appropriation reflecting further forecast increases to nominal wage growth. This does not affect the operating balance, as this is a pass-through transaction.

8. Further details of all forecast changes, including the major forecast changes above, are contained within the body of this report. Appendix B sets out all forecast changes for Vote Revenue Crown (non-departmental) in a tabulated format. This table includes tax forecasts prepared by the Treasury.

9. We have consulted on this submission with the Treasury.

Recommended action

10. We recommend that you:

(a) **note** the Preliminary BEFU 2026 forecasts in this report incorporate actual results to December 2025, are based on the Treasury's macroeconomic forecasts of 5 February 2026, and were submitted to the Treasury on 16 February 2026.

Noted Noted

(b) **note** the appropriation movements for 2025/26 for appropriations for non-departmental benefits or related expenses and non-departmental other expenses that are not established under a PLA include a buffer for appropriation management purposes and that these buffers are not recorded against allowances.

Noted Noted

(c) **approve** the following forecast changes to appropriations for non-departmental benefits or related expenses that are not established under a PLA, with a corresponding impact on the operating balance and net core Crown debt:

	$ million – increase / (decrease)					
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total Forecast Period**
Non-Departmental Benefits or Related expenses:						
KiwiSaver: Interest	0.500	0.500	0.500	1.000	1.000	3.500
KiwiSaver: Tax Credit, Contribution and Residual Entitlement	23.000	0.800	1.900	3.800	1.900	31.400
Paid Parental Leave Payments	30.000	15.000	20.000	20.000	25.000	110.000
Total Operating	**53.500**	**16.300**	**22.400**	**24.800**	**27.900**	**144.900**

Approved/Not approved Approved/Not approved

(d) **approve** the following forecast changes to appropriations for non-departmental other expenses that are not established under a PLA, with a corresponding impact on the operating balance and net core Crown debt:

	$ million – increase / (decrease)					
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total Forecast Period**
Non-Departmental Other Expenses:						
Final-year Fees Free Payments	4.000	1.000	2.000	3.000	3.000	13.000
Impairment of Debt and Debt Write-Offs Relating to Child Support	50.000	-	-	-	-	50.000
Impairment of Debt Relating to Student Loans	50.000	-	-	-	-	50.000
Impairment of Debt Relating to the SBCS	40.000	-	-	-	-	40.000
Initial Fair Value Write-Down Relating to Student Loans	62.000	34.000	22.000	14.000	10.000	142.000
Total Operating	**206.000**	**35.000**	**24.000**	**17.000**	**13.000**	**295.000**

Approved/Not approved

Approved/Not approved

(e) **note** the following forecast changes to non-departmental benefits or related expenses, non-departmental borrowing expenses, and non-departmental other expenses that are established under a PLA:

	$ million – increase / (decrease)					
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total Forecast Period**
Non-Departmental Benefits or Related Expenses - PLA:						
Best Start Tax Credit	1.000	(1.000)	(1.000)	1.000	-	-
Child Support Payments	(27.000)	(34.000)	(39.000)	(43.000)	(48.000)	(191.000)
Family Tax Credit	-	(14.000)	1.000	(21.000)	(47.000)	(81.000)
FamilyBoost Tax Credit	(7.000)	-	-	-	-	(7.000)
In-Work Tax Credit	(3.000)	(6.000)	(8.000)	(6.000)	(11.000)	(34.000)
Minimum Family Tax Credit	0.500	0.500	0.500	0.500	0.500	2.500
Total change – inc/(dec)	**(35.500)**	**(54.500)**	**(46.500)**	**(68.500)**	**(105.500)**	**(310.500)**
Non-Departmental Borrowing Expenses – PLA:						
Environmental Restoration Account Interest	0.100	0.100	0.100	0.100	0.100	0.500
Total change – inc/(dec)	**0.100**	**0.100**	**0.100**	**0.100**	**0.100**	**0.500**
Non-Departmental Other Expenses - PLA:						
KiwiSaver: Employee and Employer Contributions*	(30.000)	40.000	110.000	130.000	150.000	400.000
Total change – inc/(dec)	**(30.000)**	**40.000**	**110.000**	**130.000**	**150.000**	**400.000**
Total Operating*	**(35.400)**	**(54.400)**	**(46.400)**	**(68.400)**	**(105.400)**	**(310.000)**

* The KiwiSaver: Employee and Employer Contributions appropriation does not affect the operating balance as it is a pass-through transaction.

Noted Noted

(f) **note** that the Science, Innovation and Technology: R&D Tax Incentive appropriation is managed under Vote Revenue using forecasts developed by MBIE and that we are separately seeking approval from the Minister of Finance and the Minister of Science, Innovation and Technology for changes to this appropriation (IR2026/032 refers).

Noted Noted

(g) **agree** that all proposed changes to appropriations for 2025/26, covered by the recommendations above, be included in the 2025/26 Supplementary Estimates and that, in the interim, the increases be met from Imprest Supply.

Agreed/Not agreed Agreed/Not agreed

(h) **note** that the Table 2[2] Baseline Changes Report (attached – Appendix B) for Vote 20 sets out the forecast changes for Vote Revenue Crown (non-departmental) for the 2026 Preliminary Budget Economic and Fiscal Update.

Noted Noted

s 9(2)(a)

Nick Bradley
Enterprise Leader Finance Services - Chief Financial Officer
19 / 02 / 2026

Hon Nicola Willis
Minister of Finance
___/___/2026

Hon Simon Watts
Minister of Revenue
___/___/2026

[2] This is a technical report from Treasury's CFISnet system which sets out the quantum and authority for each change.

Background

11. Inland Revenue manages a number of non-tax items which require appropriations to cover the expenditure. Authority to spend is needed for appropriations established without a PLA. A full list of the non-departmental expenditure appropriations is attached in Appendix A.

12. We update the forecasts for these appropriations during the year to feed into the Government Budget and/or half year economic and fiscal updates. With each revision to forecasts we need joint Minister authority to change the forecast for appropriations without a PLA. If the changes are jointly approved, they will be included in the 2025/26 Supplementary Estimates and in the interim, the increases will be met from Imprest Supply.

13. Inland Revenue submitted forecasts for tax revenue and non-departmental appropriations for the Preliminary Budget Economic and Fiscal Update 2026 (Preliminary BEFU 2026 or Prelim BEFU 2026) to the Treasury on 16 February 2026. These forecasts are based on the Treasury's macroeconomic forecasts of 5 February 2026, and they incorporate actual results to December 2025. The forecasts include all Cabinet and joint Minister decisions that impact Vote Revenue made up to 16 February 2026.

14. This report seeks your joint approval for forecast changes to appropriations that are not established under a PLA. Forecast changes to appropriations established under PLA do not require approval and are also provided for your information. The body of the report briefly explains, at a high level, the main drivers of each change.

15. The preliminary forecasts are our 'best estimate' of the expected outturn as at 16 February 2026. These forecasts will be updated as part of the final Budget Economic and Fiscal Update (BEFU 2026) on 13 April 2026 and we will seek additional joint Ministerial approval for any changes required at that time. These changes may be material reflecting interim valuation updates from external valuers and the availability of more recent actual information from transactions that are cyclical in nature. Examples include 2026 student enrolment data, which can impact forecasts for final-year Fees Free payments, student loan impairment, and initial fair value write-downs for student loans. Final income tax filings and payments for the 2025 tax year may also impact tax debt impairment forecasts.

16. In addition, we have reviewed all annual non-departmental appropriations to ensure the upper limit is set at a level to enable us to appropriately manage expenses within our annual appropriations. In Budget 25 we sought Cabinet approval to set upper limits for annual appropriations (buffers) through a technical initiative. At this time, Cabinet delegated approval of future requests for buffers to joint Ministers. In this submission, we have included indicative buffers for 2025/26 for annual appropriations to help manage the risk of breaches of appropriation where the appropriation relates to impairment or volatile expenditure which is outside of Inland Revenue's control. We will confirm the buffer amounts as part of BEFU 2026 when final forecasts for 2025/26 are available. These buffers are for appropriation management purposes and are not recorded against allowances.

17. Appendix B sets out the forecast changes for Vote Revenue Crown (non-departmental) in a tabulated format. This table includes tax forecasts prepared by the Treasury.

Other matters

18. There was one Cabinet decision approved between 16 October 2026 (HYEFU 2025) and 16 February 2026 which impacts Vote Revenue non-departmental appropriations:

	$ million – increase / (decrease)					
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Reference**
Non-Departmental Other Expenses: Impairment of Debt and Debt Write-offs	(20.600)	(45.400)	(45.400)	(45.400)	(45.400)	Taxation (Use of Money Interest Rates) Amendment Regulations (No 2) 2025 CAB 25-MIN-0446, LEG-25-MIN-0251
Total Operating	**(20.600)**	**(45.400)**	**(45.400)**	**(45.400)**	**(45.400)**	

19. There were no decisions approved by joint Ministers between 16 October 2026 and 16 February 2026 that impact Vote Revenue non-departmental appropriations.

Changes to appropriations

Non-departmental benefits or related expense appropriations

20. The following table sets out the forecast changes for non-departmental benefits or related expenses that are not established under a PLA. The forecast changes require your joint approval.

	$ million – increase / (decrease)				
Non-departmental benefits or related expenses	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
KiwiSaver: Interest					
HYEFU 2025	4.000	4.000	4.000	4.000	4.000
Prelim BEFU 2026	4.500	4.500	4.500	5.000	5.000
Forecast change - inc/(dec)	0.500	0.500	0.500	1.000	1.000
KiwiSaver: Tax Credit, Contribution and Residual Entitlement					
HYEFU 2025	555.800	573.600	599.700	629.400	651.400
Prelim BEFU 2026	578.800	574.400	601.600	633.200	653.300
Forecast change - inc/(dec)	23.000	0.800	1.900	3.800	1.900
Paid Parental Leave Payments					
HYEFU 2025	740.000	770.000	805.000	845.000	885.000
Prelim BEFU 2026	770.000	785.000	825.000	865.000	910.000
Forecast change - inc/(dec)	30.00	15.000	20.000	20.000	25.000
Total forecast change – inc/(dec)	**53.500**	**16.300**	**22.400**	**24.800**	**27.900**

21. The KiwiSaver: Interest appropriation has increased by $3.5 million over the forecast period. The increase of $0.500 million in 2025/26 relates to a buffer for appropriation management purposes. The small increases in outyears allow for the potential that the increases to contribution rates in 2026 and 2028 may increase the contributions held by Inland Revenue before they are passed through to providers.

22. The KiwiSaver: Tax Credit, Contribution and Residual Entitlement appropriation covers government contributions to KiwiSaver schemes. The increase in 2025/26 relates to a buffer of $25 million for appropriation management purposes, partially offset by a small decrease to forecast reflecting a downward revision to nominal wage growth for 2025/26. This reduces contributions (to the extent that the weaker growth occurs among those contributing below the maximum qualifying amount). The modest upward revision in outyears is driven by stronger forecast nominal wage growth than expected at HYEFU, which lifts projected KiwiSaver contributions.

23. The forecast increase to the Paid Parental Leave Payments appropriation in 2025/26 reflects a stronger-than-expected outturn since HYEFU ($5 million) and a buffer of $25 million for appropriation management purposes. The higher outturn in 2025/26 flows into 2026/27 and outyears alongside a slightly larger forecast indexation adjustment. With stronger anticipated wage growth throughout the forecast period the ongoing impact of annual indexation is now also expected to be stronger.

Non-departmental other expenses

25. The following table sets out the forecast changes and Cabinet and joint Minister approvals for non-departmental other expenses that are not established under a PLA. The forecast changes require your joint approval.

	$ million – increase / (decrease)				
Non-departmental other expenses	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
COVID-19 Resurgence Support Payment					
HYEFU 2025	0.039	-	-	-	-
Prelim BEFU 2026	-	-	-	-	-
Joint Minister approval MBU 2026 – inc/(dec)	(0.039)	-	-	-	-
COVID-19 Support Payment					
HYEFU 2025	0.054	-	-	-	-
Prelim BEFU 2026	-	-	-	-	-
Joint Minister approval MBU 2026 – inc/(dec)	(0.054)	-	-	-	-
Cost of Living payment					
HYEFU 2025	0.009	-	-	-	-
Prelim BEFU 2026	-	-	-	-	-
Joint Minister approval MBU 2026 – inc/(dec)	(0.009)	-	-	-	-
Payments to Settle Residual Claims					
HYEFU 2025	-	-	-	-	-
Prelim BEFU 2026	0.102	-	-	-	-
Joint Minister approval MBU 2026 – inc/(dec)	0.102	-	-	-	-
Ex Gratia Payments					
HYEFU 2025	-	-	-	-	-
Prelim BEFU 2026	0.050	0.050	0.050	0.050	0.050
Joint Minister approval MBU 2026 – inc/(dec)	0.050	0.050	0.050	0.050	0.050
Initial Fair Value Write-Down Relating to Student Loans					
HYEFU 2025	782.000	848.000	900.000	944.000	981.000
Prelim BEFU 2026	844.000	882.000	922.000	958.000	991.000
Forecast change – inc/(dec)	62.000	34.000	22.000	14.000	10.000
Final-year Fees Free Payments					
HYEFU 2025	20.000	34.000	49.000	60.000	67.000
Prelim BEFU 2026	24.000	35.000	51.000	63.000	70.000
Forecast change – inc/(dec)	4.000	1.000	2.000	3.000	3.000
Impairment of Debt Relating to Student Loans					
HYEFU 2025	30.000	-	-	-	-
Prelim BEFU 2026	80.000	-	-	-	-
Forecast change – inc/(dec)	50.000	-	-	-	-

	$ million – increase / (decrease)				
Non-departmental other expenses	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Impairment of Debt and Debt Write-Offs Relating to Child Support					
HYEFU 2025	-	-	-	-	-
Prelim BEFU 2026	50.000	-	-	-	-
Forecast change – inc/(dec)	50.000	-	-	-	-
Impairment of Debt and Debt Write-Offs					
HYEFU 2025	1,850.000	1,430.000	1,440.000	1,410.000	1,380.000
Prelim BEFU 2026	1,829.400	1,384.600	1,394.600	1,364.600	1,334.600
Cabinet decisions – inc/(dec)	(20.600)	(45.400)	(45.400)	(45.400)	(45.400)
Impairment of Debt Relating to the SBCS					
HYEFU 2025	-	-	-	-	-
Prelim BEFU 2026	40.000	-	-	-	-
Forecast change – inc/(dec)	40.000	-	-	-	-
Total forecast change – inc/(dec)	**206.000**	**35.000**	**24.000**	**17.000**	**13.000**
Total Cabinet decisions – inc/(dec)	**(20.600)**	**(45.400)**	**(45.400)**	**(45.400)**	**(45.400)**
Total joint Minister approval MBU 2026 – inc/(dec)	**0.050**	**0.050**	**0.050**	**0.050**	**0.050**

26. As part of the 2025 October Baseline Update submission (2025 OBU), you jointly approved the creation of a new non-departmental appropriation for payments to settle residual claims (IR2025/372 refers). Once funded, this appropriation is intended to cover payments to settle residual claims after the original claim period has passed. We have sought approval for a fiscally neutral transfer of funding from the Cost of Living payment ($0.009 million), COVID-19 Support Payment ($0.054 million) and the COVID-19 Resurgence Support Payment ($0.039 million) appropriations to the Payments to Settle Residual Claims appropriation as part of the March Baseline Update (MBU) (IR2026/007 refers). The forecast for Preliminary BEFU 2026 reflects this transfer, which is still to be confirmed. As part of MBU, we also sought approval to close the Cost of Living payment, COVID-19 Support Payment and the COVID-19 Resurgence Support Payment after the transfer was completed and early confirmation of an in-principle expense transfer of the $0.102 million from 2025/26 to 2026/27.

27. As part of the 2025 OBU submission, you jointly approved the creation of a new non-departmental appropriation for ex gratia payments to customers (IR2025/372 refers). We have sought approval for a fiscally neutral transfer of $0.050 million per annum from Vote Revenue's departmental multi-category appropriation – Services for customers to the non-departmental Ex Gratia Payments appropriation as part of MBU (IR2026/007 refers). The forecast for Preliminary BEFU 2026 reflects this transfer, which is still to be confirmed.

28. The Initial Fair Value Write Down Relating to Student Loans appropriation has increased by $142 million over the forecast period due to:

    - $21 million higher write-downs from increased forecast new lending not related to final-year Fees Free (lending up $56 million);
    - $40 million higher write-downs from increased forecast final-year Fees Free lending, which is written down at 100% on lending (lending up $40 million);

- $31 million increase from changes to the write-down rate for lending not related to final-year Fees Free driven by discount rate movements; and
- $50 million added as a buffer to 2025/26 to reduce the risk of unappropriated expenditure given the expenditure is demand-driven.

29. The Final-year Fees Free Payments appropriation has increased by $4 million in 2025/26. This includes a $5 million buffer to help manage the appropriation as this is a new product and there could be volatility in the amount paid out offset by a small decrease in forecast payments of $1 million. The forecast payments have increased nominally in outyears to reflect revised payment forecasts from the Ministry of Education. These reflect a small increase in the forecast number of completions and an increase in tuition fees due to an increase in CPI. Applications for final-year Fees Free payments opened in January 2026 and forecasts may be updated through BEFU to reflect actual 2026 enrolment numbers and early experience of claims and payments.

30. We have not revised forecasts for the Impairment of Debt Relating to Student Loans, Impairment of Debt Relating to the SBCS and Impairment of Debt and Debt Write-Offs Relating to Child Support appropriations as part of Preliminary BEFU as the independent valuations to 31 December 2025 are not yet available. The increases of $50 million, $40 million and $50 million respectively in 2025/26 provide for buffers for appropriation management purposes. We will receive the interim valuations in time for BEFU. The updated information and rates in the valuation may have a significant impact on both the forecast and the buffer required. The final expense for these appropriations will not be confirmed until August 2026 when the final valuation is completed.

Impairment of Debt and Debt Write-Offs

31. The forecast for the Impairment of Debt and Debt Write-offs appropriation has not changed since HYEFU 2025, with the exception of the change as a result of the Taxation (Use of Money Interest Rates) Amendment Regulations (No 2). The forecast outturn for 2025/26 is $1,529.400 million and the appropriation upper limit is set at $1,829.400 million to allow a buffer for appropriation management purposes.

32. The overdue tax debt balance at December 2025 is below the HYEFU 2025 forecast. This in part reflects our additional compliance activity and is expected to flow through to the revised debt forecast at 30 June 2026. However, it is too early to assess the extent to which this movement will impact on the associated level of impairment.

33. In addition, the external debt valuation at 31 December is not yet available and the forecast for impairment therefore relies on the external valuation of tax debt as at 30 June 2025. We have therefore held the forecast constant with HYEFU 2025 until both the interim valuation and payment data for the February due dates are available. The updated debt balances and impairment rates from the valuation may have a significant impact on the forecast, which will be updated at BEFU.

34. The final expense for 2025/26 will not be confirmed until August 2026 after completion of the final valuation for the year.

Non-departmental benefits or related expenses - PLA

35. The following table sets out the forecast changes for non-departmental benefits or related expenses which are established under a PLA.

	$ million – increase / (decrease)				
Non-departmental benefits or related expenses - PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Best Start Tax Credit *					
HYEFU 2025	326.000	287.000	272.000	269.000	278.000
Prelim BEFU 2026	327.000	286.000	271.000	270.000	278.000
Forecast change - inc/(dec)	1.000	(1.000)	(1.000)	1.000	-
Child Support Payments					
HYEFU 2025	435.000	441.000	442.000	447.000	453.000
Prelim BEFU 2026	408.000	407.000	403.000	404.000	405.000
Forecast change - inc/(dec)	(27.000)	(34.000)	(39.000)	(43.000)	(48.000)
FamilyBoost Tax Credit					
HYEFU 2025	146.000	168.000	166.000	163.000	163.000
Prelim BEFU 2026	139.000	168.000	166.000	163.000	163.000
Forecast change - inc/(dec)	(7.000)	-	-	-	-
Family Tax Credit *					
HYEFU 2025	2,449.000	2,599.000	2,578.000	2,595.000	2,738.000
Prelim BEFU 2026	2,449.000	2,585.000	2,579.000	2,574.000	2,691.000
Forecast change - inc/(dec)	-	(14.000)	1.000	(21.000)	(47.000)
In-Work Tax Credit *					
HYEFU 2025	573.000	591.000	582.000	570.000	577.000
Prelim BEFU 2026	570.000	585.000	574.000	564.000	566.000
Forecast change - inc/(dec)	(3.000)	(6.000)	(8.000)	(6.000)	(11.000)
Minimum Family Tax Credit *					
HYEFU 2025	8.300	7.900	7.400	7.200	7.000
Prelim BEFU 2026	8.800	8.400	7.900	7.700	7.500
Forecast change - inc/(dec)	0.500	0.500	0.500	0.500	0.500
Total forecast change – inc/(dec)	**(35.500)**	**(54.500)**	**(46.500)**	**(68.500)**	**(105.500)**

* Working for Families Tax Credits

36. The Best Start Tax Credit appropriation forecast has been rephased, with only immaterial adjustments made to align expenditure with the expected timing of payments. Across the forecast period, the rephasing is fiscally neutral.

37. The forecasts for child support payments to custodial parents have been reduced by $191 million across the forecast period, reflecting a continued forecast fall in the number of cases managed by Inland Revenue, reducing both collections and amounts forwarded to receiving parents. This decline is larger than assumed in each year of the HYEFU forecasts.

38. The forecast for the FamilyBoost tax credit has decreased by $7 million in 2025/26 reflecting lower actual year-to-date expenditure than forecast at HYEFU 2025. As timing of claim activity is still being established it is unclear if this will continue into the remaining months of 2025/26 and outyears and forecasts have therefore remained unchanged.

39. The forecast for family tax credit (FTC) has decreased by $81 million over the forecast period. The revised forecast wage growth for 2026/27 has been revised up from 1.6% at HYEFU to 2.3%, which increases FTC abatement and reduces forecast expenditure. Income growth has also been revised up across all outyears, which further increases FTC abatement and lowers entitlements over time. This is partly offset by a higher April 2029 CPI indexation adjustment (7.16% compared with 6.71% at HYEFU25), and a modelling change to better calibrate to annual MSD payment frequencies, which particularly boosts the 2027/28 forecasts.

40. The forecast for in-work tax credit (IWTC) has decreased by $34 million over the forecast period. As with FTC, stronger income growth across the forecast period (relative to HYEFU) further increases IWTC abatement and reduces forecast expenditure.

41. The forecast for minimum family tax credit (MFTC) has increased by $2.5 million over the forecast period. The small increase for 2025/26 reflects a modelling adjustment for expected variability during the final-quarter square-up processes which impacts each year throughout the forecast period.

Non-departmental borrowing expenses - PLA

42. The following table sets out the forecasts for non-departmental borrowing expenses that are established under a PLA.

	$ million – increase / (decrease)				
Non-departmental borrowing expenses - PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Environmental Restoration Account Interest					
HYEFU 2025	4.100	4.100	4.100	4.100	4.100
Prelim BEFU 2026	4.200	4.200	4.200	4.200	4.200
Forecast change - inc/(dec)	0.100	0.100	0.100	0.100	0.100
Income Equalisation Interest					
HYEFU 2025	7.000	6.000	6.000	6.000	6.000
Prelim BEFU 2026	7.000	6.000	6.000	6.000	6.000
Forecast change - inc/(dec)	-	-	-	-	-
Total forecast change - inc/(dec)	**0.100**	**0.100**	**0.100**	**0.100**	**0.100**

43. The environmental restoration account and income equalisation account allow for timing changes for tax on qualifying income or expenditure and usage of both accounts is demand driven.

44. For the Environmental Restoration Account Interest appropriation there is a minor increase in each year of the forecast period to ensure interest payments for the remainder of the year reflect recent monthly expenditure.

Non-departmental other expenses

45. The following table sets out the forecasts for non-departmental other expenses that are established under a PLA.

	$ million – increase / (decrease)				
Non-departmental other expenses - PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
KiwiSaver: Employee and Employer contributions					
HYEFU 2025	10,770.000	12,360.000	13,080.000	14,190.000	15,280.000
Prelim BEFU 2026	10,740.000	12,400.000	13,190.000	14,320.000	15,430.000
Forecast change - inc/(dec)	**(30.000)**	**40.000**	**110.000**	**130.000**	**150.000**

46. KiwiSaver employee and employer contributions to scheme providers have increased by $400 million over the forecast period. In 2025/26, the small downward revision reflects slightly lower actual pass-through amounts than forecast in HYEFU 2025. From 2026/27, the increase over the forecast period since HYEFU 2025 reflects an upwards revision in forecasts of nominal wage growth. KiwiSaver employee and employer contributions are a pass-through transaction and do not impact the operating balance.

Research and Development (R&D) Tax Incentive

47. The Science, Innovation and Technology: R&D Tax Incentive appropriation is managed under Vote Revenue using forecasts developed by the Ministry of Business, Innovation and Employment (MBIE). We are separately seeking approval from the Minister of Finance and the Minister of Science, Innovation and Technology (IR2026/032 refers) for forecast changes relating to this appropriation. The following changes are included for your information.

	$ million – increase / (decrease)				
Vote Revenue **Minister of Science, Innovation and Technology**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Other Expenses Science, Innovation and Technology: R&D Tax Incentive					
HYEFU 2025	630.742	713.000	765.000	820.000	876.000
Prelim BEFU 2026	631.742	715.000	770.000	824.000	879.000
Forecast change – inc/(dec)	**1.000**	**2.000**	**5.000**	**4.000**	**3.000**

48. The increases in the Preliminary BEFU 2026 forecasts are entirely driven by an increase in Treasury's estimate of gross domestic product (GDP) across the forecast period.

Consultation

49. We have consulted with the Treasury prior to this submission.

Appendix A

The forecasts cover the following non-departmental expenditure appropriations (with an asterisk identifying expenditure items that are established under a PLA):

Benefits or related expenses:

- Best Start Tax Credit*
- Child Support Payments*
- FamilyBoost Tax Credit *
- Family Tax Credit*
- In-Work Tax Credit*
- KiwiSaver: Interest
- KiwiSaver: Tax Credit, Contribution and Residual Entitlement
- Minimum Family Tax Credit*
- Paid Parental Leave Payments

Borrowing expenses:

- Environmental Restoration Account Interest*
- Income Equalisation Interest*

Other expenses:

- Payments to Settle Residual Claims
- Ex Gratia Payments
- Cost of Living payment
- COVID-19 Resurgence Support Payment
- COVID-19 Support Payment
- Final-year Fees Free Payments
- Initial Fair Value Write-Down Relating to Student Loans
- Impairment of Debt and Debt Write-Offs
- KiwiSaver: Employee and Employer Contributions*
- Science, Innovation and Technology: R&D Tax Incentive
- Impairment of Debt and Debt Write-Offs Relating to Child Support
- Impairment of Debt Relating to Student Loans
- Impairment of Debt Relating to the SBCS

Appendix B – Table 2 report for Vote Revenue non-departmental appropriations

The attached Table 2 Baseline Changes Report sets out the forecast changes for Vote Revenue Crown (non-departmental) since HYEFU 2025 in a tabulated format. The table includes tax forecasts prepared by the Treasury.

The Table 2 Baseline Changes Report attached is for:

- Prelim BEFU 2026 - final forecasts.

Table 2: Baseline Changes Report, 2025/26 MBU, Vote 20 - 0: IRD Crown - Revenue (IRD-Crown).

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Benefits or Related Expenses								
Best Start Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Best Start Tax Credit	Fcst Adj	1,000	(1,000)	(1,000)	1,000	-	CO (18) 2	On going
Child Support Payments (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Child Support Payments	Fcst Adj	(27,000)	(34,000)	(39,000)	(43,000)	(48,000)	CO (18) 2	On going
Family Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Family Tax Credit	Fcst Adj	-	(14,000)	1,000	(21,000)	(47,000)	CO (18) 2	On going
FamilyBoost Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting FamilyBoost Tax Credit	Fcst Adj	(7,000)	-	-	-	-	CO (18) 2	On going
In-Work Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting In-Work Tax Credit	Fcst Adj	(3,000)	(6,000)	(8,000)	(6,000)	(11,000)	CO (18) 2	On going
KiwiSaver: Interest								
Non-Dept Annual Appropriation								
Buffers on Impairment and Demand-Driven Appropriations	Fcst Adj	500	-	-	-	-	CO (18) 2	On going
Cumulative forecasting changes impacting KiwiSaver: Interest	Fcst Adj	-	500	500	1,000	1,000	CO (18) 2	On going
KiwiSaver: Tax Credit, Contribution and Residual Entitlement								
Non-Dept Annual Appropriation								
Buffers on Impairment and Demand-Driven Appropriations	Fcst Adj	25,000	-	-	-	-	CO (18) 2	On going
Cumulative forecasting changes impacting KiwiSaver: Tax Credit, Contribution and Residual Entitlement	Fcst Adj	(2,000)	800	1,900	3,800	1,900	CO (18) 2	On going
Minimum Family Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Minimum Family Tax Credit	Fcst Adj	500	500	500	500	500	CO (18) 2	On going
Paid Parental Leave Payments								

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Non-Dept Annual Appropriation								
Buffers on Impairment and Demand-Driven Appropriations	Fcst Adj	25,000	-	-	-	-	CO (18) 2	On going
Cumulative forecasting changes impacting Paid Parental Leave Payments	Fcst Adj	5,000	15,000	20,000	20,000	25,000	CO (18) 2	On going
Total changes - Benefits or Related Expenses		**18,000**	**(38,200)**	**(24,100)**	**(43,700)**	**(77,600)**		
Non-Departmental Borrowing Expenses								
Environmental Restoration Account Interest (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Environmental Restoration Account Interest	Fcst Adj	100	100	100	100	100	CO (18) 2	On going
Total changes - Non-Departmental Borrowing Expenses		**100**	**100**	**100**	**100**	**100**		
Non-Departmental Other Expenses								
Cost of Living payment								
Non-Dept Annual Appropriation								
Fiscally neutral adjustment to fund the new non-departmental Payments to Settle Residual Claims appropriation	FNA	(9)	-	-	-	-	CO (18) 2	On going
COVID-19 Resurgence Support Payment								
Non-Dept Annual Appropriation								
Fiscally neutral adjustment to fund the new non-departmental Payments to Settle Residual Claims appropriation	FNA	(39)	-	-	-	-	CO (18) 2	On going
COVID-19 Support Payment								
Non-Dept Annual Appropriation								
Fiscally neutral adjustment to fund the new non-departmental Payments to Settle Residual Claims appropriation	FNA	(54)	-	-	-	-	CO (18) 2	On going
Ex Gratia Payments								
Non-Dept Annual Appropriation								
Fiscally neutral adjustment to fund the new non-departmental Ex Gratia Payments appropriation	FNA	50	50	50	50	50	CO (18) 2	On going
Final-year Fees Free Payments								
Non-Dept Annual Appropriation								
Buffers on Impairment and Demand-Driven Appropriations	Fcst Adj	5,000	-	-	-	-	CO (18) 2	On going
Cumulative forecasting changes impacting Final-year Fees Free Payments	Fcst Adj	(1,000)	1,000	2,000	3,000	3,000	CO (18) 2	On going
Impairment of Debt and Debt Write-Offs								
Non-Dept Annual Appropriation								
Taxation (Use of Money Interest Rates) Amendment Regulations (No 2) 2025	Cabinet	(20,600)	(45,400)	(45,400)	(45,400)	(45,400)	CAB-25-MIN-0446, LEG-25-MIN-0251	On going

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Impairment of Debt and Debt Write-Offs Relating to Child Support								
Non-Dept Annual Appropriation								
Buffers on Impairment and Demand-Driven Appropriations	Fcst Adj	50,000	-	-	-	-	CO (18) 2	On going
Impairment of Debt Relating to Student Loans								
Non-Dept Annual Appropriation								
Buffers on Impairment and Demand-Driven Appropriations	Fcst Adj	50,000	-	-	-	-	CO (18) 2	On going
Impairment of Debt Relating to the SBCS								
Non-Dept Annual Appropriation								
Buffers on Impairment and Demand-Driven Appropriations	Fcst Adj	40,000	-	-	-	-	CO (18) 2	On going
Initial Fair Value Write-Down Relating to Student Loans								
Non-Dept Annual Appropriation								
Buffers on Impairment and Demand-Driven Appropriations	Fcst Adj	50,000	-	-	-	-	CO (18) 2	On going
Cumulative forecasting changes impacting Initial Fair Value Write-Down Relating to Student Loans	Fcst Adj	12,000	34,000	22,000	14,000	10,000	CO (18) 2	On going
KiwiSaver: Employee and Employer Contributions (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting KiwiSaver: Employee and Employer Contributions	Fcst Adj	(30,000)	40,000	110,000	130,000	150,000	CO (18) 2	On going
Payments to Settle Residual Claims								
Non-Dept Annual Appropriation								
Fiscally neutral adjustment to fund the new non-departmental Payments to Settle Residual Claims appropriation	FNA	102	-	-	-	-	CO (18) 2	On going
Science, Innovation and Technology: R&D Tax Incentive								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting Science, Innovation and Technology: R&D Tax Incentive	Fcst Adj	1,000	2,000	5,000	4,000	3,000	CO (18) 2	On going
Total changes - Non-Departmental Other Expenses		**156,450**	**31,650**	**93,650**	**105,650**	**120,650**		
Tax Revenue								
Companies								
Non-Dept Revenue								
Cumulative forecasting changes impacting Companies	Fcst Adj	1,622,490	867,320	311,320	170,320	(167,680)	CO (18) 2	On going
Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations (No 3) 2025	Cabinet	210	280	280	280	280	CAB-25-MIN-0427, LEG-25-MIN-0236	On going

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Remedial tax issue	Other	(1,210,000)	(30,000)	(30,000)	(30,000)	(30,000)	IR2026/006 Approved by JM CO (18) 2	On going
Taxation (Use of Money Interest Rates) Amendment Regulations (No 2) 2025	Cabinet	(5,700)	(12,600)	(12,600)	(12,600)	(12,600)	CAB-25-MIN-0446, LEG-25-MIN-0251	On going
Fringe Benefit Tax								
Non-Dept Revenue								
Cumulative forecasting changes impacting Fringe Benefit Tax	Fcst Adj	20,750	14,000	18,000	12,000	13,000	CO (18) 2	On going
Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations (No 3) 2025	Cabinet	(750)	(1,000)	(1,000)	(1,000)	(1,000)	CAB-25-MIN-0427, LEG-25-MIN-0236	On going
Gaming Duties								
Non-Dept Revenue								
Cumulative forecasting changes impacting Gaming Duties	Fcst Adj	10,000	10,000	10,000	10,000	10,000	CO (18) 2	On going
Goods and Services Tax (IRD)								
Non-Dept Revenue								
Alignment of definition of employee	Other	(2,500)	(10,000)	(10,000)	(10,000)	(10,000)	IR2026/013 Approved by JM CO (18) 2	On going
Cumulative forecasting changes impacting Goods and Services Tax	Fcst Adj	447,000	665,300	647,300	530,300	414,300	CO (18) 2	On going
Taxation (Use of Money Interest Rates) Amendment Regulations (No 2) 2025	Cabinet	(12,500)	(27,300)	(27,300)	(27,300)	(27,300)	CAB-25-MIN-0446, LEG-25-MIN-0251	On going
Other Persons								
Non-Dept Revenue								
Alignment of definition of employee	Other	(2,750)	(11,000)	(11,000)	(11,000)	(11,000)	IR2026/013 Approved by JM CO (18) 2	On going
Cash basis person threshold increases to take effect from start of 2025-26 income year	Other	(200)	-	-	-	-	IR2025/488 Approved by JM CO (18) 2	On going
Clarify period required to qualify for alternative tax treatment for certain lump sum support payments	Other	200	200	200	200	200	IR2025/488 Approved by JM CO (18) 2	On going
Cumulative forecasting changes impacting Other Persons	Fcst Adj	470,400	36,200	136,200	67,200	(39,800)	CO (18) 2	On going
Employee share scheme deferral regime	Other	(50)	(200)	(200)	(200)	(200)	IR2025/488 Approved by JM CO (18) 2	On going
Foreign investment fund - introduction of the revenue account method	Other	-	(200)	(200)	(200)	(200)	IR2025/488 Approved by JM CO (18) 2	On going
Taxation (Use of Money Interest Rates) Amendment Regulations (No 2) 2025	Cabinet	(8,600)	(19,000)	(19,000)	(19,000)	(19,000)	CAB-25-MIN-0446, LEG-25-MIN-0251	On going
Source Deductions								
Non-Dept Revenue								
Cumulative forecasting changes impacting Source Deductions	Fcst Adj	274,600	690,100	1,028,100	1,305,100	1,816,100	CO (18) 2	On going
Taxation (Use of Money Interest Rates) Amendment Regulations (No 2) 2025	Cabinet	(4,600)	(10,100)	(10,100)	(10,100)	(10,100)	CAB-25-MIN-0446, LEG-25-MIN-0251	On going
Withholding Taxes								
Non-Dept Revenue								

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Cumulative forecasting changes impacting Withholding Taxes	Fcst Adj	(257,000)	93,000	601,000	744,000	631,000	CO (18) 2	On going
Total changes - Tax Revenue		**1,341,000**	**2,255,000**	**2,631,000**	**2,718,000**	**2,556,000**		
Non-Tax Revenue								
Interest on Impaired Student Loans								
Non-Dept Revenue								
Commissioner Discretion for Overseas Borrowers	Cabinet	(1)	(18)	(162)	(381)	(484)	CAB-25-MIN-0452, ECO-25-MIN-0202	2029/30
Cumulative forecasting changes impacting Interest on Impaired Student Loans	Fcst Adj	(13,999)	17,018	49,162	42,381	33,484	CO (18) 2	On going
Other non-tax revenue								
Non-Dept Revenue								
Cumulative forecasting changes impacting Other non-tax revenue	Fcst Adj	-	(25,000)	(37,000)	(48,000)	(48,000)	CO (18) 2	On going
Small Business Cashflow Scheme interest unwind								
Non-Dept Revenue								
Cumulative forecasting changes impacting Small Business Cashflow Scheme interest unwind	Fcst Adj	(1,412)	(44)	55	60	46	CO (18) 2	On going
Working for Families Tax Credit Interest and Penalties								
Non-Dept Revenue								
Cumulative forecasting changes impacting Working for Families Tax Credit Interest and Penalties	Fcst Adj	(2,000)	(4,000)	(4,000)	(5,000)	(6,000)	CO (18) 2	On going
Total changes - Non-Tax Revenue		**(17,412)**	**(12,044)**	**8,055**	**(10,940)**	**(20,954)**		
Capital Receipts								
Income Equalisation Reserve Account								
Non-Dept Revenue								
Cumulative forecasting changes impacting Income Equalisation Reserve Account	Fcst Adj	5,000	5,000	-	-	-	CO (18) 2	On going
Small Business Cashflow Scheme receipts								
Non-Dept Revenue								
Cumulative forecasting changes impacting Small Business Cashflow Scheme receipts	Fcst Adj	-	(2,000)	-	-	400	CO (18) 2	On going
Student Loans - Receipts								
Non-Dept Revenue								
Commissioner Discretion for Overseas Borrowers	Cabinet	101	1,298	3,938	2,972	(19)	CAB-25-MIN-0452, ECO-25-MIN-0202	2029/30
Cumulative forecasting changes impacting Student Loans - Receipts	Fcst Adj	8,899	6,702	7,062	7,028	19,019	CO (18) 2	On going
Total changes - Capital Receipts		**14,000**	**11,000**	**11,000**	**10,000**	**19,400**		

Classification Key

Short Name	Description	Reference
Cabinet	Cabinet policy decision	Approvals are sought in cabinet papers (refer to cabinet manual), with authority given via a cabinet minute. The authority for change should reference both supporting documents.
ECT	Expense and Capital Transfer	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding within an appropriation across financial years.
ECT ip	Expense and Capital Transfer in-principle	Defined in (Cabinet Office Circular). The portion of an ECT that can't be accurately quantified so the transfer amount has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Fcst Adj	Forecast Adjustments	Defined in (Cabinet Office Circular). Adjustments to the forecast expenditure of PLAs or where there is a pre-determined cost calcultion, or Crown Revenue.
FLoS	Front-Loading of Spending	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Bringing forward expenditure to create lasting cost savings.
FNA	Fiscally Neutral Adjustment	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding between appropriations within a financial year.
RoU	Retention of Underspends	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring underspends to the next financial year.
RoU 50%	Retention of Underspends @ 50%	Defined in CO Circular. Portion of an ROU can't accurately quantify so the transfer amount of 50% of an underspend has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Tech Adj	Technical adjustment	Defined in (Cabinet Office Circular). Technical accounting adjustments with no cash impact to the Crown, MYA spending profile changes, non-controversial appropriation title or scope changes.
SuppsJune	Offset MYA June vs Supps Difference	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the difference between the Supps Forecast and June Actual.
BudgetOY4	Offset MYA Budget OY4 Rollover	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the rollover of Budget OY4 into OBU OY4.
Return Sav	Return of savings to the Crown	Returning savings to the Crown is always encouraged. Departments can achieve this by constantly looking for efficiency gains through improvements in processes and technology.
Crwn Liab	Recognition of Existing Crown liability	Crown liabilities need to be recognised as soon as possible. These affect Non-Departmental Appropriations.
Other	Other changes outside the above criteria	There should be very few changes outside the above criteria, so if there are any they require extra scrutiny.

Inland Revenue
Te Tari Taake

Inland Revenue report: Output performance measures and targets for the 2026–27 financial year

Date:	25 February 2026	**Priority:**	Medium
Security level:	In confidence	**Report number:**	IR2026/027

Action sought

	Action sought	Deadline
Minister of Revenue	Discuss and agree the output performance measures and targets for 2026–27 to be included in the Budget 2026 documents for Vote Revenue.	6 March 2026

Contact for telephone discussion (if required)

Name	Position	Telephone
Mary Craig	Deputy Commissioner, Enterprise & Integrity Services	s 9(2)(a)
Teressa Dillon	Domain Lead, Performance and Reporting	

25 February 2026

Minister of Revenue

Output performance measures and targets for the 2026–27 financial year

Summary

1. This paper provides context and considerations for Inland Revenue's output performance measures and targets for the 2026–27 financial year for discussion with you. Following approval, the measures and targets will be included in the Estimates of Appropriations for the Government of New Zealand for the Year Ending June 2027.

Background

2. Inland Revenue (IR) uses a Performance Measurement Framework to monitor and assess progress in delivering services to New Zealanders.

3. IR's output measures form part of this broader framework and assess the delivery of services funded by Government under Vote Revenue. The measures support the assessment of whether services are delivering the intended results and contributing to IR's outcomes and delivering value for Government and New Zealanders.

4. Outcomes and the impact indicators are also monitored as part of the wider framework.

Performance measure review approach

5. IR reviews its performance measures annually to ensure they continue to reflect the services provided, focus on results that matter most and align with Government priorities.

6. Over the past five years, targets for nearly a quarter of our current 31 output measures have been increased to reflect improved performance and better productivity.

7. Our continuous improvement approach to our performance measures is reflected in the Office of the Auditor-General's 'very good' rating of IR's provision of service performance information and associated systems and controls. This is the highest rating possible, and it has been maintained at this level for many years.

8. The review process considers:

   - the need to maintain the consistency and comparability of performance information over time where possible, in line with external performance reporting standards (PBE FRS 48)
   - whether target levels remain appropriate, including opportunities to stretch targets in priority areas or where targets have not been met for two consecutive years
   - the operating context, including economic conditions and the need to manage cost pressures while continuing to deliver results.

Considerations for 2026–27 output measures

9. Our 2025–26 review involved a comprehensive update of output performance measures, including the introduction of three new measures, changes to nine measures (primarily to align with updated debt definitions) and the retirement of four measures.

10. To maintain consistency and comparability of performance measures over time, we recommend that no material changes are made to measures for 2026–27 and that the focus for this year's review on confirming that target levels remain appropriate. Our rationale for this recommendation is discussed in more detail below.

11. Some measures have intentionally been set with challenging targets, reflecting Government priorities to improve compliance and acknowledging the influence of external factors such as economic conditions on performance. These are 'stretch' targets that are set at the upper limit of historical results data we have achieved from previous years and that recognise that our achieving close to the same level of performance requires ongoing focus. Our 12 'stretch' measures and their 2025–26 targets are listed below. See page 7 for last year's results and year-end forecasts.

    Payment compliance

    - Percentage of tax payments made by customers on time (84%)
    - Percentage of tax payments made by customers on time by value (92%)
    - Percentage of tax payments made by customers within 6 months of the due date (95%)
    - Percentage of tax payments made by customers within 6 months of the due date by value (98%)
    - Percentage of New Zealand-based student loan customers who meet their obligations (95%)
    - Percentage of overseas-based student loan customers who meet their obligations (31-35%)
    - Percentage of collectable debt value over 2 years old (40% or less)
    - Cash collected for every debt dollar spent ($40.00)
    - Percentage of collectable tax debt value under an active repayment plan (improving value over baseline).

    Accuracy of reporting

    - The identified value of compliance activities over associated costs ($10.00).

    Filing compliance

    - Percentage of returns filed by customers on time (improve on previous year)
    - Percentage of returns filed within 6 months of the due date (improve on previous year).

12. Other measures have maintenance-based targets to provide flexibility in managing performance across channels and demand periods. These measures relate primarily to system-based activities such as processing returns and refunds, or to customer experience.

13. In some cases, IR may exceed target levels for certain customers or products to reduce future demand and follow up. Our 19 'maintain' measures and their 2025–26 targets are listed below. See pages 7 and 8 for last year's results and year-end forecasts.

    Helping and informing customers

    - Average speed to answer telephone calls (4 minutes and 30 seconds or less)
    - Percentage of calls answered (60%)
    - Percentage of correspondence completed within 10 working days (70%)
    - Percentage of customers who agree they found it easy to get the information they needed (70%)

- Percentage of rulings reports, adjudication reports and public items that meet the applicable purpose, logic, alternatives, consultation, and practicality standards (100%)
- Percentage of public items, adjudication cases, taxpayer rulings and short process rulings completed within agreed timeframes (90%).

Processing obligations and entitlements

- Percentage of social policy and tax registrations processed within 5 working days (85%)
- Percentage of income tax refund disbursements resulting from a return issued within 5 weeks (85%)
- Percentage of GST refund disbursements issued within 4 weeks (95%)
- Percentage of income tax returns finalised within 3 weeks (95%)
- Percentage of GST returns finalised within 3 weeks (98%)
- Percentage of KiwiSaver contributions passed to scheme providers within 2 days (98%)
- Percentage of child support assessments issued within 2 weeks (80%).

Supporting compliance

- Percentage of child support assessments paid on time (70%)
- Percentage of New Zealand liable parent child support debt cases resolved within 12 months (80%)
- Improved compliance following an audit intervention (evaluative assessment)
- Percentage of litigation judgments found in favour of the Commissioner (75%).

Policy advice

- The average quality score of papers assessed using the Policy Quality Framework (3.5 or more out of 5)
- The Minister's satisfaction with the policy advice services received (4 or more out of 5).

14. As shown in Appendix 1, none of the five output measures forecast to miss the 2025/26 year-end target will have missed their target in consecutive years.

15. Three measures currently have targets expressed as 'improve on previous year' or 'improving value over baseline'. To improve clarity and ease of interpretation, we suggest setting clear numerical targets for 2026–27. Supporting information and potential targets are provided in paragraphs 17 to 20.

16. Alongside our focus on delivering our priorities and achieving our performance measures, we have a continued focus on identifying internal efficiencies each year to manage compounding remuneration and inflationary pressures. This involves carefully balancing resources across the work programme whilst ensuring we deliver on Government expectations and priorities. Given this broader context, we consider that current target levels remain appropriate.

Potential targets for measures with 'improvement' targets

Returns filed by customers on time

17. The current target is 'improve on previous year'. A target of 85% is suggested for 2026–27 based on historical results and trend analysis – see the table below.

2022	2023	2024	2025	2026 year–end forecast
79.5%	82.9%	83.4%	85.4%	85.5%

Returns filed within 6 months of the due date

18. This is a new measure for 2025–26 with the target 'improve on the previous year'. A target of 91% is suggested for the 2026–27 year based on historical results and trend analysis – see the table below.

2022	2023	2024	2025	2026 Year–end forecast
91.4%	90.7%	90.9%	91.1%	91.0%

Collectable debt value under an active repayment plan

19. Repayment plans help customers get back on track and minimise the costs incurred by paying late. The measure is based on the value of collectable debt under a repayment plan with no missed payments compared with total collectable tax debt owed.

20. The current target for this measure is 'improving value over baseline'. A target of 22% is suggested for the 2026–27 year based on historical results and trend analysis – see the table below.

2022	2023	2024	2025	2026 Year–end forecast
19.0%	20.3%	21.7%	22.1%	21.6%

Payment compliance and debt measurement

21. Payment compliance is a key priority for IR to ensure we maximise the revenue available to the Government. As well as our output measures that focus on improving on-time payment compliance and managing late payments effectively and efficiently, we have a number of other outcome and impact performance measures within our performance measurement framework that monitor longer-term progress:

    - Total tax debt to tax revenue (an annual internationally comparable measure)
    - Cost of collecting $100 in tax revenue (annual measure)
    - Total value of on-time payments
    - Collectable debt to total tax debt
    - Repayment plan adherence
    - Tax morale customer sentiment (a survey-based measure).

Next steps

22. Officials are available to discuss IR's output measures and targets for 2026–27.

23. Subject to approval, the measures and targets will be included in the Estimates of Appropriations for the Government of New Zealand for the year ending June 2027. Draft Estimates documents will be submitted to your office as part of the suite of information produced to support Budget 2026.

24. The final Estimates documents will be submitted to you in April 2026 and will subsequently be sent to the Minister of Finance.

Recommended action

25. We recommend that you:

(a) **Consider** a discussion on Inland Revenue's output measures for 2026–27 with officials

Agreed/Not Agreed

(b) **Agree** to numerical targets for three existing measures (paragraphs 17 to 20)

Agreed/Not Agreed

(c) **Note** wider payment compliance measures that are monitored by Inland Revenue, reported in its Annual Report.

s 9(2)(a)

Mary Craig
Deputy Commissioner, Enterprise & Integrity Services, Inland Revenue

Hon Simon Watts
Minister of Revenue
/ /2026

Appendix 1—Services for Customers Multi-Category Appropriation output measures

Key	Achieved	Achieved (close to target)	Not achieved	No target (new measure in 25-26)	* Methodology differs between 2024–25 and 2025–26

	2024–25 Target	2024–25 Year-end Result	2025–26 Target	2025–26 Year-end Forecast
Measures with a stretch target				
Percentage of returns filed by customers on time	95%	96.4%*	Improve on previous year (85.4%)	85.5%
Percentage of tax payments made by customers on time	90%	88.2%*	84%	84.5%
Percentage of tax payments made by customers on time by value	94%	94.5%*	92%	93.5%
Cash collected for every debt dollar spent	$40.00	$53.08	$40.00	$35.48
Percentage of New Zealand-based student loan customers who meet their obligations	New measure from 25-26	94.8%	95%	94.3%
Percentage of overseas-based student loan customers who meet their obligations	New measure from 25-26	31.1%	31-35%	31.6%
Percentage of collectable debt value over 2 years old	40% or less	39.95%	40% or less	42.0%
Percentage of returns filed within 6 months of the due date	New measure from 25-26	91.1%	Improve on previous year (91.1%)	93.1%
Percentage of tax payments made by customers within 6 months of the due date	New measure from 25-26	94.9%	95%	95.1%
Percentage of tax payments made by customers within 6 months of the due date by value	New measure from 25-26	97.6%	98%	97.7%
Percentage of collectable tax debt value under an active repayment plan	Improving value over baseline (13.7%)	14.4%* (total tax debt)	Improving value over baseline (22.1%)	21.6%
The identified value of compliance activities over associated costs	$10.00	$11.81	$10.00	$12.00
Measures with a maintenance target				
Percentage of customers who agree they found it easy to get the information they needed	70%	74%	70%	72%
Average speed to answer telephone calls	4 mins 30 secs or less	3:00	4 mins 30 secs or less	3:17
Percentage of calls answered	60%	74.5%	60%	68.8%
Percentage of correspondence completed within 10 working days	70%	77.9%	70%	70.7%
Percentage of rulings reports, adjudication reports and public items that meet the applicable purpose, logic, alternatives, consultation, and practicality standards	100%	100%	100%	100%
Percentage of public items, adjudication cases, taxpayer rulings and short process rulings completed within agreed timeframes	90%	96.9%	90%	96.2%
Percentage of social policy and tax registrations processed within 5 working days	85%	89.9%	85%	85.8%
Percentage of income tax refund disbursements resulting from a return issued within 5 weeks	85%	92.0%	85%	91.6%
Percentage of GST refund disbursements issued within 4 weeks	95%	97.7%	95%	97.9%

	2024–25 Target	2024–25 Year-end Result	2025–26 Target	2025–26 Year-end Forecast
Percentage of income tax returns finalised within 3 weeks	95%	99.8%	95%	99.3%
Percentage of GST returns finalised within 3 weeks	98%	99.95%	98%	99.95%
Percentage of KiwiSaver contributions passed to scheme providers within 2 days	98%	99.1%	98%	98.7%
Percentage of child support assessments issued within 2 weeks	80%	88.0%	80%	88.8%
Percentage of child support assessments paid on time	70%	75.8%	70%	76.3%
Percentage of New Zealand liable parent child support debt cases resolved within 12 months	80%	84.3%	80%	85.3%
Improved compliance following an audit intervention	New measure from 25-26	N/A	Evaluative assessment	N/A
Percentage of litigation judgments found in favour of the Commissioner.	75%	85.2%	75%	Achieve
The average quality score of papers assessed using the Policy Quality Framework	3.5 or more out of 5	4.0	3.5 or more out of 5	N/A
The Minister's satisfaction with the policy advice services received	4 or more out of 5	4.0	4 or more out of 5	N/A

Inland Revenue report

Inland Revenue
Te Tari Taake

Vote Revenue: 2026 Budget Economic and Fiscal Update for the Research and Development Tax Incentive appropriation

Date	16 April 2026	**Priority**	High
Security level	Budget sensitive	**Report number**	IR2026/070

Action sought		**Deadline**
Minister of Finance	**Approve** recommendations	30 April 2026
Minister of Science, Innovation and Technology	**Approve** recommendations **Refer** report to the Minister of Finance	22 April 2026
Minister of Revenue	**Note** for your information	

Purpose
This report seeks your approval for forecast changes to the Research and Development Tax Incentive (RDTI) appropriation as part of the 2026 Budget Economic and Fiscal Update and asks you to refer the report to the Minister of Finance for her approval.

Contact for phone discussion, if required			
Name	**Position**	**Phone number**	**First contact**
Fergus Welsh	Chief Financial Officer	s 9(2)(a)	☐
Rachel Parker	Domain Lead Finance		✓

Vote Revenue: 2026 Budget Economic and Fiscal Update for the Research and Development Tax Incentive appropriation

Executive summary

1. This report seeks the Ministers of Finance and Science, Innovation and Technology (joint ministers) approval to the proposed forecast changes to the Research and Development Tax Incentive (RDTI) appropriation and outyear baselines to be included in the 2026 Budget Economic and Fiscal Update (BEFU 2026). It also advises you of the potential impact on the appropriation and outyear baselines arising from the proposed Budget 2026 initiative, should this be approved by Cabinet.

Background

2. The Research and Development Tax Incentive (RDTI) is a mechanism for supporting business investment in research and development (R&D) through the New Zealand tax system. Introduced in 2019, the RDTI provides a 15 percent tax credit for qualifying expenditure on eligible R&D activities, with the objective of increasing the level of R&D undertaken in New Zealand. The credit can be used to reduce the amount of tax a business has to pay and, for businesses in tax loss or low profit positions, a portion of the credit can be refunded in cash. In the most recent income year for which we have data, the RDTI was claimed by over 1000 businesses.
3. The RDTI appropriation is managed under Vote Revenue using forecasts developed by the Ministry of Business, Innovation and Employment (MBIE). The Minister of Science, Innovation and Technology is the appropriation minister for this appropriation.

Revised Forecasts

4. The RDTI forecast was previously updated on 16 February 2026 as part of March Baseline Update (MBU 2026) and approved by joint Ministers (refer Appendix 1, IR2026/032). Inland Revenue submitted a revised forecast to Treasury on 13 April 2026 as part of BEFU 2026, and changes in this report therefore reflect movements between MBU 2026 and BEFU 2026.
5. The forecasts are based on MBIE's RDTI fiscal-cost forecast, which extends to 2029/30. They use Treasury's BEFU 2026 macroeconomic assumptions for nominal Gross Domestic Product (GDP) as at 1 April 2026 and the 2024 R&D Survey results released by Stats NZ on 23 April 2025.
6. Any changes to the appropriation and outyear baselines due to forecast changes not impacted by new policy decisions, such as the above, require joint minister approval, being the Minister of Finance and the Minister of Science, Innovation and Technology.
7. Accordingly, we seek your agreement to the following changes to the updated forecast, which show a small reduction in the fiscal costs in the short term, followed by a minor increase from 2028/29 onwards, totalling a net $10 million decrease across the forecast period, driven by changes to Treasury's 2025/26 GDP assumptions, as follows:

	$million - increase/(decrease)				
Vote Revenue **Minister of Science, Innovation and Technology**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-departmental Other Expenses: Science, Innovation and Technology: R&D Tax Incentive	(6.000)	(10.000)	(3.000)	3.000	6.000
Total Operating	**(6.000)**	**(10.000)**	**(3.000)**	**3.000**	**6.000**

Other Matters

Cabinet decisions and the impact of proposed Budget 2026 initiatives

8. There have been no Cabinet or joint Ministers' decisions affecting the appropriation or outyear baselines since 16 February 2026.

9. However, in addition to the forecast adjustment above, as agreed with the Treasury, we have included the proposed Budget 2026 initiative in the final Science, Innovation and Technology: R&D Tax Incentive appropriation and outyear baselines in the 13 April submission revised forecasts. The initiative would reduce the non-administrative expenditure cap from $25 million to $3 million, relax mining exclusions, allow Commissioner discretion for minor errors or exceptional circumstances, and introduce in-year payments.

10. In this report we are not seeking Joint Ministers' agreement to the Budget 2026 baseline changes, as the initiative remains subject to final Cabinet decisions as part of the Budget 2026 package. However, if approved, the initiative would have the following impacts on appropriations and outyear baselines:

	$ million increase/(decrease)				
Vote Revenue **Minister of Science, Innovation and Technology**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Out-years**
Non-departmental Other Expenses Science, Innovation and Technology: R&D tax Incentive	-	(1.300)	(26.150)	(27.400)	(32.400)

11. The appropriation for 2025/26 and outyear baselines will be amended as necessary to reflect any updated decisions as a result of Cabinet's consideration of the Budget package, once these final decisions are made.

12. Subject to your joint approval of the forecasting adjustment referred to in paragraph 7 above, and Cabinet approval for the Budget 26 initiative, the final appropriated amounts the Science, Innovation and Technology R&D tax incentive for 2025/26 and outyears will be:

	$ million				
Vote Revenue **Minister of Science, Innovation and Technology**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-departmental Other Expenses: Science, Innovation and Technology: R&D tax Incentive					
MBU 2026	631.742	715.000	770.000	824.000	879.000
BEFU 2026	625.742	703.700	740.850	799.600	852.600
Total change – inc/(dec)	**(6.000)**	**(11.300)**	**(29.150)**	**(24.400)**	**(26.400)**
Forecast change – inc/(dec)	**(6.000)**	**(10.000)**	**(3.000)**	**3.000**	**6.000**
Pending Cabinet decision – inc/(dec)	**-**	**(1.300)**	**(26.150)**	**(27.400)**	**(32.400)**

Budget 2026 Estimates documentation

13. The Minister of Science, Innovation and Technology is responsible for RDTI, but it is appropriated under Vote Revenue. As part of the Budget 2026 process, the Minister of Revenue will sign off the Vote Revenue Estimates documentation on behalf of the Minister of Science, Innovation and Technology.

Consultation

14. The Treasury and Ministry of Business, Innovation and Employment have been consulted on this report.

Recommendations

We recommend that you:

1 **Note** that the baselines for the Research and Development Tax Incentive between 2025/26 to 2029/30 have a net decrease of $10.000 million across the forecast period as a result of the changes in Treasury's estimate of GDP for 2025/26.

Noted Noted

2 **Approve** the following forecast changes to the Vote Revenue Science, Innovation and Technology: R&D Tax Incentive appropriation, with a corresponding impact on the operating balance and net core Crown debt:

	$m - increase/(decrease)				
Vote Revenue **Minister of Science, Innovation and Technology**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-departmental Other Expenses: Science, Innovation and Technology: R&D tax Incentive	(6.000)	(10.000)	(3.000)	3.000	6.000
Total Operating	**(6.000)**	**(10.000)**	**(3.000)**	**3.000**	**6.000**

Approved/Not approved Approved/Not approved

3 **Agree** that the proposed change to appropriations for 2025/26, as shown in recommendation 2 above, be included in the 2025/26 Supplementary Estimates.

Agreed/Not Agreed Agreed/Not Agreed

4 **Note** a new Budget initiative "Research and Development Tax Incentive Amendments" is currently being considered by Cabinet as part of the Budget 2026 package and that the expected financial implications of this decision have been included in BEFU 2026 and will be amended if required after the Cabinet decision on the Budget 2026 package.

Noted Noted

s 9(2)(a)

Fergus Welsh
Enterprise Leader – Chief Financial Officer
Finance | Inland Revenue
16/04/2026

Hon Nicola Willis
Minister of Finance
…../……/2026

Hon Penny Simmonds
Minister of Science, Innovation and Technology
…../…../2026

[BUDGET SENSITIVE]

Inland Revenue report

Vote Revenue: 2026 Budget Economic and Fiscal Update for non-departmental expenditure appropriations

Date	20 April 2026	**Priority**	High
Security level	Budget sensitive	**Report number**	IR2026/077

Action sought		**Deadline**
Minister of Revenue	**Approve** recommendations **Refer** report to the Minister of Finance	28 April 2026
Minister of Finance	**Approve** recommendations	4 May 2026

Purpose
This report seeks your approval of forecast changes to non-permanent legislative authority Vote Revenue appropriations and outyear baselines for inclusion in the 2026 Budget Economic and Fiscal Update, and your agreement to refer it to the Minister of Finance for her approval.

Contact for phone discussion, if required

Name	**Position**	**Phone number**	**First contact**
Fergus Welsh	Enterprise Leader Finance (Chief Financial Officer)	s 9(2)(a)	✓
Rachel Parker	Domain Lead Finance		☐
Sandra Watson	Policy Lead Forecasting and Analysis		☐

Inland Revenue report

Vote Revenue: 2026 Budget Economic and Fiscal Update for non-departmental expenditure appropriations

Executive summary

1) This report seeks joint Ministers approval of the forecast changes to non-permanent legislative authority Vote Revenue appropriations and outyear baselines to be included in the 2026 Budget Economic and Fiscal Update (BEFU 2026).

2) It also advises you of forecast changes to permanent legislative authority (PLA) appropriations and Cabinet and joint Minister decisions since the preliminary Budget Economic and Fiscal Update 2026 (Preliminary BEFU), and the potential impacts of proposed Budget 2026 initiatives on appropriations and outyear baselines, if approved by Cabinet.

Background

3) Inland Revenue updates the forecasts for its appropriations during the year for inclusion in the Budget and half-year economic and fiscal updates. Each revision to forecasts for appropriations without permanent legislative authority (PLA) requires joint Minister authority (Ministers of Finance and Revenue).

4) Inland Revenue submitted updated forecasts for tax revenue and all non-departmental appropriations for BEFU 2026 to the Treasury on 13 April 2026. These forecasts reflect Treasury's updated macroeconomic assumptions as at 1 April 2026, actual results to February 2026 (with draft March updates where relevant), and all Cabinet and joint Minister decisions affecting Vote Revenue to 13 April 2026, and are compared against Preliminary BEFU forecasts.

5) This report explains forecast changes to appropriations since the Preliminary BEFU and seeks your joint approval for these changes to non-PLA appropriations. Forecast changes to appropriations established under a PLA do not require approval but are also provided for your information. All forecast changes will be included in the 2025/26 Supplementary Estimates of Appropriations and the 2026/27 Estimates of Appropriations as appropriate.

6) The updated forecasts, as submitted, incorporate forecasts for the following appropriation as well as revenue items (not covered in detail in this report), which have been prepared by other agencies:

   - The tax revenue forecast has been prepared by the Treasury.
   - The student loans lending forecast has been prepared by the Ministry of Social Development.

- The *Final-year Fees Free Payments* appropriation forecast, and the amount of annual student loan lending expected to be forgiven through final-year fees free settlements, have been prepared by the Ministry of Education.

- The forecast for the *Science, Innovation and Technology: R&D Tax Incentive* appropriation has been prepared by the Ministry of Business, Innovation and Employment (MBIE).

7) We sought approval for preliminary buffers (appropriation upper limits) for appropriations not established under a PLA as part of the Preliminary BEFU. We are seeking approval for updated buffers through BEFU 2026 for two appropriations (*Impairment of Debt Relating to Student Loans* and *Impairment of Debt and Debt Write-offs*) in relation to uncertainty caused by the ongoing conflict in the Middle East.

8) The *Science, Innovation and Technology: R&D Tax Incentive* appropriation is managed under Vote Revenue using forecasts developed by MBIE. We are separately seeking approval from the Minister of Finance and the Minister of Science, Innovation and Technology (IR2026/070 refers) for forecast changes relating to this appropriation. The final appropriation for 2025/26 and outyear baselines is included in Appendix A for your information.

Revised forecasts

Forecast changes to appropriations not established under a Permanent Legislative Authority

9) Explanations for forecast and appropriation changes across the forecast period since Preliminary BEFU for Non-Departmental non-PLA appropriations which require joint Ministers' approval are as follows:

Non-Departmental Other Expenses

	$ million – increase / (decrease)					
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total Forecast Period**
Non-Departmental Other Expenses:						
(a) Impairment of Debt and Debt Write-Offs						
Forecast change	20.600	30.400	32.400	8.400	13.400	105.200
Buffer change	150.000	-	-	-	-	150.000
Total change for approval	170.600	30.400	32.400	8.400	13.400	255.200
(b) Impairment of Debt and Debt Write-Offs Relating to Child Support	-	5.000	5.000	5.000	5.000	20.000
(c) Impairment of Debt Relating to Student Loans						
Forecast change	(30.000)	-	-	-	-	(30.000)
Buffer change	195.000	-	-	-	-	195.000
Total change for approval	165.000	-	-	-	-	165.000
(d) Initial Fair Value Write-Down Relating to Student Loans	(18.000)	6.950	30.470	32.340	32.355	84.115
(e) Final-year Fees Free Payments	(11.000)	-	0.160	(0.339)	(0.608)	(11.787)
Total forecast and buffer changes	**306.600**	**42.350**	**68.030**	**45.401**	**50.147**	**512.528**

a) The requested appropriation for the *Impairment of Debt and Debt Write-offs* appropriation for 2025/26 has increased by $170.600 million. $20.600 million of this relates to a forecast increase to expenditure and $150.000 million is related to an increase to the buffer (upper expenditure limit).

The forecast increase is driven by updated assumptions from the interim tax debt valuation to 31 December 2025 which has been received from our external valuer since Preliminary BEFU. The valuation has also increased forecast expenditure across the outyears by $84.600.

The impairment forecast is largely dependent on changes in the debt forecast. Actual overdue debt balances are close to the Preliminary BEFU forecast and on-time payment

compliance has improved (particularly for GST and PAYE) compared to the same time last year. However, consistent with previous years, significant growth in debt is expected before the end of the year as the result of key due dates in the last quarter of the financial year. We have therefore retained the preliminary BEFU debt forecast reflecting these events as well as the impacts of our additional compliance activity.

Additionally for 2025/26 only, we are seeking approval to increase the buffer by $150 million, from $300 million to $450 million, due to the current uncertainty arising from the conflict in the Middle East. The buffer is for appropriation management purposes only and does not impact on allowances. The proposed increased buffer allows for possible increases to discount rates (both higher risk-free & risk premium rates), and any potential growth in customer tax debt as a result of any flow-on impact to a customer's ability to pay arising from the conflict.

The actual expense for 2025/26 will not be confirmed until August 2026 after completion of the final valuation for the year. This is consistent with usual reporting timelines.

b) The forecast for the *Impairment of Debt and Debt Write-offs Relating to Child Support* appropriation has increased by $20 million over the forecast period. This increase reflects the reclassification of custodial parent debt owing to Inland Revenue from refundables to receivables, which will be subject to annual impairment. For the current year, the impairment expense is offset by a small forecast gain in impairment of other child support receivables.

c) The requested appropriation for the *Impairment of Debt Relating to Student Loans* has increased by $165 million for 2025/26. This reflects a forecast decrease in impairment of $30 million reflecting updated assumptions for the forecast student loan valuation at 30 June 2026. These assumptions are as at 31 December 2025 and are the best information available to inform the impairment forecast. However, since the forecast valuation there is increased risk that actual experience in the second half of the year will differ from forecast due to the current conflict in the Middle East. We are therefore seeking a $195 million increase to the buffer for 2025/26 (from $50 million, to $245 million) to help mitigate any possible adverse impacts. The buffer is for appropriation management purposes and does not impact on allowances.

d) The forecast for the *Initial Fair Value Write-Down Relating to Student Loans* appropriation has increased by $84.115 million over the forecast period. This increase largely reflects approximately $77 million of additional write-downs arising from higher forecast new lending since Preliminary BEFU that is not related to Final-year Fees Free (new lending excluding Final-year Fees Free is up $215 million). The remaining increase of approximately $7 million reflects higher forecast Final-year Fees Free lending, which is fully written down at the point of lending.

e) The forecast for the *Final-year Fees Free Payments* appropriation has decreased by $11.787 million over the forecast period, the reduction is partly due to slower receipt of applications for 2025/26 and reflects updated forecast expectations of lower cash reimbursements going forward.

Non-Departmental Benefits or Related expenses

	$ million – increase / (decrease)					
Vote Revenue **Minister of Revenue**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total Forecast Period**
Non-Departmental Benefits or Related expenses:						
f) KiwiSaver: Tax Credit, Contribution and Residual Entitlement	2.000	4.200	2.000	1.000	1.000	10.200
Total Forecast Change	**2.000**	**4.200**	**2.000**	**1.000**	**1.000**	**10.200**

f) The forecast increase of $10.200 million over the forecast period for the *KiwiSaver Tax Credit, Contribution and Residual Entitlement* appropriation is due to an uplift in employment and forecast nominal wage growth since the preliminary BEFU, which increases contributing members entitlements (up to the maximum entitlement). This increase was most significant in 2026/27, with wage growth slowing from 2027/28.

Forecast changes to appropriations under Permanent Legislative Appropriation

10) Inland Revenue also administers appropriations authorised under specific sections of the Public Finance Act 1989 in the form of PLAs. Explanations of movements in forecasts since Preliminary BEFU are provided below for Minister's information only and do not require your approval. The tables below reflect forecast changes unrelated to policy decisions.

Non-Departmental Benefits or Related Expenses

	$ million – increase / (decrease)					
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total Forecast Period**
Non-Departmental Benefits or Related expenses – PLA:						
a) Best Start Tax Credit*	-	(0.100)	3.600	10.600	(4.400)	9.700
b) Child Support Payments	2.000	1.000	1.000	-	-	4.000
c) FamilyBoost Tax Credit	1.000	-	-	-	-	1.000
d) Family Tax Credit *	-	0.200	39.000	124.800	(39.400)	124.600
e) In-Work Tax Credit *	(2.000)	(0.200)	18.400	30.400	2.300	48.900
Total Forecast Changes	**1.000**	**0.900**	**62.000**	**165.800**	**(41.500)**	**188.200**

* Working for Families Tax Credits

a) The *Best Start Tax Credit* appropriation forecast increased by $9.700 million over the forecast period. The forecasts in 2027/28 and 2028/29 were revised upward from the Preliminary BEFU forecast, due to CPI indexation being brought forward to 1 April 2028 (+5.69%), rather than 1 April 2029 (+7.19%) and being at a lower level than previously forecast. This reduction in indexation flows through to 2029/30.

b) The forecast for the *Child Support Payments* appropriation has increased by $4 million since Preliminary BEFU largely reflecting updated wage forecasts.

c) The forecast for the *FamilyBoost Tax Credit* appropriation has increased by $1 million in 2025/26 reflecting a minor adjustment to forecast based on actual year-to-date expenditure. As timing of claims following the last policy change is still being established, forecasts for the outyears are unchanged.

d) The forecast for the *Family Tax Credit* (FTC) appropriation has increased by $124.600 million over the forecast period. The CPI indexation is now expected a year earlier than at Preliminary BEFU increasing forecasts for 2027/28 and 2028/29. Forecasts decrease in 2029/30 relative to Preliminary BEFU as the earlier 2028 indexation at 5.69% is lower than was previously assumed (7.16%).

e) The forecast for the *In-Work Tax Credit* (IWTC) appropriation has increased by $48.900 million over the forecast period. IWTC is not indexed but is affected by the indexation of FTC as the two credits are abated together, with FTC abating first as incomes grow. This

means that IWTC is indirectly affected by indexation adjustments to FTC which now occur earlier, but at a lower rate of increase. This increases forecasts for 2027/28 and 2028/29, and the lower FTC rate dampens 2029/30 for IWTC relative to Preliminary BEFU assumptions.

Non-Departmental Borrowing Expenses

	$ million – increase / (decrease)					
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total Forecast Period**
Non-Departmental Borrowing Expenses – PLA:						
f) Income Equalisation Interest	-	2.000	2.000	2.000	2.000	8.000
Total Forecast Changes	-	**2.000**	**2.000**	**2.000**	**2.000**	**8.000**

f) The income equalisation account allows for timing changes for tax on qualifying income or expenditure and usage of the account is demand driven.

Non-Departmental Other Expenses

	$ million – increase / (decrease)					
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total Forecast Period**
Non-Departmental Other Expenses – PLA:						
g) KiwiSaver: Employee and Employer Contributions	(60.000)	(50.000)	(40.000)	(30.000)	(20.000)	(200.000)
Total Forecast Changes	**(60.000)**	**(50.000)**	**(40.000)**	**(30.000)**	**(20.000)**	**(200.000)**

g) The forecast for KiwiSaver employee and employer contributions has decreased by $200 million over the forecast period. The downward revision in 2025/26 reflects lower actual pass-through amounts than forecast at Preliminary BEFU, with flow-on impacts into 2026/27 and out-years, partly offset by higher nominal wage growth. As pass-through transactions, these contributions do not affect the operating balance.

Other decisions affecting the forecasts and appropriations

Cabinet and joint Minister decisions

11) The following decisions have been made between Preliminary BEFU 2026 and 13 April 2026 and are included in the final appropriation and baselines changes submitted for BEFU 2026;

Cabinet:

- Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2026 - CAB-26-MIN-0053, LEG-26-MIN-0029
- Changes to the Thin Capitalisation Settings for Infrastructure - CAB-26-MIN-0061, ECO-26-MIN-0020, and
- Increase to the In-Work Tax Credit – CAB-26-MIN-0086.

Joint Ministers:

- IR2026-012 GST and Bad Debt Deductions.

12) Furthermore, as agreed with the Treasury, the following proposed Budget 2026 initiatives were included in the final revenue forecasts and changes to appropriations submitted to the Treasury on 13 April 2026:
    - Company to Shareholder Loans - Taxation
    - Foreign Investment Funds - Tax Rule Reforms
    - Non-resident Contractors' Withholding Tax - Asset Leasing in Airline Industry
    - Donation Tax Credit Changes
    - Research and Development Tax Incentive Amendments
    - Thin Capitalisation Changes for Foreign-owned New Zealand Banking Groups
    - Non-resident Contractors' Withholding Tax – Modernisation
    - Working For Families - Family Scheme Income
    - Fringe Benefit Tax - Simplifying Motor Vehicle Rules
    - Charities and Not-For-Profits: Other Changes, and
    - Financial Arrangement Rules - Amendments to Support New Migrants.

13) We are not seeking Joint Ministers' agreement to the proposed Budget 2026 baseline changes in this report, as they remain subject to final Cabinet decisions. However as agreed with the Treasury, the BEFU forecasts incorporate the above forecasting changes, Cabinet and joint Minister decisions made between Preliminary BEFU and BEFU 2026 and the proposed Budget 2026 initiatives. These initiatives are included in Appendix A as "Pending Cabinet decisions" for your information only, to illustrate the potential impact on final appropriations and outyear baselines. Appropriations and baselines will be updated as required once Cabinet decisions are finalised.

14) Appendix B includes Table 2, the CFIS schedule detailing the changes to revenue and appropriations for Vote Revenue Crown (non-departmental) since Preliminary BEFU in a tabulated format for the 2025/26 Supplementary Estimates and the 2026 Budget Economic and Fiscal Update.

Consultation

15) We have consulted with the Treasury on this submission.

Next steps

16) Forecasts and appropriations may need to be updated following the Cabinet decisions on the Budget 2026 package. This will provide the final authority for spend for 2025/26 and the updated baselines for outyears.

Recommendations

We recommend that you:

1. **Note** the BEFU 2026 forecasts in this report incorporate actual results to February 2026, (with updates for draft March results where appropriate), are based on the Treasury's macroeconomic forecasts of 1 April 2026, and were submitted to the Treasury on 13 April 2026.

Noted Noted

2. **Approve** the following forecast changes to appropriations and increase to buffers for non-departmental other expenses that are not established under a PLA, with a corresponding impact on the operating balance and net core Crown debt:

	$ million – increase / (decrease)				
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-Departmental Other Expenses:					
Impairment of Debt and Debt Write-Offs	170.600	30.400	32.400	8.400	13.400
Impairment of Debt and Debt Write-Offs Relating to Child Support	-	5.000	5.000	5.000	5.000
Impairment of Debt Relating to Student Loans	165.000	-	-	-	-
Initial Fair Value Write-Down Relating to Student Loans	(18.000)	6.950	30.470	32.340	32.355
Final-year Fees Free Payments	(11.000)	-	0.160	(0.339)	(0.608)
Total Operating	**306.600**	**42.350**	**68.030**	**45.401**	**50.147**

Approved/Not Approved Approved/Not Approved

3. **Note** the forecast changes in 2025/26 in recommendation 2 above for the *Impairment of Debt and Debt Write-Offs* and *Impairment of Debt Relating to Student Loans* appropriations include increases to buffers of $150 million and $195 million respectively that impact operating balance but not budget allowances.

Noted Noted

4. **Approve** the following forecast changes to appropriations for non-departmental benefits or related expenses that are not established under a PLA, with a corresponding impact on the operating balance and net core Crown debt:

	$ million – increase / (decrease)				
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-Departmental Benefits or Related expenses:					
KiwiSaver: Tax Credit, Contribution and Residual Entitlement	2.000	4.200	2.000	1.000	1.000
Total Operating	**2.000**	**4.200**	**2.000**	**1.000**	**1.000**

Approved/Not Approved Approved/Not Approved

5. **Note** the forecast changes to non-departmental benefits or related expenses, non-departmental borrowing expenses, and non-departmental other expenses that are established under a PLA in paragraph 10 above.

Noted Noted

6. **Note** that the Table 2[1] Baseline Changes Report (attached – Appendix B) for Vote 20 sets out the forecast changes for Vote Revenue Crown (non-departmental) for the 2026 Budget Economic and Fiscal Update and 2025/26 Supplementary Estimates.

Noted Noted

[1] This is a technical report from Treasury's CFISnet system which sets out the quantum and authority for each change.

7. **Agree** that all proposed changes to appropriations for 2025/26, covered by the recommendations 2 and 4 above, be included in the 2025/26 Supplementary Estimates and that, in the interim, the increases be met from Imprest Supply.

Agree / Disagree	Agree / Disagree

s 9(2)(a)

Fergus Welsh

Enterprise Leader - Chief Financial Officer

Finance | Inland Revenue

20 April 2026

Hon Nicola Willis Minister of Finance / /2026	Hon Simon Watts Minister of Revenue / /2026

Appendix A

Overview of appropriations

17) The following tables show the final appropriation changes as submitted to the Treasury on 13 April 2026, and are included for your information. Explanations for forecast changes, and background on Cabinet and joint Ministers decisions and pending Budget 2026 initiatives are included in the main body of the report. As noted these are intended to illustrate the potential impact on final appropriations and outyear baselines, and appropriations and baselines will be updated as required once Cabinet decisions are finalised.

Non-Departmental Benefits or Related Expenses appropriations – non-PLA

	$ million				
Non-Departmental Benefits or Related Expenses – Non-PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
KiwiSaver: Interest					
Prelim BEFU 2026	4.500	4.500	4.500	5.000	5.000
Forecast change	-	-	-	-	-
Revised BEFU 2026	4.500	4.500	4.500	5.000	5.000
KiwiSaver: Tax Credit, Contribution and Residual Entitlement					
Prelim BEFU 2026	578.800	574.400	601.600	633.200	653.300
Forecast change	2.000	4.200	2.000	1.000	1.000
Revised BEFU 2026	580.800	578.600	603.600	634.200	654.300
Paid Parental Leave Payments					
Prelim BEFU 2026	770.000	785.000	825.000	865.000	910.000
Forecast change	-	-	-	-	-
Revised BEFU 2026	770.000	785.000	825.000	865.000	910.000
Total Non-departmental Benefits or Related Expenses – Non-PLA Revised BEFU 2026	**1,355.300**	**1,368.100**	**1,433.100**	**1,504.200**	**1,569.300**

Non-Departmental Benefits or Related Expenses - PLA

	$ million				
Non-Departmental Benefits or Related Expenses - PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Best Start Tax Credit *					
Prelim BEFU 2026	327.000	286.000	271.000	270.000	278.000
Forecast change	-	(0.100)	3.600	10.600	(4.400)
BEFU 2026 (Pre Budget 2026)	327.000	285.900	274.600	280.600	273.600
Pending Budget 2026 Initiatives	-	0.100	0.400	0.400	0.400
Revised BEFU 2026	327.000	286.000	275.000	281.000	274.000

	$ million				
Non-Departmental Benefits or Related Expenses - PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Child Support Payments					
Prelim BEFU 2026	408.000	407.000	403.000	404.000	405.000
Forecast change	2.000	1.000	1.000	-	-
Revised BEFU 2026	410.000	408.000	404.000	404.000	405.000
FamilyBoost Tax Credit					
Prelim BEFU 2026	139.000	168.000	166.000	163.000	163.000
Forecast change	1.000	-	-	-	-
Revised BEFU 2026	140.000	168.000	166.000	163.000	163.000
Family Tax Credit *					
Prelim BEFU 2026	2,449.000	2,585.000	2,579.000	2,574.000	2,691.000
Forecast change	-	0.200	39.000	124.800	(39.400)
BEFU 2026 (Pre Budget 2026)	2,449.000	2,585.200	2,618.000	2,698.800	2,651.600
Pending Budget 2026 Initiatives	-	0.800	3.000	3.200	3.400
Revised BEFU 2026	2,449.000	2,586.000	2,621.000	2,702.000	2,655.000
In-Work Tax Credit *					
Prelim BEFU 2026	570.000	585.000	574.000	564.000	566.000
Forecast change	(2.000)	(0.200)	18.400	30.400	2.300
Cabinet decisions	79.000	259.000	29.000	-	-
BEFU 2026 (Pre Budget 2026)	647.000	843.800	621.400	594.400	568.300
Pending Budget 2026 Initiatives	-	0.200	0.600	0.600	0.700
Revised BEFU 2026	647.000	844.000	622.000	595.000	569.000
Minimum Family Tax Credit *					
Prelim BEFU 2026	8.800	8.400	7.900	7.700	7.500
Forecast change	-	-	-	-	-
Revised BEFU 2026	8.800	8.400	7.900	7.700	7.500
Total Non-Departmental Benefits or Related Expenses - PLA Revised BEFU 2026	**3,981.800**	**4,300.400**	**4,095.900**	**4,152.700**	**4,073.500**

* Working for Families Tax Credits

Non-Departmental Borrowing Expenses - PLA

	$ million				
Non-Departmental Borrowing Expenses - PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Environmental Restoration Account Interest					
Prelim BEFU 2026	4.200	4.200	4.200	4.200	4.200
Forecast change	-	-	-	-	
Revised BEFU 2026	4.200	4.200	4.200	4.200	4.200
Income Equalisation Interest					
Prelim BEFU 2026	7.000	6.000	6.000	6.000	6.000
Forecast change	-	2.000	2.000	2.000	2.000
Revised BEFU 2026	7.000	8.000	8.000	8.000	8.000
Total Non-Departmental Borrowing Expenses - PLA Revised BEFU 2026	**11.200**	**12.200**	**12.200**	**12.200**	**12.200**

Non-Departmental Other Expenses – Non PLA

	$ million				
Non-Departmental Other Expenses – Non PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Payments to Settle Residual Claims					
Prelim BEFU 2026	0.102	-	-	-	-
Forecast change	-	-	-	-	-
Revised BEFU 2026	0.102	-	-	-	-
Ex Gratia Payments					
Prelim BEFU 2026	0.050	0.050	0.050	0.050	0.050
Forecast change	-	-	-	-	-
Revised BEFU 2026	0.050	0.050	0.050	0.050	0.050
Initial Fair Value Write-Down Relating to Student Loans					
Prelim BEFU 2026	844.000	882.000	922.000	958.000	991.000
Forecast change	(18.000)	6.950	30.470	32.340	32.355
BEFU 2026 (Pre Budget 2026)	826.000	888.950	952.470	990.340	1,023.355
Pending Budget 2026 Initiatives	-	20.050	25.530	26.660	27.645
Revised BEFU 2026	826.000	909.000	978.000	1,017.000	1,051.000
Final-year Fees Free Payments					
Prelim BEFU 2026	24.000	35.000	51.000	63.000	70.000
Forecast change	(11.000)	-	0.160	(0.339)	(0.608)
BEFU 2026 (Pre Budget 26)	13.000	35.000	51.160	62.661	69.392
Pending Budget 2026 Initiatives	-	-	0.840	2.339	2.608
Revised BEFU 2026	13.000	35.000	52.000	65.000	72.000
Impairment of Debt Relating to Student Loans					
Prelim BEFU 2026	80.000	-	-	-	-
Forecast change	(30.000)	-	-	-	-
Buffer change	195.000	-	-	-	-
Revised BEFU 2026	245.000	-	-	-	-

	$ million				
Non-Departmental Other Expenses – Non PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Impairment of Debt and Debt Write-offs Relating to Child Support					
Prelim BEFU 2026	50.000	-	-	-	-
Forecast change	-	5.000	5.000	5.000	5.000
Revised BEFU 2026	50.000	5.000	5.000	5.000	5.000
Impairment of Debt and Debt Write-Offs					
Prelim BEFU 2026	1,829.400	1,384.600	1,394.600	1,364.600	1,334.600
Forecast change	20.600	30.400	32.400	8.400	13.400
Buffer change	150.000	-	-	-	-
Cabinet decision	-	5.000	1.000	-	-
BEFU 2026 (Pre Budget 2026)	2,000.000	1,420.000	1,428.000	1,373.000	1,348.000
Pending Budget 2026 Initiatives	-	-	2.000	2.000	2.000
Revised BEFU 2026	2,000.000	1,420.000	1,430.000	1,375.000	1,350.000
Impairment of Debt Relating to the SBCS					
Prelim BEFU 2026	40.000	-	-	-	-
Forecast change	-	-	-	-	-
Revised BEFU 2026	40.000	-	-	-	-
*Science, Innovation and Technology: R&D Tax Incentive					
Prelim BEFU 2026	631.742	715.000	770.000	824.000	879.000
Forecast change	(6.000)	(10.000)	(3.000)	3.000	6.000
BEFU 2026 (Pre Budget 2026)	625.742	705.000	767.000	827.000	885.000
Pending Budget 2026 Initiatives	-	(1.300)	(26.150)	(27.400)	(32.400)
Revised BEFU 2026	625.742	703.700	740.850	799.600	852.600
Total Non-Departmental Other Expenses – Non PLA Revised BEFU 2026	**3,799.894**	**3,072.750**	**3,205.900**	**3,261.650**	**3,330.650**

* *Approval is not required as part of this paper. We are separately seeking approval from the Minister of Finance and the Minister of Science, Innovation and Technology (IR2026/070 refers) for forecast changes relating to this appropriation.*

Non-Departmental Other Expenses – PLA

	$ million				
Non-Departmental Other Expenses - PLA	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
KiwiSaver: Employee and Employer Contributions					
Prelim BEFU 2026	10,740.000	12,400.000	13,190.000	14,320.000	15,430.000
Forecast change	(60.000)	(50.000)	(40.000)	(30.000)	(20.000)
Total Non-Departmental Other Expenses - PLA Revised BEFU 2026	**10,680.000**	**12,350.000**	**13,150.000**	**14,290.000**	**15,410.000**

Appendix B - Table 2 Baseline Changes Reports for Vote Revenue non-departmental

The attached Table 2 Baseline Changes Reports sets out the forecast changes for Vote Revenue Crown (non-departmental) since Preliminary BEFU in a tabulated format. The table includes tax forecasts prepared by the Treasury.

The Table 2 Baseline Changes Reports attached are for:

- 2025/26 Supplementary Estimates (SUPPS 2025/26)
- 2026 Budget Economic and Fiscal Update (BEFU 2026).

Table 2: Baseline Changes Report, 2026 Budget (BEFU), Vote 20 - 0: IRD Crown - Revenue (IRD-Crown).

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Benefits or Related Expenses								
Best Start Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Best Start Tax Credit	Fcst Adj	-	(100)	3,600	10,600	(4,400)	CO (18) 2	On going
Working For Families - Family Scheme Income	Cabinet	-	100	400	400	400	Decision TBC	On going
Child Support Payments (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Child Support Payments	Fcst Adj	-	1,000	1,000	-	-	CO (18) 2	On going
Family Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Family Tax Credit	Fcst Adj	-	200	39,000	124,800	(39,400)	CO (18) 2	On going
Working For Families - Family Scheme Income	Cabinet	-	800	3,000	3,200	3,400	Decision TBC	On going
In-Work Tax Credit (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting In-Work Tax Credit	Fcst Adj	-	(200)	18,400	30,400	2,300	CO (18) 2	On going
Increase to the In-work Tax Credit	Cabinet	-	259,000	29,000	-	-	CAB-26-MIN-0086	On going
Working For Families - Family Scheme Income	Cabinet	-	200	600	600	700	Decision TBC	On going
KiwiSaver: Tax Credit, Contribution and Residual Entitlement								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting KiwiSaver: Tax Credit, Contribution and Residual Entitlement	Fcst Adj	-	4,200	2,000	1,000	1,000	CO (18) 2	On going
Total changes - Benefits or Related Expenses		**-**	**265,200**	**97,000**	**171,000**	**(36,000)**		
Non-Departmental Borrowing Expenses								
Income Equalisation Interest (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting Income Equalisation Interest	Fcst Adj	-	2,000	2,000	2,000	2,000	CO (18) 2	On going
Total changes - Non-Departmental Borrowing Expenses		**-**	**2,000**	**2,000**	**2,000**	**2,000**		
Non-Departmental Other Expenses								
Final-year Fees Free Payments								
Non-Dept Annual Appropriation								

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Cumulative forecasting changes impacting Final-year Fees Free Payments	Fcst Adj	-	-	160	(339)	(608)	CO (18) 2	On going
Increasing Tuition Fees - Impacts Related to Student Loans and Final-year Fees Free Payments	Cabinet	-	-	840	2,339	2,608	Decision TBC	On going
Impairment of Debt and Debt Write-Offs								
Non-Dept Annual Appropriation								
Company to Shareholder Loans - Taxation	Cabinet	-	-	2,000	2,000	2,000	Decision TBC	On going
Cumulative forecasting changes impacting Impairment of Debt and Debt Write-Offs	Fcst Adj	-	30,400	32,400	8,400	13,400	CO (18) 2	On going
GST and bad debt deductions	Fcst Adj	-	(1,200)	(1,200)	(1,200)	(1,200)	CO (18) 2 IR2026/012	On going
GST and bad debt deductions	Fcst Adj	-	1,200	1,200	1,200	1,200	CO (18) 2 IR2026/012	On going
Increase to the In-work Tax Credit	Cabinet	-	5,000	1,000	-	-	CAB-26-MIN-0086	On going
Impairment of Debt and Debt Write-Offs Relating to Child Support								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting Impairment of Debt and Debt Write-Offs Relating to Child Support	Fcst Adj	-	5,000	5,000	5,000	5,000	CO (18) 2	On going
Initial Fair Value Write-Down Relating to Student Loans								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting Initial Fair Value Write-Down Relating to Student Loans	Fcst Adj	-	6,950	30,470	32,340	32,355	CO (18) 2	On going
Increasing Tuition Fees - Impacts Related to Student Loans and Final-year Fees Free Payments	Cabinet	-	20,050	25,530	26,660	27,645	Decision TBC	On going
KiwiSaver: Employee and Employer Contributions (PLA)								
Non-Dept Other Appropriation								
Cumulative forecasting changes impacting KiwiSaver: Employee and Employer Contributions (PLA)	Fcst Adj	-	(50,000)	(40,000)	(30,000)	(20,000)	CO (18) 2	On going
Science, Innovation and Technology: R&D Tax Incentive								
Non-Dept Annual Appropriation								
Cumulative forecasting changes impacting Science, Innovation and Technology: R&D Tax Incentive	Fcst Adj	-	(10,000)	(3,000)	3,000	6,000	CO (18) 2	On going
Research and Development Tax Incentive Amendments	Cabinet	-	(1,300)	(26,150)	(27,400)	(32,400)	Decision TBC	On going
Total changes - Non-Departmental Other Expenses		**-**	**6,100**	**28,250**	**22,000**	**36,000**		
Tax Revenue								
Companies								
Non-Dept Revenue								
Changes to the Thin Capitalisation Settings for Infrastructure	Cabinet	-	(10,000)	(10,000)	(10,000)	(10,000)	ECO-26-MIN-0020, CAB-26-MIN-0061	On going

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Charities and Not-For-Profits: Other Changes	Other	-	s 9(2)(f)(iv)				Decision TBC	On going
Cumulative forecasting changes impacting Companies	Fcst Adj	-	(295,700)	(319,900)	396,450	590,850	CO (18) 2	On going
Fringe Benefit Tax - Simplifying Motor Vehicle Rules	Other	-	20	70	70	70	Decision TBC	On going
Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2026	Cabinet	-	380	380	380	380	CAB-26-MIN-0053, LEG-26-MIN-0029	On going
Thin Capitalisation Changes for Foreign-owned New Zealand Banking Groups	Cabinet	-	3,200	13,100	14,400	14,500	Decision TBC	On going
Fringe Benefit Tax								
Non-Dept Revenue								
Cumulative forecasting changes impacting Fringe Benefit Tax	Fcst Adj	-	15,430	17,620	19,620	11,620	CO (18) 2	On going
Fringe Benefit Tax - Simplifying Motor Vehicle Rules	Other	-	(60)	(250)	(250)	(250)	Decision TBC	On going
Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2026	Cabinet	-	(1,370)	(1,370)	(1,370)	(1,370)	CAB-26-MIN-0053, LEG-26-MIN-0029	On going
Gaming Duties								
Non-Dept Revenue								
Cumulative forecasting changes impacting Gaming Duties	Fcst Adj	-	(1,000)	(6,000)	(5,000)	(5,000)	CO (18) 2	On going
Goods and Services Tax (IRD)								
Non-Dept Revenue								
Cumulative forecasting changes impacting Goods and Services Tax	Fcst Adj	-	(393,000)	127,000	447,000	586,000	CO (18) 2	On going
Other Indirect Taxes								
Non-Dept Revenue								
Cumulative forecasting changes impacting Other Indirect Taxes	Fcst Adj	-	10,000	2,000	11,000	9,000	CO (18) 2	On going
Other Persons								
Non-Dept Revenue								
Charities and Not-For-Profits: Other Changes	Other	-	-	s 9(2)(f)(iv)			Decision TBC	On going
Company to Shareholder Loans - Taxation	Cabinet	-	31,000	28,000	46,000	40,000	Decision TBC	On going
Cumulative forecasting changes impacting Other Persons	Fcst Adj	-	(19,700)	16,930	172,750	240,030	CO (18) 2	On going
Donation Tax Credit Changes	Cabinet	-	(1,500)	15,300	19,000	19,000	Decision TBC	On going
Financial Arrangement Rules - Amendments to Support New Migrants	Other	-	(700)	(580)	(450)	(330)	Decision TBC	On going
Foreign Investment Funds - Tax Rule Reforms	Cabinet	-	(17,100)	(16,600)	(17,100)	(17,500)	Decision TBC	On going
Source Deductions								
Non-Dept Revenue								
Cumulative forecasting changes impacting Source Deductions	Fcst Adj	-	(188,050)	(52,800)	50,200	202,200	CO (18) 2	On going
Non-resident Contractors' Withholding Tax - Asset Leasing in Airline Industry	Cabinet	-	(4,200)	(4,200)	(4,200)	(4,200)	Decision TBC	On going
Non-resident Contractors' Withholding Tax - Modernisation	Cabinet	-	(750)	(3,000)	(3,000)	(3,000)	Decision TBC	On going

	Classification	2025/26 $000	2026/27 $000	2027/28 $000	2028/29 $000	2029/30 $000	Authority for Change	Final Year Funding
Withholding Taxes								
Non-Dept Revenue								
Charities and Not-For-Profits: Other Changes	Other	-	s 9(2)(f)(iv)				Decision TBC	On going
Cumulative forecasting changes impacting Withholding Taxes	Fcst Adj	-	(121,990)	32,010	83,860	149,860	CO (18) 2	On going
Total changes - Tax Revenue		**-**	**(996,000)**	**(165,000)**	**1,219,000**	**1,821,000**		
Non-Tax Revenue								
Interest on Impaired Student Loans								
Non-Dept Revenue								
Cumulative forecasting changes impacting Interest on Impaired Student Loans	Fcst Adj	-	721	2,629	5,411	8,130	CO (18) 2	On going
Increasing Tuition Fees - Impacts Related to Student Loans and Final-year Fees Free Payments	Cabinet	-	279	1,371	2,589	3,870	Decision TBC	On going
Other non-tax revenue								
Non-Dept Revenue								
Cumulative forecasting changes impacting Other non-tax revenue	Fcst Adj	-	(20,000)	(20,000)	(20,000)	(20,000)	CO (18) 2	On going
Small Business Cashflow Scheme interest unwind								
Non-Dept Revenue								
Cumulative forecasting changes impacting SBC interest unwind	Fcst Adj	-	245	72	66	(3)	CO (18) 2	On going
Working for Families Tax Credit Interest and Penalties								
Non-Dept Revenue								
Cumulative forecasting changes impacting Interest on Working for Families Interest and Penalties	Fcst Adj	-	(1,000)	(1,000)	(1,000)	(1,000)	CO (18) 2	On going
Total changes - Non-Tax Revenue		**-**	**(19,755)**	**(16,928)**	**(12,934)**	**(9,003)**		
Capital Receipts								
Income Equalisation Reserve Account								
Non-Dept Revenue								
Cumulative forecasting changes impacting Income Equalisation Reserve Account	Fcst Adj	-	5,000	5,000	5,000	5,000	CO (18) 2	On going
Small Business Cashflow Scheme receipts								
Non-Dept Revenue								
Cumulative forecasting changes impacting Small Business Cashflow Scheme receipts	Fcst Adj	-	11,410	2,430	1,728	152	CO (18) 2	On going
Student Loans - Receipts								
Non-Dept Revenue								
Cumulative forecasting changes impacting Student Loan - Receipts	Fcst Adj	-	6,872	12,886	15,338	15,277	CO (18) 2	On going
Increasing Tuition Fees - Impacts Related to Student Loans and Final-year Fees Free Payments	Cabinet	-	128	1,114	2,662	4,723	Decision TBC	On going
Total changes - Capital Receipts		**-**	**23,410**	**21,430**	**24,728**	**25,152**		

Classification Key

Short Name	Description	Reference
Cabinet	Cabinet policy decision	Approvals are sought in cabinet papers (refer to cabinet manual), with authority given via a cabinet minute. The authority for change should reference both supporting documents.
ECT	Expense and Capital Transfer	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding within an appropriation across financial years.
ECT ip	Expense and Capital Transfer in-principle	Defined in (Cabinet Office Circular). The portion of an ECT that can't be accurately quantified so the transfer amount has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Fcst Adj	Forecast Adjustments	Defined in (Cabinet Office Circular). Adjustments to the forecast expenditure of PLAs or where there is a pre-determined cost calcultion, or Crown Revenue.
FLoS	Front-Loading of Spending	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Bringing forward expenditure to create lasting cost savings.
FNA	Fiscally Neutral Adjustment	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding between appropriations within a financial year.
RoU	Retention of Underspends	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring underspends to the next financial year.
RoU 50%	Retention of Underspends @ 50%	Defined in CO Circular. Portion of an ROU can't accurately quantify so the transfer amount of 50% of an underspend has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Tech Adj	Technical adjustment	Defined in (Cabinet Office Circular). Technical accounting adjustments with no cash impact to the Crown, MYA spending profile changes, non-controversial appropriation title or scope changes.
SuppsJune	Offset MYA June vs Supps Difference	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the difference between the Supps Forecast and June Actual.
BudgetOY4	Offset MYA Budget OY4 Rollover	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the rollover of Budget OY4 into OBU OY4.
Return Sav	Return of savings to the Crown	Returning savings to the Crown is always encouraged. Departments can achieve this by constantly looking for efficiency gains through improvements in processes and technology.
Crwn Liab	Recognition of Existing Crown liability	Crown liabilities need to be recognised as soon as possible. These affect Non-Departmental Appropriations.
Other	Other changes outside the above criteria	There should be very few changes outside the above criteria, so if there are any they require extra scrutiny.

Table 2: Baseline Changes Report, 2025/26 Supps, Vote 20 - 0: IRD Crown - Revenue (IRD-Crown).

	Classification	2025/26 $000	Authority for Change	Final Year Funding
Benefits or Related Expenses				
Child Support Payments (PLA)				
Non-Dept Other Appropriation				
Cumulative forecasting changes impacting Child Support Payments	Fcst Adj	2,000	CO (18) 2	N/A
FamilyBoost Tax Credit (PLA)				
Non-Dept Other Appropriation				
Cumulative forecasting changes impacting FamilyBoost Tax Credit	Fcst Adj	1,000	CO (18) 2	N/A
In-Work Tax Credit (PLA)				
Non-Dept Other Appropriation				
Cumulative forecasting changes impacting In-Work Tax Credit	Fcst Adj	(2,000)	CO (18) 2	N/A
Increase to the In-work Tax Credit	Cabinet	79,000	CAB-26-MIN-0086	N/A
KiwiSaver: Tax Credit, Contribution and Residual Entitlement				
Non-Dept Annual Appropriation				
Cumulative forecasting changes impacting KiwiSaver: Tax Credit, Contribution and Residual Entitlement	Fcst Adj	2,000	CO (18) 2	N/A
Total changes - Benefits or Related Expenses		**82,000**		
Non-Departmental Other Expenses				
Final-year Fees Free Payments				
Non-Dept Annual Appropriation				
Cumulative forecasting changes impacting Final-year Fees Free Payments	Fcst Adj	(11,000)	CO (18) 2	N/A
Impairment of Debt and Debt Write-Offs				
Non-Dept Annual Appropriation				
Buffers on Impairment and Demand-Driven Appropriations	Fcst Adj	150,000	CO (18) 2	N/A
Cumulative forecasting changes impacting Impairment of Debt and Debt Write-Offs	Fcst Adj	20,600	CO (18) 2	N/A
GST and bad debt deductions	Fcst Adj	(1,200)	CO (18) 2 IR2026/012	N/A
GST and bad debt deductions	Fcst Adj	1,200	CO (18) 2 IR2026/012	N/A
Impairment of Debt Relating to Student Loans				
Non-Dept Annual Appropriation				
Buffers on Impairment and Demand-Driven Appropriations	Fcst Adj	195,000	CO (18) 2	N/A

	Classification	2025/26 $000	Authority for Change	Final Year Funding
Cumulative forecasting changes impacting Impairment of Debt Relating to Student Loans	Fcst Adj	(30,000)	CO (18) 2	N/A
Initial Fair Value Write-Down Relating to Student Loans				
Non-Dept Annual Appropriation				
Cumulative forecasting changes impacting Initial Fair Value Write-Down Relating to Student Loans	Fcst Adj	(18,000)	CO (18) 2	N/A
KiwiSaver: Employee and Employer Contributions (PLA)				
Non-Dept Other Appropriation				
Cumulative forecasting changes impacting KiwiSaver: Employee and Employer Contributions (PLA)	Fcst Adj	(60,000)	CO (18) 2	N/A
Science, Innovation and Technology: R&D Tax Incentive				
Non-Dept Annual Appropriation				
Cumulative forecasting changes impacting Science, Innovation and Technology: R&D Tax Incentive	Fcst Adj	(6,000)	CO (18) 2	N/A
Total changes - Non-Departmental Other Expenses		**240,600**		
Tax Revenue				
Companies				
Non-Dept Revenue				
Changes to the Thin Capitalisation Settings for Infrastructure	Cabinet	(2,500)	ECO-26-MIN-0020, CAB-26-MIN-0061	N/A
Cumulative forecasting changes impacting Companies	Fcst Adj	395,310	CO (18) 2	N/A
Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2026	Cabinet	190	CAB-26-MIN-0053, LEG-26-MIN-0029	N/A
Fringe Benefit Tax				
Non-Dept Revenue				
Cumulative forecasting changes impacting Fringe Benefit Tax	Fcst Adj	6,680	CO (18) 2	N/A
Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2026	Cabinet	(680)	CAB-26-MIN-0053, LEG-26-MIN-0029	N/A
Gaming Duties				
Non-Dept Revenue				
Cumulative forecasting changes impacting Gaming Duties	Fcst Adj	(4,000)	CO (18) 2	N/A
Goods and Services Tax (IRD)				
Non-Dept Revenue				
Cumulative forecasting changes impacting Goods and Services Tax	Fcst Adj	(421,000)	CO (18) 2	N/A
Other Indirect Taxes				
Non-Dept Revenue				

	Classification	2025/26 $000	Authority for Change	Final Year Funding
Cumulative forecasting changes impacting Other Indirect Taxes	Fcst Adj	9,000	CO (18) 2	N/A
Other Persons				
Non-Dept Revenue				
Company to Shareholder Loans - Taxation	Cabinet	7,000	Decision TBC	N/A
Cumulative forecasting changes impacting Other Persons	Fcst Adj	(127,775)	CO (18) 2	N/A
Foreign Investment Funds - Tax Rule Reforms	Cabinet	(4,225)	Decision TBC	N/A
Source Deductions				
Non-Dept Revenue				
Cumulative forecasting changes impacting Source Deductions	Fcst Adj	(134,950)	CO (18) 2	N/A
Non-resident Contractors' Withholding Tax - Asset Leasing in Airline Industry	Cabinet	(1,050)	Decision TBC	N/A
Withholding Taxes				
Non-Dept Revenue				
Cumulative forecasting changes impacting Withholding Taxes	Fcst Adj	(26,000)	CO (18) 2	N/A
Total changes - Tax Revenue		**(304,000)**		
Non-Tax Revenue				
Interest on Impaired Student Loans				
Non-Dept Revenue				
Cumulative forecasting changes impacting Interest on Impaired Student Loans	Fcst Adj	(1,000)	CO (18) 2	N/A
Other non-tax revenue				
Non-Dept Revenue				
Cumulative forecasting changes impacting Other non-tax revenue	Fcst Adj	(15,000)	CO (18) 2	N/A
Small Business Cashflow Scheme interest unwind				
Non-Dept Revenue				
Cumulative forecasting changes impacting SBC interest unwind	Fcst Adj	(268)	CO (18) 2	N/A
Working for Families Tax Credit Interest and Penalties				
Non-Dept Revenue				
Cumulative forecasting changes impacting Interest on Working for Families Tax Credit Interest and Penalties	Fcst Adj	(1,000)	CO (18) 2	N/A
Total changes - Non-Tax Revenue		**(17,268)**		
Capital Receipts				
Income Equalisation Reserve Account				
Non-Dept Revenue				

	Classification	2025/26 $000	Authority for Change	Final Year Funding
Cumulative forecasting changes impacting Income Equalisation Reserve Account	Fcst Adj	40,000	CO (18) 2	N/A
Small Business Cashflow Scheme receipts				
Non-Dept Revenue				
Cumulative forecasting changes impacting Small Business Cashflow Scheme receipts	Fcst Adj	23,621	CO (18) 2	N/A
Student Loans - Receipts				
Non-Dept Revenue				
Cumulative forecasting changes impacting Student Loan - Receipts	Fcst Adj	(1,000)	CO (18) 2	N/A
Total changes - Capital Receipts		**62,621**		

Classification Key

Short Name	Description	Reference
Cabinet	Cabinet policy decision	Approvals are sought in cabinet papers (refer to cabinet manual), with authority given via a cabinet minute. The authority for change should reference both supporting documents.
ECT	Expense and Capital Transfer	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding within an appropriation across financial years.
ECT ip	Expense and Capital Transfer in-principle	Defined in (Cabinet Office Circular). The portion of an ECT that can't be accurately quantified so the transfer amount has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Fcst Adj	Forecast Adjustments	Defined in (Cabinet Office Circular). Adjustments to the forecast expenditure of PLAs or where there is a pre-determined cost calcultion, or Crown Revenue.
FLoS	Front-Loading of Spending	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Bringing forward expenditure to create lasting cost savings.
FNA	Fiscally Neutral Adjustment	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring funding between appropriations within a financial year.
RoU	Retention of Underspends	Defined in (Cabinet Office Circular Financial changes that can be approved by Joint Ministers). Transferring underspends to the next financial year.
RoU 50%	Retention of Underspends @ 50%	Defined in CO Circular. Portion of an ROU can't accurately quantify so the transfer amount of 50% of an underspend has been approved in-principle. 1st time can count in fiscal forecasts is OBU.
Tech Adj	Technical adjustment	Defined in (Cabinet Office Circular). Technical accounting adjustments with no cash impact to the Crown, MYA spending profile changes, non-controversial appropriation title or scope changes.
SuppsJune	Offset MYA June vs Supps Difference	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the difference between the Supps Forecast and June Actual.
BudgetOY4	Offset MYA Budget OY4 Rollover	This is a subset of the Technical Adjustments classification for neutral changes to the MYA spending profile to offset the rollover of Budget OY4 into OBU OY4.
Return Sav	Return of savings to the Crown	Returning savings to the Crown is always encouraged. Departments can achieve this by constantly looking for efficiency gains through improvements in processes and technology.
Crwn Liab	Recognition of Existing Crown liability	Crown liabilities need to be recognised as soon as possible. These affect Non-Departmental Appropriations.
Other	Other changes outside the above criteria	There should be very few changes outside the above criteria, so if there are any they require extra scrutiny.

Inland Revenue report

Inland Revenue
Te Tari Taake

Budget 2026 Estimates for Vote Revenue – Vote Minister sign-off

Date	1 May 2026	**Priority**	High
Security level	Budget Sensitive	**Report number**	IR2026/139

Action sought		**Deadline**
Minister of Revenue	**Sign and forward** the attached near final *Estimates of Appropriations 2026/27 for Vote Revenue* and a draft letter to the Minister of Finance. **Sign and forward** the attached near final *Supplementary Estimates of Appropriations 2025/26 for Vote Revenue* and a draft letter to the Minister of Finance.	5 May 2026

Purpose

This report seeks your approval for the following near final Budget 2026 documents for Vote Revenue and associated letters to the Minister of Finance:

- The Estimates of Appropriations 2026/27, and
- The Supplementary Estimates of Appropriations 2025/26.

All appropriation Ministers are being asked to approve near final Estimates documents prior to Cabinet decisions on the Budget package scheduled for Thursday 7 May.

Contact for phone discussion, if required

Name	**Position**	**Phone number**	**First contact**
Fergus Welsh	Chief Financial Officer	s 9(2)(a)	☐
Darren Cheevers	Domain Lead Finance		✓
Rachel Parker	Domain Lead Finance		☐

Budget 2026 Estimates for Vote Revenue – Vote Minister sign-off

Background

1 As part of the Budget Estimates process, one appropriation Minister is required to confirm to the Minister of Finance, on behalf of all appropriation Ministers for the Vote, that the Estimates documentation is accurate and suitable for publication.

2 You are responsible for all appropriations under Vote Revenue except the non-departmental other expenses appropriation for R&D Tax Incentive payments, which sits with the Minister of Science, Innovation and Technology. That Minister has separately approved the relevant funding movements and forecasts, and these have been appropriately reflected in the Estimates documentation. The Minister is aware that you will be signing the Vote Revenue Estimates documents (IR2026/070 refers).

3 Cabinet is scheduled to agree the 2026 Budget package on Thursday 7 May, which is later than the original date of Tuesday 28 April.

4 Delays in the Budget process have affected some Votes, including Vote Revenue. As a result, some of the final stages of the Budget process need to run in parallel.

5 The due date for appropriation Ministers to approve the Estimates documents remains Tuesday 5 May. Given delays in the Budget process, this date could be extended to Thursday 7 May should you require additional time.

6 We seek your approval for the following near final Estimates documents:

- The Estimates of Appropriations 2026/27 for Vote Revenue, and
- The Supplementary Estimates of Appropriations 2025/26 for Vote Revenue.

7 As this approval is being sought prior to final Cabinet decisions, subsequent changes to these documents may be required. The Estimates documents include all known Budget initiatives as at 30 April 2026 that have been agreed by Budget Ministers for Cabinet endorsement at the 7 May 2026 meeting. We will advise you of any material changes required, following Cabinet decisions.

8 A full list of Budget 2026 initiatives, agreed by Budget Ministers to date, that impact Vote Revenue is provided in Attachment A. This list includes the Revenue portfolio initiatives that the Minister of Finance and you have previously approved (IR2026/112 refers). The list also includes an initiative led from the Tertiary Education portfolio that impacts Vote Revenue.

9 The titles of initiatives in the Estimates documents align with the Budget package report for Cabinet. These titles may change following final decisions from the Minister of Finance and the Treasury on how they will be described in Budget Day documentation.

10 The Estimates document includes the output performance measures and targets for the 2026/27 financial year that you have previously approved (IR2026/027 refers).

The Estimates documents review process

11 The two near final Estimates documents have been through an appropriate quality assurance process subject to the caveats noted in paragraph 15 below and are free of material errors and omissions.

12 We will update the Estimates documents where there are any changes to the expected Cabinet decisions on the Budget package and we will advise you of any material changes. The Treasury and ourselves may also make editorial corrections to these documents prior to publication if required.

13 The non-departmental forecasts for tax are provided by the Treasury tax forecasting team and are based on the final Treasury macroeconomic forecasts dated 24 April 2026. The appropriations and forecasts for social policy appropriations are based on the final Treasury macroeconomic forecasts dated 1 April 2026.

14 For the near final Estimates documents (attached) as Chief Financial Officer I confirm that the information provided:

- is consistent with the policies and performance expectations of the government, and has been prepared in accordance with the Public Finance Act 1989
- reflects known Budget initiatives as at 30 April 2026, that have been agreed by Budget Ministers for Cabinet approval at the 7 May 2026 meeting
- has been prepared in the required format, and in accordance with the guidance that has been issued by the Treasury
- has been appropriately reviewed by Inland Revenue's senior leaders – with a particular focus on strategic information, such as statements on what an appropriation is intended to achieve and the measures used to track performance, and
- while delays in the Budget process have reduced the time available to finalise these documents, Inland Revenue has made every effort to apply appropriate quality assurance processes to ensure these documents are free of material errors and omissions.

Caveats to near final Estimates documents

15 The following caveats apply to the near final Estimates documents and the endorsements in the previous section:

- the content of the Estimates documents are subject to final Cabinet decisions to be agreed at the 7 May 2026 meeting, and therefore maybe be subject to further changes
- the titles and descriptions of initiatives are subject to change, following final decisions from the Minister of Finance and the Treasury on how they will be described in Budget Day documentation, and
- s 9(2)(g)(i)

Recommendations

I recommend that you:

1. **Note** that delays in the Budget process have affected some Votes, including Vote Revenue, and as a result we are seeking your approval for the near final versions of the Vote Revenue Estimates documents ahead of final Budget decisions being made by Cabinet.

2. **Note** that we will advise you if there are any subsequent material changes to our Vote Revenue Estimates documents.

3. **Sign and forward** the following documents:
   - the Estimates of Appropriations 2026/27 for Vote Revenue (near final)
   - the letter to the Minister of Finance for the Estimates
   - the Supplementary Estimates of Appropriations 2025/26 for Vote Revenue (near final), and
   - the letter to the Minister of Finance for the Supplementary Estimates.

   Signed and forwarded

s 9(2)(a)

Fergus Welsh
Chief Financial Officer
Inland Revenue
1 May 2026

Hon Simon Watts
Minister of Revenue
/ /2026

Attachments:
- Attachment A – Budget 2026 initiatives that impact Vote Revenue
- Letter to the Minister of Finance - 2026/27 Estimates: Ministerial Sign-off for Vote Revenue
- Letter to the Minister of Finance - 2025/26 Supplementary Estimates: Ministerial Sign-off for Vote Revenue
- Near final Estimates of Appropriations 2026/27
- Near final Supplementary Estimates of Appropriations 2025/26.

Attachment A – Budget 2026 initiatives that impact Vote Revenue

The known Budget 2026 initiatives agreed by Budget Ministers up to 30 May 2026, that impact Vote Revenue include:

Initiatives (departmental):

- Baseline Savings – Inland Revenue
- Compliance Activities - Increased Investment
- Research and Development Tax Amendments - Departmental Impact

Initiatives (non-departmental):

- Charities and Not-for-profits - Taxation and Changes to Settings
- Company Loans to Shareholders - Taxation Rules
- Compliance Activities - Increased Investment - Non-departmental Impact
- Ensuring FamilyBoost Reaches More Families
- Financial Arrangement Rules Amendments to support New Migrants[1]
- Foreign Investment Funds - Tax Rule Reforms
- Increase to the In-Work Tax Credit (Budget 2026 pre commitment)
- Non-resident Contractors' Tax - Exemption for Aircraft Asset Leasing
- Non-resident Contractors' Tax - Modernisation
- Research and Development Tax Incentive – Reducing the Cap for Internal Non-administrative Software Expenditure and Other Amendments
- Simplifying Motor Vehicle Fringe Benefit tax Rules[1]
- Thin Capitalisation Changes for Foreign-owned New Zealand Banking Groups[1]
- Thin Capitalisation for Infrastructure Projects - Return of Funding
- Working For Families – Family Scheme Income
- Working for Families – Residency Requirements and Information Sharing (tagged contingency)

Initiatives led by other portfolios (non-departmental)

- Increasing Tuition Fees - Impacts Related to Student Loans and Final-year Fees Free Payments.

[1] This initiative is charged to the Tax Scorecard, which sits outside Budget allowance.

Hon Simon Watts

Minister of Climate Change
Minister of Local Government
Minister of Revenue
Minister for Auckland

5 May 2026

Hon Nicola Willis
Minister of Finance
Parliament Buildings
WELLINGTON

Dear Minister

2026/27 Estimates: Ministerial Sign-off for Vote Revenue

I advise that the near final *Estimates of Appropriations 2026/27 and Supporting Information* documents for Revenue, for which Inland Revenue is the administering department, have been completed – and that it is accurate and suitable for publication. I confirm that the information provided:

- is consistent with the policies and performance expectations of the government, and has been prepared in accordance with the Public Finance Act 1989
- is consistent with the proposed appropriations to be set out in the Appropriation (2026/27 Estimates) Bill, existing appropriations and financial authorities, and includes funding decisions I am aware of as at 30 April 2026 that are subject to final Cabinet decisions to be agreed at the 7 May 2026 meeting, and therefore maybe be subject to further changes
- with Cabinet decisions up to 30 April 2026
- is provided in the required format, and has been prepared in accordance with the guidance that has been issued by the Treasury
- has been through an appropriate quality assurance process and is free of material errors and omissions, and
- has, where it relates to an appropriation that is the responsibility of another Minister, been approved by the Minister responsible for that appropriation.

In signing this statement, I acknowledge that I and the other Ministers responsible for appropriations in this Vote are responsible for the information for Vote Revenue administered by Inland Revenue included in the *Estimates of Appropriations 2026/27 and Supporting Information*.

Should any changes be required to the Vote Revenue 2026/27 Estimates after Cabinet decisions on the Budget package, my officials will work with the Treasury to ensure these are included.

Yours sincerely

Hon Simon Watts
Minister of Revenue
On behalf of all Ministers responsible for appropriations in Vote Revenue

Private Bag 18041, Parliament Buildings, Wellington 6160, New Zealand | +64 4 817 6814 | s.watts@ministers.govt.nz

Hon Simon Watts

Minister of Climate Change
Minister of Local Government
Minister of Revenue
Minister for Auckland

5 May 2026

Hon Nicola Willis
Minister of Finance
Parliament Buildings
WELLINGTON

Dear Minister

2025/26 Supplementary Estimates: Ministerial Sign-off for Vote Revenue

I advise that the near final *Supplementary Estimates of Appropriations 2025/26 and Supporting Information* documents for Revenue, for which Inland Revenue is the administering department, have been completed – and that it is accurate and suitable for publication. I confirm that the information provided:

- is consistent with the policies and performance expectations of the government, and has been prepared in accordance with the Public Finance Act 1989
- is consistent with the proposed appropriations to be set out in the Appropriation (2025/26 Supplementary Estimates) Bill, existing appropriations and financial authorities, and includes funding decisions that are subject to final Cabinet decisions I am aware of as at 30 April 2026 to be agreed at the 7 May 2026 meeting, and therefore maybe be subject to further changes
- is provided in the required format, and has been prepared in accordance with the guidance that has been issued by the Treasury, and
- has been through an appropriate quality assurance process and is free of material errors and omissions, and
- has, where it relates to an appropriation that is the responsibility of another Minister, been approved by the Minister responsible for that appropriation.

In signing this statement, I acknowledge that I and the other Ministers responsible for appropriations in this Vote are responsible for the information for Vote Revenue administered by Inland Revenue included in the *Supplementary Estimates of Appropriations 2025/26 and Supporting Information*.

Should any changes be required to the Vote Revenue 2025/26 Supplementary Estimates after Cabinet decisions on the Budget package, my officials will work with the Treasury to ensure these are included.

Yours sincerely

Hon Simon Watts
Minister of Revenue
On behalf of all Ministers responsible for appropriations in Vote Revenue

Private Bag 18041, Parliament Buildings, Wellington 6160, New Zealand | +64 4 817 6814 | s.watts@ministers.govt.nz

Inland Revenue report

Inland Revenue
Te Tari Taake

Vote Revenue: 2026 June Technical Adjustment Request

Date	26 May 2026	**Priority**	High
Security level	Budget sensitive	**Report number**	IR2026/154

Action sought		**Deadline**
Minister of Revenue	**Approve** the recommendations; and **Refer** the attached report to the Minister of Finance	1pm Thursday 4 June 2026

Purpose
This report seeks your approval to submit a request for a non-departmental in-principle expense transfer for Vote Revenue to the Minister of Finance and a small forecast increase as a result of a rounding difference in a Budget 2026 financial recommendation, and your agreement to refer the attached report to the Minister of Finance for her approval as part of the 2025/26 June technical adjustment process.

Contact for phone discussion, if required

Name	**Position**	**Phone number**	**First contact**
Fergus Welsh	Enterprise Leader Finance (Chief Financial Officer)	s 9(2)(a)	☐
Rachel Parker	Domain Lead Finance		✓

Vote Revenue: 2026 June Technical Adjustment Request

Executive summary

1. The June technical adjustment process allows a department to seek Joint Ministers' approval for limited technical adjustments under CO (18) 2: Proposals with Financial Implications and Financial Authorities. This authority enables adjustments affecting the current financial year to be approved after Budget Day but before year end.
2. This report seeks your approval to submit a non-departmental in-principle expense transfer (IPET) for Vote Revenue to the Minister of Finance as part of the 2025/26 June technical adjustment process in relation to the Payments to Settle Residual Claims appropriation.
3. The proposed IPET has been entered into the Treasury CFISnet system as required by the Treasury. A templated system generated report to the Minister of Finance is attached for your signature.
4. In addition, this report seeks your joint approval for a $285,000 forecasting increase to the approved Final-year Fees Free Payments appropriation in 2029/30 and outyears, and will align the baseline to the financial recommendation associated with Cabinet's decision to end final-year fees free funding which currently differ due to rounding.
5. Neither of the changes contained in this update require Cabinet decisions at this time.

In principle-expense transfer

6. The Payments to Settle Residual Claims appropriation covers payments to eligible recipients for residual claims from entitlements which Inland Revenue previously administered.
7. Although applications for these entitlements are closed and only minimal payments have been made in 2025/26, a small number of disputed claims may still arise in the future. These claims are uncertain in timing and value, but may result in payment obligations at short notice, and therefore, an appropriation must be retained in order to incur expenditure when a liability arises and needs to be funded.
8. Accordingly, we are seeking to transfer unused funding of up to $102,000 from 2025/26 to 2026/27. This will enable already approved funds to be available to meet the costs of any claims received in 2026/27 from the appropriation.
9. No funding is allocated to this appropriation in 2026/27. We may therefore need to seek early confirmation of this transfer, should we require funding to settle any claims received between 1 July 2026 and the October Baseline Update (when in-principle expense transfers are usually confirmed).
10. We have calculated the maximum amount requested using a conservative approach. This request is for appropriation management purposes only, and we are continuing to forecast no expenditure for 2026/27 (consistent with the Estimates of Appropriations for the Government of New Zealand for the year ended 30 June 2027).
11. Full details, including the reason for this request, are outlined in Annex 1 attached to this letter and have also been provided to the Treasury via the Crown Financial Information System (CFIS).
12. If a transfer is not supported, we will need to fund any costs from the departmental baseline and a joint ministerial approval for a fiscally neutral transfer from departmental appropriations to the Payments to Settle Residual Claims appropriation will be required.

Final-Year Fees Free Payments

13. On 20 April 2026, as part of the 2026 Budget Economic and Fiscal Update, we sought and received joint Ministerial approval for a $608,000 forecast decrease in 2029/30 (and outyears) for the Final-year Fees Free Payments appropriation (IR2026-077 refers).
14. As part of final Budget 2026 decisions, Cabinet subsequently approved the cessation of the final-year fees free scheme and the ending of funding for the scheme from 2028/29. Due to rounding, the approved appropriation for 2029/30 and outyears was $285,000 lower than the approved financial recommendation in the Budget 2026 Cabinet paper. As a result, a $285,000 forecast increase is required. This increase is currently unapproved, and we are therefore seeking your approval to submit a forecast adjustment to the Minister of Finance.

Consultation

15. We have discussed the contents of these requests with the Treasury.

Next steps

16. If you agree to this request, please refer the attached letter and accompanying schedule to the Minister of Finance by 1pm Thursday 4 June 2026.

Recommendations

We recommend that you:

1. **note** the Inland Revenue request and reasons for requiring an in-principle expense transfer (IPET) in Appendix 1;

2. **note** the request is for an in-principle expense transfer of up to the following maximum amount of operating from 2025/26 to 2026/27:

	$ million – increase / (decrease)				
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-Departmental Other Expenses: Payments to Settle Residual Claims	(0.102)	0.102	-	-	-
Total Operating	**(0.102)**	**0.102**	**-**	**-**	**-**

3. **authorise** the Minister of Finance and the Minister of Revenue to jointly agree the final amount to be transferred, following completion of the 2025/26 audited financial schedules, with no impact on the operating balance and/or net core Crown debt across the forecast period;

   authorised/not authorised

4. **note** Inland Revenue may seek an early confirmation of the full amount of the available expense transfer for request ID 627 to avoid the risk of any unappropriated expenditure should funding be required prior to other IPETs being agreed at the October Baseline Update;

5. **note** there is no funding allocated for this appropriation in 2026/27, and Inland Revenue have calculated the maximum amount requested using a conservative approach;

6. **note** Cabinet agreed to cease the final-year fees free scheme and end funding from 2028/29, however due to rounding, the 2029/30 and outyears appropriation was set $285,000 below the approved financial recommendation, requiring a corresponding $285,000 forecast increase;

7. **approve** the following forecast change to the Final-year Fees Free Payments Non-departmental Other Expenses appropriation, to align forecasts with Cabinet's decision to end final-year fees free funding, with a corresponding impact on the operating balance and net core Crown debt:

	$ million – increase / (decrease)				
Vote Revenue **Minister of Revenue**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-Departmental Other Expenses: Final-year Fees Free Payments	-	-	-	-	0.285
Total Operating	**-**	**-**	**-**	**-**	**0.285**

approved/not approved

8. **agree** to sign the attached latter and accompanying schedule and forward them to the Minister of Finance by 1pm Thursday 4 June 2026.

agreed/disagreed

s 9(2)(a)

Fergus Welsh

Enterprise Leader Finance (Chief Financial Officer)
Inland Revenue

26 May 2026

Hon Simon Watts

Minister of Revenue

/ /2026

4 June 2026

Hon Nicola Willis
Minister of Finance
Parliament Buildings
WELLINGTON

2025/26 June Technical Adjustment Process

Submission for Vote Revenue (IRD-Crown)

Introduction

This report covers those items requiring technical adjustments for Vote **Revenue (IRD-Crown)** through the June Technical Adjustment Process.

I confirm that none of the changes contained in this update require Cabinet decisions at this time.

The Annex 1 referred to below is attached to this letter and has also been provided to the Treasury via the CFISnet System.

The proposed technical adjustment is as follows:

Changes Requiring Approval of Joint Ministers

In-Principle Expense Transfer

The identifier and name of the proposed in-principle expense transfer is listed below, and the full detail of the request is outlined in Annex 1.

Request ID	Request Title
627	Payments to Settle Residual Claims

Final-Year Fees Free Payments

On 20 April 2026, as part of the 2026 Budget Economic and Fiscal Update, Inland Revenue sought and received joint Ministerial approval for a $608,000 forecast decrease in 2029/30 (and outyears) for the Final-year Fees Free Payments appropriation (IR2026-077 refers).

As part of final Budget 2026 decisions, Cabinet subsequently approved the cessation of the final-year fees free scheme and the ending of funding for the scheme from 2028/29. Due to rounding, the approved appropriation for 2029/30 and outyears was $285,000 lower than the approved financial recommendation in the Budget 2026 Cabinet paper. As a result, a $285,000

forecast increase is required. This increase is currently unapproved and Inland Revenue are therefore seeking our approval for the forecast adjustment of $285,000.

Recommendations

I support these changes and recommend that you:

1. **note** Vote Revenue's request for an in-principle expense transfer of up to $102,000 as detailed in the attached annex;

2. **authorise** the Minister of Finance and Minister of Revenue jointly to agree the final amount to be transferred, following completion of the 2025/26 audited financial statements, with no impact on the operating balance and/or net core Crown debt across the forecast period;

   authorised/not authorised

3. **note** Cabinet agreed to cease the final-year fees free scheme and end funding from 2028/29, however due to rounding, the 2029/30 and outyears appropriation was set $285,000 below the approved financial recommendation, requiring a corresponding $285,000 forecast increase;

4. **approve** the following forecast change to the Final-year Fees Free Payments Non-Departmental Other Expenses appropriation, to align forecasts with Cabinet's decision to end final-year fees free funding, with a corresponding impact on the operating balance and net core Crown debt:

	$ million – increase / (decrease)				
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-Departmental Other Expenses: Final-year Fees Free Payments	-	-	-	-	0.285
Total Operating	**-**	**-**	**-**	**-**	**0.285**

approved/not approved

Hon Simon Watts

Minister of Revenue

……./……./2026

Approved/not approved

Hon Nicola Willis

Minister of Finance

……./……./2026

Annex 1: Requests for Vote Revenue (IRD-Crown)

Proposal No: 627

Vote:	Revenue (IRD-Crown)
Appropriation Administrator:	Inland Revenue Notional for tax
Title:	Payments to Settle Residual Claims
Proposal Type:	In Principle Expense and Capital Transfer
Authority For Change:	CO(18) 2 para 43 and 45
Treasury Recommendation:	With Minister of Finance for decision

1. **note** that the Payments to Settle Residual Claims appropriation funding is intended to settle any late and residual claims for ceased entitlements and as such is demand driven and paid to claimants at short notice based on the outcome of dispute resolution. As such, the receipt and settlement of claims are not in the control of Inland Revenue and Inland Revenue requires an in-principle transfer of up to the following maximum amount of operating from 2025/26 to 2026/27:

	To	Proposed Distribution of Transfer			
Vote Revenue (IRD-Crown)	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30**
Minister of Revenue	**$000**	**$000**	**$000**	**$000**	**$000**
Non-Departmental Other Expenses					
Payments to Settle Residual Claims	(102)	102	-	-	-
Total	**(102)**	**102**	**-**	**-**	**-**

2. **note** there is no funding allocated for this appropriation in 2026/27, and Inland Revenue have calculated the maximum amount requested using a conservative approach;

3. **note** that Inland Revenue may seek an early confirmation of the full amount of the available expense transfer for the amount in recommendation 1 above to avoid the risk of unappropriated expenditure should funding be required to meet any expenditure prior to other IPETs being agreed at the October Baseline Update;

4. **authorise** the Minister of Finance and Minister of Revenue jointly to agree the final amount to be transferred, following completion of the 2025/26 audited financial statements, with no impact on the operating balance and/or net core Crown debt across the forecast period.

authorised/not authorised

Cabinet Office Circular Criteria

Responses as submitted by the Department via CFISnet

Project details

The Payments to Settle Residual Claims appropriation funding is intended to settle any late and residual claims for ceased entitlements.

Causal factors for the delay

These payments are demand driven and paid to claimants at short notice based on the outcome of dispute resolution. As such, the receipt and settlement of claims are not in the control of Inland Revenue and Inland Revenue requires an in-principle expense transfer to transfer anticipated underspends from 2025/26 to 2026/27 to avoid any potential breach of appropriation in 2026/27.

Previous transfers and mitigation plan

Funding for this appropriation was transferred from the COVID-19 Resurgence Support Payments, COVID-19 Support Payments and the Cost of Living payments appropriation during 2025/26 to amalgamate funding for residual claims. No additional funding was sought for this appropriation through baseline updates. Inland Revenue will continue to work with the Treasury to identify alternative mechanisms to maintain funding in outyears.

Reasons why these costs cannot be met from the proposed baseline year

The appropriation is not currently funded beyond 2025/26. These claims are uncertain in timing and value, but may result in payment obligations at short notice, and therefore, an appropriation must be retained in order to incur expenditure when a liability arises and needs to be funded. No expenditure was incurred against this appropriation in 2025/26 but the appropriation may be required in 2026/27. .

[IN CONFIDENCE]

Inland Revenue
Te Tari Taake

POLICY AND REGULATORY STEWARDSHIP

Tax policy report: Charities and not-for-profits overview

Date:	20 March 2024	**Priority:**	Low
Security level:	In Confidence	**Report number:**	IR2024/110

Action sought

	Action sought	Deadline
Minister of Revenue	**Note** the contents of this report **Refer** a copy of this report	19 April 2024

Contact for telephone discussion (if required)

Name	Position	Telephone
Stewart Donaldson	Principal Policy Advisor	s 9(2)(a)
Samantha Putt	Policy Advisor	

20 March 2024

Minister of Revenue

Charities and not-for-profits overview

Purpose

1. This report provides you with an overview of the charities and not-for-profits (NFPs) sector and related tax policy matters. This context may be useful for future tax policy reports and for matters that may be raised with you by stakeholders and other Ministers.

2. This report does not purport to contain a detailed analysis and description of each matter. Rather, it seeks to inform you of the potential range of matters and makes some comment on their attributes so that you can discuss which matters you want to further consider. The appendix contains a summary of these items.

3. We recommend you note this report and invite you to meet with officials to discuss the contents.

Background

Charities and NFPs framework

4. Charities and NFPs make important contributions to the wellbeing of New Zealanders. The sector supports efforts to bolster our social, human, and natural capital. The economic activities of the sector also affect the accumulation of physical and financial capital in the New Zealand economy. These factors form the basis for the tax exemptions and deduction frameworks provided to charities and NFP organisations.

5. The broad policy setting for this sector is that the Government supports charities and NFPs by providing targeted tax concessions. Inland Revenue administers charitable tax exemptions from income tax, fringe benefit tax, goods and services tax and resident withholding tax. We also approve donee status, which gives tax benefits to people donating to these organisations. NFPs that benefit from the widest range of tax concessions will be registered charities that are well regulated, publicly transparent and provide public benefit. Donation tax incentives have the objective of reinforcing and encouraging giving to approved donee organisations. Income tax and donation benefits for charities with charitable purposes outside New Zealand are restricted.

6. Some of the policy options for this sector will need to be considered in the context of broader objectives the Government has for the sector.

Charities and NFPs statistics on Inland Revenue systems

7. There are approximately 90,000 NFPs on Inland Revenue's system. These include:

    7.1 29,000 tax-exempt charities. Based on accounts filed on the public charities register for 2022–23, tax-exempt charities control $81 billion of assets, employ 138,000 people full time (5% of the New Zealand workforce), benefit from 170,000 volunteers each week and contribute about 5% of GDP.

7.2 20,000 tax-exempt amateur sports bodies.

7.3 1,000 tax-exempt local and regional promotion bodies (beautification societies).

7.4 28,000 NFPs that are not tax exempt. About 24,000 of these have net income below a $1,000 deduction threshold available for NFPs, so they do not file income tax returns or pay income tax. About 4,000 file income tax returns and report a taxable income, taxable loss or zero net income.

Recent legislative and regulatory change for the sector

8. This sector has been subject to legislative and regulatory change over recent years. Significant changes include:

8.1 The Incorporated Societies Act 2022, which requires approximately 23,000 incorporated societies to re-register by April 2026 and annually report using the same accounting standards as registered charities.

8.2 The Charities Amendment Act 2023, which introduced a number of changes for 29,000 registered charities. The changes include a new requirement for large charities to report the reasons why they are accumulating funds.

8.3 The External Reporting Board (XRB) has introduced changes to the threshold size of some reporting tiers for registered charities, incorporated societies and other public benefit entities. The focus has been to make it easier for small charities to apply the standards and for larger charities to adopt new service performance reporting standards.

Current policy work

9. There are three projects involving this sector that our policy staff are currently involved with.

Disposals of trading stock at below market value

10. In January 2024, you agreed to progress work related to disposals of trading stock at below market value. Cabinet agreed to the changes on 26 February 2024. These changes will benefit donee organisations because businesses will be able to donate trading stock to them and claim tax deductions on an ongoing basis. These changes are being progressed in an Amendment Paper to the Taxation (Annual Rates for 2023–24, Multinational Tax, and Remedial Matters) Bill.

Requests for overseas donee status

11. Every year there are requests from New Zealand charities with overseas purposes to be granted overseas donee status. Overseas donee status is an exception to the current law that restricts tax benefits for donations to charities with New Zealand purposes. Decisions to give overseas donee status that meet certain Cabinet criteria, such as the relief of poverty, sickness, or the ravages of war or natural disaster, or other overseas development aid objectives, require legislative change.

12. We plan to report to you in April 2024 about the next tranche of requests for overseas donee status for inclusion in the next taxation Bill, scheduled for introduction in August 2024. We will also report to you about the recent request from Sir Don McKinnon, Chair of the NZ Memorial Museum Trust – Le Quesnoy, for permanent overseas donee status.

Regulatory stewardship

13. Later this year Inland Revenue will complete a regulatory stewardship report on donation tax credits. While this report is not primarily policy-related, it may contain policy recommendations that you decide to include on a future Tax and Social Policy Work Programme.

Future policy work

14. A range of potential tax policy matters affecting this sector are identified in the Appendix. Two of these matters will be reported to you shortly and are summarised below.

Simplifying the law for NFPs (including the tax treatment of member transactions)

15. The most pressing tax issue for the NFP sector is whether member trading transactions, subscriptions and levies should be subject to income tax, and if so, whether the law should be simplified for small NFPs to minimise their compliance costs. It is an issue that causes ongoing difficulties from an operational perspective and creates significant uncertainty for NFPs.

16. Inland Revenue has recently determined that, under existing law, NFP member transactions are taxable and that NFP subscriptions and levies may be taxable under ordinary concepts or as income from a business. Member trading transactions are typically any transaction that occurs within a circle of membership, such as bar and restaurant sales at a working men's club.

17. However, in practice, NFPs currently interpret the existing law differently. Very large NFPs, typically with tax advisors, are likely to be reporting member transactions as taxable (and deducting related expenses). However, few medium or small NFPs report member transactions as taxable (or deduct related expenses). No NFPs currently pay tax on subscriptions and levies.

18. Operationalising the most recent Inland Revenue view is expected to be a change to the status quo for about 9,000 NFPs. Many small and medium NFPs are likely to be required to file tax returns and pay income tax for the first time. This is because net income from member transactions and some subscriptions and levies will result in their taxable income exceeding $1,000, the concessionary threshold available for most NFPs that are not already tax exempt.

19. Inland Revenue could notify the sector of its current interpretation of existing law (it has not done so yet), or this matter could be included on the Tax and Social Policy Work Programme so that a policy response can be considered. A policy response may have a fiscal cost, but this would depend on which policy option(s) are progressed.

20. We will report to you on this issue in detail in the April–June quarter.

Integrity matter regarding donor-controlled charities

21. Donor-controlled charities are registered charities that are controlled by the settlor, the settlor's family, or associates. They raise tax integrity concerns because they can access tax benefits such as the donation tax credit and income tax exemption, but unlike other charities they do not have arm's length governance or distribution policies. In other countries these charities must comply with certain rules to qualify for tax concessions, however that is not the case in New Zealand.

22. The volume and value of donor-controlled charities are growing. s 6(c) [redacted]

23. We will report to you on policy issues concerning these charities in detail in the April–June quarter.

Next steps

24. Officials will provide you with reports on the pressing matter involving simplifying the law for NFPs, as well as the integrity matter regarding donor-controlled charities, in the April–June quarter.

25. We would welcome the opportunity to discuss any other matters raised in this report with you.

26. We are aware that Minister Louise Upston may write to you on certain tax matters and both she and Minister Nicola Willis have an interest in this sector. We recommend you share this paper with them, so that they are kept informed of this context.

Consultation with the Treasury

27. The Treasury was informed about this report.

Recommended action

We recommend that you:

28. **note** the contents of this report, and

    Noted

29. **refer** a copy of this report to the Minister of Finance for their information, and

    Referred/Not referred

30. **refer** a copy of this report to the Minister of Community and Voluntary Sector for their information.

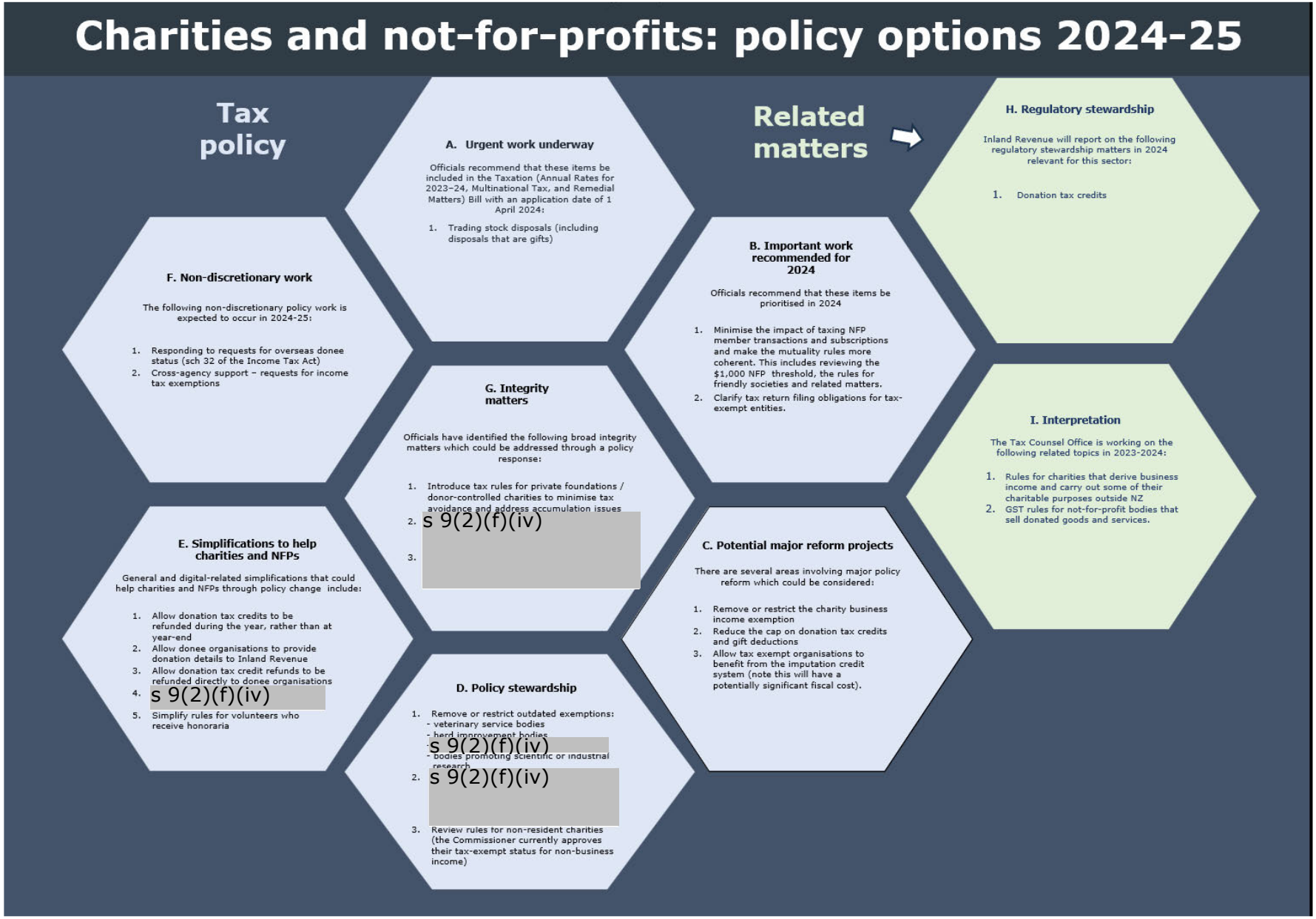
    Referred/Not referred

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
Policy and Regulatory Stewardship

Hon Simon Watts
Minister of Revenue
/ /2024

Appendix: Charities and not-for-profits – tax policy options



Inland Revenue
Te Tari Taake

POLICY AND REGULATORY STEWARDSHIP

Tax policy report: **Volunteers and honoraria: advice and response to the Minister for the Community and Voluntary Sector**

Date:	10 April 2024	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2024/161

Action sought

	Action sought	Deadline
Minister of Revenue	**Agree** to recommendations **Sign** the attached letter	10 April 2024

Contact for telephone discussion (if required)

Name	Position	Telephone
Stewart Donaldson	Principal Policy Advisor	s 9(2)(a)
Lucy England	Senior Policy Advisor	

10 April 2024

Minister of Revenue

Summary

Purpose

1. On 27 March 2024 the Minister for the Community and Voluntary Sector wrote to you outlining her concern that the tax rules relating to volunteers receiving honoraria may result in unreasonable compliance costs and policy overreach in some areas. One of her priorities is to minimise operational barriers for community organisations and the volunteers who support them.

2. This report explains the tax treatment of honoraria payments and outlines possible issues with the treatment that could be further explored by officials. A draft response to the Minister's letter is attached.

Background

3. On 20 March 2024 we provided you an overview of the charities and not-for-profits sector and related tax policy matters [IR2024/110 refers]. The appendix to that report included a list of possible simplifications to help charities and not-for-profits. One option was to simplify the rules for volunteers who receive honoraria.

4. As we noted in the overview, we will provide a further report to you in the June 2024 quarter with options to simplify the tax rules for not-for-profits (including the tax treatment of member transactions). As part of this, we will include advice on simplifications to the rules for volunteers who receive honoraria.

5. Any policy changes arising out of the simplification report could be included in the 2025–26 omnibus taxation bill following a period of thorough consultation with the sector. In discussions with officials, sector representatives have made clear their view that work in relation to member transactions in particular should not be rushed through, given the complexity and number of affected organisations.

Current law

6. In 2009 amendments were made to clarify the tax treatment of payments made to persons undertaking voluntary activity as follows:

    - an amount derived by a person in undertaking a voluntary activity is income of the person, unless –

    - the amount is a reimbursement payment to cover actual expenses incurred by a volunteer, or a reasonable estimate of the expenditure incurred by them, in which case it is exempt income of the volunteer.

7. Under this regime, payments that are 'honoraria' are taxable. An "honorarium" is defined as a below market rate amount received by a person for providing services that in the normal course no payment would be provided for. Honoraria are schedular payments, meaning the payer must withhold tax at 33%. Recipients of schedular payments over $200 must file an IR3 income tax return and financial

statements. They must also separately pay ACC levies as well as any other social policy obligations.

8. Alternative treatment exists for honoraria paid by Fire and Emergency New Zealand (FENZ) to their volunteers. This treatment was enacted in 2019 in response to a submission by FENZ to the Finance and Expenditure Committee citing concerns with compliance costs imposed by the schedular payment regime for volunteers. The amendment treats honoraria paid by FENZ to volunteers as salary and wages, so that they are subject to PAYE. This means that FENZ volunteers are no longer required to file income tax returns or financial statements, pay their own ACC levies or their own social policy payments. However, it also means they are not able to deduct their expenses. Officials did not consider extending this treatment beyond FENZ given the nature of the amendment which was made specifically in response to a narrow submission by FENZ to the Finance and Expenditure Committee.

Possible areas of reform

9. The following items could be further explored if you would like to progress work on tax issues relating to volunteers as part of the Tax Policy Work Programme.

Opt-in to PAYE regime for payments of honoraria

10. To reduce compliance costs for volunteers, community organisations could be given the option to treat payments of honoraria as salary and wages so that they are subject to the PAYE regime, as is the case for FENZ volunteers. The organisation could still reimburse the volunteer for their expenses without generating a tax liability.

Volunteer definition

11. The current definition of "volunteer" for the purposes of the reimbursement income exemption requires that the person 'undertake freely in New Zealand' an activity that benefits the community or another person and for which there is no purpose or intention of private pecuniary profit for the person.

12. The requirement that the activity take place in New Zealand is an issue when volunteers undertake work offshore for a New Zealand based organisation. For example, FENZ sent firefighters to Australia to assist with the emergency response to the 2019-20 bush fires. In relation to their activity in Australia, the firefighters would not be considered "volunteers" and therefore would be required to pay income tax on reimbursement payments made by FENZ to them for their work in Australia. This issue has previously been raised with PaRS in relation to missionaries.

13. This could also be addressed in our report to you in the June quarter.

Consultation

14. We have provided this report to the Department of Internal Affairs for their information.

Next steps

15. We will provide further advice on progressing simplifications to the tax treatment of honoraria as part of a wider report on possible tax simplifications not-for-profits in the June 2024 quarter.

Recommended action

We recommend that you:

16. **note** that officials will provide you further advice on reforming the tax treatment of honoraria as part of a wider report on simplifying the tax rules for not-for-profits in the June 2024 quarter, with a view to any reform being included in the 2025–26 omnibus taxation bill, and

    Noted

17. **sign** a copy of the attached letter to the Minister for the Community and Voluntary Sector.

    Signed/Not signed

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
Policy and Regulatory Stewardship

Hon Simon Watts
Minister of Revenue
/ /2024

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: Tax policy options for the not-for-profit sector

Date:	17 July 2024	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2024/237

Action sought

	Action sought	Deadline
Minister of Revenue	**Agree** to recommendations	6 August 2024

Contact for telephone discussion (if required)

Name	Position	Telephone
Peter Frawley	Policy Lead	s 9(2)(a)
Stewart Donaldson	Principal Policy Advisor	
Lucy England	Senior Policy Advisor	

17 July 2024

Minister of Revenue

Tax policy options for the not-for-profit sector

Purpose

1. On 20 March 2024 we provided you with an overview of the not-for-profit (NFP) sector.[1] The report included information about the 90,000 NFPs on IR systems, recent legislative change for the sector, and a summary of current policy work. We indicated that we would provide you with more advice about tax policy options for the charitable and not-for-profit sector.

2. This report provides further policy context and recommends that you consider a number of possible NFP policy items for inclusion on the Tax and Social Policy Work Programme (TSPWP). It also provides requested advice on tax policy issues concerning the income tax exemption for charity business income.

3. Depending on which issues are progressed, there could be broad impacts on the NFP sector and the communities they serve. At this stage we have not made an assessment about what the overall impact might be.

4. We have supplemented this report with a detailed report about the tax treatment of not-for-profit member transactions and options for simplification (IR2024/238 refers).

5. We plan to report to you on the draft TSPWP shortly. At that point, some trade-offs may be required if you consider resources are better deployed progressing other priorities. A more detailed report about the charity business income tax exemption will be provided in August.

Background

Tax concessions

6. New Zealand adopted a policy of exempting charities from taxes as early as 1879, when broad exemptions were given to all not-for-profit organisations. Underlying this policy is a view that the Government should give up some of its taxing rights to support certain organisations which provide a public benefit.

7. Tax concessions should be subject to continual monitoring and review. They should effectively meet policy objectives relative to alternative methods of providing assistance. They should also align with the Government's Revenue Strategy, ensuring the tax system finances public expenditure in a fair and efficient way, economic decisions are biased as little as possible, and there are limits to the number of tax provisions that provide preferential treatment.

8. The existing concessionary tax treatment for NFPs generally varies depending on the extent of the public benefit they provide. It is made up of income tax exemptions, tax concessions for donors , GST concessions, and FBT concessions for certain employees. Charities registered under the Charities Act 2005 and school boards of trustees exempted under the Education and Training Act 2020 typically

[1] IR2024/110 *Charities and not-for-profits overview*

receive most of these concessions. Clubs and societies which benefit their members and provide minimal public benefit receive fewer tax concessions.

9. The concessions which exist today have developed over many years:

- in the 1940s the current tax exemption for charity business and non-business income was legislated;
- in the 1950s income tax exemptions were introduced for regional promotion, veterinary, herd improvement and scientific research bodies;
- in the 1960s donation tax incentives were introduced for individuals (extended to companies in the 1970s and Māori authorities in the 2000s);
- from the 1970s, NFPs received a de minimis exemption so that small organisations did not have to file income tax returns (initially $500 income in 1972, which increased to $1,000 from 1979);
- in the 1980s GST and FBT concessions were introduced for NFPs;
- in the 2000s the Charities Commission was established and the size of donation tax incentives were substantially increased.

10. These concessions allow the sector to be categorised for tax purposes:

- tax charities – entities registered under the Charities Act 2005 whose status generally results in an income tax exemption. This category also includes a small number of non-resident charities approved as a tax charity by the Commissioner;
- donee organisations – whose status gives tax benefits to donors who make monetary donations to them. This category includes schools and educational institutions, charities and organisations with cultural, philanthropic and benevolent purposes;
- charitable organisations – organisations that benefit from various concessions under the FBT rules (effectively a subset of donee organisations); and
- other not-for-profit organisations – not otherwise covered above but with a public character and which can access tax exemptions and/or other administrative concessions.

11. The sector can alternatively be viewed with a regulation lens, which demonstrates the complex environment within which NFPs and charities operate. NFPs are typically charitable trusts and societies incorporated under the Charitable Trusts Act 1957, societies incorporated under the Incorporated Societies Act 2022, companies registered under the Companies Act 1993, or unincorporated entities. The former three categories of NFPs are regulated by MBIE. The Ministry of Justice administers the Charitable Trusts Act. If NFPs have charitable purposes they may also qualify to voluntarily register under the Charities Act 2005 (to access tax concessions) and they are regulated by DIA. In addition, the Attorney General is the "protector of charities" and can inquire into any charity (whether registered under the Charities Act or not).

International comparison

12. Most OECD countries provide income tax exemptions and donor tax concessions for the sector although there can be significant differences in their design. For example:

- New Zealand's donation tax concessions are generous compared with most other countries and benefit a wide range of NFPs (for example, we allow a concession for donations to religious organisations whereas Australia does not);
- We do not allow tax exempt entities to receive imputation credit refunds, whereas Australia refunds franking credits to tax exempt entities;
- We provide an exemption for charity business income, whereas most other OECD countries do not;
- We do not have specific rules for private charitable foundations (donor-controlled charities), in contrast to Australia, Canada and the US.

Stakeholder priorities

13. Tax concessions for NFPs have been considered and publicly consulted in almost every tax review, from the 1967 Ross Report through to the 2018 Tax Working Group. They have also been mentioned in related reviews, such as the 2018 Charities Act Modernisation Review. Two issues often raised by stakeholders within the NFP sector are discussed below.

Review the charitable purpose definition

14. Stakeholders have called for a review of the charitable purpose definition which determines which entities are eligible for tax concessions. For example, a submitter on the Taxation (Annual Rates for 2023-24, Multinational Tax, and Remedial Matters) Bill, Sue Barker Charities Law, recommended that no further "piecemeal" amendments be made to the tax rules for charities pending the commencement and completion of a first principles post-implementation review of the Charities Act, including subjecting the definition of charitable purpose to a comprehensive review.

15. We note that the current Minister of the Community and Voluntary Sector has ruled out a first principles review (including a review of charitable purpose) at this time.

16. For context, Charities Services within DIA is responsible for administering the Charities Act 2005 and determining whether entities can register under that Act. To be registered as a charity, an organisation must have charitable purposes and its purposes and activities must provide benefits to the public.

17. There are four categories of charitable purposes in the Charities Act:
    - Relieving poverty
    - Advancing education
    - Advancing religion
    - Other purposes beneficial to the community.

18. The Charities Act extended the common definition of charitable purpose to include the promotion of amateur sport in certain circumstances. It also extended the public benefit test to include charities whose beneficiaries are related by blood. This means an Iwi working for its people can register as a charity and be tax exempt.

19. The courts have interpreted these purposes more broadly over the years as society has changed.

20. An entity must register under the Charities Act and also be considered by the Commissioner of Inland Revenue to have charitable purposes in order to qualify for an income tax exemption and other tax concessions. The definition of charitable

purpose that is used by the charities regulator is, for practical purposes, the same as that used by Inland Revenue.

21. Previous Governments have generally rejected approaches by certain taxpayers to change the Income Tax Act to confirm they are eligible for charity tax concessions. This is on the basis that a taxpayer-specific amendment would remove oversight of the entity by the charity regulator under the Charities Act. A notable exception is the tax exemption provided for community housing trusts and companies. This specific tax exemption was legislated in 2016 because the charitable status of community housing providers who provide financial assistance to low-income households to purchase their own home was not clear.

22. Our advice is that a review of charitable purpose should be part of a review of the Charities Act rather than the Income Tax Act. We also note that any extension of the definition of charitable purpose is likely to have a direct impact on tax exemptions and donor concessions and therefore have a fiscal cost.

Refunding imputation credits to charities/exempt entities

23. Tax exempt organisations are currently unable to benefit from the imputation credit system because the credits are non-refundable. The only exception is for tax exempt organisations that invest in Māori authorities, as Māori authorities can convert imputation credits into refundable Māori authority tax credits.

24. Stakeholder groups such as Philanthropy New Zealand have lobbied to introduce some form of imputation credit refundability. They point out that the lack of refundability creates a distortion which biases exempt entities towards investing in debt securities, overseas equities, untaxed NZ equities, or investing directly in their own businesses.

25. Our advice is that a decision to refund imputation credits makes sense in the context of maintaining the exemption for business activities of charities. However, a policy change will have a fiscal cost (based on 2020 estimates the cost could be $70m-$100m per annum) and would need to be carefully worked through to prevent a range of tax avoidance arrangements.[2] Further, if you intend to remove the exemption for business activities of charities, then a change to refund imputation credits would need to be carefully considered to ensure the policy settings are coherent. While there are policy options to reduce the fiscal cost and deter avoidance under the current legislative settings, we do not intend to provide further policy advice on this option unless you would like it added to the TSPWP.

Potential areas of reform

26. There are several potential areas of tax reform for the sector which could be undertaken at the same time or consecutively over a period of time. We recommend that any change is subject to public consultation, for example by way of a Government discussion document.

Member transactions and options for simplification

27. Inland Revenue and the sector consider the most pressing NFP tax issue to be the tax treatment of income derived by NFPs from trading with their members, including

[2] Imputation credits are likely to be streamed to tax-exempt entities if they can seek refunds of the credits. For example, shares could be sold to tax-exempt entities immediately before an imputed dividend distribution and the imputation credit refund could be shared between the vendor and purchaser through the sale price of the shares.

membership subscriptions and levies. This issue is discussed in more detail in IR2024/238.

Policy objective

28. Consistent with a broad-based low-rate framework, NFPs should generally pay tax on their net income. This is supplemented by an objective of reducing compliance costs for NFPs which derive small amounts of income which may justify a de minimis type exemption.

Framework

29. The policy framework taxes profits from NFP member transactions, either at an entity level or member level where profits are paid to members as rebates. NFPs that have a constitution that prohibits a distribution of property to members are eligible for a deduction from net income (currently up to $1,000).

Analysis

30. Before 2003, the Commissioner's interpretation of the law was that income derived from member transactions was not taxable. However, this interpretation was withdrawn in 2003. The Commissioner intends to publicly consult on operationalising a new interpretation in late 2024 which states that trading income derived by an association (such as an NFP) from transacting with its members is taxable. The new interpretation also states that income derived by an association in relation to membership subscriptions, fees and levies may be taxable in line with ordinary income concepts. This is a shift from current IR guidance which says these are not taxable.

31. We estimate that 9,000 not-for-profits are not currently reporting income from member transactions, subscriptions fees and levies and will be affected by this new interpretation. Operationalising the new interpretation would result in a fiscal gain of between $10-20 million per annum. This gain would not impact on allowances. The affected groups would include a wide range of NFPs including service providers, social clubs including cosmopolitan clubs, professional associations, industry groups and unions.

Policy options

32. We support the new interpretation from a policy perspective as it aligns with normal income tax principles and a broad-base low-rate framework. However, if you are concerned about the impacts of the new interpretation on the sector, we recommend that you commission policy work on possible ways to mitigate some of these impacts for small NFPs (which may have a fiscal cost). We also recommend that you consider addressing related policy issues including return-filing obligations for NFPs, the resident withholding tax (RWT) exemption for NFPs, and related out-of-date income tax exemptions including the substitutable exemption for member transaction income that exists for friendly societies and credit unions.

Charitable business income tax exemption

Policy objective

33. The policy objective for the charitable income tax exemption is to support charities subject to the regulation and public reporting requirements of the Charities Act 2005,[3] for the reasons outlined at paragraph 6.

Framework

34. The income tax exemption framework for registered charities takes a "destination of income" approach. This means that income is tax exempt if it is derived by a registered charity and is ultimately destined for a charitable purpose. Income can be accumulated for many years within a registered charity, or within its registered business subsidiaries, and will still qualify for the tax exemption.[4]

35. The framework provides income tax exemption on a targeted basis. Since 1940, charity business income has been exempt to the extent the registered charity carries out its charitable purposes in New Zealand, whereas charity investment income is wholly exempt. The policy rationale for this distinction was articulated in the following policy advice in 1940:

    "In the case of business income, the tax-free charity obtains a definite advantage over competitors and should not be allowed to use that advantage except for charitable purposes in New Zealand. In the case of investment income, the asset (whether money or land) is lent to others to use in their business operations in consideration of the payment of interest or rent at market rates [and full exemption is given wherever the investment income is used]."

Analysis

36. Most OECD countries, with the notable exceptions of Australia, New Zealand and Malta, have responded to a widespread perception that exempting business income from tax may create an unfair competitive advantage, as well as revenue loss concerns. These countries have either restricted the commercial activities a charitable entity can engage in, or they tax commercial income if the commercial income is unrelated to charitable purpose activities and is accumulated. This is commonly referred to as "unrelated business income".

37. The policy setting for charitable business income tax exemption should be considered in the context of the policy setting for imputation credits. The latter does not allow tax exempt organisations to benefit from imputation credit refunds. This creates several investment distortions including a bias for charities to carry out business activities themselves. As a result, a high proportion of New Zealand charities engage in business activity. This activity includes property development, farming, tourism, fishing, electricity generation and distribution and food production. s 6(c)

38. Commercial activities carried out by Māori collective entities, such as Māori Trust Boards and Post Settlement Governance Entities, tend to be concentrated in the property, forestry, and fisheries sector. A number of these activities, in particular

[3] From 2020-21, businesses must be registered charities in order to access the charity business income tax exemption. Previously a business carried on by, or for the benefit of, a registered charity could access the exemption without being a registered charity.

[4] The Department of Internal Affairs (Charities Services) have introduced a new annual requirement that, from 2024-25, medium and large sized registered charities report how they plan to use their accumulated funds.

fisheries settlement assets, are conducted using registered charities. The purpose of these entities is usually to fund the wider social and economic aspirations of the relevant iwi over a multi-generational time horizon.

39. In practice, the current rules for charity business income which distinguish domestic and international charitable purposes are difficult to apply and enforce. For the last three years, the department's Tax Counsel Office has consulted on how these rules should be interpreted.

40. Removing the tax exemption for passive investment and business income would be consistent with New Zealand's broad-base, low-rate (BBLR) tax policy framework as it would broaden the tax base.

41. Removing the charity business income tax exemption only would result in a fiscal gain. Our estimate is that the gain could be between $60m and $200m per annum. However, the quantum of the gain will be significantly affected by policy design and any behavioural responses. There will be a distortion if passive income remains untaxed.

42. International experience suggests that removing a business income tax exemption would not raise significant amounts of tax revenue and would be subject to ongoing dispute and litigation. In the US, where an unrelated business income tax was introduced at a federal level in the 1950s and is a stable regime with few legislative amendments, litigation typically focuses on whether a trade or business exists and whether the trade or business is substantially related to charitable purposes.[5]

43. Any change to the status quo will result in strong push-back from a large part of the charitable sector. Many charities view business activities as a means to have diverse and sustainable income, in addition to grants and donations. Any change would increase compliance costs for affected charities, which they may attempt to mitigate by restructuring, behaviour change, and/or seeking an increase in Government support by way of grants. Many will contend that taxing profits accumulated in their businesses will ultimately impact directly on people in need, as the amount of benefits delivered to those people in future will be reduced by the tax collected and related compliance costs.

Policy options

44. Policy options for the charity business income tax exemption include to maintain the status quo, consult on integrity measures to make the status quo more effective, or consult on moving towards a new framework that would tax more business income of charities. We will report separately to you in August with more detail on these policy options.

Donation concession cap

Policy objective

45. The policy objective for donation tax incentives is to reinforce and encourage giving.

[5] Professor Mark Sidel, University of Wisconsin-Madison, presenter at the 2024 Charity Law Association of Australia and New Zealand (CLAANZ) Annual Conference on 4 July 2024.

Framework

46. The donation framework restricts tax concessions to qualifying donations[6] which must be made to approved donee organisations. The concessions are subject to a maximum claim (cap).

47. Individuals claim donation tax credits (DTCs) which are 33 1/3% of the amount donated. Companies and Māori authorities are eligible for gift deductions, which typically have a tax value of 28% and 17.5% respectively.

Analysis

48. New Zealand's donation tax incentive for individuals is generous by international standards. This is due to a combination of factors:

- it is payable as a refundable tax credit, whereas the norm is to allow a donation income tax deduction,
- it is set at a relatively high rate of 33 1/3%,
- it has a high maximum claim (cap), and
- the list of eligible donee organisations is relatively large.

49. Prior to 2008-09 there was a $630 maximum DTC limit for individuals and a five percent deduction limit on donations made by companies and Māori authorities. However, since 2008-09 the total amount of qualifying donations has been capped at the individual donor's taxable income and, for companies and Māori authorities, at their net income. This means the Crown is in effect forgoing revenue that could be spent on Government priorities and is instead directed towards the preferred causes of individuals donors. The increase in the cap has also resulted in an increase in donation fraud and arrangements involving tax avoidance.

50. The aggregate value of DTC claims increases every year. For the year ending 31 March 2023, $1.1 billion donations were subject to tax claims, with a tax value of $341m. Approximately 350,000 individuals make claims each year, with 63% of the value of donations going to religious organisations, 8% to schools and 29% to other donee organisations.

51. An academic (Amy Cruickshank) has recently looked at how responsive reported donations are to the credit.[7] She concluded that the current DTC design is not "Treasury efficient" as the absolute value of elasticity is less than 1. Based on her research, for every $1 in credit given by government, reported donations increase by $0.40 to $0.70 on average. Since the elasticity may reflect both reporting effects and an actual donation response, the actual donation response could be anything between zero, or very small, "up to" the reported donation elasticity. This means the increase in donations due to the DTC is less than foregone tax revenue of the government. However, she notes that this efficiency consideration should be weighed against other policy objectives. For example, whether DTC credits are justifiable because they empower the community to decide funding priorities.

Policy options

52. Our advice is to consider reducing donation tax incentives to manage the associated tax expenditures and counter the incentives for fraud and tax avoidance. The impact of the change could be softened by providing more flexible rules, for example

[6] These are restricted to money and in-kind donations are generally excluded, with the exception of donated trading stock, which is subject to new rules from 1 April 2024.
[7] Source: Cruickshank, A. (2022). Elasticity of reported donations: Bunching evidence from New Zealand. *Working Papers in Public Finance*, Victoria University Chair in Public Finance (21/2022).

allowing DTC refunds to be made immediately instead of at year-end (see simplification reform options, below).

53. Depending on the level, a lower DTC cap could affect a relatively small volume of donors and result in a significant fiscal gain. For example, if eligible donations were capped at $15,000 (a maximum DTC of $5,000), this would result in a revenue gain of approximately $60 million per annum and reduce claims for approximately 8,000 donors (just over 2% of the 350,000 donors who currently make DTC claims).

54. While this change would be relatively simple to implement, it would impact on donor behaviour, which is difficult to estimate (behaviour change has not been taken into account in the above estimate) and may require one or more additional policy responses. For example:

- Some donors may make donations through companies they control, which are subject to a higher cap on donations of money (the company net income) and can obtain tax concessions for donations of trading stock which are not capped. The corporate gifting cap would need to be reviewed for a DTC policy change to be coherent.
- Some donors may use family trusts to distribute beneficiary income to charities (which would not be subject to income tax).

Donor-controlled charities

55. The term "donor-controlled charity" refers to charities registered under the Charities Act 2005 that are controlled by the settlor, the settlor's family, or associates. They include what are often referred to as private foundations.

56. Donor-controlled charities receive significant tax benefits. s 6(c)

s 9(2)(g)(i)

57. Comparable countries such as the US, Canada and Australia specifically define donor-controlled charities in their tax legislation. Tax concessions are only available if these charities comply with rules relating to associated party transactions and minimum distributions. In New Zealand donor-controlled charities are not defined and they can access the same tax concessions as other publicly supported charities. As such, individuals can establish a charity and access donor and charity tax benefits while retaining control over the charity's governance, investment decisions and transactions.

58. We are aware of examples where donor-controlled charities have entered into transactions with persons associated with the settlor that may not be on arm's length terms. These transactions give rise to valuation issues and can result in circular wealth transfers from the foundation back to the settlor and their associates. Existing anti-avoidance provisions, including a donation-specific provision effective from April 2019, can be difficult to apply in these situations, particularly due to the lack of specific rules for donor-controlled charities.

59. We are also aware of examples where donor-controlled charities and their donors have accessed significant tax concessions, however, the charities have accumulated funds and distributed minimal or no amounts for the public benefit. We are concerned about timing mismatches between a charity accessing a tax concession and applying the relevant funds towards a public benefit when donors effectively control the charitable funds within a charity.

60. Any reform for donor-controlled charities would have the policy objective of changing donor behaviour to ensure donations made to donor-controlled charities are used for charitable purposes. This behaviour change is likely to be fiscally neutral, or have only a small fiscal gain depending on the design of the reform to reduce timing mismatches. Potential changes have not been costed at this stage.

61. Our advice is to consider reform to address tax-related issues with donor-controlled charities.

Concessions which are difficult to justify

62. There are several concessions available to NFPs which in our view have become out-of-date and/or are difficult to justify today. These are outlined below. There will be a fiscal gain if the concessions are narrowed or removed, however potential changes have not been costed at this stage.

s 9(2)(f)(iv)

Tax exemptions introduced in the 1950s

69. Some income tax exemptions have outlived their original purpose. Exemptions for veterinary clubs, herd improvement bodies, bodies promoting scientific or industrial research, s 9(2)(f)(iv) , date back to the 1950s. Entities benefitting from them may now be revenue-generating businesses competing directly with taxpaying businesses or may provide funding to those private

s 9(2)(f)(iv)

businesses. Others may qualify to register as tax exempt charities, so the existence of these exemptions results in unnecessary complexity and inconsistent tax outcomes for NFPs that are factually similar.

70. The revenue that would result from removing these exemptions has not been quantified. Approximately 100 veterinary service bodies, 100 herd improvement bodies s 6(c) , 100 bodies promoting scientific or industrial research, s 9(2)(f)(iv) could be affected. The final impact would depend on changes to other settings, including the approach that is taken to NFP member trading transactions and subscriptions, discussed in IR2024/238.

71. Our advice is to consider reform with a view to removing income tax exemptions which are no longer justified.

Tax exemption for non-resident charities

72. Non-resident charities which carry out all of their charitable purposes outside New Zealand can apply to the Commissioner to obtain a tax exemption for their non-business income derived in New Zealand. This includes rental income from property investment, dividend income from securities or interest income from money deposited in a bank account.

73. The Commissioner will approve the application if in his view the non-resident charities have a charitable purpose and are unable to register under the Charities Act because they have no significant presence in New Zealand.

74. The policy rationale for this tax exemption is to treat non-resident charities and New Zealand resident charities consistently on charitable purpose grounds, so non-business income is tax exempt irrespective of where charitable purposes are carried out. Providing a tax exemption to non-resident charities also removes barriers for them to invest in New Zealand. Without an exemption they would require a higher pre-tax return in order to invest here.

75. Our view is that this rationale is no longer justified. There are weak grounds to provide a tax exemption for non-business income derived by non-resident charities which have no charitable purposes in New Zealand, when other non-resident entities are subject to tax on their New Zealand non-business income.

76. Australia does not offer the same concessionary treatment for non-resident charities. Instead, they must satisfy an "in Australia" requirement to obtain an income tax exemption. This requirement means that charities that do not have a physical presence in Australia, do not incur expenditure or pursue their objectives principally in Australia, do not have the Australian equivalent of New Zealand's donee status, and will not qualify for an income tax exemption in Australia.

77. At present approximately 300-400 non-resident charities have obtained this approval in New Zealand, although some of these organisations may no longer be active or no longer have investments here. They are typically non-resident universities, religious organisations and private charitable foundations which have been granted tax exemption status in their own jurisdiction. Most are located in the USA, the UK and Australia.

78. Our advice is to consider reform with a view to removing the income tax exemption for New Zealand non-business income derived by non-resident charities which have no charitable purposes in New Zealand.

Simplifications relating to volunteers and donations

79. There is a range of policy options which could enhance measures that support the NFP sector. This could take into account the broader (non-tax) context of how the Government wants to support the sector. Three potential priorities are listed below. The exact fiscal impact of each hasn't been assessed but would depend on design and behavioural response. Simplification suggestions directly relevant to the tax treatment of not-for-profit member transactions are discussed in IR2024/238.

Volunteers

80. In April 2024 we provided the Minister of Revenue an overview of the income tax rules relating to volunteers and honoraria, in response to a letter from the Minister for the Community and Voluntary Sector [IR2024/161 refers].

81. Under current rules, payments made to volunteers that are 'honoraria' are taxable. An 'honorarium' is defined as a below market rate amount received by a person for providing services that in the normal course no payment would be provided for. Honoraria are schedular payments, meaning the payer must withhold tax at 33%. Recipients of schedular payments over $200 are asked to provide additional information if they receive an automatic assessment (as they have the opportunity to deduct related expenses). They must also separately pay ACC levies as well as any other social policy obligations.

82. Alternative treatment was enacted in 2019 for honoraria paid by Fire and Emergency New Zealand (FENZ) to their volunteers. The amendment treats these specific honoraria as salary and wages, so that they are subject to PAYE. This means that FENZ volunteers receive automatic assessments without a request for information, and no longer pay their own ACC levies or their own social policy payments. Officials did not consider extending this treatment beyond FENZ at the time, given the amendment was made specifically in response to a narrow submission by FENZ to the Finance and Expenditure Committee.

83. The definition of 'volunteer' for the purposes of the reimbursement income exemption could also be reviewed. At present, the definition requires the volunteer activity to take place in New Zealand. This is an issue when volunteers undertake work offshore for a New Zealand based organisation.

84. Our advice is to consider reform with a view to simplifying the tax rules for volunteers.

Donations

85. Simplifying the rules for donation tax credits could reinforce and encourage charitable giving, would give the rules more integrity, and in some cases reduce compliance and administrative costs.

86. Three simplification suggestions have been raised with officials in the past. We anticipate some of these suggestions and further insights will be raised in the Inland Revenue regulatory stewardship review of donation tax credits currently underway and due to report later this year. The fiscal impact of these suggestions has not been quantified at this stage.

87. These suggestions could be considered instead of, or in addition to, a review of the donation concession cap as outlined above.

Allow donation tax credit refunds to be released before year-end

87.1 Currently, DTC refunds cannot be released to donors until after the conclusion of a tax year, and in some cases not until an income tax return is

filed. A large number of claims are made at this time which puts pressure on Inland Revenue to risk-assess, verify and refund DTCs within a narrow timeframe. Research has also found that donation tax incentives will be more effective if refunds are given closer to the time of the donation. Policy officials could consult with a view to allowing DTCs to be refunded before year-end in certain circumstances.

Allow donee organisations to provide donation details to Inland Revenue

87.2 Donors wishing to claim a DTC refund must provide their donation details and receipts to either Inland Revenue or their tax agent. This can be a time-consuming process for donors, tax agents and Inland Revenue. To reduce compliance and administration costs and improve integrity, donee organisations could instead be offered the option of electronically providing details to Inland Revenue about the donations they have received which Inland Revenue could then use to pre-populate DTC refund claims. The feasibility of implementing this option in a given timeframe would need to be tested. We note that a similar proposal relating to FamilyBoost would have taken between 2-3 years to implement and was not progressed for this reason. The design would also need to ensure this approach reinforces and encourages giving, rather than create a fiscal cost with no change to donation behaviour.

Allow donation tax credit refunds to be refunded directly to donee organisations

87.3 Many donors use their DTC refunds to make further donations. At present, Inland Revenue does not allow DTC refunds to be made into the bank accounts of anyone other than the donor (and certain tax intermediaries). Some donors and donee organisations have requested a simplification that would enable donation tax credits to be refunded directly to the bank account of one or more donee organisations. Allowing DTC refunds to go directly to a donee organisation could simplify the process for donors and encourage further charitable giving.

88. Our advice is to consider reform with a view to simplifying the tax rules for donation tax credits.

Consultation

89. The report was reviewed by The Treasury and the Department of the Prime Minister and Cabinet. It was provided to the Department of Internal Affairs and the Ministry for Business, Innovation and Employment for their information.

Next steps

90. We recommend that you consider adding NFP matters to the TSPWP. The scope of a NFP review could include several options, as described above.

91. We plan to report to you on the draft TSPWP shortly. At that point, some trade-offs may be required if you consider resources are better deployed progressing other priorities.

92. A more detailed report about the charity business income tax exemption will be provided in August.

93. We recommend that any changes are subject to public consultation, for example by way of a Government discussion document.

94. If you wish to progress this work, we recommend discussing this with the Minister of Finance and the Minister for the Community and Voluntary Sector in due course.

Recommendations

We recommend that you:

a) **note** that we will report separately to you about the charity business income tax exemption in August.

Noted

b) **agree** to consider including items involving charities/not-for-profits on the Tax and Social Policy Work Programme as part of your upcoming discussions with officials on that Programme.

Agreed/Not agreed

c) If you agree to (b), **note** that report IR2024/238 contains specific recommendations in relation to not-for-profit member transactions and related options for simplification.

Noted

d) If you agree to (b), **agree** that the scope of the charities/not-for-profits work to be considered for the TSPWP would include:

		Minister of Revenue
(i)	a review of the donations tax credit cap **(fiscal gain)**;	Agreed Not agreed
(ii)	concessions which are difficult to justify **(fiscal gain)**;	Agreed Not agreed
(iii)	donor-controlled charities **(fiscally neutral / small fiscal gain)**;	Agreed Not agreed
(iv)	simplifications relating to volunteers and donations **(fiscally neutral / small fiscal cost subject to design)**;	Agreed Not agreed
(v)	allowing imputation credits to be refunded to charities / exempt entities **(fiscal cost – we do not recommend this option)**.	Agreed Not agreed

e) **refer** a copy of this report to the Minister of Finance.

Referred/Not referred

f) **refer** a copy of this report to the Minister for the Community and Voluntary Sector for their information.

Referred/Not referred

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
Inland Revenue

Hon Simon Watts
Minister of Revenue
/ /2024

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **The income tax treatment of not-for-profit member transactions and options for simplification**

Date:	17 July 2024	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2024/238

Action sought

	Action sought	Deadline
Minister of Revenue	**Agree** to recommendations	6 August 2024

Contact for telephone discussion (if required)

Name	Position	Telephone
Stewart Donaldson	Principal Policy Advisor	s 9(2)(a)
Lucy England	Senior Policy Advisor	

17 July 2024

Minister of Revenue

The income tax treatment of not-for-profit member transactions and options for simplification

Purpose

1. This report outlines the Commissioner of Inland Revenue's currently unpublished interpretation of the income tax rules relating to transactions between a not-for-profit body (NFP) that is not exempt from tax and its members (the "new interpretation") and outlines the impact of the new interpretation on the NFP sector.

2. The Commissioner intends to publicly consult on the new interpretation in late 2024 with a view to operationalising it soon after. We estimate that 9,000 not-for-profits are not currently reporting income from member transactions, subscriptions fees and levies and will be affected by this new interpretation. The affected groups would include a wide range of NFPs including service providers, social clubs including cosmopolitan clubs, professional associations, industry groups and unions.

3. We support the new interpretation from a policy perspective. However, if you are concerned about the impacts of the new interpretation on the sector, we recommend that you commission policy work on possible ways to mitigate some of these impacts for small NFPs (which may have a fiscal cost). We also recommend that you consider addressing related policy issues including return-filing obligations for NFPs, the resident withholding tax (RWT) exemption for NFPs, and related out-of-date income tax exemptions including the exemption for member transaction income that exists for friendly societies and credit unions.

4. We recommend you discuss this possible work with officials as part of your discussions with them on the Tax and Social Policy Work Programme (the TSPWP).

5. This report supplements IR2024/237 which provides a general overview of tax policy options for the not-for-profit sector.

Background

6. The Income Tax Act 2007 contains specific rules relating to transactions carried out between an association and its members ("member transactions"), such as the sale of food and drinks by a cosmopolitan club to its members.

7. Before 2003, the Commissioner's interpretation of the law was that income derived from member transactions was not taxable. However, this interpretation was withdrawn in 2003 on the basis that it was not supported by the legislation.

8. Inland Revenue has not published a clear alternative view since then, and in practice member transactions have been subject to inconsistent tax treatment by taxpayers. This inconsistent treatment was identified by IR compliance staff and escalated to the department's Tax Counsel Office (TCO), and in 2022 an updated interpretation was outlined in a draft operational statement. The new interpretation confirms that income derived from member trading transactions is in fact taxable and that related expenditure is deductible.

9. The new interpretation also states that membership subscriptions, fees and levies may be taxable for NFPs under ordinary concepts of income. This is a shift from current IR guidance which says these are not taxable.

10. The new interpretation is consistent with standard income tax principles and a broad-base low-rate framework. However, operationalising the new interpretation would have implications for approximately 9,000 NFPs which have not been returning income from member trading transactions and membership subscriptions, fees and levies collected by them. For this reason, external stakeholders (for example, CA ANZ) have previously recommended that IR consider a policy response to the new interpretation before it is operationalised.

11. The affected NFPs primarily include incorporated societies. As explained in IR2024/110, incorporated societies are currently undertaking considerable reorganisation with approximately 24,000 societies making a decision whether to re-register under the Incorporated Societies Act 2022 between October 2023 and April 2026. As part of re-registration they will need to prepare a compliant constitution and in some cases adopt new processes. It is therefore timely to raise and address the new interpretation to provide more certainty for NFPs which are deciding whether to re-register.

The Commissioner's new interpretation of the law

The tax treatment of member transactions

12. The new interpretation states that trading income derived by an association (such as an NFP) from transacting with its members is taxable. Expenditure incurred by an association in deriving income from transactions with their members is deductible in line with the general deduction rules.

13. An association that is able to distribute surpluses derived from their member transactions to members can claim a deduction for these distributions. An association that provides members with a distribution equal to the full amount of its surplus in the same income year will therefore not have a net tax liability in relation to their member transactions. However, not all associations can distribute amounts to members; for example, associations that are incorporated societies have clauses in their governing documents preventing them from making distributions. Most NFPs will have a non-distribution clause in their constitution, and this clause is also required for them to access the standard NFP $1,000 deduction (described in more detail at paragraph 20).

14. The new interpretation is different to IR's previous interpretation, withdrawn in 2003, which states that member transactions are not taxable. It also overrides the common law principle that associations are not taxable on income derived from within their circle of membership to a significant extent.

15. We support the new interpretation on member transactions from a policy perspective as it aligns with normal income tax principles and a broad-base low-rate framework. However, it raises legitimate questions about the appropriate level of compliance costs imposed on small NFPs for little to no fiscal gain.

The tax treatment of membership subscriptions, fees and levies

16. The new interpretation also states that income derived by an association in relation to membership subscriptions, fees and levies may be taxable in line with ordinary income concepts. This will depend on the circumstances of the NFP in question. A fact-specific enquiry is required and examples will be provided in guidance when the new interpretation is consulted on and subsequently operationalised. This

position differs from current IR published advice that subscriptions and levies are not income for tax purposes.

17. We also support this view from a policy perspective as it accords with standard income tax principles and a broad-base low-rate framework, and note again that it raises questions about the appropriate level of compliance costs for small NFPs.

Illustrative example: operationalising the new interpretation for a chartered club

The South Wellington Metropolitan Club Inc (the Club) is an incorporated society with 3,000 members. The Club has a rule prohibiting distribution of assets to members on wind-up.

Its clubrooms are a popular place for members and non-members to spend time playing a variety of games and eating and drinking in the restaurant and bar.

Members pay subscriptions to belong to the Club and visit the clubrooms but the Club charges for many activities and all food and beverages must be purchased from the Club.

Tax treatment

The Club is required to return as business income the amounts it charges for activities and for food and beverage supplied to both members and non-members.

The Club is also required to include subscription revenue in its annual income tax return. This is because the Club's rules prohibit distributions to members on wind up and because the nature of the Club's activities mean it is operating on a commercial level and so the subscriptions are not capital but are income derived from a business.

The Club can deduct expenditure incurred in running the restaurant, bar, events, and also any expenditure on activities that generate income, such as collecting subscriptions.

Impact of the new interpretation on NFPs

18. A summary of the tax status of entities within the NFP sector, based on 2022 data, is provided in the Appendix. Out of the 90,000 NFPs shown as active on Inland Revenue's records, most are tax exempt and not affected by the matters raised in this paper. We estimate that up to 29,000 NFPs are not tax exempt and either report taxable income or losses (4,000) or are not filing returns because they consider their income falls below $1,000 (25,000) (due to the standard $1,000 NFP deduction).

19. Out of the 29,000 non-tax exempt NFPs, we estimate that 9,000 are not currently reporting income from member transactions, subscriptions fees and levies. This aligns with what we have heard anecdotally from external stakeholders – different auditors and agents take different approaches to NFPs and their member transactions.

20. If these NFPs reported their member transactions as income, some of them would see a net reduction in their tax liability (as their available deductions would exceed their taxable income); however, most would see a net increase. Operationalising the new interpretation would therefore result in a fiscal gain of between $10-20 million per annum. This gain would not impact on allowances.[1]

21. The affected groups would include a wide range of NFPs including service providers, social clubs including cosmopolitan clubs, professional associations, industry groups and unions.

[1] The fiscal gain arises from the operationalisation of *existing law*. This would not typically be positively charged against allowances but instead will have a positive impact on the total Crown operating balance before gains and losses. Conversely, under the fiscal management approach any measures designed to mitigate the impact of the interpretation on NFPs that have a fiscal cost would be charged against an allowance.

Policy options to mitigate the impact of the draft position on NFPs

22. The Commissioner plans to publicly consult on the new interpretation in late 2024 with a view to operationalising the new interpretation shortly after on a prospective basis. However, if you are concerned about the abovementioned impacts of the new interpretation on the sector, we recommend that you commission policy work on possible ways to mitigate some of these impacts for small NFPs and address related policy issues. The following matters could be considered as part of a policy response.

The $1,000 standard deduction for not-for-profits

23. All NFPs are currently entitled to a standard $1,000 deduction to offset against their income. This policy effectively means the first $1,000 of NFP income is tax-free. It was put in place to reduce compliance costs for smaller NFPs, however, it is poorly targeted given it is available to all NFPs regardless of their size. Additionally, the $1,000 amount has not been updated since 1979.

24. The new interpretation will result in a number of NFPs having more income to return than previously, which will further reduce the effectiveness of the $1,000 deduction.

25. To mitigate the effect of the new interpretation and more effectively reduce compliance costs for NFPs, we recommend reviewing the size and design of the $1,000 standard NFP deduction (alongside return-filing issues, discussed below). There is no policy rationale for providing a large NFP with a concessionary deduction to offset against their income. However, there may be some rationale for providing a concession to smaller NFPs – recognising that the additional revenue collected from taxing these smaller NFPs may not offset the additional compliance costs incurred by them.

26. Alternative policy options to the $1,000 deduction are likely to result in some fiscal cost, the value of which would be design dependent.

Reviewing the tax treatment as outlined in the new interpretation

27. We do not recommend changing the law to make member trading transactions non-taxable, as was done in Australia. This approach does not align with a broad-base low-rate framework and would come at a fiscal cost. Although it would enforce the status quo practice for a number of smaller NFPs, many large NFPs are already correctly following the new interpretation and returning income in relation to these transactions. Our preference is to provide more targeted relief to smaller NFPs, as could be achieved through a review of the $1,000 deduction.

28. Further, we do not recommend changing the law to make membership subscriptions, fees and levies non-taxable in all circumstances. Although this approach would reduce compliance costs for NFPs, who, under the new interpretation would be required to individually assess on the specific facts whether or not the amounts are income, it would come at a fiscal cost and would not be consistent with a broad-base low-rate framework. Any inconsistency between the tax treatment of member trading transactions and membership subscriptions would provide an opportunity for NFPs to structure transactions with members to reduce their tax liability. Our preference is to consider providing more targeted relief for small NFPs, as could be achieved through a review of the $1,000 deduction.

Return-filing obligations for NFPs

29. A review of the $1,000 NFP deduction would also necessitate a review of the return-filing rules for NFPs. However, irrespective of whether you choose to review this deduction, we recommend that the return-filing rules for NFPs be simplified.

30. Currently, NFPs that are not tax-exempt (which includes 15,000-20,000 clubs and societies) are required to file income tax returns. In practice IR has not enforced this rule for NFPs because it imposes compliance costs on them for no revenue or administrative benefit. Out of approximately 4,000 NFPs that do file tax returns, 1,000 file nil tax returns at unnecessary cost to them.

31. We recommend clarifying the return-filing rules so that inactive and small NFPs are either not required to file income returns or are required to file a simple self-assessment return to confirm they fall within a de minimis threshold. A de minimis threshold would be linked to any changes to the $1,000 NFP deduction.

32. There would be no fiscal impact associated with a change to NFP filing requirements.

RWT-exemption for NFPs

33. Currently, NFPs with income under $1,000 or another full income tax exemption can apply for a resident withholding tax (RWT) exemption. NFPs with this exemption do not have RWT deducted from interest and dividends paid to them. NFPs only have to apply for this exemption once, which means they are not prompted to update their status if their situation changes. We recommend reviewing the requirements for accessing this concession alongside any review of the $1,000 NFP deduction.

Removing out-of-date income tax exemptions

34. The operationalisation of the guidance on member transactions may cause some well-advised NFPs to apply for other income tax exemptions. This includes the exemption for all income derived by friendly societies and credit unions (other than their income from trading with non-members). This exemption was originally justified on the basis of the common law principle that transactions between associations and their members are not taxable and so is inconsistent with IR's new interpretation.

35. As well as this exemption, there are a number of other NFP exemptions which are not justified on policy grounds. These are discussed in IR2024/237.

36. Removing one or more of these concessions would have a positive fiscal impact.

Consultation

37. The report was reviewed by The Treasury and the Department of the Prime Minister and Cabinet. It was provided to the Department of Internal Affairs and the Ministry for Business, Innovation and Employment for their information.

Next steps

38. The Commissioner intends to publicly consult on the new interpretation of the income tax treatment of member transactions in late 2024.

39. We recommend that you consider including a project on the TSPWP on options to mitigate the impact of the new interpretation and address related policy issues. We recommend you discuss this possible project with officials as part of your discussions on setting the TSPWP.

40. If you decide to add this work to the TSPWP, this project would be publicly consulted on alongside consultation on Inland Revenue's new interpretation.

Recommended action

We recommend that you:

41. **note** that Inland Revenue plans to publicly consult on operationalising its new interpretation of the law concerning the tax treatment of member transactions and membership subscriptions in late 2024, with a view to operationalising the interpretation soon after.

    Noted

42. **note** the new interpretation would have a significant impact on many not-for-profits. A number of these NFPs may face increased compliance costs and have more tax to pay as a result of operationalisation of the new interpretation.

    Noted

43. **agree** to one of the following options:

    1.1. **Option 1 (no policy response)** – IR will proceed with consultation on the new interpretation in late 2024 with a view to operationalising the interpretation soon after.

    Agreed/Not agreed

    1.2. **Option 2 (policy response – officials' recommended option)** – consider including a project on the Tax and Social Policy Work Programme to potentially mitigate the impact of the new interpretation and address related policy issues. The project could include a review of all or some of the following:

        1.2.1. The standard NFP $1,000 deduction.

        1.2.2. The return-filing rules for NFPs.

        1.2.3. The RWT exemption for NFPs.

        1.2.4. Removing out-of-date income tax exemptions.

    Agreed/Not agreed

44. **refer** a copy of this report to the Minister of Finance for their information;

    Referred/Not referred

45. **refer** a copy of this report to the Minister for the Community and Voluntary Sector and the Minister for Commerce and Consumer Affairs for their information.

    Referred/Not referred

s 9(2)(a)

Stewart Donaldson
Principal Advisor
Inland Revenue

Hon Simon Watts
Minister of Revenue
/ /2024

Appendix - Snapshot of the tax status of entities within the NFP sector

Category	Tax status	Volume[2]
Registered charities	Mostly exempt[3]	34,000[4]
Bodies promoting amateur games and sports	Exempt	22,000
s 9(2)(f)(iv)		
Friendly societies and credit unions	Mostly exempt[5]	100
Bodies promoting scientific or industrial research	Exempt	100
Herd improvement bodies	Exempt	100
Veterinary service bodies	Exempt	100
Various miscellaneous exempt categories	Exempt	100
Not-for-profits with income below $1,000	No net taxable income	25,000
Not-for-profits with taxable income / loss	Taxable income/loss	4,000
Total		s 9(2)(f)(iv)

[2] These figures are approximate, rounded, and may be subject to data coding errors.
[3] Registered charities are mostly exempt from income tax. However, a registered charity's business income is taxable in certain circumstances (for example, a portion of business income is taxable when charitable purposes are carried on outside New Zealand, and all business income is taxable when a person with some control over the business can divert income to the benefit of another person). In addition, most registered charities that are council-controlled organisations are subject to income tax.
[4] This total is higher than the 28,000 registered charities reported by Charities Services because IR records the branches of charities as separate entities for tax purposes.
[5] Friendly societies are exempt from tax on all income except for trading transactions with non-members.

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POLICY

TE TAI ŌHANGA
THE TREASURY

Tax policy report: Charity business income tax exemption

Date:	30 August 2024	**Priority:**	Medium
Security level:	Sensitive - Budget	**Report number:**	IR2024/199 T2024/2396

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to recommendations	19 September 2024
Minister of Revenue	**Agree** to recommendations	19 September 2024

Contact for telephone discussion (if required)

Name	Position	Telephone
Stewart Donaldson	Principal Policy Advisor	s 9(2)(a)
Paul Quirke	Senior Analyst, Tax Strategy	
Peter Frawley	Policy Lead	

30 August 2024

Minister of Finance
Minister of Revenue

Executive summary

1. This report responds to the Minister of Revenue's request for more information about the charity business income tax exemption to inform decisions about the charity component of the tax and social policy work programme. The report supplements information about the charity business income tax exemption provided in recent reports (T2024/1992, IR2024/292 and IR2024/237 refers). A further report will be provided in early September with additional information about donor-controlled charities (private foundations) and donation concessions.

2. We understand that your concerns centre on whether the income tax exemption for charitable businesses provides a competitive advantage for those businesses. This issue is often raised by other business owners competing with the charitable businesses.

3. The argument is that the income tax exemption enables charities to retain untaxed profits for further investment, while other taxable businesses must invest from after-tax profits. This allows a charity to grow its assets and funds more rapidly than a taxable business. The tax exemption is considered by the charitable sector to be a valuable contribution by Government.

4. While it is somewhat complex and counter-intuitive, we consider any competitive advantage distortions are much more minor than usually assumed. In particular, the view that "tax is a cost, so anyone who doesn't pay it must have a competitive advantage" is inaccurate. Both charities and taxpaying businesses face the same pre-tax returns on their investments and so their opportunity cost to invest in a business remains the same. Likewise, the charitable business does not have an incentive to undercut the taxable business on price.[1] This view is supported by successive Australian reviews, including the Henry Tax Review.[2]

5. Our advice is that a policy change focusing on the charity business income tax exemption would create significant distortions if passive income remains untaxed. However, we do think that there is an underlying tax policy issue with the extent to which a range of charitable entities including, but not limited to, charity businesses, are accumulating surpluses rather than distributing or applying those surpluses for the benefit of their charitable activities.

6. Despite our conclusions above, most OECD countries have either restricted the commercial activities a charitable entity can engage in through their equivalent of the New Zealand Charities Act 2005, or they tax commercial income if the commercial income is unrelated to charitable purpose activities and is accumulated. New Zealand, Australia and Malta are the only countries that exempt income of charity businesses.

[1] This view is discussed in more detail in the Tax Working Group officials' paper "Charities and the not-for-profit sector: Background Paper for Session 13 of the Tax Working Group" 6 July 2018.
[2] "Australia's future tax system Report to the Treasurer December 2009 Part Two Detailed analysis volume 1 of 2" page 209.

7. Removing or restricting the charity business income tax exemption would result in a fiscal gain, however the quantum of the gain is uncertain. Our estimate is that the gain could be between $60 million and $200 million per annum but this would be affected by policy design and any behavioural responses. The net gain for Government could be lower if charities reduce their services and there is a corresponding increase in demand for Government support.

8. While we do not recommend further work on removing the exemption just for the business income of charities, we do not have a strong view on whether charities should be taxable on all their income – this depends on the level of support the Government wants to provide to charities.

9. We recommend focusing on specific issues with tax concessions for charities and not-for-profits. For example, the excess accumulation of certain untaxed funds (including excess accumulations in donor-controlled charities) and reviewing out-of-date exemptions.

Recommended action

We recommend that you:

10. **agree** to not doing further work on removing the income tax exemption just for the business income of charities.

Agreed/Not agreed	Agreed/Not agreed

11. **agree** to focus on specific issues with tax concessions for charities and not-for-profits including accumulation practices and existing exemptions (excluding the business income tax exemption) to ensure they remain fit for purpose.

Agreed/Not agreed	Agreed/Not agreed

12. **agree** to raise charitable purpose definition concerns you may have (if any) with the Minister for the Community and Voluntary Sector, Hon Louise Upston.

Agreed/Not agreed	Agreed/Not agreed

13. **note** a further report to inform decisions about the charity component of the tax and social policy work programme will be provided in early September with additional information about donor-controlled charities (private foundations) and donation concessions.

Noted	Noted

s 9(2)(a)

Jean Le Roux
Manager
The Treasury

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2024

Hon Simon Watts
Minister of Revenue
/ /2024

Purpose

14. On 15 August 2024 the Minister of Revenue asked for more information about the charity business income tax exemption to inform decisions about the charity component of the tax and social policy work programme. The information in this report supplements information about the charity business income tax exemption provided in recent reports (T2024/1992, IR2024/292 and IR2024/237 refers). A further report to inform decisions about the charity component of the tax and social policy work programme will be provided in early September with additional information about donor-controlled charities (private foundations) and donation concessions.

Framework

15. The income tax exemption framework for charities registered under the Charities Act takes a "destination of income" approach. This means that income is tax exempt if it is ultimately destined for a charitable purpose. Income can be accumulated for many years within a registered charity and will still qualify for the tax exemption.

16. The framework provides income tax exemption on a targeted basis. Since 1940, charity business income has been tax exempt to the extent the registered charity carries out its charitable purposes in New Zealand, whereas charity investment income is wholly exempt.

17. The framework relies on tax exempt charities being regulated and publicly accountable. Prior to 2020−21, any business could access the charity business income tax exemption without regulation or public accountability, provided it was carried on by, or for the benefit of, a registered charity. Since 2020−21, all businesses must be registered and report under the Charities Act to be eligible for the charity business income tax exemption. Charities Services, within the Department of Internal Affairs, will register charity businesses as charities in their own right provided business profits are used to advance charitable purposes.

18. Relevant to policy issues raised in this report, the tax framework for charities sits alongside the imputation credit framework, which does not allow tax-exempt organisations to benefit from imputation credit refunds. This creates several investment distortions including a bias for charities to carry out business activities themselves for the business to access a tax exemption. This distortion contributes to a high proportion of New Zealand charities engaging in business activities.

Problem definition

19. The term "charitable purposes", which determines which entities are eligible for charity income tax exemption, is not defined within the Revenue Acts, but is instead defined in the Charities Act, for which the Department of Internal Affairs holds stewardship in its role in the Community and Voluntary Sector portfolio. If you are concerned about the charitable purpose definition this could be addressed by a review of the Charities Act rather than the Revenue Acts.

20. New Zealand charities support the current charity business income tax exemption and emphasise the role that businesses play in generating funds for the charitable sector. Charities view business activities as a diverse and sustainable income, in addition to grants and donations. They note charity businesses provide other benefits for the economy, such as employment. They also note that the income tax exemption offsets the disadvantages that charities face in accessing capital (unlike for-profits, they cannot access equity investors because they cannot provide private benefits).

21. Other parts of the community, often owners of taxpaying businesses, raise concerns that tax exemption gives charitable businesses an unfair competitive advantage. Some suggest it is sufficient for charitable businesses to rely on the existing gift tax deduction provision to obtain tax relief rather than allowing charitable businesses to access a full tax exemption.

22. Information published by Charities Services on the Charities Register shows there are many businesses accessing the charity business tax exemption in New Zealand, including property development, farming, tourism, fishing, electricity generation and distribution, and food production businesses. The fiscal cost of not taxing charity business income is significant.

23. In our view, the main tax problem is not one of competitive advantage but a broader issue of profit accumulation by a range of charitable entities including, but not limited to, charity businesses. This view is discussed below.

Competitive advantage

24. There is a widespread belief that the income tax exemption for charities provides them with a significant competitive advantage over for-profit businesses. This view assumes that:

    24.1 Charities can retain untaxed profits for further investment, while for-profit organisations must invest from after-tax profits.

    24.2 This allows the charity businesses to grow more rapidly than taxable businesses.

    24.3 Large-scale entities could potentially use this advantage to undercut competitors or deter new entrants.

25. Our view is that any competitive advantage distortions are much more minor than usually assumed. In particular, the view that "tax is a cost, so anyone who doesn't pay it must have a competitive advantage" is inaccurate.[3]

26. Both charities and taxpaying businesses face the same pre-tax returns on their investments. A charity's alternative to running a business (e.g., investing in securities) is also tax-free, so their opportunity cost remains the same. A simple investment example is shown in Figure 1, below.

[3] This view is discussed in more detail in the Tax Working Group officials' paper "Charities and the not-for-profit sector: Background Paper for Session 13 of the Tax Working Group" 6 July 2018.

Figure 1: Investment example

A charity and a taxpaying business each have $10,000 to invest.

Option A: Invest in a business venture yielding 10% return

Option B: Invest in bonds yielding 10% return

Charity:

Business venture: $10,000 × 10% = $1,000 (tax free)

Bonds: $10,000 × 10% = $1,000 (tax free)

Taxpaying business (assuming 30% tax rate):

Business venture: $10,000 × 10% = $1,000, after tax: $700

Bonds: $10,000 × 10% = $1,000, after tax: $700

Key observations:

The charity ends up with more money than the taxpayer in both cases.

However, for each of the charity and the taxpayer, the business venture and the bonds yield exactly the same result.

Neither the charity nor the taxpayer has an inherent financial incentive to choose the business venture over the bonds, or vice versa.

27. In principle, the tax concession does not impart a competitive advantage because a trading operation owned by a charity faces the same incentives as a commercial entity when it comes to setting its prices. Its tax-exempt status alone should not lead to undercutting of rivals. A simple predatory pricing example is shown in Figure 2, below.

Figure 2: Predatory pricing example

A charity and a taxpaying business both consider lowering prices to gain market share.

Charity:

Year 1: Losses $1,000

Year 2: Profits $3,000

Net gain: $2,000

Taxpaying business (30% tax rate):

Year 1: Losses $1,000, tax benefit: $300, net loss: $700

Year 2: Profits $3,000, tax: $900, net profit: $2,100

Net gain: profit before tax $2,000, tax cost $600, net profit after tax $1,400

Key observations:

The relationship between gains and losses remains consistent (2:1) regardless of tax status. Taxation effectively "shrinks" both the positive and negative outcomes for the business, but does not alter the fundamental risk−reward proposition compared to the charity.

28. Our view is consistent with successive Australian reviews of commercial activities in the charitable sector. For example, Australia's future tax system review (the Henry Tax Review[4]), published in 2010, found:

"In relation to pricing, NFP [not-for-profit] organisations, like for-profit organisations, will seek to maximise their profits in support of their philanthropic activities. Accordingly, it appears that the income tax exemption does not provide an incentive for NFP organisations to undercut the prices of their for-profit competitors; rather, NFP organisations follow the same pricing policies as their competitors to maximise their profits."

29. In its 2019 report,[5] the Tax Working Group (TWG) considered that the underlying issue is not one of unfair advantage over commercial entities' trading operations, but the extent to which charities are accumulating surpluses rather than distributing or applying those surpluses for the benefit of their charitable activities.

30. There are other tax distortions impacting on the charitable sector. For example, tax-exempt entities are currently unable to benefit from imputation credits and therefore a level of taxation will apply to these otherwise exempt entities. This absence of refundability creates both passive and active investment distortions, including a bias for charities to carry out business activities themselves instead of holding shares in companies that carry out the activities. However, any change in the current imputation credit refundability policy would raise concerns about tax planning and fiscal cost. According to past estimates, imputation credit refundability could benefit 2,500 to 3,000 charities and the revenue cost could be $70 million to $100 million per annum.

Accumulation

31. Current tax rules allow all charities, including those that derive business income, to accumulate tax-exempt surpluses and grow their net assets rather than distributing or applying those surpluses for the benefit of their charitable purpose. This is known as the "destination of income" approach.

32. One of the primary concerns with the destination of income approach is the timing mismatch between the tax benefit and the ultimate public benefit being achieved. In some instances, the mismatch can exist for decades.

33. Charities often cite specific reasons to accumulate funds and from 2024 most charities must publicly provide reasons for accumulation under the Charities Act. Typically, funds will be accumulated to save for the acquisition or construction of capital assets, to prepare for large crises in the future, or to take an intergenerational view towards the management of assets.

34. There are currently 29,000 charities registered under the Charities Act. Our analysis indicates that about 600 to 700 of these charities are medium/large charities that are predominantly trading and with a reported growth in net assets of more than 10% per annum from 2017 to 2020.

35. Our analysis indicates that the proportion of predominantly trading medium/large charities experiencing significant growth is similar to the proportion of all medium/large charities experiencing significant growth. This means reducing accumulation by businesses will not address all accumulation timing differences occurring within the sector.

[4] "Australia's future tax system Report to the Treasurer December 2009 Part Two Detailed analysis volume 1 of 2" s 9(2)(f)(iv)

[5] "Future of Tax: Final Report Volume I – Recommendations", Tax Working Group, 21 February 2019

The status quo

36. The current rule that charity business income is tax exempt only to the extent the charity carries out its charitable purposes in New Zealand is difficult to apply in practice. To provide clarity and guidance, the Tax Counsel Office has publicly consulted on a draft Interpretation Statement and will release the final statement shortly.

Revenue protection

37. Removing the charity business income tax exemption would result in a fiscal gain. The quantum of the gain would be affected by policy design and behaviour change. Our estimate is that the gain could be between $60 million and $200 million per annum. This estimate assumes small charities below a de minimis of $140,000 expenditure retain full tax exemption.

38. Our fiscal estimates have a high level of uncertainty. Neither Inland Revenue nor other agencies have formally estimated this exemption before, so there is no existing New Zealand methodology to apply. Charitable income tax exemption is not a quantified tax expenditure in Australia, Canada or the United Kingdom so there is no comparable international methodology to follow. The range of behaviour responses could reduce the estimated revenue gains.

39. Apportionment and over-allocation of expenditure to taxable charity trading activity would be one of the biggest issues of concern when charity trading activity cannot directly access an income tax exemption.

40. If the policy option is to tax "unrelated" business income, the definition of "unrelated" business income could be regularly litigated s 6(c)

41. s 6(c)

42. Removing the tax exemption would be consistent with the Government's BBLR tax policy framework because it would broaden the tax base. However, it would create a distortion if passive income remains untaxed. Accordingly, the revenue benefit from taxing the business income of charities would need to be weighed against the cost of this distortion.

International approaches to charity business income tax exemption

43. According to a 2020 OECD study of 40 countries,[6] New Zealand, Australia and Malta are the only countries that exempt income of charity businesses. Most other countries have either restricted the commercial activities a charitable entity can engage in through their equivalent of New Zealand's Charities Act 2005, or they tax commercial income if the commercial income is unrelated to charitable purpose activities and is accumulated. The rationale is typically a response to unfair competition claims, a desire to separate risk from the charity's assets, and/or to reduce the fiscal cost of not taxing business income.

44. For example, the UK and Canada will not register a charity when its purpose includes the carrying out of trade, unless that trade directly supports its charitable purposes. This means charities can use charity-trading subsidiaries to raise funds, but they will not qualify for income tax exemption. The US has an unrelated business income

[6] "OECD Tax Policy Studies: Taxation and Philanthropy No.27" 2020

tax, which means if a charity's business activities are not substantially related to furthering the charitable purpose, the income from such activities will be taxable.

45. Rules in the UK, US and Canada aim to prevent businesses receiving a tax exemption, while still supporting charitable activities carried out by their owners. However, these rules are hard to design and enforce. The common problems are:

- Difficulty in determining whether a business activity is "related" or "unrelated" to a charitable purpose.
- Challenges in apportioning and allocating expenditure to taxable charitable trading activities.
- Complications in managing working capital due to incentives to donate profits to parent charities to receive a deduction.
- Creation of potentially distortionary incentives for how charities structure their business activities.
- Administrative burden for both charities and tax authorities in navigating and enforcing complex rules.

Potential tax policy responses

Maintain the status quo

46. The status quo could be maintained, noting that it will be affected by two useful recent developments:

46.1 The Department of Internal Affairs (Charities Services) has introduced a new annual requirement that, from 2024−25, medium and large sized registered charities report how they plan to use their accumulated funds.

46.2 The Tax Counsel Office will release an Interpretation Statement shortly to provide clarity and guidance about how the current legislation should be applied.

47. The decision to progress a tax policy response to charitable business activity issues could be deferred until information from the Charities Act's new reporting requirements is analysed and until policy issues (if any) are identified from the application of the Tax Counsel Office Interpretation Statement.

Undertake policy work that may result in taxing more business income of charities

48. Policy options could be targeted to reduce the scope of the current charity business income tax exemption, such as moving the tax policy setting from a "destination of income" approach to an "unrelated business" approach.

49. Moving to an "unrelated business" approach would increase tax revenue and discourage accumulation by charities with business income because they will be incentivised to apply their income to their charitable purpose to minimise their tax liability. It may also provide an opportunity for the existing business tax rules to be simplified for smaller charities.

50. However, this option would have a negative impact on the coherence of the tax system because non-business income such as investment income would still be exempt. It would have significant compliance costs for affected charities within the

sector, which charities may attempt to mitigate by seeking an increase in Government support by way of grants.

51. Finally, our analysis shows that, though there are exceptions, charities that derive business income do not appear to have a greater predisposition to accumulate funds than other charities.

52. As noted above, some charities may have good reasons to accumulate funds (for example, to save for the acquisition or construction of capital assets, to prepare for large crises in the future, or to take an intergenerational view towards the management of assets), so changes to the current income tax exemption should only be made if these charities could be adequately protected.

Undertake policy work to address accumulation and other tax issues

53. Rather than undertaking policy work on removing the charity business income tax exemption, other responses involving tax concessions for charities and not-for-profits could be explored. For example, the excess accumulation of certain untaxed funds (including excess accumulations in donor-controlled charities) and reviewing out-of-date exemptions.

Recommended approach

54. We do not recommend further work on removing the exemption just for the business income of charities. We do not have a strong view on whether charities should be taxable on all their income – this depends on the level of support the Government wants to provide to charities.

55. s 9(2)(f)(iv)

Next steps

56. A further report will be provided in early September with additional information about donor-controlled charities (private foundations) and donation concessions.

57. If you wish to progress this work and agree with our recommended approach, the next steps would be:

    57.1 Inform the Minister for the Community and Voluntary Sector.

    57.2 Publicly announce a targeted review of specific tax concessions and practices related to charities and not-for-profits.

    57.3 Include this review on the published tax and social policy work programme, providing opportunity to consult.

    57.4 Clearly define the scope to include:

    - accumulation practices, particularly in donor-controlled charities
    - existing exemptions (excluding the business income tax exemption) to ensure they remain fit for purpose.

Consultation

58. Matters raised in this report were discussed with the Department of Internal Affairs.

Priority Routine

Te Tari Taiwhenua
Internal Affairs

Community and Voluntary Sector briefing

Hon Nicola Willis
Minister of Finance

Hon Simon Watts
Minister of Revenue

Copy to: Hon Louise Upston
Minister for the Community and Voluntary Sector

Title: **Overview of 'charitable purpose' under the Charities Act 2005**

Date: 20 September 2024

Key issues
This briefing accompanies two reports you are receiving from Inland Revenue and the Treasury to support your decisions on the Tax and Social Policy Work Programme. You have requested information about 'charitable purpose' in New Zealand to provide you with further context for charities-related tax matters. This briefing provides you with background information on the definition of charitable purpose under the Charities Act 2005, its development, and stakeholder views. Inland Revenue and the Treasury have been consulted on this briefing.

Action sought	Timeframe
Note the contents of this briefing	At your convenience

Contact for telephone discussions (if required)

Name	Position	Contact Number	Suggested 1st contact
Department of Internal Affairs			
Louise Cooney	Policy Manager	s 9(2)(a)	✓
Alicia Bunge	Senior Policy Analyst		
Inland Revenue			
Stewart Donaldson	Principal Policy Advisor	s 9(2)(a)	

Return electronic document to:	Alicia Bunge, s 9(2)(a)
Cohesion document reference	6EYAVYC5ZNWP-1088189731-626
Ministerial database reference	CVS20244176
Inland Revenue document reference	BN2024/387

s 9(2)(a)

Louise Cooney
Policy Manager

Purpose

1. You have requested information about 'charitable purpose' in New Zealand as context for charities related tax matters that Inland Revenue has briefed you on. This briefing provides you with background information on the definition of charitable purpose under the Charities Act 2005, its development, and stakeholder views.
2. This briefing accompanies two reports you are receiving from Inland Revenue and the Treasury to support your decisions on the Tax and Social Policy Work Programme [IR2024-359/ T2024-2572 and IR2024-360 refer]. Inland Revenue and the Treasury have been consulted on this briefing.

'Charitable purpose' is a complex legal concept which continues to evolve

Charitable purpose falls into four categories that provide benefit to the public

3. The law on what is considered "charitable" goes back to the concept of charity set out in England's *Statute of Charitable Uses 1601* (also known as the *Statute of Elizabeth*) and is based on more than 400 years of case law. Broadly, to be charitable, and as set out in the Charities Act 2005 (the Act), an organisation must have purposes to:
    - 3.1 relieve poverty;
    - 3.2 advance religion;
    - 3.3 advance education; or
    - 3.4 promote any other purpose which the courts have decided is beneficial to the community and does not provide private benefits (e.g. protecting the environment, advancing health).
4. An organisation's purpose and activities must provide a defined and identifiable benefit to the public. For example, maintaining a public park directly benefits the public. Providing a student scholarship that leads to a more educated society for everyone is a less direct but clearly identifiable public benefit.
5. An organisation's purpose is not considered charitable if a private benefit outweighs the overall public benefit. Home ownership can be an example of this. Case law says that while housing is a basic need and right, providing home ownership is not. Providing housing can be charitable but needs to be connected to a charitable purpose (for example under the purpose of relieving poverty, an organisation can operate nonprofit residential accommodation for senior citizens of low or modest income or providing transitional homes for those experiencing homelessness).
6. An organisation can have non-charitable purposes, but these must be ancillary to their charitable purposes if they want to be a registered charity under the Act. **Appendix A** provides further examples of activities that organisations may pursue to meet the definition of having a charitable purpose.

Court decisions continue to shape the meaning of charitable purpose in New Zealand

7. New Zealand's courts make decisions on what it means to have a charitable purpose. Over the years, as society has changed, the courts have recognised many new charitable purposes (linked to the four categories discussed above) which meet new social needs in New Zealand.

8. The most complex and high-profile legal decisions generally relate to advocacy. Advocacy is charitable when it is clearly connected to an organisation's charitable purpose (e.g. preventing the suffering of animals by opposing research and testing that causes harm to animals). However, some forms of advocacy may fall outside of what the courts recognise as a charitable purpose (e.g. supporting a singular, discriminatory view which excludes others).

9. Advocacy has been the subject of court cases in recent years. For example, a 2022 Supreme Court decision held that Family First New Zealand does not qualify for registration as a charity under either the advancement of education (its activities lacking the balance required to advance education in a charitable sense), or other purposes beneficial to the community (its advocacy for the traditional family to the disadvantage of other forms of family being discriminatory).[1]

Stakeholders have varying views on the definition of charitable purpose

10. When considering the Charities Bill 2004 (which later became the Act), the Social Services Committee did not recommend amending the definition of charitable purpose. The reasoning was that the majority of the committee did not believe that "expanding the definition of charitable purpose will offer any significant benefit" and there were concerns that "amending the definition would be interpreted by the Courts as an attempt to widen or narrow the scope of charitable purposes, or change the law in this area, which was not the intent of the bill".[2]

11. Since the Act was passed in 2005, there have been requests from a number of sector representatives and other interested parties for a review of the definition of charitable purpose to ensure the definition appropriately reflects New Zealand society.

12. The most recent publicly gathered views on charitable purpose come from submitter feedback from public consultation in 2019 on a review of the Act. While charitable purpose was outside scope of the review, varying views as to how charitable purpose should be defined were still shared by submitters.

13. Some questioned whether advancement of religion should still be a charitable purpose with associated tax benefits noting the growing number of people without religious affiliation. Others wanted a review of the 'advancing education' purpose given the meaning of 'advancing education' has evolved over the past 400 years and New Zealand has universal education and schools receive government funding.

14. Other stakeholders wanted the Act to mention specific purposes such as advancing culture, protecting the environment and providing affordable housing (instead of having them subsumed under 'any other purpose'). Some wanted the Act to specifically note concepts specific to Te Ao Māori (e.g. to ensure the definition does not limit the activities of iwi organisations to benefit their people such as economic development initiatives and savings schemes for iwi members).

[1] Attorney-General v Family First New Zealand [2022] NZSC 80.

[2] Charities Bill 2004 (108-2) (select committee report) at 3.

15. Some stakeholders also wanted more clarity as to how advocacy relates to charitable purpose. Some argued that charities needed more freedom to advocate to fulfil their purpose, while others acknowledged the need for limits.

Hon Nicola Willis
Minister of Finance

_____/_____/_____

Hon Simon Watts
Minister of Revenue

_____/_____/_____

Appendix A: Examples of what the four charitable purposes entail

Charitable purpose	Examples
Relieve poverty	An organisation's purpose is to provide relief and is directed at people who are poor, in need, aged, or suffering genuine hardship from a temporary or long-term change in their circumstances. An organisation may relive poverty, for example, by: • providing the poor with a food bank; • operating and maintaining a shelter for the homeless and by providing counselling and other similar programmes; or • providing and operating non-profit residential accommodation for persons of low income or senior citizens of low or modest income.
Advance religion	An organisation advances a set of beliefs that constitute a religion and aim to pass on the religious beliefs to others by spreading its message and taking positive steps to sustain and increase the religious belief. (A religion is being defined here as having a body of structured and clear doctrines and canons of conduct.) An organisation may advance religion, for example, by: • Teaching the religious tenets, doctrines, observances and culture associated with the faith or religion; • establish, maintain and support a house of worship with services conducted in accordance with the tenets and doctrines of the faith or religion; or • establish and maintain a religious day school.
Advance education	An organisation's purpose is to provide some form of education and ensure learning is passed on to others. This includes formal education, training and research in specific areas of study and informal education in the development of individual capabilities, competencies and understanding. An organisation may advance education, for example, by: • operating schools; • providing courses and seminars on a topic (e.g. on parenting); • educating the public in music performance and composition through workshops and recitals; or • providing a mentorship programme to Māori film and video artists.
Promote other purposes beneficial to the community	An organisation's purpose is very similar to the spirit and intent of those purposes listed in the Preamble to the *Statute of Elizabeth* or very similar to a charitable purpose as decided by the courts. An organisation may promote other purposes, for example, by: • promoting the preservation of places of historic interest or natural beauty; • establishing a recreation facility for a community; or • providing a crisis line for troubled children and young people.

Inland Revenue
Te Tari Taake

POLICY

TE TAI ŌHANGA
THE TREASURY

Tax policy report: Donation tax concession caps

Date:	20 September 2024	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2024/359 T2024/2572

Action sought

	Action sought	**Deadline**
Minister of Finance	**Agree** to recommendations	4 October 2024
Minister of Revenue	**Agree** to recommendations	4 October 2024

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**	**Suggested first contact**
Stewart Donaldson	Principal Policy Advisor	s 9(2)(a)	✓
Paul Quirke	Senior Analyst, Tax Strategy, The Treasury		
Peter Frawley	Policy Lead		
Jacob Hawker	Policy Advisor		

20 September 2024

Executive summary

1. This report responds to the Minister of Revenue's request for more information about donation tax concession caps to inform decisions about the charity component of the tax and social policy work programme (TSPWP). We understand that your concerns centre on who uses the donation tax credit (DTC) mechanism at present, whether donation caps change behaviour, and what elasticity analysis exists.

2. Approximately 350,000 individuals account for over 90% of the $1.1 billion of donations receiving tax concessions each year. The main recipients of these donations are religious organisations (63% of individual donations), other charitable organisations (29%) and schools (8%).

3. A significant reduction in donation caps for individuals will potentially reduce DTC claims by approximately $50 million per annum. This cap would only affect 8,000 or 2% of donors, leaving over 340,000 or 98% of donors unaffected.[1]

4. A donation cap reduction is likely to have minimal impact on donations to schools, because most school donations are low value. It will have a significant impact on donations to religious organisations because these donations are the highest in value.

5. Research into elasticity indicates that New Zealand DTCs are not "treasury efficient". Treasury efficiency compares the incremental increase in donations against the revenue a government forgoes through the DTC. The DTC can generally be considered treasury efficient if the absolute value of the elasticity of donations is greater than 1, meaning the DTC incentivises an increase in donations that is greater than the loss of government revenue from funding the DTC. For every $1 in DTC provided by the Government, research has found that reported donations to charities in New Zealand increases by $0.40 to $0.70 on average. That means the additional donations generated by the tax credit are less than the loss of government revenue from funding the credit.

6. If you wish to reduce the cost of the DTC to the Government, our advice is to explore a lower donation cap for individuals, payroll giving, companies and Māori authorities. This will:

    6.1 improve the efficiency of the tax concessions, and

    6.2 mitigate fraud and tax avoidance concerns.

7. Depending on the design of a lower donation cap, it could result in a significant revenue gain, which could support an economic growth package while only impacting a small proportion of donors.

8. A lower donation cap would likely require several related policy settings to be adjusted. This includes the current rules for trading stock donated by businesses, trust income allocations to tax exempt entities such as charities, and the charity deregistration tax calculation, which assumes donations of money to charities have been eligible for donation tax concessions.

[1] This estimate differs from the $60 million referred to in IR2024/237 because it includes assumptions about donor behaviour and is based on more recent data available.

9. The net fiscal gain for the Government has not been quantified. If a change in the donation tax concession reduces charity donation income, charities may reduce their services. This may result in an increase in demand for government support and a lower net fiscal gain compared to the $50 million per annum reduction in DTC claims.

10. If you want to progress this work as part of Budget 25, or as part of work that is publicly announced on the TSPWP, we suggest you:

    10.1 Inform the Minister for the Community and Voluntary Sector, because it may be relevant for The Hon Louise Upston's plans to double philanthropic giving.

    10.2 Decide whether you will include work on simplification measures at the same time.

    10.3 Indicate to officials whether you need any further analysis of particular cap levels or other advice.

Purpose

11. On 15 August 2024 the Minister of Revenue asked for more information about donation tax concession caps to inform decisions about the charity component of the TSPWP. The information in this report supplements information about donation caps provided in recent reports (T2024/1992, IR2024/292 and IR2024/237 refers). Other charity-related matters, concerning donor-controlled charities and the definition of charitable purpose, have been reported separately at the same time as this report (IR2024/360 and BN2024/387 refers).

Details of tax concession claims

12. Inland Revenue and the Treasury publish some donation statistics annually.[2] Although the Inland Revenue donation data is shared with Statistics New Zealand, this is not currently available on the Integrated Data Infrastructure (IDI) for research purposes because it has not been identified as a priority by Statistics New Zealand. Therefore, there is very little published research involving tax concession data.

Most tax concessions are claimed by individuals

13. For the year ending 31 March 2023, donations of money totalling approximately $1.1 billion were subject to tax concession claims, with a tax cash value of $348 million.

14. Approximately 350,000 individuals made DTC claims. These had a tax cash value of $317 million, which is just over 90% of the total tax value of all donations tax concessions.

15. Tax claims made by individuals fall into two categories:

    15.1 Individuals can donate and file a claim with Inland Revenue each year.

    15.2 Individuals can donate via payroll giving. This scheme was introduced from 2010. Employees receive an immediate reduction in tax by way of the tax

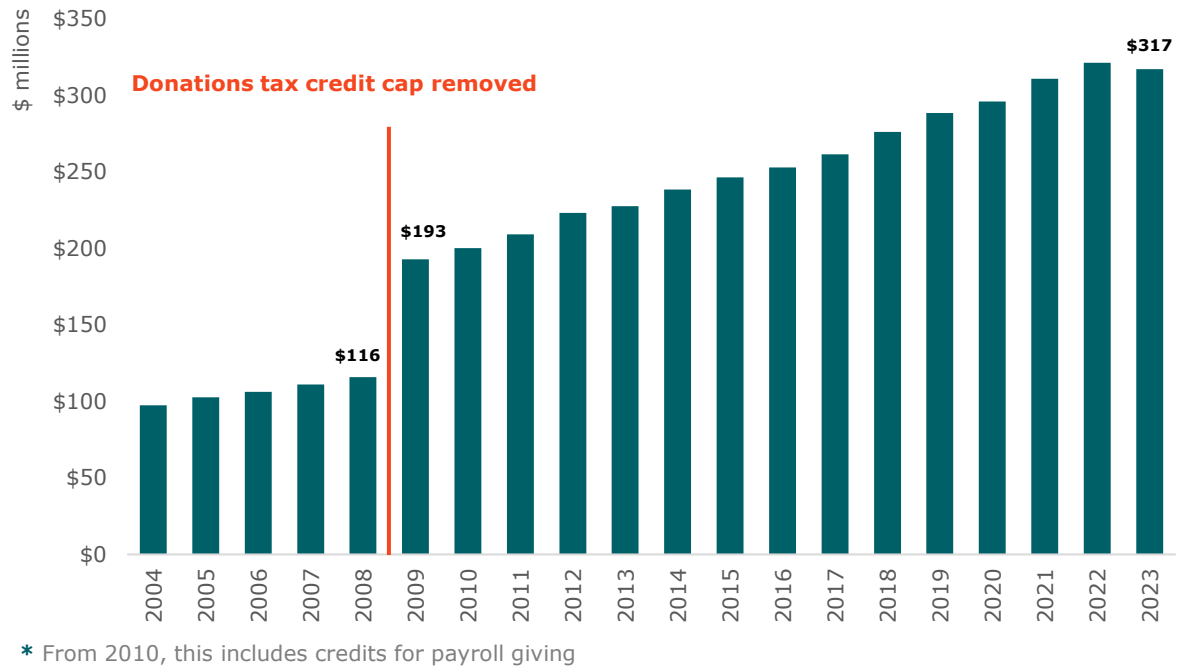
[2] Inland Revenue publishes Donation tax credits statistics (ird.govt.nz). The breakdown includes the average DTC claimed per person, the number of people who claimed DTCs, and the total DTC claimed by type of recipient organisation. The Treasury publishes data for payroll giving, corporate and Māori authority gift deductions in the annual Tax Expenditure Statement.

credit each pay period, eliminating the need to collect and keep receipts to claim tax relief on gifts at the end of the year.

16. A significant change was made to the maximum DTC claim from the 2008–09 year. Prior to the 2008–09 year there was a $630 per annum maximum DTC limit for individuals (based on donations of $1,890). From 2008–09 the annual maximum limit was raised to 33 1/3% of the donor's taxable income.

17. As shown in **Figure 1**, individual DTC claims increased by 66% in the year of the DTC cap change (2008–09) compared to the prior year. The increase of $77 million significantly exceeded the forecast at the time, which anticipated an additional cost of $25 million for individuals and companies (PAD2010/186 refers). This indicates donor behaviour in response to donation cap changes is difficult to forecast.

Figure 1: **Individual donation tax credit claims*** increased by 66% when the cap was removed

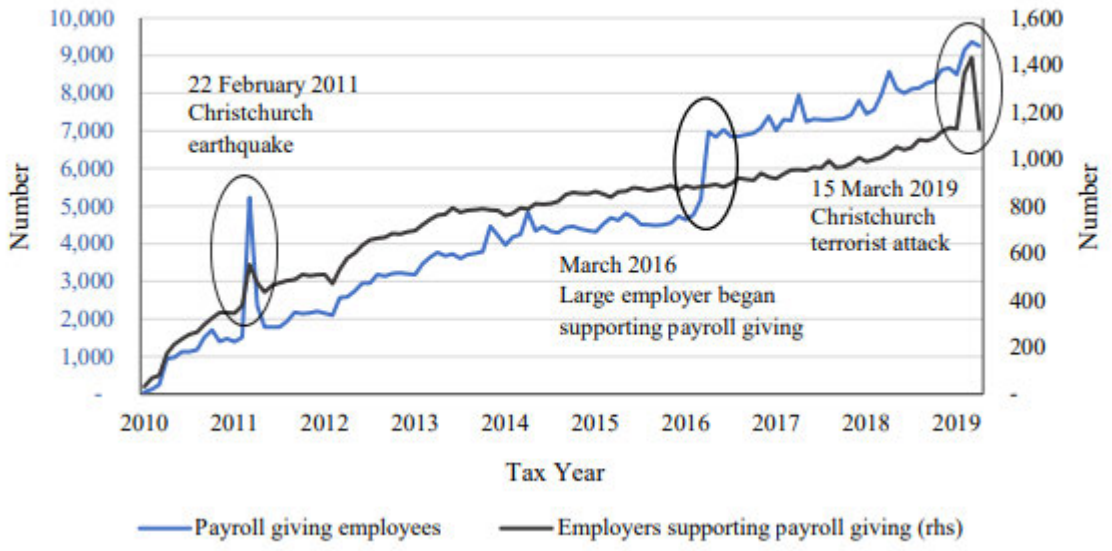


* From 2010, this includes credits for payroll giving

18. As shown in **Figure 2**,[3] payroll giving claims have grown steadily since 2010. They are more responsive to one-off events such as the Christchurch earthquake in 2011 and the Christchurch terrorist attack in 2019 because the claims can be made immediately, unlike other DTC claims which are made annually. The take-up and impact of payroll giving is low, accounting for less than 1% of donations reported to Inland Revenue. This is due to several reasons, including a lack of awareness of the scheme, employer compliance costs, and policy design. Occasionally, very large one-off donations are made through the scheme, so it will need to be considered if a lower DTC cap is put in place for individuals.

[3] Figure based on Inland Revenue data, sourced from Cruickshank, A. (2023) "Survey of Charitable Giving in New Zealand", Chair in Public Finance Working Paper 03/2023, Victoria University of Wellington, New Zealand, September 2023.

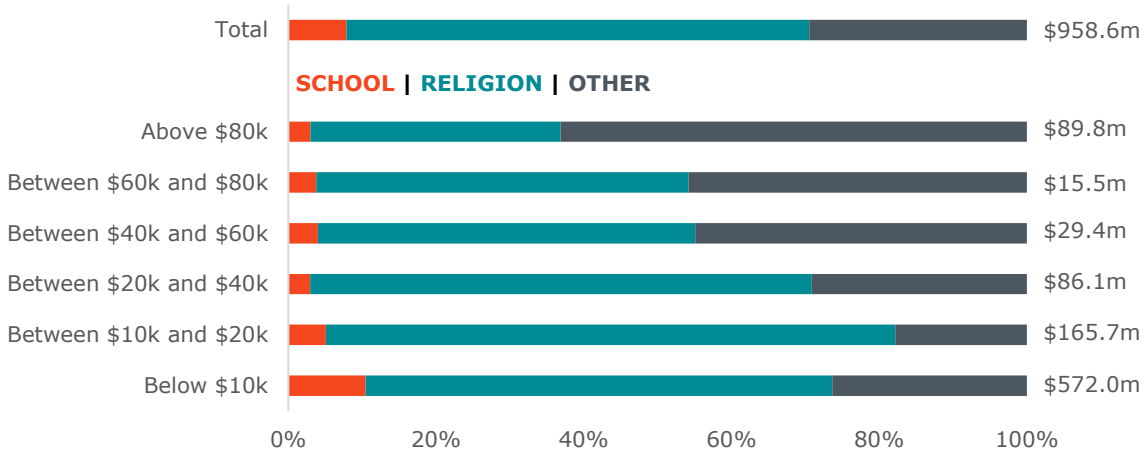
Figure 2: Number of Payroll Giving Employees and Employers



Recipients of donations subject to tax concessions

19. When individuals submit a DTC claim they are asked to classify the recipients of their donations into three categories – religious organisations, schools, and "other". Based on these classifications, approximately 63% of the value of donations goes to religious organisations, 8% to schools and 29% to other organisations.[4] These percentages have been relatively consistent for many years. As shown in **Figure 3**, smaller donation amounts tend to favour schools and religion relative to larger donations.

Figure 3: Smaller donations favour **schools** and larger donations favour **religious organisations**



[4] The categories of "religious organisations" and "schools" are subject to individual donor interpretation so they are indicative only.

The impact of a change is difficult to determine

20. Significant reductions in donation tax concession caps will impact volumes of donors who donate above the cap, values of DTCs, and types of donation recipients, depending on where any cap is set. The impact on amounts donated is difficult to determine, as some donors may reduce the amount they donate in absence of a DTC, whereas other donors may continue to donate the same amount.

21. Figure 4 compares a cap set at $15,000 in donations ($5,000 DTCs) [5] with a cap set at $4,500 in donations ($1,500 DTCs).

Figure 4: Donation Tax Credit caps of $15,000 and $4,500

Donation cap	DTC	Donations affected ($m) pa (approx)	DTC revenue gain ($m) pa (approx)	Revenue gain as a % of total claims	Number of donors impacted (approx)	% of donors impacted
$15,000	$5,000	$150	$50	16%	8,000	2%
$4,500	$1,500	$380	$126	40%	56,000	16%

22. If the cap was set at $15,000 in donations ($5,000 DTCs):

22.1 s 6(c) [redacted]

22.2 **It is likely to have less impact on donations to schools.** Our modelling shows donations to schools are lowest in value compared to other categories. In the year ending March 2023, individuals who reported total donations of over $15,000 paid $9 million to schools ($3 million DTCs). About 100 of these individuals donated just to schools (typically to school charitable foundations).

Donation tax concessions for entities and trusts

23. Companies and Māori authorities can claim tax deductions for donations of money. The maximum deduction was increased significantly for companies and Māori authorities, capped to net income, from the 2008–09 year. Immediately prior to this change, the deduction was limited to 5% of net income. Closely held companies were not eligible for any donation deduction prior to 2008–09 unless they were quoted on the official list of a recognised stock exchange, on the basis that eligible companies needed to be subject to greater public scrutiny and disclosure requirements.

24. Approximately 5,000 companies and 40 Māori authorities make DTC claims each year. For the year ending 31 March 2023, the tax cash value of these DTC claims was $25 million (for $90 million donations) and $6 million (for $32 million donations) respectively. Inland Revenue does not collect information about the recipients of corporate or Māori authority donations.

25. Although trusts are not eligible for donation deductions, they can allocate beneficiary income directly to tax exempt charities and not pay tax on that income. The allocation to charities is not subject to a cap. In 2022–23, approximately 400 trusts allocated $160 million to charities, with a tax cash value of approximately $53 million. Inland Revenue trust disclosure data indicates that not all income

[5] The $50 million revenue gain estimate in Figure 4 differs from the $60 million referred to in IR2024/237 because it includes assumptions about donor behaviour and is based on more recent data available.

allocated to charities is actually paid to them and a policy response may be warranted. We will report on this matter to the Minister of Revenue separately.

26. Businesses, including companies, sole traders and trading trusts, may donate trading stock to a donee organisation and claim a tax deduction for the cost or opening book value of that trading stock. This deduction is not subject to any cap because the policy intent was to minimise the compliance and administrative costs for businesses and Inland Revenue. This rule applies to trading stock donated on or after 1 April 2024.

Research suggests the tax concession is an inefficient way of encouraging donations

27. There is a limited amount of research about the impact of tax incentives on donation behaviour in New Zealand and Australia. However, research undertaken by New Zealand academic Amy Cruickshank[6] and the Australian Productivity Commission[7] contains useful insights discussed below.

Elasticity of donations

28. New Zealand adopted a policy of providing tax concessions for charities as early as 1879. Donation-specific tax concessions were introduced in 1962 to reinforce and encourage giving. Underlying this policy is a view that the Government should use the tax system to support certain organisations that provide a public benefit.

29. One way to determine the effectiveness of a DTC for incentivising donations is by assessing whether it is "treasury efficient". Treasury efficiency compares the incremental increase in donations against the revenue a government forgoes through the DTC. The DTC can generally be considered treasury efficient if the absolute value of the elasticity of donations is greater than 1, meaning the DTC incentivises an increase in donations that is greater than the loss of government revenue from funding the DTC.

30. Cruickshank explored how effective the New Zealand DTC is at increasing charitable giving by estimating the elasticity of reported donations.[8] Her research found that the DTC is not treasury efficient because the absolute value of the elasticity of reported donations is estimated to be between 0.4 to 0.7. This means for every $1 in DTC provided by the Government, reported donations to charities increases by $0.40 to $0.70 on average. In other words, not all the tax concession is being passed on to the charitable cause. Instead, some of it is being retained by the donors.

31. Cruickshank concluded:

> "The important policy implication of the findings is that the price elasticity of demand of actual donations is inelastic (less than one in absolute value) meaning that the additional donations generated by the tax credit are less than the loss of government revenue from funding the credit."

32. The Australian Productivity Commission found that the price elasticity of giving in Australia has a wider range – from 0.48 to 1.67. However, there are a number of

[6] Cruickshank, A. (2022). Elasticity of Reported Donations: Bunching Evidence from New Zealand. *Working Papers in Public Finance*, Victoria University Chair in Public Finance (WP21/2022)
[7] "Future foundations for giving: Inquiry Report" Australian Government Productivity Commission, 10 May 2024
[8] Cruickshank entered into a formal agreement with Inland Revenue to access administrative data on DTCs claimed between 2000 and 2018. No other researcher has access to this data because it is not in the Statistics NZ IDI (see paragraph 12). Her study has the advantage of observing changes in donation behaviour following an increase to the fixed dollar ceiling for donations in 2002–03 and its removal in 2008–09.

complexities modelling for Australia compared to New Zealand. One important difference is that Australia's donation tax concessions follow a tax **deduction** model rather than a **credit** model, so concessions in Australia are affected by the donor's marginal tax rate and changes in effective marginal tax rates over time. That is not the case in New Zealand, where all individual donors receive a tax concession of 33 $^{1}/_{3}$%.

33. Both Cruickshank and the Australian Productivity Commission noted that whether the DTC is treasury efficient is not the only factor that should be considered when setting a DTC cap.[9] This is because treasury efficiency does not account for the costs and benefits of giving. Other factors include:

    33.1 Delivering support through government grants, as an alternative to a DTC, may not be efficient because the Government may have imperfect information.

    33.2 Additional giving incentivised by a DTC can improve social capital.

    33.3 The community is empowered when the Government cedes some control over where revenue is directed.

Efficiency may increase if the tax concession is more timely

34. The timing of tax incentives for charitable giving affects the elasticity of donations. Academic research on DTCs in Quebec found that providing the tax benefit closer to the time of the donation increased the number of donations because donors value the tax benefit more if they receive it earlier.[10]

35. A policy change to allow DTC refunds to be released to donors closer to the time of the donation could increase the number of reported donations (and the elasticity of donations). As noted above, the payroll giving scheme already allows for DTCs to be refunded closer to the time of giving. Encouraging uptake of this scheme, as well as reviewing the policy design, could be included in a donations tax package to make the tax credit more effective.

DTC regulatory stewardship review

36. Inland Revenue has been carrying out a regulatory stewardship review of the DTC. That review is being submitted to an Inland Revenue internal committee on 2 October 2024. The draft findings concluded that while the regime performs adequately, there are significant opportunities for improvement and reform.

37. Any changes required as a result of the review would be considered against various organisational priorities. Policy changes need to be weighed against the TSPWP, while operational changes must be evaluated in the context of internal enterprise priorities.

[9] A recent paper challenges the idea of treasury efficiency being a relevant metric: Kaplow, Louis. "Optimal Income Taxation and Charitable Giving". NBER Working Paper No. 31752, October 2023. That paper points out that if increased taxes that tax income at a higher rate can be levied on those who donate to charities, then efficiency can be improved even if the treasury efficiency is below 1. This is because they will pay the same amount of income tax (through the replicating tax) but the "price" of giving can be set to match the public benefit of giving. This is true but the replicating tax seems unlikely to be levied in reality.

[10] Source: Hickey, R., Minaker, B., & Abigail Payne, A. (2019). "The Sensitivity of Charitable Giving to the Timing and Salience of Tax Credits". *Melbourne Institute Working Paper No. 02/19* Melbourne Institute: Applied Economic & Social Research.

Other factors may have a greater impact on donating to charities

38. A notable international trend is that fewer donors are donating to charities that offer tax incentives. This indicates tax incentives are often not the most important factor for motivating charitable giving.[11] Cruickshank noted that the trend may be due, in part, to more donations going directly to people in need (for example, via crowdsourcing).

39. Other considerations that may have a greater effect on donation behaviour include:[12]

    39.1 Creating an environment that fosters a culture of giving. Educating and informing people can encourage those who give to do so more often and may encourage those who don't currently donate to do so.

    39.2 The ability of organisations to fundraise publicly.

    39.3 Reducing the compliance burden on donors who are eligible to claim a tax concession.

Potential tax policy responses

Explore a lower donation cap

40. There are several ways to target or cap donation tax incentives, such as reducing the maximum amount of a claim, reducing the rate (currently 33⅓% for DTCs) and restricting eligible donee organisations.

41. Our advice is to explore a lower donation cap for individuals, payroll giving, companies and Māori authorities (IR2024/237 refers). This will reduce integrity concerns when fraud and tax avoidance could occur. Depending on the design, it could result in a significant revenue gain but only impact on a small proportion of donors.

42. A lower donation cap will require several related policy settings to be considered. This includes the current rules for trading stock donated by businesses, trustee income allocations to tax exempt entities such as charities, and the charity deregistration tax calculation, which assumes donations of money to charities have been eligible for donation tax concessions.[13]

43. The net gain for the Government will also need to be considered. If a change in the donation tax concession reduces charity donation income, some charities may reduce their services, resulting in an increase in demand for government support.

Explore simplifications for donors

44. Our advice is to consider a lower donation cap in conjunction with simplification measures. These simplifications could include allowing DTC refunds to be released before year-end (IR2024/237 refers) and mitigate, to some extent, concerns likely to be raised by donors and the charitable sector.

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[11] "Future foundations for giving: Inquiry Report" Australian Government Productivity Commission, 10 May 2024, (p. 3).
[12] Source: Charities Aid Foundation, (2016). "Donation States: An international comparison of the tax treatment of donations". https://www.cafonline.org/docs/default-source/about-us-publications/fwg4-donation-states
[13] The deregistration tax rules are designed to claw back tax benefits if a registered charity deregisters. Gifted assets that are not money are currently excluded from the rules, but gifts of money are included on the assumption that the donors have received tax benefits.

Next steps

45. If you want to progress this work as part of Budget 25, or as part of work that is publicly announced on the TSPWP, we suggest you:

    45.1 Inform the Minister for the Community and Voluntary Sector, because it may be relevant for The Hon Louise Upston's plans to double philanthropic giving.

    45.2 Decide whether you will include work on simplification measures at the same time.

    45.3 Indicate to officials whether you need any further analysis of particular cap levels or other advice.

Recommended action

We recommend that you:

1. **Include** donation tax concession caps as a sensitive Budget project for officials to undertake further analysis.

   Hon Nicola Willis — Hon Simon Watts

   Agreed/Not agreed — Agreed/Not agreed

   OR

   Include donation tax concession caps on the published TSPWP for officials to undertake further analysis.

   Hon Nicola Willis — Hon Simon Watts

   Agreed/Not agreed — Agreed/Not agreed

   OR

   Stop work on this initiative.

   Hon Nicola Willis — Hon Simon Watts

   Agreed/Not agreed — Agreed/Not agreed

2. **Include** related donation simplification measures in the further analysis to be undertaken by officials, if this initiative is to continue.

   Hon Nicola Willis — Hon Simon Watts

   Agreed/Not agreed — Agreed/Not agreed

s 9(2)(a)

Jean Le Roux
Manager
The Treasury

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2024

Hon Simon Watts
Minister of Revenue
/ /2024

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: Donor-controlled charities

Date:	20 September 2024	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2024/360

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to recommendations	4 October 2024
Minister of Revenue	**Agree** to recommendations	4 October 2024

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Stewart Donaldson	Principal Policy Advisor	s 9(2)(a)	✓
Peter Frawley	Policy Lead		
Libby Young	Policy Advisor		

20 September 2024

Executive summary

1. This report responds to the Minister of Revenue's request for more information about donor-controlled charities to inform decisions about the charity component of the tax and social policy work programme (TSPWP).

2. Donor-controlled charities can access the same tax concessions as other charities. However, they are not subject to specific integrity rules despite the donor retaining control over how donations are spent. From a tax perspective this raises three areas of concern:

   - The current high donation tax credit (DTC) cap can result in DTC abuse when there are circular transactions between donors, charities they control, and their associates.
   - The absence of arm's length boards and investment policies can result in abuse of the charity income tax exemption involving transactions that are not on arm's length terms. These include loans, investments and asset acquisitions.
   - The absence of a minimum distribution rule for donor-controlled charities is more likely to result in unrestricted accumulation and a significant timing mismatch between the tax benefit and the ultimate public benefit being achieved, compared to charities with independent boards and trustees.

3. These areas of concern are addressed in Australia, where donor-controlled charities[1] must maintain a current investment strategy, investment transactions must be arm's length on commercial terms unless favourable to the fund, and the funds must distribute a minimum amount each year. Canada and the United States have similar rules. The United Kingdom has specific anti-tax avoidance rules that tackle abuse when there are circular transactions involving donations and the Charity Commission actively monitors charity reserves.

4. The volume of medium and large significant donor-controlled charities in New Zealand is low but the fiscal amounts involved are significant, s 6(c)

5. We recommend exploring tax integrity policy options based on overseas experience, such as defining donor-controlled charities in legislation and restricting donation tax concessions and income tax exemptions unless certain requirements are met.

6. Introducing tax-specific donor-controlled charity rules is likely to result in improved tax integrity rather than raise tax revenue.

7. If a decision is made to significantly reduce the current donation tax concession caps (T2024/2572, IR2024/359 refers), tax integrity issues involving donor-controlled charities will also reduce but will still exist. In our view, policy options should continue to be explored even if the donation cap is significantly reduced.

8. If you wish to progress this work as part of Budget 25, or as part of work that is publicly announced on the TSPWP, we suggest you:

   8.1 s 9(2)(f)(iv)

   8.2 Define the scope to include:

[1] Defined in Australia as "private ancillary funds".

- accumulation practices in donor-controlled charities, and
- transactions between donor-controlled charities and associated persons that raise tax integrity concerns.

8.3 Indicate to officials whether you need any further analysis of donor-controlled charity information or other advice.

Purpose

9. On 15 August 2024, the Minister of Revenue asked for more information about donor-controlled charities to inform decisions about the charity component of the TSPWP. The information in this report supplements information about donor-controlled charities provided in recent reports (T2024/1992, IR2024/292 and IR2024/237 refers). Other charity-related matters, concerning donation tax concession caps and the definition of charitable purpose, have been reported separately at the same time as this report (IR2024/359, T2024/2572 and BN2024/387 refers).

Tax treatment of donor-controlled charities

Definition of donor-controlled charities

10. The term donor-controlled charity refers to a charity registered under the Charities Act 2005 that is controlled by the donor, the donor's family, or associates. Donor-controlled charities may take the organisational structure of either charitable trusts or limited liability companies.

Tax benefits received by donor-controlled charities

11. Donor-controlled charities can access the same tax concessions as other publicly supported registered charities. They are exempt from income tax, have donee status so that their donors can claim DTCs or gift deductions, and are exempt from fringe benefit tax (FBT) in some circumstances.

12. Donors can establish a donor-controlled charity and receive donation tax concessions (a return of one third of the amount donated) for any qualifying donations made to the charity. Since 2008–09, the total qualifying donations for a year has been capped at the donor's taxable income in the year the donations were made (a much higher cap than the $1,890 previously allowed for individuals and the 5% of net income allowed for companies). More information about donation caps is discussed in IR2024/359.

Financial position of donor-controlled charities

13. s 6(c)

Issues with tax treatment of donor-controlled charities

14. We have analysed large donor-controlled charities on the Charities Register and have summarised behaviours that take advantage of the current settings for

charities (refer to Annex 1 for more detail). There are two issues with the current policy settings as they apply to donor-controlled charities.

Control

15. There is no requirement under the Charities Act for donor-controlled charities, or any registered charities, to have arm's length boards or investment policies. The founders can retain full control over the operation, governance, investments, and charitable distributions. Due to this level of control, donor-controlled charities and associated persons can engage in circular transactions that are not on arm's length terms.

16. Examples of these transactions include:

    16.1 The charity making a loan with a below market interest rate to the donor or associate.

    16.2 The charity purchasing an asset from the donor or associate, potentially at an above market rate.

    16.3 The charity investing in companies closely held by the donor or an associated person.

17. These transactions can raise valuation issues and result in wealth transfers from the charity to the donor and their associates. Some of these cases can be addressed by existing anti-avoidance provisions, however relying on anti-avoidance provisions is difficult and resource intensive.

Accumulation

18. Current rules allow all charities to accumulate tax-exempt surpluses and grow their net assets. One of the primary tax policy concerns with unrestricted accumulation is the timing mismatch between the tax benefit and the ultimate public benefit being achieved. Some charities may have good reasons to accumulate funds (for example, to save for the acquisition or construction of capital assets), however the reasons to accumulate are not as strong for donor-controlled charities, particularly if their sole purpose is to fundraise for other charities.

19. The tax policy concern about accumulation is heightened for donor-controlled charities because without an independent board they can more easily accumulate funds than other charities. Donor-controlled charities may have no immediate desire to distribute charitable funds and instead accumulate so the fund can be self-sustaining in the future. This is why minimum distribution rules and associated person rules have been adopted for donor-controlled charities in some other countries.

20. The ability for donors of donor-controlled charities to receive donation concessions immediately, while being able to minimise the charity's distributions and invest funds in related entities, indicates New Zealand has unusually loose rules around donor-controlled charities.

International comparisons

New Zealand is an international outlier

21. New Zealand is an outlier in taking a "hands off" approach to donor-controlled charities. Australia, Canada and the United States have specific rules for these types of organisations. In the United Kingdom, these entities are treated the same as

other charities. However, the United Kingdom's focus on attracting international philanthropists provides a different context for that approach.

Governance and investment policies

22. In Australia, "private ancillary funds" must maintain a current investment strategy and investment transactions must be on arm's length terms, unless favourable to the fund or a deductible gift recipient.

23. Canadian foundations are not allowed to engage in any related or unrelated business activity.

24. In the US, private foundations are restricted from making certain transactions with donors or their associates. Prohibited transactions include the sale or lease of property, lending money, and providing goods or services. A private foundation may own no more than 20% of an unrelated business. There are also restrictions on private foundations making "jeopardizing investments" that are unusual or speculative, such as commodity futures and options.

25. In the United Kingdom, all charities must demonstrate that their spending is in line with their charitable objects. Donor-controlled charities can potentially be used for tax avoidance purposes. There are specific anti-tax avoidance rules (tainted charity donations rules) that tackle abuse when there are circular transactions involving donations.

Accumulation

26. Australia, Canada and the United States require private foundations to distribute a minimum amount each year:

    26.1 Australia's minimum distribution is 5% of the market value of the charity's net assets in the previous year

    26.2 Canada's minimum distribution is either 3.5% or 5% of the average value of the charity's property not directly used in charitable activities or administration, depending on whether the value of the property is above or below $1 million.

    26.3 The United States minimum distribution is 5% of the total fair market value of the charity's non-charitable-use assets.

27. Generally, the policy rationale is to ensure that foundations funded with tax-relieved contributions (and often controlled by donors) provide some immediate public benefit even when a foundation intends to operate in perpetuity.

28. In Canada, before 2023, charities could carry forward excess distributions for five years and seek approval to accumulate funds for specific projects.

29. There are no minimum distribution rules in the United Kingdom. However, United Kingdom regulation does not allow charities (including foundations) to accumulate resources without a good reason for doing so. Charities must develop, publish and apply a reserves policy, which is monitored by the Charity Commission.

Donations

30. In Australia, private ancillary funds are funded by gifts from associated parties and the trustee of a fund must not solicit donations from the public. There is a limit on the total amount of donations a fund can accept from unrelated parties (up to 20% of the market value of the fund's assets).

31. In the US, deductions for donations to charities are limited to a maximum of 50% of the donor's income for public charities and 30% for private foundations.

Accumulation within fundraising charities: DIA consultation in 2019–20

32. As part of the work to modernise the Charities Act, officials from the Department of Internal Affairs (DIA) consulted on whether low distribution levels by "fundraising charities", which make grants to other charities but do not carry out charitable activities themselves, could undermine public trust and confidence in the charitable sector.

33. Submitters from the sector did not consider this was a problem. They advised that charitable purposes can be furthered by accumulating funds within any type of charity, including fundraising charities, and "an approach to focus on a newly defined class of charities was arbitrary, too simplistic, and would be very difficult to implement". They emphasised that all charities must be established for charitable purposes and that the only requirement is that funds, when distributed, must be for public benefit and not for private benefit.

34. In response to stakeholder feedback, DIA did not pursue policy options involving minimum distribution levels for fundraising charities and instead focused on the matter of transparency. However, DIA introduced a new reporting requirement. For years beginning on or after 1 April 2024 medium and large charities[2] must report annually about how they plan to use their accumulated funds.

35. Issues relating to timing mismatches between charitable tax concessions and delayed public benefit were not analysed by DIA because tax issues were excluded from the terms of reference of its work.

Potential tax policy responses

36. Any reform for donor-controlled charities would have the policy objective of changing donor behaviour to ensure donations made to donor-controlled charities are used for charitable purposes. This behaviour change is likely to be fiscally neutral or have only a small fiscal gain depending on the design of the reform to reduce timing mismatches. Potential changes have not been costed at this stage.

Status quo

37. The decision to progress a tax policy response to charitable business activity issues could be deferred until information from the new Charities Act reporting requirements is analysed. If you do not want to progress policy work at this stage, we will continue to monitor and report on integrity issues relating to donor-controlled charities as they arise.

38. We do not recommend this approach. Information disclosed by charities under the new reporting requirements may shed light on why charities are accumulating funds but will not help address tax policy concerns with donors obtaining a private benefit due to timing mismatches between donations and donor-controlled charities providing delayed or no public benefit. The new reporting requirements will also not help address concerns with circular, non-arm's length transactions.

Explore tax policy options to address issues with donor-controlled charities

39. We recommend exploring tax policy options to improve the fairness and integrity of charitable tax concessions in relation to donor-controlled charities. This could

[2] With operating payments above $140,000 per annum.

include defining donor-controlled charities in legislation and restricting donation tax concessions and income tax exemptions unless certain requirements are met. Restrictions could be targeted at larger donor-controlled charities to minimise the impact on smaller charities.

40. Restrictions could be introduced to require transactions between donor-controlled charities and associated persons to be on arm's length terms or prohibited outright. This would limit the ability for donors to transfer wealth out of the charity through non-arm's length transactions or circular arrangements. Instead, or in conjunction, anti-avoidance provisions could be introduced for the specific arrangements involving transactions with associated persons.

41. Minimum distribution rules could be designed to require donor-controlled charities to make a minimum charitable distribution each year. This would mitigate concerns about donors obtaining a private benefit from timing mismatches between the donor donating to a donor-controlled charity and the charity delaying providing any public benefit.

42. Distribution rules could be complex in design, particularly regarding what type of expenditure qualifies as a charitable distribution if donor-controlled charities would be allowed to directly undertake charitable work themselves. These rules may also result in monitoring and compliance administration costs for Inland Revenue. Despite this, we think the tax issues warrant a policy response. There is international precedent for minimum distribution rules, as Australia, Canada and the United States follow a similar approach.

Next steps

43. If you wish to progress this work as part of Budget 25, or as part of work that is publicly announced on the TSPWP, we suggest you:

    43.1 s 9(2)(f)(iv)

    43.2 Define the scope to include:

    - accumulation practices in donor-controlled charities, and
    - transactions between donor-controlled charities and associated persons that raise tax integrity concerns.

    43.3 Indicate to officials whether you need any further analysis of donor-controlled charity information or other advice.

Recommended action

We recommend that you:

1. **Include** donor-controlled charities as a sensitive Budget project for officials to undertake further analysis.

   Hon Nicola Willis — Agreed/Not agreed

   Hon Simon Watts — Agreed/Not agreed

   OR

   Include donor-controlled charities on the published TSPWP for officials to undertake further analysis.

   Hon Nicola Willis — Agreed/Not agreed

   Hon Simon Watts — Agreed/Not agreed

   OR

   Stop work on this initiative.

   Hon Nicola Willis — Agreed/Not agreed

   Hon Simon Watts — Agreed/Not agreed

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2024

Hon Simon Watts
Minister of Revenue
/ /2024

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: Charities and not-for-profits: Proposed 2025 public consultation

Date:	5 December 2024	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2024/454

Action sought

	Action sought	Deadline
Minister of Revenue	**Agree** to recommendations	20 December 2024

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Stewart Donaldson	Principal Advisor	s 9(2)(a)	☒
Philip Marshall	Senior Policy Advisor		☐

5 December 2024

Minister of Revenue

Charities and not-for-profits: Proposed 2025 public consultation

Purpose

1. Following confirmation of a charities/not-for-profit project on the tax and social policy work programme (TSPWP), this report seeks your agreement for a discussion document to be prepared, as well as agreement on the proposed topics and timeline for that document.

Background

2. The TSPWP, published on 13 November 2024, includes a project focusing on elements of charities and not-for-profits.

3. As part of reporting to you on the scope of that TSPWP project, you agreed that it would consider:

   - accumulation practices of charitable entities, including charitable businesses [IR2024-199 refers]
   - donor-controlled charities [IR2024-360 refers]
   - outdated exemptions that are difficult to justify [IR2024/237 refers]
   - options for mitigating the impact of Inland Revenue's soon to be released interpretation on not-for-profit member transactions and related policy issues [IR2024/238 refers], and
   - simplifications relating to volunteers and donations [IR2024-237 refers].

4. We also refer to the noting report IR2024/110: Charities and not-for-profits overview.

Discussion document

5. To progress the charities/not-for-profit TSPWP project, we recommend public consultation through a discussion document (the Discussion Document).

6. The Discussion Document would:

   - set out the charities/not-for-profit sector issues that the Government wishes to address, and
   - seek feedback on a range of solutions for addressing the issues identified.

7. Officials will then use the feedback received to inform advice to you on possible legislative changes.

8. s 9(2)(g)(i)

s 9(2)(g)(i)

Proposed timeframes

9. If you agree to proceeding with the Discussion Document as described, we recommend a publication date in late May/early June 2025.

10. A publication date in late May/early June 2025 means the Discussion Document would be out for consultation after:

    - s 9(2)(f)(iv)
    - the Budget in May 2025.

11. If you agree to a late May/early June 2025 publication date, we anticipate providing you with a draft of the Discussion Document in March 2025 for your feedback, with a final draft being considered by Cabinet in May 2025.

12. We agree with stakeholders that an extended consultation period is preferrable and therefore recommend an eight week consultation period.

Confirmation of topics to be included in Discussion Document

13. Based on previous reporting and discussions with you on the scope of this project, we recommend that the Discussion Document include the following topics:

    - integrity issues related to donor-controlled charities and the accumulation practices of fundraising charitable entities, including commercial businesses that are charities
    - not-for-profit member transactions and related matters
    - outdated exemptions that are difficult to justify, and
    - simplifications relating to volunteers and donation tax credits.

14. These topics are further described in the Appendix to this report.

15. From past reports, it is our understanding that none of the proposed topics are Budget sensitive and therefore can be included in the Discussion Document.

16. We note that you will also have another opportunity to make decisions on the content of the Discussion Document, including adding or removing topics, when we report to you with a draft Discussion Document in March 2025.

17. In the course of preparing the Discussion Document, we may identify additional issues that could also be included. We will identify any such issues when we report to you with the draft in March 2025.

s 9(2)(f)(iv)

19. s 9(2)(f)(iv)

20.

Early stage discussions with key stakeholders

21. As part of preparing the Discussion Document, we will engage with certain key stakeholders in the not-for-profit sector. This will allow us to test our thinking and proposed options before public release of the Discussion Document. This will also give us an indication about how proposed options may land with the not-for-profit sector more generally.

22. We will also engage with overseas revenue authorities to learn from their experiences dealing with similar charities/not-for-profit tax issues.

Proposed timeframes

23. We propose the following timeline for the preparation of the Discussion Document, consultation, reporting and possible legislation:

Date	Milestone
March 2025	Draft Discussion Document provided to you for comment
May 2025	Discussion Document to Cabinet for approval
Late May/early June 2025	Publication of Discussion Document
July/August 2025	Consultation period for Discussion Document
September/October 2025	Reporting to you on submissions and recommendations for legislative changes

24. We will provide you with a draft of the Discussion Document in March 2025, at which point you will have a further opportunity to consider the content and proposed options before you take it to Cabinet for approval.

s 9(2)(f)(iv)

Consultation

27. The Treasury and the Department of Internal Affairs were consulted as part of preparing this report.

Next steps

28. Subject to your agreement, we will begin drafting the Discussion Document with the intention of providing you with a draft for your consideration in March 2025.

29. We recommend that a copy of this report be referred to the Minister of Finance and the Minister for the Community and Voluntary Sector.

Recommended action

We recommend that you:

1. **Agree** that officials should prepare a Discussion Document for tax matters affecting the charities and not-for-profit sector.

   Agreed/Not agreed

2. If you agree to Recommendation 1, then **agree** that the following topics (further described in the Appendix to this report) be included in the Discussion Document:

   (a) integrity issues related to donor-controlled charities and the accumulation practices of fundraising charitable entities, including commercial businesses that are charities

   Agreed/Not agreed

   (b) not-for-profit member transactions and related matters

   Agreed/Not agreed

   (c) outdated exemptions that are difficult to justify, and

   Agreed/Not agreed

   (d) simplifications relating to volunteers and donation tax credits.

   Agreed/Not agreed

3. If you agree to Recommendation 1, then **agree** to a target publication date for the Discussion Document of late May/early June 2025.

   Agreed/Not agreed

4. s 9(2)(f)(iv) [redacted]

Noted

5. **Note** that the Discussion Document would be taken to Cabinet for approval in May 2025.

Noted

6. **Refer** a copy of this report to the Minister of Finance and the Minister for the Community and Voluntary Sector.

Referred/Not referred

s 9(2)(a) [redacted]

Stewart Donaldson
Principal Policy Advisor
Inland Revenue

Hon Simon Watts
Minister of Revenue
/ /2024

Appendix: Description of proposed Discussion Document topics

Topic One: Integrity issues related to donor-controlled charities and the accumulation practices of fundraising charitable entities, including commercial businesses that are charities

1. For this topic, we propose exploring options for improving the fairness and integrity of charitable tax concessions for charities and charitable businesses. This would include options for:

    1.1 defining donor-controlled charities in legislation

    1.2 restricting donation tax concessions and income tax exemptions for donor-controlled charities unless certain requirements are met, such as:

        1.2.1 maintaining a current investment strategy

        1.2.2 meeting minimum annual distribution thresholds, and

        1.2.3 ensuring reinvestment transactions are at arm's length on commercial terms, and

    1.3 exploring a minimum distribution threshold for certain fundraising charitable entities, including commercial businesses that are charities.

Topic Two: Not-for-profit member transactions and related matters

2. For this topic, we propose exploring options for mitigating the impacts of Inland Revenue's yet-to-be published guidance on the taxability of mutual transactions (including some subscriptions), as well as options for reducing compliance costs for not-for-profits, including:

    2.1 reviewing the size and design of the $1,000 standard not-for-profit deduction

    2.2 clarifying and simplifying the return-filing rules for not-for-profits, so that inactive or small not-for-profits are either not required to file an income tax return, or are only required to file a simple self-assessment return confirming they fall within a de minimis threshold, and

    2.3 clarifying the rules related to how not-for-profits with taxable income under $1,000, or a specific income tax exemption, apply for and confirm their ongoing eligibility for the RWT exemption.

Topic Three: Outdated exemptions that are difficult to justify

3. For this topic, we propose exploring whether the following tax exemptions are still appropriate in the context of New Zealand's broad-base, low-rate approach to taxation:

    3.1 s 9(2)(f)(iv)

    3.2 non-resident charity tax exemption

    3.3 friendly societies tax exemption

    3.4 bodies promoting scientific or industrial research income tax exemption

    3.5 veterinary service body income tax exemption, and

3.6 herd improvement body income tax exemption.

Topic Four: Simplifications relating to volunteers and donation tax credits

4. For this topic, we propose exploring issues and possible policy solutions relating to compliance costs faced by volunteers receiving honoraria, and taxpayers claiming donation tax credits. This would include exploring:

4.1 an option for honoraria paid to volunteers to be treated as "salary or wages" rather than as a schedular payment, allowing volunteers to receive automatic assessments, and to have ACC levies and social policy amounts withheld at source by the payer.

4.2 options for allowing volunteers to be paid non-taxable honoraria under a certain threshold amount

4.3 ways to simplify the requirements for customers claiming donation tax credits, based on recommendations in the donation tax credit regulatory stewardship review.

Inland Revenue
Te Tari Taake

Policy
Taukaea
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New Zealand

T. 04 890 1500

Briefing note

Reference: BN2024/504

Date: 11 December 2024

To: Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Helen Kuy

From: Stewart Donaldson
Phil Marshall

Subject: Charities and not-for-profits consultation: Scope and timing changes

Purpose

1. In IR2024/454 *Charities and not-for-profits: Proposed 2025 public consultation* we recommended topics for a charities and not-for-profits discussion document and proposed an issue date of late May/early June 2025.

2. The Minister asked for a briefing note setting out an alternative timeline, along with advice on any implications, if the scope is expanded to include business income of charities and the consultation document does not go through Cabinet.

Scope

3. We understand the Minister wants advice on the implications of extending the scope of public consultation to include removing the income tax exemption for the business income of charities.

4. If the Minister decides to extend the scope, we will put up a report confirming the decision because it reverses the earlier decision in T2024/2396, IR2024/199.

5. As we advised previously, moving to an approach of taxing charity business income when the business activity is unrelated to a charitable purpose can be complex. We anticipate that if a consultation document includes this option, the consultation will be at a relatively high level rather than a detailed level. Alternatively, if the Minister would like consultation to occur on details, our advice would be to allow an additional month in the below timeline so that details can be worked through. This would mean a final consultation document would be provided to the Minister in April/May 2025.

6. s 6(c)

s 6(c)

7. Our strong advice would be to put the consultation document through Cabinet given the politically sensitive nature of the work and the very high public interest.

8. Feedback we have received from accounting and legal firms is that it would be helpful for the Government to make a public statement about the extent of the policy review of charities and not-for-profits sooner rather than later. They have indicated that their clients are "on edge" and second-guessing what the Government intends to do.

Alternative timeline

9. We think it would be feasible to have a draft consultation document with the extended scope ready in late March/early April 2025. We would provide the Minister with a working draft in late February/early March 2025.

10. The following timeline for the preparation of the consultation document, consultation, reporting and possible legislation:

Date	Milestone
February/March 2025	Consultation document (working draft) provided to the Minister for comment
March/April 2025	Final consultation document provided to the Minister
April-June 2025	Publication and consultation
July/August 2025	Reporting to the Minister on submissions and recommended next steps

11. Matters that could affect this timeline include:

    - The Minister has a meeting scheduled with the Minister of Finance and the Minister for the Community and Voluntary Sector on 30 January 2025 to discuss the Government's approach to the sector.

12. s 9(2)(f)(iv)

    - It is possible that charity-related tax matters could be included in the May 2025 Budget.

Consultation with the Treasury

13. The Treasury was not consulted about this briefing note.

Stewart Donaldson
Principal Policy Advisor
s 9(2)(a)

s 6(c)

Inland Revenue
Te Tari Taake

POLICY/TAUKAEA

TE TAI ŌHANGA
THE TREASURY

Tax policy report: Reducing expenditure on donation tax concessions

Date:	11 December 2024	**Priority:**	Medium
Security level:	[IN CONFIDENCE] Sensitive - Budget	**Report number:**	IR2024/482 T2024/3292

Action sought

	Action sought	Deadline
Minister of Finance	Agree to an option set out in the Appendix	28 January 2025
Minister of Revenue	Agree to an option set out in the Appendix	28 January 2025

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Peter Frawley	Policy Lead Inland Revenue	s 9(2)(a)	☒
Brandon Sloan	Principal Policy Advisor Inland Revenue		☐
Paul Quirke	Senior Analyst Treasury		☐

11 December 2024

Minister of Finance
Minister of Revenue

Reducing expenditure on donation tax concessions

Purpose

1. This report seeks decisions on whether and how to reduce the expenditure on donation tax concessions. This report follows our previous advice: *Donation tax concessions cap* (IR2024/359, T2024/2572, 20 September 2024 refers).[1]

Executive summary

2. You sought additional advice on donation tax concessions, with particular focus on the donation tax credit, as a Budget 2025 project. Options for reducing this expenditure are set out in more detail in the attached Appendix *Options for reducing the tax expenditure connected with the donation tax credit*.

3. The broad options are:

   3.1 Remove the credit and all other tax measures that support donations to donees. This option is consistent with the Government's broad-base, low-rate tax policy framework.

   3.2 Lower the maximum threshold (cap) above which donations cease to be eligible for the donation tax credit. The current maximum threshold is described in terms of a taxpayer's taxable income. The options presented are a deep cut, a moderate cut, and a conservative cut to the cap. These options assume the tax credit remains at $33^{1}/_{3}$%.

   3.3 Reduce the percentage value of the tax credit to 25%. This option should also be supported by a reduction in the maximum cap above the options set out in this report. This option is efficient but applies to all donors who claim a tax credit (around 350,000 individuals).

4. Any change to the donation tax credit system would also need to be supported by additional changes to the rules for payroll giving, and company and Māori authority tax deductions, which are substitutable forms of providing donations to the donee sector that also attract tax benefits. These are discussed in paragraphs 34 to 42.

5. In our view, the earliest the proposed changes could be implemented is for the 2026–27 income year, meaning an effective date of 1 April 2026 for most individual taxpayers.

6. The Department of Internal Affairs (DIA) has been consulted, and its view is set out in paragraphs 56 to 61. We recommend that before you decide on a preferred option you meet with the Minister for the Community and Voluntary Sector on 30 January 2025.

[1] Earlier advice (IR2024/237, 17 July 2024 and IR2024/292, 8 August 2024) has also been provided on the tax treatment of the not-for-profit sector. Our recent report IR2024/454, 5 December 2024, provided advice on a proposed discussion document that will include initiatives to simplify the tax rules for volunteerism, and the donation tax credit.

7. Subject to your decision on the options contained in the Appendix, we will report to you again in late February 2025 seeking final policy approval, including any additional amendments to ensure the integrity of your preferred option.

8. Inland Revenue will include the high-level estimates contained in this report as a Vote Revenue placeholder initiative for the Treasury's Budget initiatives template on 23 December 2024, pending a future decision on whether this initiative is invited into the Budget process.

Context

There are good reasons to support charitable giving

9. The reasons that governments seek to promote charitable giving are:

   9.1 Donee organisations may help governments to further social objectives, such as increasing support to those members of society who are disadvantaged, and to foster a more caring and cohesive society.

   9.2 The activities of donee organisations may provide wider benefits to society over and above the value of the tax benefits received by the recipient or the supplier of the activity.

   9.3 The activities of donee organisations may be more responsive to the needs of society and able to deliver timely programmes that respond to changing social needs. Donations to such organisations can provide an effective indicator of the extra goods and services that society feels are needed.

   9.4 There may be wider benefits to society if the government relaxes its prerogative on taxes by supporting civil society because it allows the development of activities that may not otherwise exist if left to either the government or the commercial sectors.

Tax policy settings are aimed at encouraging giving

10. Post-2009, tax policy settings have been designed to encourage a culture of charitable giving. The objective is to create the outcomes noted in paragraph 9, and create financial resilience for donee organisations by tax incentivising the private sector (households and businesses) to contribute financial resources. The trade-off for creating these outcomes is the revenue cost (expenditure).

11. We note that the Minister for the Community and Voluntary Sector has recently commissioned work from the DIA to explore ways to grow the private sector's contribution to the charitable sector. The Minister has asked for this work to be done in collaboration with Philanthropy New Zealand.

12. New Zealand is not alone in this objective. We also note that the current Australian Government aims to double the level of charitable giving to Australian charities by 2030.[2] Apart from adjusting some eligibility criteria[3] for when a donation can benefit from a tax concession, we are not aware of any changes to current tax policy settings to achieve this aim.

[2] https://ministers.treasury.gov.au/ministers/andrew-leigh-2022/media-releases/harnessing-generosity-boosting-philanthropy Finding 4.1. The Commission noted that there was no compelling evidence to support a case for adjusting Australia's tax deduction settings for gifting.
[3] This relates to when an entity qualifies as a "deductible gift recipient". Australia operates a tax deduction method for supporting donations. This applies to individuals as well as companies. Donations to religious institutions are not eligible for tax benefits.

Problem definition: Donation tax credit

Expenditure on donation tax credit is growing

13. Expenditure on the donation tax concessions has grown since the change to the income cap (from the previous monetary cap) in 2009. This resulted in an increase in donation tax credit claims of 66% (2008–09) compared to the prior year.[4] This outcome was not a result of an increase in the number of individuals donating, but an increase in the total amount of donations claimed by a reduced pool of donors.

14. For the year ending 31 March 2023, donations of money totalling approximately $1.1 billion were subject to tax concession claims, with a tax cash value of approximately $350 million. Approximately $315 million of this $350 million represents the value of donation tax credits paid to around 350,000 individuals.

15. Despite these values, Inland Revenue's most recent stewardship review (2024) into the donation tax credit system indicated that there is low general public awareness of the tax credit.[5] This suggests that the current system subsidises the behaviour of those who are already prepared to donate, and there is an upside financial expenditure risk if the concession is promoted more actively.

16. New Zealand's donation tax incentive for individuals is generous by international standards. This is due to a combination of settings:

    16.1 it is payable as a refundable tax credit

    16.2 the credit is set at a relatively high rate

    16.3 it has a high maximum claim (cap), and

    16.4 the list of eligible donee organisations is relatively large.

17. In terms of managing the tax expenditure, we consider that its cost could be reduced by changing the settings in paragraphs 16.2 and 16.3 above. There are, in our view, strong taxpayer compliance and administrative strengths with retaining a flat-rate tax credit system. We also recommend that any changes to the list of eligible donee organisations should not be considered unless it is in the context of a wider review of the definition of charitable purpose.[6]

Evidence suggests tax concessions are not effective at encouraging giving

18. We previously commented on a 2022 paper from Victoria University of Wellington by Amy Cruickshank, on the "treasury efficiency" of the donation tax credit.[7] Cruickshank concluded that for New Zealand, the donation tax credit did not appear to be an effective means of encouraging additional donations. A similar study in Australia by its Productivity Commission (July 2024) found that while some donors were more likely to donate more due to tax benefits, an increase in income was a stronger indicator of a household's decision to donate more.

19. If the cost of Inland Revenue's administration of the donation tax credit system is also considered (including its vetting of claims, stewardship of payroll giving, and compliance activity), then current tax policy settings do not appear to be an efficient means of positively encouraging charitable giving.

20. International research often reaches mixed conclusions about the efficacy of tax incentives to encourage charitable giving, and like the Australian Productivity

[4] IR2024/359, T2024/2572 refers.
[5] The donation tax credit (rebate) had a higher profile prior to 2000 when it formed part of the IR5 individual tax return. The rebate had the effect of reducing end of year tax liabilities rather than being a stand-alone refundable tax credit.
[6] BN2024/387 refers.
[7] Ibid footnote 4.

Commission, typically find that income levels, personal beliefs, and macroeconomic conditions are more powerful motivators.[8] United States-based studies have observed, however, that a reduction in tax benefits produced a decrease in charitable giving. The decrease was more observable for non-religious charities, particularly those directed at the relief of poverty.

There are growing integrity concerns

21. Inland Revenue has observed a growing number of instances when donations can be part of an arrangement when alleged fraud or aggressive tax planning is involved. The current high cap significantly contributes to this behaviour.

22. For the year ending June 2024, Inland Revenue disallowed donation tax credit claims worth $31 million (relating to donations of $93 million). Approximately 85% of these claims were ineligible (for example, claims for non-monetary gifts or claims to entities that are not donee organisations) and, approximately 15% of these claims were fraudulent.

23. In addition, Inland Revenue has reviewed charities that have entered into arrangements with a donor to access donation tax concessions generally. This was part of Inland Revenue's compliance and binding ruling work. These arrangements can result in circular wealth transfers from the charity back to the donor and their associates. The arrangements also raise issues about whether the charity is genuine, has a valid charitable purpose, and whether it has only been established to accumulate arrangements with a donor to access donation tax concessions generally. Existing anti-avoidance provisions, including a donation-specific provision that was effective from April 2019, can be difficult to apply in these situations.

24. Reducing the value of the donation tax concessions, with a particular focus on the donation tax credit, could be a way of minimising these behaviours.

Options for reducing cost of donation tax credit

25. The Appendix sets out five possible options for Ministers to consider if the donation tax credit cap is to be reduced. We have assessed the options in terms of their impact on donors, donees, Inland Revenue, and government revenue. We have also indicated the likely cost of administering the changes.

26. The Appendix provides a range of options that trade-off fiscal sustainability against the positive social outcomes that charities provide. If fiscal sustainability is a priority, then you may prefer a deep cut to the donation tax credit threshold, or the removal of all donation tax concessions. Alternatively, if the priority is social outcomes, then you might prefer a more moderate or a conservative cut to the donation tax credit threshold.

27. We expect individual households would feel the impact of any policy change differently depending on (a) their initial decision to donate, and (b) whether the donor decides to claim a donation tax credit. As such, the effect of reducing or abolishing the credit is difficult to predict with any degree of certainty because we are unable to verify the tax sensitivity of donation decisions by donors.

[8] "Tax incentives for charitable giving: New findings from the TCJA", National Bureau of Economic Research, July 2024, Xiao Han, Daniel M Hungerman, Mark Ottoni-Wilhelm; "Tax Prices and Charitable Giving: Projected Changes in Donations Under the 2017 TCJA", November 2019, Jonathan Meer and Benjamin A Priday; and "Reforming Charitable Tax Incentives: Assessing Evidence and Policy Options" the Tax Policy Center, November 2018, Joseph Rosenberg and Eugene Steuerle.

Impact on households/donors

28. For some donors, changing the level of entitlement may impact existing giving commitments and consumption decisions.[9] A moderate cut in entitlements on the other hand would likely leave the majority of donation decisions by donors unaffected apart from large value one-off donations, for example, donations that concern the development of infrastructure assets, such as the construction of buildings, and other capital assets.

29. High-wealth households are considered tax sensitive when making donation decisions. In our recent report on the trust disclosures post-implementation review,[10] it was observed that discretionary trusts can be used as a means for these households to "donate", that is, distribute discretionary beneficiary income to a charitable donee, and reduce tax payable on trustee income. The tax benefit attached to this behaviour can produce a tax savings higher than that offered by the donation tax credit. However, we consider that the fiduciary duties trustees owe to all the beneficiaries of the trust would likely impose a natural limitation to this observable trend.

Impact on donee organisations

30. Inland Revenue does not hold readily available details about the donee organisations that benefit the most from donations eligible for tax concessions.[11] However, as an illustration, the publicly available data on the charities register indicates the following charities received the largest amount of monetary donations for the financial years ending in 2023.

s 6(c)



[9] For example, the payment of special character or building fund donations to an integrated or private school is a consumption decision. Another example could be a donor's decision to support a large community asset on the expectation that the after-tax cost of the donor's contribution is reduced by the donation tax credit.
[10] IR2024/481 refers.
[11] As noted in IR2024/359, the Inland Revenue categorises recipients of monetary donations into three categories: religious organisations (63%), schools (8%), and "other" (29%).

31. Donee organisations will be sensitive to a reduction in the donation tax credit cap and will be concerned about a reduction in donor financial support.

Financial impacts (revenue and administration)

32. Given the number of options set out in the Appendix, the estimates on the likely revenue impact of the options, including their impact on Inland Revenue, have been prepared using high-level assumptions. Once you have decided on your preferred option, we will finalise these amounts.

33. We note that a reduction in the donation tax credit cap could support administrative improvements, including paying donation tax credit claims more regularly throughout the year.[12] This type of initiative could help the broader government aim being promoted by the Minister for the Community and Voluntary Sector, to increase the private sector's support for the donee sector.

Measures needed to support reduction in donation tax credit cap

34. A reduction in the donation tax credit cap would need to be supported by other changes to the Income Tax Act 2007. The credit could be substituted by other tax benefits such as:

    34.1 Deductions for donations made by companies. The deduction reduces the company's taxable income and has a tax value of 28%. This deduction is subject to a net income threshold cap. Deductions are not permitted if the company is in tax loss.

    34.2 Deductions for donations made by Māori authorities. Similar to companies above, the deduction reduces the Māori authority's taxable income and has a tax value of 17.5%. This deduction is also subject to the same limitations in paragraph 34.1.

    34.3 Payroll giving (which provides a real-time tax credit for donations employees make via their salary and wages and has a tax value of $33^1/_3$%).

35. The implications for these deductions and credit are explained in more detail in paragraphs 36 to 42. If Ministers prefer a deep or moderate cut to the donation tax credit threshold, a return to the earlier 2009 threshold limits for companies and Māori authorities should be considered. These thresholds limited total donation tax deductions to a maximum amount equal to 5% of net taxable income.

Deductions for donations made by companies

36. A traditional view of companies is that that their activities should solely relate to the interests of shareholders. If companies wish to donate, it is a matter between the company and its shareholders, and not the Government. The Government shifted from this view in 1972 when it introduced tax deduction rules for companies for monetary donations. In practice, companies operating in local communities will often make donations to benefit activities in those communities and promote goodwill because they now apply good citizen principles to their business. Some, but not all, of this support could be substituted as tax deductible marketing and sponsorship, but these categories of expenditure will often come with GST implications. Also, for some payments it may be difficult to establish a business purpose. Therefore, from a simplicity point of view, the company may wish to treat the support as a donation.

[12] The current system relies on annual taxable income to calculate a taxpayer's final donation tax credit entitlement. This is why donation tax credits are typically paid out by Inland Revenue between May and June after the end of the prior tax year because this is when all the relevant income information about the taxpayer for that prior year has been received. A study found that Canadian donations increased after a policy allowed for the earlier release of tax credits for donations supporting the Haiti earthquake recovery and relief effort in 2010.

37. For the 2022–23 income year, company return disclosures showed around $90 million was deducted for payments to donee organisations.

Deductions for donations by Māori authorities

38. In the 2023 year, 53 Māori authorities recorded donations totalling $32 million, s 6(c) For these larger Māori authorities, the introduction of a donation tax cap, like that described in paragraph 35 would likely have an immaterial impact relative to their reported taxable income.

39. For smaller-scale Māori authorities, however, any recommendations that amend current processes could have a material impact due to the role that organisation plays in its local community when supporting cultural, sporting, and other social events. Such support would typically be provided in the form of koha (donations) as appropriate to tikanga. Inland Revenue has observed, since the inception of the Māori authority regime, smaller-scale Māori authorities can find it difficult to comply and additional constraints (such as reinstating a cap on donations) could have a detrimental effect on this compliance.

40. We will include a Treaty analysis consistent with the expectations set out in CO (19) 5: *Te Tiriti o Waitangi/Treaty of Waitangi Guidance,* on the implications of changing the tax deduction rules for donations made by Māori authorities in our next report.

Payroll giving

41. The purpose of payroll giving is to provide the donor with a real-time tax credit. Modelled on a similar scheme in the United Kingdom, the credit reduces the amount of PAYE withheld on an employee's salary and wages. About 1,800 employers offer payroll giving and 14,000 employees use it, with about $7 million donated in the year ending March 2023.

42. If Ministers prefer a deep or moderate reduction in the donation tax credit cap, we would recommend either the repeal, or redesign, of payroll giving. Enforcing a lower cap on payroll giving would likely require interventions to employee entitlements, which would be challenging for employers, and if a square up is needed, this would possibly result in debt implications and additional costly re-work for Inland Revenue, including additional taxpayer contact.

Implementation and transition considerations

43. Implementing the changes outlined in the Appendix would have costs for both donee organisations (managing donor commitments), and Inland Revenue (educating donors and donee organisations, and systems implementation). To this end, we would consider the earliest the changes could be implemented is for the 2026–27 income year. This would start 2 October 2025 for early filing taxpayers, and 1 April 2026 for most individual taxpayers.

44. We would not recommend retrospectively applying the proposed changes discussed in this report. We also do not recommend applying the changes from a date of announcement that is part-way through an income year because this would be problematic for Inland Revenue from a systems perspective.

45. Post-reform, Inland Revenue would need to manage two processes over a four-year period (the four-year time bar) for late claims for donations made before the 2026–27 tax year. This would be an additional commitment of resource for Inland Revenue, and this is reflected in the expected administrative impacts set out in the Appendix.

46. Inland Revenue would require new funding for Vote Revenue implementation (capital, operating, depreciation and capital charge). Inland Revenue has no

capacity to partially fund or fully fund such initiatives without directly impacting core service delivery, tax revenue, tax debt or system change, and maintenance capacity. At this stage, we have not assessed the capital and/or operating split of these cost estimates. Further, the cost estimates may change depending on the cumulative impact of these proposals and other initiatives that Inland Revenue may be required to deliver.

47. Changes to tax policy affecting entitlements may create an intertemporal shift in donating behaviour for those donors that have sufficient discretionary funds. A reduction in entitlements is therefore likely to bring forward donor commitments in some cases.[13]

Officials' recommended option

48. The private provision of donations to donee organisations has a range of positive external social benefits. Previous governments have, since 1962, used the tax system to incentivise the creation of those social benefits, with the last significant change in 2009, which resulted in a relaxation of the statutory constraints that applied to the donation tax concessions generally. The 2009 changes also resulted in the introduction of payroll giving (2010). Overall, the purpose of the 2009 reforms was to encourage a culture of charitable giving.

49. Since then, Inland Revenue has observed that a few taxpayers are using the donation tax concessions to produce circular wealth transfers from the charity back to the donor and their associates. Some of these arrangements are tax aggressive, but do not necessarily meet the threshold of being tax avoidance.

50. We also note that the Cruickshank study suggests that the 2009 reforms have not been successful in increasing the amount of monetary donations to donee organisations relative to the cost of the tax benefits to the Government.

51. These observations strongly suggest that the current threshold cap is inefficient and should be reduced for tax integrity reasons.

52. We consider the best option (assuming the retention of the current tax credit rate of $33^{1}/_{3}$%) is a deep reduction in the threshold (Option 2 in the Appendix). The DIA has concerns with this option as set out paragraphs 56 to 61.

53. Option 2 supports fiscal sustainability, efficiency, and mitigates Inland Revenue's increasing integrity concerns. This option would, however, be a significant change to current tax policy settings, which are directed towards encouraging a culture of charitable giving (that is, a return to pre-2009 conditions). Effects of this option are:

    53.1 Inland Revenue would probably process more donation tax credit claims as households allocate receipts across income earners to maximise entitlements.

    53.2 Households that have discretionary funds could bring forward donation commitments to take advantage of current entitlements in the income year prior to the option starting.

    53.3 Middle to high Equity Index schools, school building funds, and poverty-focused charities may call for additional direct government support.

    53.4 A low threshold would see New Zealand become an international outlier relative to Australia and other countries that seek to encourage donations, particularly from high-income individuals and households.

[13] Ibid Footnote 8. Tax Incentives for Charitable Giving: New Findings from the TCJA.

Consultation

54. Due to Budget processes and conventions, the advice in this paper has not been informed by (and has not had the benefit from) the views and opinions of stakeholders. While we have applied our best judgement based on information available to us (qualitative and anecdotal), some of the effects and impacts of the advice described in this report on donors and donees may be under- or over-stated.

55. Anecdotally, we have heard, on an in-confidence basis, a handful of tax practitioners express an opinion that there is merit in reducing the current tax threshold for the donation tax credit. We suspect, however, that their preferred threshold would be higher than the ones proposed in this report.

Department of Internal Affairs comment

56. The DIA has significant concerns with the preferred option (Option 2) put forward by the Treasury and Inland Revenue. A deep reduction to the donation tax credit cap as outlined in this report would likely have a detrimental effect on the charitable sector in terms of financial resilience and its ability to deliver goods and services to the communities in which it operates. There are many legitimate reasons for charitable giving, particularly when government services are not available or present, or when new areas of need are identified. Further, a priority for the Minister for the Community and Voluntary Sector is to grow philanthropic giving, something that is likely to be negatively impacted by reducing the donation tax credit cap.

57. In recent years, the pandemic, large-scale adverse weather events and broader economic challenges such as inflation, have affected the ability of charities and other not-for-profits to fundraise and sustain their operations. Reducing the potential tax benefit to people who make such donations may compound this. Efforts to fundraise or find new ways to make money can often take resources away from delivering the purpose of charities.

58. The proposed deep cut is likely to result in an overall decrease in donations – both the number made, and the amount donated (as estimated by this paper at 56,000 donors) as one of the incentives to make larger donations is removed. If such a reduction were to occur, there might be an expectation for government to fund more charitable entities to make up the shortfall.

59. If a change in the donation tax credit cap does proceed, the DIA would prefer either the moderate reduction or conservative reduction, particularly if other changes in tax policy are going to be considered, such as examining the tax status of charitable business.

60. The DIA would support work to boost the integrity of the wider not-for-profit tax space by changing arrangements of donor-controlled charities or examining the impact of a minimum distribution to charitable purpose by such charities. The DIA also considers payroll giving to be a useful mechanism and does not support its removal entirely should that be proposed. We would also support improvements to the payroll giving system.

61. Before deciding on your preferred option in the Appendix, the DIA recommends that you meet with the Minister for the Community and Voluntary Sector to discuss the proposals.

Next steps

62. Subject to your decisions on your preferred option, we will report again in late February 2025 with a paper to Cabinet seeking its approval to your preferred approach. The advice will also seek your agreement to the additional supporting measures required to the tax deduction rules for companies, and Māori authorities,

and the payroll giving rules to ensure the integrity of your preferred option. We will also confirm the financial implications of the reform package, including any new funding requirements to support Inland Revenue's implementation.

63. In the interim, Inland Revenue will add a placeholder initiative into the Treasury CFISnet system on 23 December 2024 pending final policy decisions and subject to an invite into the Budget 2025 process from the Minister of Finance.

64. A copy of this report should also be referred to the Minister for the Community and Voluntary Sector for her information prior to your meeting with Minister Upston on 30 January 2025.

Recommended action

We recommend that you:

1. **agree** to either:

   1.1 **indicate** on the Appendix (mark "yes" or "no") what options you would like us to consider for further advice in late February 2025.

   Indicated/Not indicated Indicated/Not indicated

   OR

   1.2 **instruct** us to stop work on reducing the tax expenditure connected with the donation tax credit and other donation tax concessions.

   Instructed/Not instructed Instructed/Not Instructed

2. **invite** your preferred option to reduce the expenditure on the donation tax credit into Budget 2025.

   Invite/Not invited Invite/Not invited

3. **discuss** the content of this report and the Appendix with the Minister for the Community and Voluntary Sector.

   Discussed/Not discussed Discussed/Not discussed

s 9(2)(a)

s 9(2)(a)

Jean Le Roux
Manager
The Treasury

Peter Frawley
Policy Lead
Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

Appendix: Options for reducing the tax expenditure connected with the donation tax credit

Options	Total annual donations $	Maximum value of tax credit (rounded to the nearest $1)	Estimated impacts*				Recommended/ comment	Minister of Finance	Minister of Revenue
			Donors	Donees	Additional administrative costs for Inland Revenue	Fiscal implications		Indicate preference	Indicate preference
1. Remove all tax benefits for donations to donee organisations	$0	$0	Decisions by households are affected as the cost of donating increases. 100% of individual donors affected. **Around 350,000 donors.**	Regular giving to religious institutions is unlikely to be affected because donors appear to be price insensitive. Other charities, including integrated and private schools may be strongly affected. Public schools would likely need to seek alternative assistance from the Crown.	Small-scale implication costs $0.5 million. Resources applied to monitoring donation tax credit claims would be reassigned within Inland Revenue.	$311 million increase a year. Note that some of the revenue savings would need to be recycled to fund grants to the sector.	No. There are simplification benefits with this option, but it would have a material impact on donee organisations. We would expect some donations to be brought forward in the year before application.	Yes / No	Yes / No
2. Deep reduction in the maximum threshold	$4,500	$1,500	Decisions by some households are affected as the cost of donating above the threshold increases, particularly large donations. 84% of individual donors are unaffected. **Around 56,000 donors are affected.**	Regular giving to religious institutions is unlikely to be affected because donors appear to be price insensitive. Other charities, including integrated and private schools may be affected and see a reduction in donation income.	Medium-scale implication costs $1 million, with $0.50 million ongoing costs. Increased number of tax credit claims (but not necessary value) as households allocate receipts across income earners to maximise entitlements. This may lead to additional taxpayer contact.	$106 million increase a year. Note that some of the revenue savings may need to be recycled to fund grants to the sector.	Yes (Officials' recommended option). The trade-off is that the Government may be expected to provide additional support to donees. This option would make New Zealand an outlier internationally in terms of having a low threshold. We would expect some donations to be brought forward in the year before application.	Yes / No	Yes / No
3. Moderate reduction in the maximum threshold	$15,000	$5,000	Most decisions by individual donors (97.7%) are unaffected, but high-value discretionary donations may be affected. **Around 8,000 donors affected.**	Schools (public, integrated and private are unlikely to be affected, apart from school building funds).	Medium-scale implication costs $1 million, with $0.50 million ongoing costs.	$40 million increase a year.	Some impact on donor decisions but this balances against tax integrity concerns. A change in the donation cap would have a positive impact on tax integrity and reduce the tax value of tax aggressive arrangements.	Yes / No	Yes / No
4. Conservative reduction in the maximum threshold	$60,000	$20,000	Most decisions by individual donors are unaffected (99.8%), but high-value discretionary donations may be affected. **Around 660 donors are affected.**	Most donees unaffected except those that rely on large donations from high-wealth individuals.	Medium-scale implication costs $1 million, with $0.50 million on going costs.	$17 million increase a year.	Some impact on donor decisions but this balances against tax integrity concerns. A change in the donation cap would have a positive impact on tax integrity and reduce the extent of tax aggressive arrangements.	Yes / No	Yes / No
5. Reduce the value of the tax credit to 25% (*should be accompanied by a reduced threshold*)	N/A	N/A	Most decisions by individual donors are affected and the after-tax cost of donating is increased. 100% of individual donors affected. **Around 350,000 donors.**	If the amount of the tax benefit is reduced, donees could be in a worse position than the status quo.	Low-scale initial set up costs $0.5 million, with $0.5 million ongoing costs.	$86 million increase a year.	This is an efficient option. A change in the tax credit rate would increase the cost of donating for every donor relative to the status quo. Whereas a change in the donation cap increases the cost of donating for a small proportion of donors.	Yes / No	Yes / No

* These Inland Revenue estimates are high level and illustrative only. Each estimate is separate to each specific option. Combining options such as Option 5 with Options 2 to 4 would need to be separately evaluated.

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Briefing note

Reference: BN2025/032

Date: 31 January 2025

To: Revenue Advisor, Minister of Finance – Emma Grigg / Felicity Barker
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Helen Kuy

cc: Peter Mersi, Commissioner
David Carrigan, Deputy Commissioner
Graeme Morrison, Policy Director
Maraina Hak, Policy Director
Phil Whittington, Policy Director
Joanne Petrie, Executive Support Advisor to the Commissioner
Jill Compton, PA to Deputy Commissioner
Governance, Ministerial & Ministerial Services
Jayne Beggs, Director, Department of Internal Affairs

From: Stewart Donaldson
Philip Marshall

Subject: Summary of the "charity business income tax exemption" issue

Background

1. The Minister of Finance's office has asked for a brief summary of the "charity business income tax exemption" issue.

2. A brief summary is attached. This draws on previous advice (IR2024/199, T2024/2396 and IR2024/237 refers).

Consultation with the Treasury

3. The Treasury was informed of this briefing note.

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
s 9(2)(a)

Charity business income tax exemption

Background

1. The tax policy framework for the charitable sector is based on the principle that Government should give up some of its taxing rights to support organisations which provide a public benefit.

2. The framework takes a "destination of income" approach. This means that business and non-business income is tax exempt if it is derived by a registered charity and is ultimately destined for a charitable purpose. Income can be accumulated for many years and will still qualify for the tax exemption.

3. New Zealand's approach to taxing business income is at odds with most OECD countries, with the exceptions of Australia and Malta. Other countries have either restricted the commercial activities a charitable entity can engage in, or they tax commercial income unrelated to charitable purpose activities. This is largely in response to revenue loss concerns and/or a widespread perception that exempting business income from tax may create an unfair competitive advantage.

4. Business activity covered by the current charity income tax exemption includes property development, farming, tourism, fishing, electricity generation and distribution and food production. Commercial activities carried out by Māori collective entities, such as Māori Trust Boards and Post Settlement Governance Entities, tend to be concentrated in the property, forestry, and fisheries sectors. A number of these activities—in particular fisheries settlement assets—are conducted using registered charities. The purpose of these entities is usually to fund the wider social and economic aspirations of the relevant iwi over a multi-generational time horizon.

Officials' advice

5. Our view is that any competitive advantage distortions are much more minor than usually assumed. The tax concession does not impart a competitive advantage because a trading operation owned by a charity faces the same incentives as a commercial entity when it comes to setting its prices. Its tax-exempt status alone should not lead to undercutting of rivals as the charity could alternatively earn non-business income that is tax-exempt.

6. The most compelling case for reviewing the current settings is to address revenue loss concerns. Tax concessions have a 'cost', that is, they reduce government revenue, and therefore shift the tax burden to other taxpayers. It is sensible to regularly review whether the extent of support being provided to charities through the tax system is appropriate. We estimate that removing the charity business income tax exemption would result in a fiscal gain which could range between $60 million and $200 million per annum depending on policy design and behaviour change.

7. However, taxing charity business income would create a distortion if non-business income remains untaxed. Accordingly, the revenue benefit from taxing the business income of charities would need to be weighed against the cost of this distortion.

8. On balance, the Treasury and Inland Revenue have recommended that the charity business income exemption **not be removed** and that other issues around tax concessions be explored.

Practical considerations

9. International experience suggests that removing a business income tax exemption may not raise significant amounts of tax revenue because of behaviour change (for example, transferring tax deductible costs from a tax-exempt charity into a taxable business). In addition, some boundary issues (for example, whether certain activity is within the definition of a "business") would be subject to ongoing dispute and litigation.

10. To progress a policy option to remove or restrict the current business income exemption, officials would publicly consult on the rationale for a change to the current setting. We would also consult on potential unintended consequences, along with seeking views on three main policy design features:

    - The definition of "business income" which would no longer be tax exempt
    - A de minimis threshold which would ensure small-scale business activity would remain tax exempt
    - Mechanisms to ensure only income accumulated within a business is subject to tax and income distributed for charitable purposes remains tax exempt.

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Briefing note

Reference: BN2025/042

Date: 7 February 2025

To: Revenue Advisor, Minister of Finance – Felicity Barker
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Helen Kuy
Private Secretary, Minister for the Community and Voluntary Sector – Jess Watt

cc: Peter Mersi, Commissioner
David Carrigan, Deputy Commissioner
Graeme Morrison, Policy Director
Kerryn McIntosh-Watt, Policy Director
Phil Whittington, Policy Director
Joanne Petrie, Executive Support Advisor to the Commissioner
Jill Compton, PA to Deputy Commissioner
Governance, Ministerial & Ministerial Services

From: Stewart Donaldson
Phil Marshall

Subject: **Taxation and the not-for-profit sector: Updated officials' issues paper and timeline**

Background

1. On 4 February 2025 we provided you a first draft of the officials' issues paper *Taxation and the not-for-profit sector.* We subsequently discussed the draft with Ministerial advisors and now attach an updated draft.

Updated draft

2. From our perspective this updated draft is complete, subject to minor editorial changes.

3. The updated draft has not changed substantively from the first draft. However, the following matters arising from the discussion with Ministerial advisors may be worth noting.

De minimis options for small sale trading activities

4. While we have not expressed any preference, we have highlighted in paragraph 2.29 that if a de minimis threshold for small scale trading activities was set at $5 million expenses per annum, less than 1,300 charities (out of a total of 29,000 charities) would be potentially affected by a policy change. This may reduce concerns by small charities that they could all be affected by a policy change.

Examples

5. More examples to illustrate Inland Revenue concerns have been included in this update, such as the donor-controlled charity examples in paragraph 3.6.

s 9(2)(f)(iv)

Inland Revenue's donation tax credit (DTC) regime stewardship review

7. The draft issues paper refers to the DTC stewardship review in Chapter 4. Inland Revenue will publish the review report on Monday 10 February. There will be no corresponding media release, however we anticipate the review will get public attention after the issues paper is released. The draft issues paper will be updated with the relevant link along with any other minor editorial changes next week. Once we receive feedback from submitters, Inland Revenue will cost the fiscal impacts and the departmental costs to implement and administer any DTC simplification proposals.

Next steps

8. An updated draft timeline for the approval and consultation process is also attached.

9. Officials will report to Ministers with a draft Cabinet paper on Tuesday 11 February, so that Ministerial consultation can begin on Wednesday 12 February.

Consultation with the Treasury

10. The Treasury was informed of this briefing note.

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
s 9(2)(a)

Taxation and the not-for-profit sector: Draft timeline for public consultation

M	T	W	T	F
10 Feb	11 **Report to Ministers with draft Cabinet paper**	12 **Ministerial consultation begins** (minimum 5 days before lodgement)	13	14
17 Feb **Cabinet speaking notes and Q&As to MoR's office**	18	19	20 **Cabinet paper lodgement**	21
24 Feb **Cabinet decision on release of paper** **Consultation begins**	25	26	27	28
3 Mar	4	5	6	7
10 Mar	11	12	13	14
17 Mar	18	19	20	21
24 Mar	25	26	27	28
31 Mar **Consultation closes**	1 Apr	2	3	4
7 Apr **Cabinet paper (and RIS) on business income to Ministers**	8	9	10 **Cabinet paper lodgement**	11
14 Apr **Final Cabinet B25 decisions**	15 **Budget moratorium begins**	16	17	18

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Briefing note

Reference: BN2025/047

Date: 10 February 2025

To: Revenue Advisor, Minister of Finance – Emma Grigg / Felicity Barker
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Helen Kuy

cc: Peter Mersi, Commissioner
David Carrigan, Deputy Commissioner
Graeme Morrison, Policy Director
Maraina Hak, Policy Director
Phil Whittington, Policy Director
Joanne Petrie, Executive Support Advisor to the Commissioner
Jill Compton, PA to Deputy Commissioner
Governance, Ministerial & Ministerial Services

From: Stewart Donaldson
Jacob Hawker

Subject: Revenue impact of charity business income and other not-for-profit income tax exemption proposals

Background

1. On 10 February 2025 you asked for more fiscal information in relation to:

   - the proposed charity business income tax exemption changes
   - the proposed income tax exemption changes.

Charity business income tax exemption

2. The fiscal implications for removing or restricting the charity business income tax exemption are in the range of $60m-$200m.[1] The range reflects estimates for two policy options: taxing all charity business income above a $140,000 de minimis threshold, and taxing business income unrelated to a charitable purpose for large charities.

3. The fiscal estimate for taxing all charity business income (whether the charity business activities are related to charitable purpose or not) is approximately $200m per annum. This assumes small charities below a de minimis of $140,000 expenditure per annum retain full tax exemption. Officials subsequently recommended that only "unrelated" charity business income be subject to tax and that is the basis of the proposed consultation, so referring to this figure in the issues paper would not be directly relevant.

[1] BN2025/026 and IR2024/199, T2024/2396 refer.

4. The fiscal estimate for taxing charity business income unrelated to charitable purpose is approximately $60m per annum. Because it is very difficult to identify charity business income unrelated to charitable purpose on the public charities register, this estimate is based on the financial accounts of 20 known significant charities with unrelated business income. Given that the estimate is based on only 20 entities, it is a conservative estimate for taxing charity unrelated business income. However, the range of behaviour responses are likely to significantly impact on revenue gains and until the policy is finalised there is a high level of uncertainty involved. Because of this uncertainty, our advice is not to refer to it in the issues paper.

Proposed income tax exemption changes

5. We have provided examples of not-for-profits potentially affected by four income tax exemptions in the Appendix. We have included financial information for these specific not-for-profits, taken from the financial statements publicly available on the Incorporated Societies register, to give a sense of how much income could be subject to tax.

6. Inland Revenue has not formally costed the removal of these exemptions because there are significant information gaps. For example, some large entities accessing these exemptions are companies and trusts, which do not provide financial statements to the public or to Inland Revenue and have not been included in these tables.

7. Based on the number of entities claiming the exemptions, the most affected are bodies promoting scientific and industrial research (approximately 1,000). The other exemptions are claimed by approximately 50-100 entities each.

8. s 9(2)(f)(iv)

9. The exemption for veterinary service bodies would be the second priority. We are aware that this industry has both not-for-profit and for-profit entities offering the same services, so the rationale for the exemption is the weakest.

10. Because there is a lack of reliable data for all exemption categories, our recommendation is to consult on all four exemptions at the same time. This will allow us to formally report on the reasons to retain, remove or restrict them and a final decision can be made based on robust information.

Consultation with the Treasury

11. The Treasury was informed of this briefing note.

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
s 9(2)(a)

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Briefing note

Reference: BN2025/044

Date: 11 February 2025

To: Revenue Advisor, Minister of Finance – Emma Grigg
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Helen Kuy

From: Brandon Sloan

Subject: **Reducing expenditure on donation tax credits – follow up advice**

Purpose

1. This briefing note compares and contrasts two policy approaches for reducing the Government's expenditure on the donation tax credit. The approaches are capping the tax credit and reducing the rate of the tax credit.

Context

2. On 30 January 2025, Ministers Willis, Upston, and Watts, met to discuss a work programme on the tax treatment of charities. Part of that meeting involved a discussion of the options presented in report IR2024/482; T2024/3292 dated 11 December 2024, which considered options to reduce the Government's expenditure on the donation tax credit.
3. Two of those options were discussed at the meeting:
   - Capping the value of the donation tax credit (we have recommended it be capped to $1,500 – being one-third of total annual monetary gifts of $4,500).
   - Reducing the rate of the donation tax credit (the example given was 25%, currently the rate of the tax credit is 33.33%).
4. Following that meeting, the Minister of Finance's office asked for summary information about the fiscal impact and relative complexity of implementing a cap on donor entitlements or changing the rate of entitlement.

Comparative analysis of approaches (Table)

5. The attached table (High-level comparison: Reducing expenditure on donation tax credits) compares and contrasts the two policy approaches in paragraph 3 and highlights the potential number of taxpayers affected (individuals who donate), what additional tax policy changes would be needed to support a reduction in donor tax credit entitlements, and the revenue consequences.
6. Under both approaches, changes would be needed to employer payroll systems for those who offer payroll giving (around 1,200 employers with 9,000 gifting employees).

Relationship of donation tax credit work with proposed consultation document "Taxation and the not-for-profit sector"

7. Ministers recently commissioned a consultation paper from Inland Revenue seeking public comment on a range of integrity and simplification measures relating to the tax concessions available to not-for-profit entities (BN2025/042, dated 7 February 2025 refers). To the extent that these measures deal with the relationship between donors and donees (for example, rules for donor-controlled charities), the tax base concerns we raised in report IR2024/482; T2024/3292 with the donation tax credit are reduced.

8. The two approaches in paragraph 3 therefore turn on their revenue and efficiency effects, as described in the attached Table.

Cash flow impact on households (Graph)

9. The attached graph (Changing donation tax credit entitlements) below shows how the policy approaches could affect the donation tax credit entitlements of individuals compared to the status quo:

    - Status quo: Individual donors are entitled to a tax credit of 33.33% capped to the amount of their taxable income. This reduces the after-tax cost of a monetary gift of $1 to $0.67 up to the cap.
    - Scenario one: Individual donors are entitled to a tax credit of 33.33% capped to when total annual donations equal $4,500. This reduces the after-tax cost of a monetary gift of $1 to $0.67 up to the cap. Scenario one would largely reintroduce the statutory limitations to that entitlement that existed in 2009.
    - Scenario two: Individual donors are entitled to a tax credit of 25% capped to the amount of their taxable income. This reduces the after-tax cost of a monetary gift of $1 to $0.75 up to the cap.

10. The Graph is **not** a distributional analysis of the effect of reducing donation tax credit entitlements to households. We do not hold information about the price sensitivity of households in respect of their gifting decision-making. However, we are anecdotally aware of the following:

    - High wealth income households are reportedly sensitive to the after-tax cost of gifting.
    - Households that are in the practice of regularly gifting for religious purposes are generally price insensitive to the after-tax cost of gifting.
    - Changes in tax settings that reduce households' donor tax entitlements tend to negatively affect gifting to non-religious charities, more than gifting to religious charities.

Consultation

11. The Treasury was consulted as part of the preparation of this briefing note. Their comments are reflected in this advice.

12. The Department of Internal Affairs was informed about this briefing note.

Next steps

13. For the work on reducing the value of the donation tax credit to be progressed as part of Budget 25, Ministers should consider the recommendations in our December 2024 advice and signal their preferred option. We will provide additional advice on that option in anticipation of a decision being taken at Cabinet in March 2025.

Brandon Sloan
Principal Policy Advisor – Taukaea/Policy, Inland Revenue
s 9(2)(a)

Table: High-level comparison: Reducing expenditure on donation tax credits[1]

Reducing donation tax credit cap to $4,500 (a tax credit of $1,500) with supporting tax base protection measures

Revenue	• $106 million increase a year ($371 million over the forecast period 2025–26 to 2028–29). Imposing a cap could initially be revenue negative because a proportion of donors may bring forward gifting commitments prior to the cap taking effect ($15 million decrease).
Number of potentially affected taxpayers	• Around 56,000 individuals, 5,000 companies, and 40 Māori authorities. The lower cap would preserve tax credit entitlements for donations up to $4,500 relative to the status quo but would not provide an additional incentive for donations above the cap.
Compliance cost implications	• Elevated compliance costs for individuals, companies, and Māori authorities. The impact on Māori authorities would need further analysis as per CO 19 (5) Treaty of Waitangi Guidance for Agencies.
Administration implications	• Medium-scale implication costs $1 million, with $0.50 million ongoing costs. Increased number of tax credit claims (but not necessary value) as households allocate receipts across income earners to maximise entitlements. This may lead to additional taxpayer contact.
Summary	• This approach raises the most revenue over the forecast period, but it is more complex because of the supporting changes needed to the tax deduction rules for companies and Māori authorities to ensure the integrity of the proposed cap. Effectively it returns tax policy for supporting donations to pre-2009 settings, and supports the integrity of the tax system.

Reducing the rate of donation tax credit to 25%

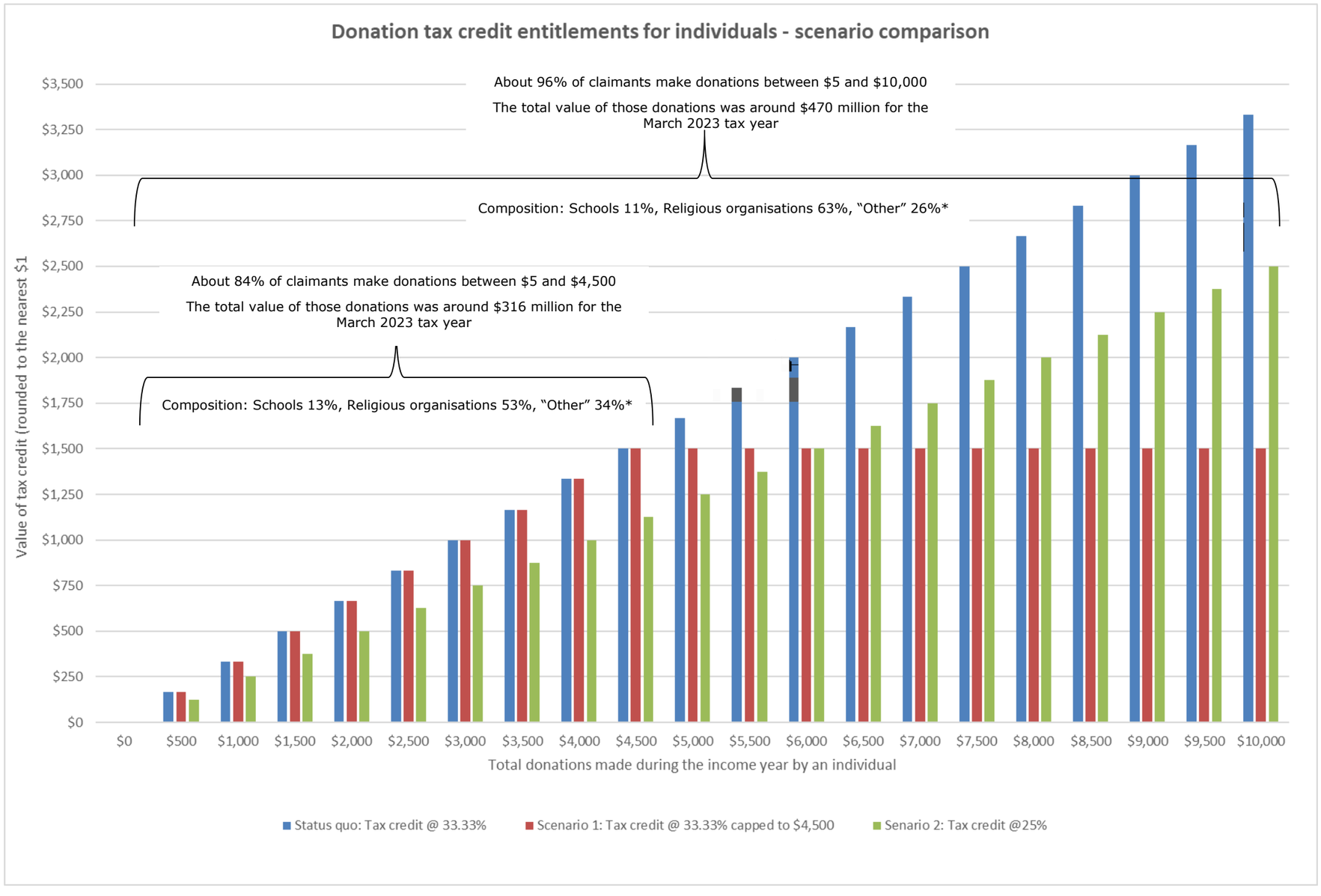
Revenue	• $86 million increase a year ($290 million over the forecast period 2025–26 to 2028–29).
Number of potentially affected taxpayers	• Around 350,000 donors would be affected (all individual taxpayers who interact with the donation tax credit system would be affected by the lower rate).
Compliance cost implications	• Expected to be low scale.
Administration implications	• Low-scale initial set up costs $0.5 million, with $0.5 million ongoing costs.
Summary	• This approach raises less revenue over the forecast period but continues to support post-2009 tax policy settings for donations (at a reduced rate). It is the easiest to implement (for example, no supporting changes needed to the tax deduction rules for companies and Māori authorities), and continues to support high value gifting (at a reduced rate).

[1] These Inland Revenue estimates are high level and illustrative only. In the absence of consultation (due to Budget processes) our observations on possible taxpayer/donor behavioural change are based on anecdotal evidence. Both options require changes to the payroll giving rules.

Graph: Changing donation tax credit entitlements

The Graph illustrates the following:

- A low threshold cap preserves tax credit entitlements for donations up to $4,500 relative to the status quo but does not provide an additional incentive for donations above the cap.
- Reducing the rate of the credit impacts the entitlements of lower annual amounts of giving but continues to incentivise higher gifting values (but at a lower rate than the status quo).



* As per our earlier advice the aggregate composition of all donations claimed through the donation tax credit system is schools 8%, religious organisations 63%, "other" 29%.

Inland Revenue
Te Tari Taake

POLICY/TAUKAEA

TE TAI ŌHANGA
THE TREASURY

Tax policy report: Reducing expenditure on donation tax credit – further advice on options

Date:	13 March 2025	**Priority:**	Medium
Security level:	Sensitive - Budget	**Report number:**	IR2025/079 T2025/635

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to recommendations	18 March 2025
Minister of Revenue	**Agree** to recommendations	18 March 2025

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Peter Frawley	Policy Lead Inland Revenue	s 9(2)(a)	☐
Brandon Sloan	Principal Policy Advisor Inland Revenue		☒
Jean Le Roux	Manager Tax Strategy The Treasury		☐
Paul Quirke	Senior Analyst The Treasury		☐

13 March 2025

Minister of Finance
Minister of Revenue

Reducing expenditure on donation tax credit – further advice on options

Purpose

1. This report seeks your agreement to an option that reduces the Government's expenditure on the donation tax credit (and supporting measures). If you agree to an option, we recommend you invite your preferred option and the associated financial impacts into the Budget 2025 process.

Executive summary

2. In December 2024 we reported to you on options to reduce the Government's expenditure on donation tax concessions, with a particular focus on the donation tax credit (IR2024/482; T2024/3292 refers). In that advice, while we noted the positive benefits of charitable gifting and activities of donee organisations,[1] we considered there are good reasons to change current tax policy settings for monetary gifts because:

    2.1 Recent academic literature has suggested that the donation tax credit is not a cost-effective way to encourage additional monetary gifting to donee organisations.

    2.2 Inland Revenue has observed that some taxpayers are using the donation tax concessions to produce circular wealth transfers from the donee organisation to the donor and their associates. Some of these arrangements have been tax aggressive, and high value.

3. In that advice we compared changes to the threshold ceiling and to the rate of the donation tax credit. We recommended reducing the donation tax credit threshold ceiling to $4,500 (a tax credit of $1,500) as a means of supporting fiscal sustainability, efficiency, and mitigating Inland Revenue's increasing integrity concerns. We noted this option would require additional supporting measures that would affect the tax deduction rules for companies and Māori authorities, and the possible need to repeal payroll giving.

4. Subsequent to the December 2024 advice, Ministers met on 30 January 2025 to discuss the implications of the advice with the Minister for the Community and Voluntary Sector, including fiscal sustainability.

5. For decisions to be taken as part of Budget 2025, this report provides further advice on the following options (summarised in Table 1, attached):

    5.1 Reduce the donation tax credit ceiling to $4,500. Estimated fiscal effect of **$371 million** over the forecast period. This option was our recommended option in our December 2024 advice because it has a strong integrity focus.

    5.2 Reduce the rate of the donation tax credit to 25%. Estimated fiscal effect of **$290 million** over the forecast period. This option is the simplest to implement.

6. One important difference between these options is the effect on school donations. Under the ceiling option, the vast majority of monetary gifts requested by state

[1] "Donee organisation" for example, includes registered charities, schools, tertiary institutions, and other bodies with philanthropic, benevolent, or cultural purposes.

schools would still receive full value for the donation tax credit. Under the rate option, all tax credits for monetary gifts would fall. A gift of $1,000 would receive a $250 tax credit instead of $333.33.

7. All the options impact payroll giving to some degree, with the ceiling option (paragraph 5.1) the most likely to increase compliance costs on employers and create system complexity, thereby reducing the attractiveness of the scheme for users, and possibly lead to its decline in use. We also note that a low ceiling creates the risk of end-of-year tax debts for employees who use payroll giving.

8. We recommend you invite your preferred option and the associated financial impacts into the Budget 2025 process. Amendments implementing the change should be included in Budget night legislation to ensure that employers, tax agents, software providers, donors and donees have adequate notice about the change in entitlements.

9. Subject to your decisions on the options in this report, we will report again in the week beginning 24 March 2025 seeking your agreement to the detailed design of the option. This will enable you to have the complete proposal ready for Budget 2025. This later report, for example, if you agree to reduce the ceiling on donation tax credit entitlements, would seek your agreement to change the tax deduction rules for companies and Māori authorities, and seek decisions regarding the future of the payroll giving rules including whether they should be repealed.

10. A copy of this report should be referred to the Minister for the Community and Voluntary Sector for her information.

Recommended action

11. We recommend that you:

		Minister of Finance	**Minister of Revenue**
(a)	**Indicate** your preferred option from the following options:		
(i)	**Agree** to cap value of the donation tax credit to total monetary gifts in an income year to $4,500 (a tax credit of $1,500). Estimated fiscal effect of $**371 million** over the forecast period.	Agreed/ Not agreed	Agreed/ Not agreed
OR			
(ii)	**Agree** to reduce the rate of the donation tax credit to 25%. Estimated fiscal effect of **$290 million** over the forecast period.	Agreed/ Not agreed	Agreed/ Not agreed
OR			
(iii)	**Commission** work on another option.	Commissioned/ Not commissioned	Commissioned/ Not commissioned
(b)	**Invite** the initiative you have chosen in recommendation (a) and the associated financial impacts into the Budget 2025 process.	Invited/ Not invited	N/A
(c)	**Agree** to include the necessary amendments giving effect to your preferred option in recommendation (a)(i) (or (ii) in Budget night legislation, with effect from 1 April 2026.	Agreed/ Not agreed	Agreed/ Not agreed

(d)	**Refer** a copy of this report to the Minister for the Community and Voluntary Sector for their information.	N/A	Referred/ Not referred

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Jean Le Roux
Manager, Tax Strategy
The Treasury

Peter Frawley
Policy Lead
Policy/Taukaea

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

Context

12. We previously reported to you on a number of options that would have the effect of reducing the Government's expenditure on the donation tax credit (IR2024/482; T2024/3292, dated 11 December 2024).[2]

13. On 30 January 2025 at a joint Ministers' meeting with the Ministers of Finance, the Minister for the Community and Voluntary Sector, and the Minister of Revenue, two of the options in the December 2024 advice were discussed:[3]

    13.1 Capping the value of the donation tax credit to a total annual monetary gifts ceiling of $4,500 (a tax credit of $1,500, based on the current rate of $33^1/_3$%) (Reducing the donation tax credit dollar ceiling).

    13.2 Reducing the rate of the donation tax credit to 25% (Reducing the donation tax credit rate).

Other developments: Inland Revenue consultation with not-for-profit sector

14. Inland Revenue officials released an issues paper on 24 February 2025 about a range of possible changes to the tax settings for not-for-profits.[4] The changes suggested in that document have the potential to ameliorate the tax base risks identified in the December 2024 advice with respect to donor-controlled charities.

Our earlier recommendation: Reducing donation tax credit dollar ceiling

15. The December 2024 advice, among other options, recommended a reduction in the value of the total amount of monetary gifts that would be eligible for the donation tax credit. Reducing the dollar ceiling to $4,500 (a tax credit of $1,500) is intended to:

    15.1 Deal with tax integrity concerns, particularly circular arrangements between donors and donee organisations (donor-controlled charities), and reduce the financial incentives attaching to fraudulent claims.

    15.2 Raise revenue for Budget 2025 (around **$371 million** over the forecast period 2025/26 to 2028/29).

16. Our recommendation to reduce the donation tax threshold ceiling also responds to New Zealand specific academic research that concluded that the donation tax credit is not an effective tool for increasing the household contribution to the charitable sector.[5]

17. We consider that the case for reducing the ceiling is strong because it is useful for dealing with high-value aggressive tax planning, from an integrity perspective, and note that it raises more revenue over the forecast period than the other options that were discussed in the December 2024 advice.

18. It is, however, a more complex and costly option to implement, and elevates compliance costs for individuals, employers, companies, and Māori authorities relative to the status quo. For example, Inland Revenue expects that the volume of donation tax credit claims would increase as households allocate gifting receipts across income earners to maximise entitlements.

[2] This advice built on earlier reports about the tax settings for the charitable sector (IR2024/237, 17 July 2024, and IR2024/292, 8 August 2024).
[3] Under both options, the tax credit payable to the individual would be subject to taxable income limits, for example, under Option 1 the credit would be based on the lower of the individual's taxable income or $4,500.
[4] CAB-25-MIN-0038 refers.
[5] Cruickshank, A (2024) *Government financial support for charitable sector in New Zealand*, Victoria University of Wellington, New Zealand.

19. The option's complexity arises because a threshold ceiling of $4,500 is effectively a return to pre-2009 tax policy settings for monetary gifts. As such:

    19.1 A range of supporting tax integrity measures are needed, including restricting monetary gift tax deductions for companies and Māori authorities to 5% of their net taxable income.[6] These measures are intended to prevent donors from gifting using other entity types in substitution of individual gifting.[7] These additional measures are expected to be marginally revenue positive (around $5 million over the forecast period).

    19.2 Employers and software providers would need to update payroll giving systems to reflect the threshold cap. Not changing payroll giving would otherwise give individuals who are employees a substitutable method to provide monetary gifts that benefit from a tax concession above the reduced ceiling.

20. Unless payroll giving is repealed or left to run independently of the donation tax credit system,[8] Inland Revenue would need to develop new applications to ensure that donations from payroll giving are squared up with donations made via the donation tax credit system. Excess credits could create tax debts for individuals. This tax debt would accrue use of money interest. Individuals who practice gifting using payroll giving and who change employer, or have multiple employers, or gift directly are at most risk for this tax debt.[9]

21. Currently, the overall contribution that payroll giving makes to total monetary gifting is small scale (around $7 million a year – year ending March 2023). Given the likely compliance costs that employers and software developers are likely to incur to ensure that payroll giving settings are aligned with the proposal, it is possible that the number of employers offering payroll giving or employee participation in the scheme may decline. Ministers may therefore want to consider if payroll giving should be repealed.[10] Removing payroll giving would have benefits in terms of reducing employer- and employee-related compliance costs.[11]

22. As noted in our December 2024 advice, reducing the donation tax credit ceiling would make New Zealand a conservative outlier relative to other OECD countries that seek to encourage donations using tax credits to incentivise gifting by individuals and households. Table 2, attached, illustrates the practices (2020) of OECD members who use tax credits to incentivise financial and non-financial gifts to the not-for-profit sector.

23. We will report again on the detailed design of the ceiling and its implications for payroll giving, companies and Māori authorities if this is your preferred option.

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[6] It is possible that trust structures could be used as well, but our initial assessment is that the risk is immaterial and has low probability over the short to medium term. We would monitor behaviour via trust returns to determine if an additional policy response is needed.

[7] Because the tax deduction rules for Māori authorities are designed along similar principles as the deduction rules for companies, we consider changes to both sets of rules are necessary. In terms of the guidance set out in CO 19 (5) *Treaty of Waitangi Guidance for Agencies*, these measures would impact on specific Māori entitlements under the Māori authority tax rules.

[8] Even if a ceiling is created for payroll giving, in the absence of a square up for payroll giving and entitlements under the donation tax credit system, households and individuals would be able to maximise entitlements under both rules and therefore obtain a maximum tax credit entitlement per employer and under the donation tax credit system.

[9] This is because the new employer, or other employer, would have no way of knowing about the individual's gifting practices to trigger a payroll intervention. The problem would also arise for households that, for example, claim a tax credit for school activity donations using the donation tax credits system as well as regularly gifting using payroll giving.

[10] Noting that in the longer term, Inland Revenue is contemplating the feasibility of providing in-year refunds of donation tax credits.

[11] Employers could still choose to facilitate gifting on behalf of their employees outside of the tax system.

Reducing donation tax credit ceiling is revenue negative for first year

24. The December 2024 advice noted that reducing the donation tax credit ceiling is expected to drive a strong behavioural response as individuals with available discretionary funds bring forward gifting commitments. Assuming the proposal applies from 1 April 2026,[12] reducing the donation tax credit ceiling to $4,500 is expected to be revenue negative in the first year of application by around $15 million.

25. We have considered if an earlier application date could be used, however:

    25.1 For various reasons, a part year application materially escalates the cost of implementation for Inland Revenue, employers, tax agents, software developers, and donee organisations.

    25.2 Retrospectively applying the proposal to 1 April 2025 (the 2025–26 income year, starting 2 October 2024 for early filing taxpayers) would raise the issue of taxpayers' legitimate expectations about their entitlements. For example, employers would not be able to comply with requirements for which they have not been given notice about (as such, implementing a ceiling to payroll giving would have to be deferred).[13] We would also expect that legislation implementing the change would receive negative comment about its retrospective application as part of the Bill's Bill of Rights analysis.

Reducing donation tax credit rate to 25%

26. The advice in our December 2024 report used 25% as a suggested new tax credit rate, which was arrived at using the following principles:

    26.1 the rate should be based on a simple fraction, and[14]

    26.2 the rate continues to reflect the policy objectives set in 1962, and more recently in 2009, to:

        26.2.1 encourage a culture of charitable giving in New Zealand, and

        26.2.2 reduce the charitable sector's reliance on the Government for direct financial provision (grants and service contracts).

27. The Government's continued support for monetary gifts recognises that donee organisations may:

    27.1 help governments to further social objectives

    27.2 provide wider benefits to society over and above the value of the tax benefits received by the recipient or the supplier of the activity, and

    27.3 be more responsive than government or commercial sectors to the needs of society and provide extra goods and services when and where they are required.

28. This option also raises revenue for Budget 2025 (around **$290 million** over the forecast period 2025/26 to 2028/29). We noted that reducing the rate of the donation tax credit was a simpler option, and still incentivised high-value monetary gifts. The trade-off is that the option retains a high ceiling, and therefore has less of an integrity focus. The revenue gain is achieved by increasing the after-tax cost of an individual providing a monetary gift. For example, a monetary gift of $100 would have an after-tax cost of $75, an increase of around $8.33 compared to the

[12] The start of the 2026–27 income year.
[13] Transitional savings rules would also be needed for deceased estates and permanently departing taxpayers.
[14] For example, 25% is the next step down from the current rate of $33\frac{1}{3}$%. 20% would be two steps down from the current rate. There is no precise science behind the rate because it is a function of how much the Government wants to spend on donation tax credit entitlements.

status quo.[15] If Ministers consider that there should be a stronger focus on fiscal sustainability, the donation tax credit rate could be further reduced to 20%, which would provide around **$467 million** over the forecast period.

29. Reducing the rate of the tax credit has comprehensive application to everyone that claims the donation tax credit, estimated to be around 350,000 individuals.

30. Reducing the rate of the donation tax credit would also apply to employers who offer payroll giving to their employees (around 1,800 employers with 14,000 gifting employees in the year ended March 2023). They would need to change their payroll system to ensure alignment with the new tax credit rate. We do not foresee the same complications arising for payroll giving as described in paragraph 21 because the current income ceiling threshold is retained.

31. Reducing the rate of the tax credit to 25%, with the current taxable income ceiling, would mean that New Zealand's tax policy settings for monetary gifts remains reasonably generous relative to the other OECD countries in Table 2 (attached).

Expected impacts on households (donors) and donee organisations

32. As noted in our December 2024 advice, reducing individual taxpayer entitlements for monetary gifts would increase the after-tax cost of those gifts. This may have cost of living implications for some households that use the donation tax credit to help reduce the cost of those gifts, such as school donations. The Graph (attached) illustrates that for lower value monetary gifts, a ceiling option largely preserves existing entitlements, but a rate change has a material effect on the after-tax cost. For example, a $500 school donation (for camp and other education activities under the Education and Training Act 2020) would give rise to a tax credit of $125 (under a 25% tax credit) rather than $166.66 under the status quo.[16] Inland Revenue does not have distributional information relating to household or individual gifting decisions or price sensitivity relating to decisions to gift. We are aware, however, from anecdotal evidence that:

    32.1 High-income households are reportedly sensitive to the after-tax cost of gifting. Reducing the rate of the tax credit therefore continues to incentivise higher value monetary gifts relative to reducing the donation tax credit ceiling.

    32.2 Households that regularly gift for religious purposes are generally price insensitive to the after-tax cost of gifting. Changing the rate of the tax credit is therefore unlikely to elicit a significant behavioural response for those households.

    32.3 Changes in tax settings that reduce households' donor tax entitlements are more likely to negatively affect gifting decisions to non-religious charities, such as the relief of poverty. These charities may have to reduce their services or seek additional direct government support. Inland Revenue does not hold information about which donee organisations benefit the most from monetary gifts that are eligible for the donation tax credit. However, as an illustration, Table 3 (attached) indicates the registered charities that received the largest amounts of monetary gifts for the financial year ending June 2023. As noted in our December 2024 advice, donee organisations affected by a reduction in donor income may reduce the volume of goods

[15] Under the status quo, the after-tax cost of a monetary gift of $100 is around $66.67.
[16] This is relevant for education providers under the Education and Training Act 2020 that are not participating in the School Donation Scheme. The School Donation Scheme allows state, and state-integrated schools and kura with an equity index (EQI) of 432 or higher to elect to receive a direct payment from the Crown rather than ask parents and caregivers for donations (except for overnight camps). The scheme is designed to ease the pressure and expectations put on households by donation payments. https://www.education.govt.nz/education-professionals/schools-year-0-13/funding-and-financials/school-donations-scheme

and services provided to the communities they support, or seek direct financial support from the Government.

32.4 If and to the extent that they are affected, middle- to high-equity index schools, school building funds, and poverty-focused charities may call for additional direct government support.

33. Recent research by Cruickshank (2024) into New Zealand's donation tax credit scheme provides evidence the donation tax credit is not "Treasury efficient" - meaning the Government spends more in tax credits than the additional charitable donations generated. Specifically, the research estimates that for every dollar of tax credit, donors increase their charitable contributions by less than a dollar, with donation elasticities ranging between -0.3 and -0.7.

34. This finding is consistent with international research on charitable giving tax incentives. Studies by Fack and Landais (2010) in France[17] and Almunia et al. (2020)[18] in the United Kingdom similarly found donation elasticities less than one, indicating that tax credits typically generate less in additional donations than the Government foregoes in tax revenue. The New Zealand research extends this international evidence, suggesting that the current tax concessions for monetary gifts may not be an optimal use of public funds.

35. The inefficiency implies that taxpayers largely retain a portion of the tax credit for themselves, rather than channelling the full value (or more) into charitable donations. While the tax credit may still serve broader policy goals, such as encouraging giving and supporting the charitable sector, from a purely fiscal perspective, the research suggests the likely outcome of reducing the credit (through the ceiling or the rate) is that the Government saves more money than the reduced donations to the donee organisations.

Administration implications

36. The December 2024 report gave a broad indication of the expected administration costs connected with the options discussed in this report. Once you have selected your preferred option, we will confirm the expected implementation and ongoing operational costs. Inland Revenue proposes to self-fund the departmental costs of this initiative, subject to a cumulative cost assessment of all Budget initiatives that impact Vote Revenue.

37. Implementing the changes recommended in this report has costs for donee organisations (managing donor commitments), Inland Revenue (educating donors and donee organisations, and systems implementation), and software providers and employers (updating payroll systems for the new rate). To this end, we would consider the earliest the changes could be implemented is for the 2026/27 income year, being 1 April 2026 for most individual taxpayers.

Financial implications[19]

38. For illustrative purposes, the tables below show the expected tax revenue implications of the options discussed in this report. As noted in paragraph 24, changes to tax policy affecting entitlements are expected to create a timing shift in donating behaviour for those donors that have sufficient discretionary funds. This behaviour has been reflected in the forecasts.

[17] Fack, G., & Landais, C. (2010). Are tax incentives for charitable giving efficient? Evidence from France. American Economic Journal: Economic Policy, 2(2), 117-41.
[18] Almunia, M., Guceri, I., Lockwood, B., & Scharf, K. (2020). More giving or more givers? The effects of tax incentives on charitable donations in the UK. Journal of Public Economics, 183.
[19] As per our December 2024 advice, removing all tax benefits for monetary gifts to donee organisations would likely increase revenue by $311 million a year.

Reducing donation tax credit ceiling to $4,500 (*excluding supporting integrity measures*)

	$m – increase/(decrease)				
Vote Revenue **Minister of Revenue**	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29 & outyears**
Crown Revenue and Receipts: Tax Revenue – Other Persons	-	(15.000)	106.000	138.000	142.000
Total Operating	**-**	**15.000**	**(106.000)**	**(138.000)**	**(142.000)**

Reducing donation tax credit to 25%

	$m – increase/(decrease)				
Vote Revenue **Minister of Revenue**	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29 & outyears**
Crown Revenue and Receipts: Tax Revenue – Other Persons	-	16.000	86.000	93.000	95.000
Total Operating	**-**	**(16.000)**	**(86.000)**	**(93.000)**	**(95.000)**

Legislative vehicle and application date

39. The changes recommended in this report require amendments to the Income Tax Act 2007 and the Tax Administration Act 1994. For the reasons in paragraph 37, the amendments should be included in Budget night legislation, with effect on and after 1 April 2026. This is to ensure that affected groups have adequate notice about the changes to their entitlements.

40. Developing the amendments to give effect to the recommendations in this report allows some legislative aspects of the donation credit rules in the Income Tax Act and the Tax Administration Act to be clarified. These remedial amendments should accompany the substantive reform recommended in this report. Cabinet approval for these machinery changes is not required and the changes will be developed as part of the Budget night legislation.

Consultation

41. Due to Budget processes, the advice in this report has not been informed by, and has not had the benefit from, the views of external stakeholders. While we have applied our best judgement based on information available to us (qualitative and anecdotal), some of the effects and impacts of the advice described in this report on donors and donees may be under- or over-stated.

The Department of Internal Affairs

42. Consistent with their view in the December 2024 advice, the DIA has concerns about changing the donation tax credit scheme. In terms of the options proposed in the current paper, the DIA prefer a reduction in percentage credit rather than a ceiling on credits individuals can claim. The reduction in the rate should, however, be no lower than 25%. DIA note that reducing expenditure on the donation tax credit is likely to have a detrimental effect on the value of donations made to charities. Many charities rely heavily on donations to deliver goods and services to the communities in which they operate. A reduction in donation income may mean more charities seek direct funding from the Government.

43. The DIA also reiterates that they would like Inland Revenue to consider improvements to the payroll giving system, which will be affected by any changes to the donation tax credit scheme. They consider payroll giving could be better utilised to improve regular donation behaviour among New Zealanders.

Next steps

44. Subject to your decisions on your preferred option, we will provide further advice on the detailed design of that option.

45. A copy of this report should be referred to the Minister for the Community and Voluntary Sector for her information, prior to your meeting with Minister Upston.

Table 1: High-level comparison: Reducing expenditure on donation tax credits

Option 1: Reducing donation tax credit dollar ceiling to $4,500 (a tax credit of $1,500) with supporting tax base protection measures

Revenue	**$371 million** increase over the forecast period 2025/26 to 2028/29). Imposing a ceiling could be initially revenue negative because a proportion of donors may bring forward gifting commitments prior to the ceiling taking effect ($15 million decrease).
Number of potentially affected taxpayers	Around 56,000 individuals, 5,000 companies, and under 100 Māori authorities. The lower ceiling would preserve tax credit entitlements for monetary gifts by individuals up to $4,500 relative to the status quo but would not provide an additional incentive for gifts above the cap.
Compliance cost implications	Elevated compliance costs for individuals, companies, Māori authorities, employers, and software providers.
Administration implications	Large one-off implementation costs, and small ongoing costs. Inland Revenue expects an increased number of tax credit claims (but not necessary value) as households allocate receipts across income earners to maximise entitlements. This may lead to additional taxpayer contact. We consider that payroll giving may not remain viable under this option.
Summary	This approach is more complex because of the supporting changes needed to the tax deduction rules for companies and Māori authorities to ensure the integrity of the proposed cap. Effectively it returns tax policy for supporting monetary gifts to pre-2009 settings and supports the integrity of the tax system. The payroll giving rules may need to be repealed.

Option 2: Reducing donation tax credit rate to 25%

Revenue	**$290 million increase** over the forecast period 2025/26 to 2028/29.
Number of potentially affected taxpayers	Around 350,000 donors would be affected (all individual taxpayers who interact with the donation tax credit system would be affected by the lower rate).
Compliance cost implications	Expected to be low scale.
Administration implications	Small one-off implementation costs, and small/medium ongoing costs over the short term.
Summary	This approach raises more revenue over the forecast period and continues to support post-2009 tax policy settings for monetary gifts (at a reduced rate), including payroll giving. It is the easiest to implement (e.g., no supporting changes needed to the tax deduction rules for companies and Māori authorities) and continues to support high value gifting (at a reduced rate).

Table 2: Limitations to personal income tax credits (*OECD Taxation and Philanthropy*, November 2020*

Country	Tax credit	Ceiling
Belgium	45% (proposal to reduce to 30% if enacted 2025)	Total amount of the donation may not exceed 10% of income or EUR375,350 per spouse. (approx. NZ$676,000).
Canada	15% – 33%	Up to 75% of net income can be claimed (monetary gifts).
Chile	35% – 50%	Credits for donations to charity, and education, culture and sport are limited to 20% of the amount of the donation, to a monthly taxable unit of 320, approx. US$20,500 (approx. NZ$34,400).
Columbia	25%	Credit limited to 25% of the individual's tax liability (excess can be carried over to the following year).
France	66%	20% of taxable income.
Greece	20%	Total amount of the donation may not exceed 5% of taxable income.
Israel	35%	The credit cannot exceed 30% of taxable or NIS10.2 million (approx. $4.9 million).
Italy	30% (35% for specific bodies)	Up to EUR30,000 of total giving (approx. NZ$54,000).
Japan	40%	Total donated amount cannot exceed 40% of taxable income and the value of the tax credit cannot exceed 25% of income tax liability.
New Zealand	33.33%	Total amount of the donation may not exceed 100% of taxable income.
Portugal	25%	The tax credit cannot exceed 15% of tax liability (not limited for donations to public institutions).
Sweden	25%	Tax credit cannot exceed SEK3,000 (approx. NZ$520).

* List excludes countries that provide a tax deduction for monetary gifts. Note this table is a snapshot and illustrative only. The table does not reflect the wider tax and transfer environment that applies in the respective jurisdictions above. Amounts converted into NZ$ as per Inland Revenue's determination for February 2025. Google, 10 March 2025.

Most other OECD countries, including Australia and the United States, allow 100% tax deductions for monetary gifts. Ceilings apply to the total amount that can be deducted, but not always, for example Singapore allows a deduction of 250% without limit

Table 3: Illustrative list of charities reporting large monetary donation income in 2023*

s 6(c)

*(*excludes government grants, legacies, and non-monetary donations when available; based on returns filed with Charities Services that may be grouped or ungrouped; **indicative** only*)

Graph: Changing donation tax credit entitlements*

The Graph illustrates the following:

A low threshold cap preserves tax credit entitlements for monetary gifts up to $4,500 relative to the status quo but does not provide an additional incentive for gifts above the cap.

Reducing the rate of the credit impacts the entitlements of lower annual amounts of giving but continues to incentivise higher gifting values (but at a lower rate than the status quo).

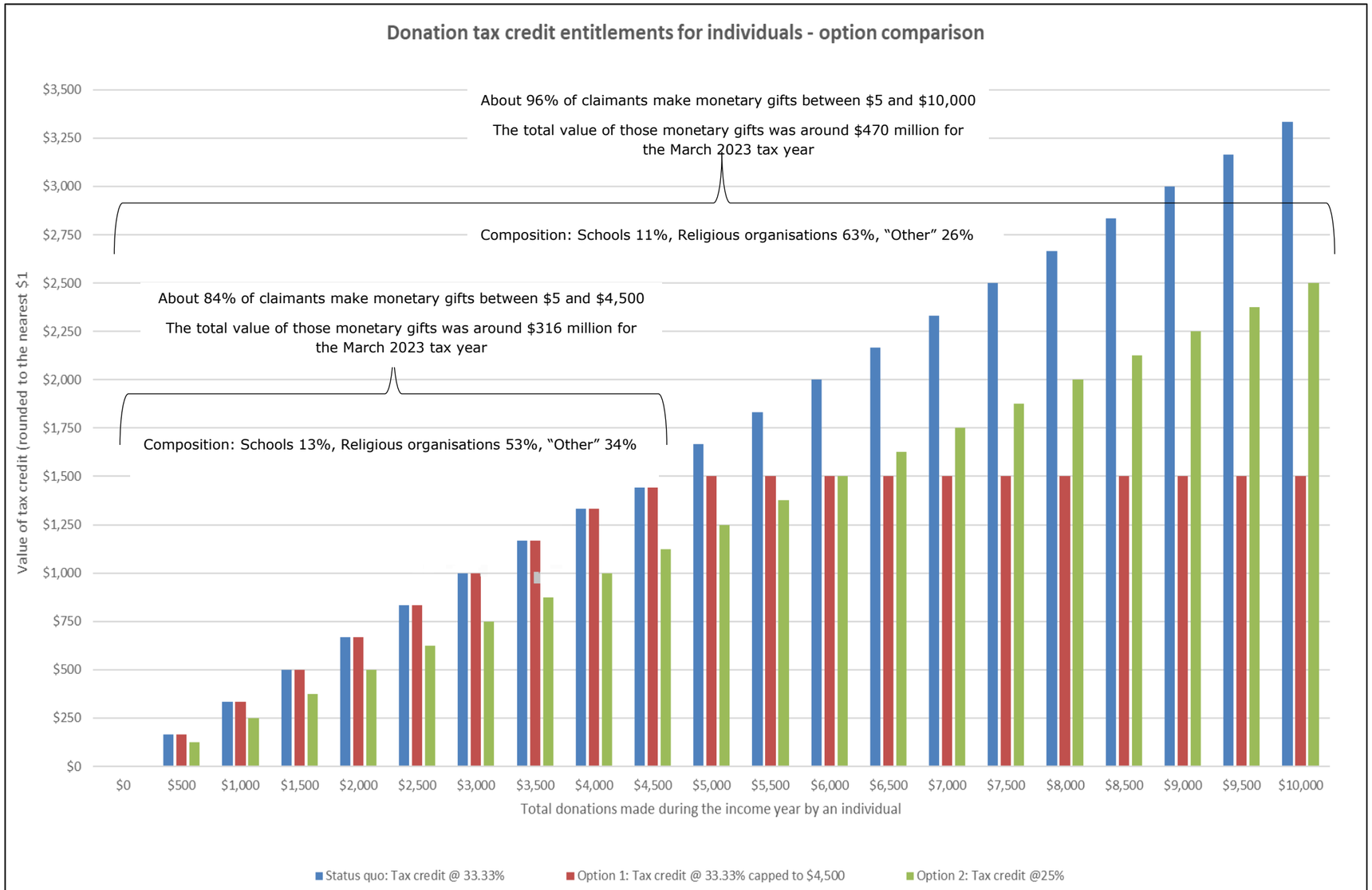
Options description and key

Status quo: Individual donors are entitled to a tax credit of $33^1/_3$% capped to the amount of their taxable income.

Option 1: Individual donors are entitled to a tax credit of $33^1/_3$% capped to when total annual monetary gifts is $4,500 (or taxable income, if lower).

Option 2: Individual donors are entitled to a tax credit of 25% capped to the amount of their taxable income. If the rate of the tax credit were 20%, the value of the tax credit would be proportionally reduced.

* Assumes the taxpayer has sufficient taxable income to support the donation tax credit.



As per our earlier advice, the aggregate composition of **all** donations claimed through the donation tax credit system is schools 8%, religious organisations 63%, "other" 29%.

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Briefing note

Reference: BN2025/135

Date: 21 March 2025

To: Revenue Advisor, Minister of Finance – Carl Harris
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Helen Kuy

From: Stewart Donaldson

Subject: **Taxation of not-for-profits: Possible in-principle decisions**

Purpose

1. At the joint Ministers' meeting on 17 March 2025 the Minister of Finance asked whether, in respect of the "taxation of not-for-profits" project, Ministers could make in-principle decisions for Budget 2025 and then further consult on some of the details.

Background

2. The officials' issues paper, "Taxation and the not-for-profit sector" was released on 24 February 2025 with a closing date for submissions of 31 March 2025 (IR2025/039 refers). The paper addressed five specific issues:

   - charity business income tax exemptions
   - donor-controlled charities
   - not-for-profit and friendly society member transactions and related matters
   - tax exemptions that may no longer be fit for purpose
   - tax simplification for volunteers and donation tax concessions.

3. At the time of writing this briefing note, Inland Revenue officials have met with approximately 35 stakeholder groups and received approximately 130 written submissions. We anticipate receiving significantly more submissions by the closing date.

Possible in-principle decisions for Budget 2025

4. We will report to Ministers after the close of consultation and we anticipate that Ministers will then make decisions about what issues will and will not progress.

5. At this stage in the process, we anticipate the following in-principle decisions could be made for Budget 2025.

A. Charity business income tax exemptions

6. This issue is the most complex and is the primary focus for most submissions and discussions with officials. Typical concerns raised are:

    - The consultation needs more time to deal with such complex issues.
    - The definition of "unrelated" business activity will be complicated and problematic.
    - Certain groups should be excluded from the changes due to their specific circumstances.
    - The focus should be on those that might be abusing the current exemption rather than applying a change more generally.
    - Changes will result in restructuring and will distract affected charities from carrying out their charitable purposes, while not raising a lot of revenue.

7. In April, once all submissions have been considered, we will provide advice to Ministers and seek an in-principle decision as to whether we are to continue or cease policy work on this issue. Part of our advice on the "continue work" option will include recommended high-level policy design features that could be applied and a fiscal estimate within a range.

8. Because of the complexity of this issue and design considerations, if Ministers choose to make an in-principle decision to tax charity business income, our preferred approach would be to announce further consultation on the detailed design issues with a view to introducing legislation in the 2026–27 annual rates Bill. If you want to make an in-principle decision to consult further, we note that because the fiscal implications are highly dependent on the policy design, we would recommend against managing any fiscal impacts against the Budget 2025 allowance.

B. Donor-controlled charities

9. At this stage, the idea of introducing integrity rules for donor-controlled charities is receiving mixed support from submissions and discussions, with most appreciating that there are integrity issues that need to be addressed. Charities that could be affected will want to provide further advice on the detail of any change.

10. In April, once all submissions have been considered, we will report on the submissions received and ask Ministers to make an in-principle decision on whether we continue policy work on this issue. As part of our advice, we will also outline the high-level policy design features to be considered if work is to continue. At this stage we do not expect there will be fiscals associated with the potential integrity rules for donor-controlled charities.

11. If Ministers were to make an in-principle decision to continue work on this issue, our preferred approach would be to immediately proceed to targeted consultation with charities likely to be affected, with a view to introducing legislation in the 2025–26 annual rates Bill.

C. Not-for-profit and friendly society member transactions and related matters

12. Based on submissions and discussions to date, this issue has attracted a lot of interest, with many submitters wanting further details about Inland Revenue's updated view contained in the issues paper that member transactions, particularly subscriptions, could be subject to tax in some circumstances. Although this issue does not involve significant fiscals or tax avoidance issues, it raises integrity

concerns when the tax rules are unclear and/or not being complied with by a large number of not-for-profits.

13. In April, once all submissions have been considered, we will seek a decision from Ministers on which of the following approaches they prefer:

14. Inland Revenue immediately consults on its draft operational statement, including its updated interpretation of the current law. These submissions can then be considered together with the policy submissions received on the issues paper.

15. Under this approach we would anticipate introducing legislation in the 2026–27 annual rates Bill. Although this approach might prolong uncertainty, it will give the sector more time to consider the long-standing issues and legislative options, which we understand is the sector's preferred approach to managing changes. This approach would be officials' recommended option.

16. Progress a law change now to legislate for the in-practice status quo for most not-for-profits that receive subscription income. A law change could distinguish between subscriptions that provide indirect member benefits (would not be taxable) and subscriptions that provide direct commercial member benefits (would be taxable).

17. Although this approach would provide more immediate certainty to the sector, it may not provide enough time for the sector to consider the issues and legislative options, and may result in unintended consequences.

18. If Ministers decided to progress a law change under this approach, we would begin targeted consultation with a view to introducing legislation in the 2025–26 annual rates Bill.

D. Tax exemptions that may no longer be fit for purpose

19. It is too soon to tell what issues will be raised by submitters because these exemptions typically affect a small number of not-for-profits.

20. In April, after all submissions have been considered, we will report to Ministers on submissions and seek in-principle decisions on whether each specific tax exemption is to remain or be repealed. For some exemptions there may be a case for additional integrity measures rather than outright repeal.

21. Our preferred approach would be to follow Ministers' in-principle decisions with legislation to be introduced in the 2025–26 annual rates Bill. We will need to advise you of any fiscal impacts depending on what exemptions you want to repeal or change.

E. Tax simplification for volunteers and donation tax concessions

22. It is too soon to tell what new simplification ideas will be raised by submitters. At this stage there is general support for the simplifications suggested in the issues paper.

23. In April, once all submissions have been considered, we would make recommendations on what simplifications should be progressed, weighing the fiscal and administration costs with the level of public support and the likely benefits. We would provide fiscal estimates for each proposed change, however at this stage we anticipate either no, or minor, fiscal costs, just administrative costs.

24. Our preferred approach would be to follow any in-principle decisions with legislation to be introduced in the 2025–26 annual rates Bill. If there is to be simplification for donation tax credits, our advice would likely be that this may be useful to announce in Budget 2025 if other donation tax credit changes are progressed in Budget 2025.

These could then be viewed as part of a broader package of donation tax credit changes.

Summary

25. Subject to our further advice and in-principle decisions from Ministers, as part of Budget 2025 the Minister of Finance could announce:

26. The charity business income tax exemption will be restricted for certain businesses, with details subject to further public consultation.

27. Donor-controlled charities will be subject to specific tax rules.

28. Inland Revenue will undertake further public consultation on not-for-profit and friendly society member transactions and related matters before final decisions are made to change the current law.

29. Certain tax exemptions will be repealed or subject to further integrity rules.

30. Simplifications will be made that will benefit volunteers and donors who are eligible to claim donation tax credits.

31. There will be a fiscal impact for most of these issues, so decisions will need to be made before the Budget moratorium.

Consultation with the Treasury

32. The Treasury was informed about this briefing note.

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
s 9(2)(a)

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Briefing note

Reference: BN2025/149

Date: 28 March 2025

To: Revenue Advisor, Minister of Finance – Emma Grigg
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Helen Kuy

From: Brandon Sloan

Subject: **Reducing expenditure on donation tax credits – impact if school activity donations are treated differently**

1. s 9(2)(g)(i)

2. On 27 March 2025, you asked for our comment if the current rate ($33^1/_3$%) of the donation tax credit was retained for monetary gifts relating to school activities under the Education and Training Act 2020 and other education providers.[1] We also note that donations to school building funds are within scope of the donation tax credit in terms of supporting an education purpose.

3. This note has been prepared to support Budget Ministers' discussions at their next meeting on Tuesday, 1 April 2025.

Context

4. An important difference between the options discussed in our 13 March 2025 advice is the effect on school donations. Under the ceiling option, the majority of monetary gifts requested by state schools would still receive the value for the donation tax credit capped to $1,500. Under the rate option, tax credits for all monetary gifts would reduce. For example, a gift of $1,000 would receive a $250 tax credit instead of $333.33.

Implications of treating school activity donations differently from other monetary gifts

5. Differentiating the treatment of school activity donations from monetary gifts to other donee organisations, would:

   - Complicate the donation tax credit scheme and payroll giving schemes by introducing multiple credit rates depending on the purpose of the monetary gift.

[1] QB 18/10 Income tax – state schools and donation tax credits, and QB 18/11 Income tax – state integrated schools and donation tax credits. These two "Questions we've been asked" (QWBAs) explain when a parent's payment to a school will be a gift, so that the school can issue a donation tax receipt to the parent. A payment will be a gift when it is voluntary, does good for the school, and the parent obtains no material benefit or advantage in return for making the payment.

- Reduce the expected amount of revenue that would otherwise be saved by $21 million over the forecast period.[2]
- Increase compliance costs for donors, and weaken the overall predictability of the donation tax credit system.
- Introduce value-judgements as to why monetary gifts to some donees attract higher-tax preferences over others. For example, for some individuals, donations to the Red Cross in response to a national emergency, or to a charitable international development aid organisation may be perceived to have higher and better per dollar outcomes than an equal value monetary gift to a New Zealand school. Once a distinction is made, we would expect continual lobbying from interested groups on behalf of their donors and donees for a higher tax benefit for their monetary gifts.
- Increase IRD's implementation and ongoing administration costs by:
  - requiring the allocation of additional resource to vet the purpose of donations that donors declare are for educational purposes, and
  - dealing with additional taxpayer contacts regarding the calculation of their donation tax credit entitlements under a multi-rate system.
- Reduce the integrity of the current donation tax credit by incentivising monetary payments to be recharacterised for activity fees (which are entitled to the donation tax credit), as opposed to the payment of school attendance dues, which are not. This is already a contentious area of tax law interpretation.
- Create higher compliance costs for employers (to the extent they allow payroll donations to state and integrated schools), and tax agents in terms of attesting to whom the donation is made and for what purpose.

6. Providing a different tax credit treatment for school activity donations would likely favour households that have children attending schools that have not elected into the Government's school donation programme. For example, state, and state-integrated schools and kura with an equity index (EQI) of 432 or higher can elect to receive a direct payment from the Crown rather than ask parents and caregivers for donations (except for overnight camps).

7. s 9(2)(g)(i)

Consultation with the Treasury

8. The Treasury was consulted on this briefing note, and their comments have been reflected in this briefing note.

Next steps

9. Our advice to date has assumed a simple model for reducing the Government's expenditure on the donation tax credit. If Ministers want to consider a complex model, such as a multi-rate or a ceiling and rate change hybrid, this could not be delivered in time for Budget 2025. Instead, we would suggest that Ministers consider prioritising this initiative on the Government's tax and social policy work programme for delivery for a later financial year.

10. We would be happy to discuss the content of this briefing note with you.

Brandon Sloan
Principal Policy Advisor
s 9(2)(a)

[2] As previously reported on 13 March 2025, reducing the rate of the donation tax credit to 25% is expected to reduce the Government's expenditure by $290 million over the forecast period 2025/26 to 2028/29.

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Briefing note

Reference: BN2025/155

Date: 31 March 2025

To: Revenue Advisor, Minister of Finance – Emma Grigg
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Helen Kuy

From: Brandon Sloan

Subject: **Reducing expenditure on donation tax credits – delivery of an option to retain current donation tax credit entitlements for school donations**

1. This note has been prepared to support Budget Ministers' discussions at their next meeting on Tuesday, 1 April 2025.

2. You have asked if Inland Revenue could deliver a modification to the proposed reduction in the donation tax credit from $33^{1}/_{3}$% to 25%, that would retain existing entitlements for donations to schools and other education providers. Inland Revenue could deliver the modification by 1 April 2026.

Delivery implications

3. Currently, the entitlement to a donation tax credit for monetary gifts to education providers is broadly framed and based on whether an entity is recognised by the Ministry of Education, or is an entity established for charitable, benevolent, philanthropic or cultural purposes.[1] This scope includes monetary gifts for school building funds, special character donations, school camps and other out of the class (EOTC) activities, and registered charities connected with schools and other education providers.

4. If these settings were retained, it would be possible for Inland Revenue to deliver this modification by 1 April 2026.

5. If a multi-rate donation tax credit system were introduced, Inland Revenue would:

   - allocate additional resource to test the purpose of donations that donors declare are for educational purposes,
   - receive additional taxpayer contacts regarding the calculation of their donation tax credit entitlements under a multi-rate system, and
   - consider increasing audit activity into the donation tax credit system and payroll giving to maintain the integrity of the system.

[1] QB 18/10 Income tax – state schools and donation tax credits, and QB 18/11 Income tax – state integrated schools and donation tax credits. These two "Questions we've been asked" (QWBAs) explain when a parent's payment to a school will be a gift, so that the school can issue a donation tax receipt to the parent. A payment will be a gift when it is voluntary, does good for the school, and the parent obtains no material benefit or advantage in return for making the payment.

Revenue implications

6. As payments of school donations are within existing baselines, removing them from the proposed reduction in the donation tax credit to 25% would mean that the proposed initiative would raise $269 million over the forecast period (or $21 million less than previously reported).[2] (This assumes Inland Revenue's current classification of donations to education providers.)

How many taxpayers claim donation tax credits in respect of school activity donations

7. About 61,000 individuals claimed donation tax credits connected with school donations for the year ending 31 March 2023. The value of monetary gifts captured under Inland Revenue's current donation tax credit classification for the 2023 tax year is around $75 million.[3] So far 51,200 (incomplete) have claimed to 31 March 2024. The numbers claiming a donation tax credit has declined from the mid-to-high 70,000 since the introduction of the Government's School Donation programme. By value, donations to schools represents around 8% of total donations that are processed for donation tax credits.

Consultation

8. The Treasury was informed of this briefing note.

9. Given available timelines we have not consulted with the Ministry of Education. s 9(2)(g)(i)

[2] $290 million less $21 million for the forecast period 2025/26 to 2028/29.
[3] On average 350,000 individuals claim the donation tax credit. The total amount value of monetary gifts that are processed by Inland Revenue for the 2023 tax year is about $950 million.

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **Taxation and the not-for-profit sector - submission summary and next steps**

Date:	4 April 2025	**Priority:**	High
Security level:	Sensitive - Budget	**Report number:**	IR2025/146

Action sought

	Action sought	Deadline
Minister of Finance Minister of Revenue	**Agree** to recommendations **Note** the contents of this report	7 April 2025

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Stewart Donaldson	Principal Policy Advisor	s 9(2)(a)	☒
Peter Frawley	Policy Lead		☐
Phil Marshall	Senior Policy Advisor		☐

4 April 2025

Minister of Finance
Minister of Revenue

Taxation and the not-for-profit sector: submission summary and next steps

Purpose

1. This report provides a high-level overview of the submissions received on the five topics covered in the officials' Issues Paper, *Taxation and the not-for-profit sector* (the Issues Paper).

2. We recommend that you direct officials to provide detailed reports on each of the five topics by the end of June 2025, followed by further consultation where required, with a view to Ministers making final policy decisions in December 2025.

Background

3. The Government's tax and social policy work programme (TSPWP), published on 13 November 2024, included a project focusing on elements of charities and not-for-profits (NFPs). In January 2025, Ministers confirmed that the Issues Paper would cover the following topics (BN2025/030 refers):

   3.1 the charity business income exemption;

   3.2 donor-controlled charities;

   3.3 NFP member transactions and related matters;

   3.4 exemptions that may not be fit for purpose; and

   3.5 tax simplification for volunteers and donation tax concessions.

4. On 24 February 2025, Cabinet approved the release of the Issues Paper that same day together with a five-week consultation period ending on 31 March 2025.

Consultation and submissions

5. Prior to public consultation, officials liaised with the Department of Internal Affairs, the Ministry of Business, Innovation and Employment (MBIE), the Ministry for Culture and Heritage, the Ministry for Primary Industries and the Ministry of Foreign Affairs and Trade.

6. In total, over 900 written submissions were received, with over 400 on the final day. In addition, during the consultation period, officials met over 40 peak bodies, sector groups and large charities during the consultation period.

7. Given the short period of time between consultation closing and the preparation of this report, we have extracted the key themes of the submissions received and quoted from two large iwi submissions (see **Appendix A**). We have not had sufficient time to discuss matters with submitters or carry out detailed analysis, which we propose doing in subsequent detailed reports provided to Ministers by the end of June 2025.

8. Common general themes from submitters were:

   8.1 *Timeframe and process:* Many submitters said the consultation needs more time to deal with such complex issues. It was also submitted that a large number of small charities and NFPs may not have been aware of the Issues Paper and will therefore not have had an opportunity to make their views known to officials. Submitters suggested that further consultation with the sector and other stakeholders should be undertaken before any decisions are made to proceed.

   8.2 *NFPs provide a net benefit, not a net cost, for Government:* Many submitters said that the fiscal cost of NFP tax exemptions is only one side of the equation and that NFPs save government expenditure and provide a net gain for Government. Some submitters said a full cost/benefit analysis should be undertaken to determine the true net position for Government.

   8.3 *There is an insufficient problem definition:* Some submitters said the Issues Paper lacked clarity about the "problem case" especially since the paper stated that no competitive advantage is afforded to tax-exempt charitable businesses.

   8.4 *It is better to focus on "bad actors":* Submitters said the focus should be on strengthening existing regulatory oversight for those abusing the current exemptions rather than introducing blanket tax measures. Some submitters suggested that narrowing the definition of "charitable purpose" in the Charities Act 2005 may be a more appropriate way to deal with "bad actors" and/or applying the existing anti-avoidance provisions.

   8.5 Consideration of the Treaty of Waitangi: Submitters, including iwi, said the consultation did not consider the unique circumstances of iwi and Māori entities. This includes considering entities established to receive Treaty of Waitangi settlement assets.

Analysis

9. The submission themes and officials' initial comments for the five topics covered in the Issues Paper are outlined below.

A. Charity business income tax exemptions

10. This issue was the most complex and was the primary focus for most submissions and discussions with officials.

Observations, concerns and potential impacts

11. Typical observations and concerns raised by submitters were:

   11.1 *Views on competitive advantage*: While some submitters, including economists, agreed with Inland Revenue's view outlined in the Issues Paper that the charity business tax exemption did not give charity businesses a competitive advantage, other submitters disagreed on this point. Some submitters provided examples of competitive advantages charities held in parts of the building, food and healthcare sectors. Some charities acknowledged that when a charity's annual distributions are less than the corporate tax rate, this allows a charity to grow its balance sheet faster than a private enterprise. Some thought that any advantage from the tax exemption was nonetheless offset by restrictions faced by charities in terms of raising equity, borrowing, and by the additional scrutiny and transparent reporting requirements of registered charities.

11.2 *A change is not warranted:* Some submitters said New Zealand's charitable framework has traditionally followed a "destination of income" approach, recognising that what matters is where the money ultimately goes, not its original source. It was also submitted that the proposals in the Issues Paper represented a fundamental shift from this principle that would have far-reaching consequences.

11.3 *Complexity including definitional issues:* Many submitters said the definition of "unrelated" business activity would need to be clear to avoid ongoing litigation. For example, the submission from BestStart stated their business activities are in early childhood education, which directly relates to the charitable purpose of advancing education. It was also submitted that there would need to be apportionment of income and costs if business activity was not quarantined within a separate entity.

11.4 *Cases for exclusions for iwi and certain groups:* Certain groups said they should be excluded from any proposed changes due to their specific circumstances. This included various Treaty settlement entities that are charities, some of which have investment arrangements with external investors that rely on the current arrangements (also refer to **Appendix A** for specific points made by large iwi).

11.5 *It is unlikely that any substantial revenue would be collected:* A number of submitters were sceptical that much revenue would be collected if the charity business income tax exemption was removed.

11.6 *Alternative proposal – minimum distribution rule:* Several submitters, including charities that run large commercial businesses, said setting a minimum annual distribution requirement would be a more effective policy response to address concerns the Government has on accumulation of funds within charity businesses. One charity suggested this minimum distribution rate be above the corporate (28%) or trust (39%) tax rates to "increase the impact of charities in our community today and negate any comparative advantage a charitable business has with the private sector".

12. Typical potential impacts of change identified by submitters were:

12.1 *Additional government investment would be required:* Removing the charities business income tax exemption would likely result in the Government having to allocate further funding to deliver the essential services currently provided by charities to avoid social costs.

12.2 *Change would impact on delivery and growth and have international investment implications:* A change could raise concerns among international investors who are attracted to New Zealand's stable investment environment and therefore undermine economic growth. Change would result in restructuring and add "deadweight" accounting regulatory costs that distract affected charities from carrying out their charitable purposes. Change would also result in a reduction in the number of staff or charitable programmes.

12.3 *Investment bias:* A change would reduce the appetite for charities to invest in riskier business activity and instead invest more in passive investments.

Conclusions

13. There is nothing raised in submissions that changes our initial advice, which was **not to** progress this initiative (IR2024/199 refers). Submissions have reinforced the issues relating to complexity and compliance costs, and raised an argument for

specific exemptions for income derived from Treaty Settlement assets. In our view, the primary rationale for continuing work in this area remains twofold:

13.1 to examine why New Zealand should be an international outlier in its approach to exempting charity business income; and

13.2 to ensure the amount of support the Government provides charities through a business income tax exemption is appropriate.

B. Donor-controlled charities

14. The idea of introducing integrity rules for donor-controlled charities received both positive and negative support from submitters. However, we note that the donor-controlled charities proposals are complex, and many submitters did not understand who would be affected.

Observations, concerns and potential impacts

15. Typical observations and concerns raised by submitters were:

15.1 *There was an acknowledgment that some integrity issues need to be addressed*: Submitters that supported proposed changes agreed that the integrity concerns we have observed need to be addressed.

15.2 *Specific rules are not warranted:* Some submitters took the view that the existing legislative regime for registered charities is already rigorous and robust enough. They said creating specific rules would impose unnecessary compliance costs for all donor-controlled charities. Other submitters said they had not observed integrity concerns with donor-controlled charities and felt they could not support specific rules without detailed analysis of the scale of the problem.

15.3 *There are legitimate reasons to accumulate:* Some submitters said there are a number of legitimate reasons why a charity may delay the release of funds, such as accumulating for long-term infrastructure and sustainability. It was submitted that any minimum distribution requirement must recognise the extent to which an affected charity's asset base is already committed.

15.4 *Definitions must be clear:* Definitional issues were raised by submitters, for example:

15.4.1 an overly wide definition runs the risk of capturing a number of Māori organisations and charities controlled by another organisation or charity;

15.4.2 there should be clarity about whether donor advised funds (such as the s 6(c)) could be affected;

15.4.3 compliance costs could reduce if the "control" definition was consistent with New Zealand accounting standards (NZ IFRS 10 Consolidated Financial Statements); and

15.4.4 there is also complexity in what type of expenditure would qualify as a distribution, such as time spent advising other charities, or the social return on impact investing.

16. Typical potential impacts of change identified by submitters were:

16.1 *Donations may not be made:* Some submitters said rules for donor-controlled charities would discourage and hinder private, proactive

philanthropy. Some donors would want to have conditions attached to a donation to their private foundation, s 6(c) . It was submitted that some may not donate if these conditions were prohibited.

16.2 *Minimum distribution rules increase compliance costs:* Some submitters said if an asset threshold is used for a minimum distribution rule, smaller charities would need to revalue their assets and incur more compliance costs.

16.3 *A minimum distribution would erode their asset base:* It was submitted that some charities would not be able to meet a minimum distribution requirement without selling assets. This would reduce their ability to provide future charitable distributions, and some charities may not survive in the long term.

16.4 *Prohibiting related-party investments limits growth of charities*: Some submitters pointed out that many related-party investments are on terms favourable to the charity involved, and this supports the long-term financial growth of the charity. Instead, it was submitted, investments should be required to be at market rates rather than prohibited outright.

Conclusions

17. Submissions have not resulted in us changing our initial advice that reform is necessary to improve the integrity of the tax rules for donor-controlled charities. We recommend targeted consultation on the detailed design to ensure there are workable definitions and rules.

18. We consider that some of the concerns submitters have raised could be mitigated by final policy design. For example, exceptions to the minimum distribution rule could be allowed when accumulation meets certain criteria.

19. If a decision is made not to reduce the donation tax credit ceiling or rate (IR2025/079 refers), we consider that this would increase the need for integrity measures for donor-controlled charities.

C. NFP and friendly society member transactions and related matters

20. This issue attracted a lot of interest, with broad support for making changes to reduce compliance costs for NFPs. Submitters wanted further details about Inland Revenue's updated view, referred to in the Issues Paper, that member subscriptions could be subject to tax in some circumstances.

21. Although the Issues Paper did not seek views on the technical aspects of the updated view, a number of submitters disagreed with the correctness of Inland Revenue's updated view. Some submitters emphasised that further consultation with the sector is required before any changes in approach are made.

Observations, concerns and potential impacts

22. Typical observations and concerns raised by submitters were:

22.1 *Take all NFPs out of the income tax system:* Some submitters said NFPs should receive a full income tax exemption, as is the case for amateur sports bodies, on the basis that they also provide important benefits to the community.

22.2 *Member subscriptions should remain non-taxable*: If Inland Revenue's updated view is confirmed, meaning that membership subscriptions would

be potentially taxable, some submitters said a law change should be considered to ensure they remain non-taxable, in recognition of the important role NFPs provide to their communities.

22.3 *Support for a de minimis (tax-free) threshold:* There was near-universal support from those that submitted on the mutuality topic that the $1,000 income tax deduction was too low and should be increased. Proposed options ranged from $2,000 to $100,000 with most supporting a threshold of around $10,000. Other submitters suggested linking the threshold to the tiered approach used for charities.

22.4 *Support for simplification of filing requirements:* There was also broad support for simplifying filing requirements for small-scale NFPs as well as the retention of the RWT exemption.

23. Typical potential impacts of change identified by submitters were:

23.1 *Financial pressure:* If Inland Revenue's updated view is confirmed, and member subscriptions were to become taxable, this would place a significant amount of financial pressure on NFPs. Smaller NFPs may face closure on the basis that they would no longer be financially viable. Other NFPs may increase prices for membership subscriptions.

23.2 *Reduction of services:* Financial pressure could result in the reduction of services and benefits provided to members and the community.

Conclusions

24. As stated in the Issues Paper, Inland Revenue will consult on its draft operational statement now that consultation on the Issues Paper has closed. It is important that this occurs as soon as possible to provide the sector with clarity around Inland Revenue's updated view and to provide an opportunity for submissions to be made on the technical correctness of that view.

25. Regardless of whether Inland Revenue confirms or changes its view on the taxability of member subscriptions and member transactions generally, we recommend further policy analysis be carried out on this issue after the operational statement consultation, and on the related issues covered in the Issues Paper.

D. Tax exemptions that may no longer be fit for purpose

26. The fringe benefit tax (FBT) exemption attracted significant interest, while fewer submissions were received in relation to the other six income tax exemptions.[1] The majority of submitters were against the removal of the exemptions, with only the veterinary services exemption receiving more balanced feedback.

27. Some submitters said the exemptions are not justified due to integrity and fairness concerns. However, other submitters said the exemptions are justified because they support the delivery of public services and provide a net gain rather than a loss for the Government. They said to remove the exemptions would impose significant compliance, restructuring and administrative costs without raising a large amount of revenue.

[11] The Issues Paper discussed the income tax exemptions for friendly societies/credit unions, veterinary service bodies, local/regional promotional bodies, herd improvement bodies, promoting scientific/industrial research bodies, and non-resident charities.

Observations, concerns and potential impacts

28. Typical observations and concerns raised by submitters were:

    28.1 *FBT exemption:* Submitters said this exemption should be retained because it allows charities to attract and retain staff. Many submitters expressed significant concerns that any changes to the exemption would increase compliance costs and reduce service delivery, and that any decision should only take place after the broader FBT policy review.

    28.2 Veterinary service bodies exemption: NFP veterinary clinics submitted that this exemption should be retained whereas private veterinary clinics submitted that the exemption should be removed.

    28.3 Non-resident charity tax exemption: Some submitters expressed support for reviewing the exemption due to perceived fairness and integrity concerns resulting from the lack of reporting requirements for these entities compared to New Zealand-resident charities.

    28.4 Friendly societies and credit unions exemption: Submitters on this issue almost universally expressed significant concerns that removing this exemption would undermine the core purpose of friendly societies and credit unions to support their members. The three credit unions said it would weaken their ability to compete in a concentrated financial market where they already have a disadvantage due to their smaller size and restrictions on raising capital.

29. Typical potential impacts of change identified by submitters were:

    29.1 *FBT exemption:* Removal of this exemption would require reviewing and renegotiating remuneration policies and employees' remuneration. This would detract from charities focusing their time and resources on delivering services that are of public benefit.

    29.2 Veterinary services bodies exemption: NFP veterinary clinics submitted that the removal of the exemption would result in the consolidation of public and private vets and therefore reduced competition. Alternatively, private veterinary clinics said removing the exemption would result in less price undercutting and fairer competition.

    29.3 Non-resident charity tax exemption: Submitters said removal of this exemption may discourage large overseas charities from making passive investments in New Zealand, which would be an economic loss for New Zealand.

    29.4 Friendly societies and credit unions exemption: Submitters said if this exemption was removed, these entities would have to pass the additional taxation and compliance costs onto their members.

    29.5 Local and regional promotional bodies exemption: Local and regional promotional bodies and Business Associations said removal of this exemption would reduce the delivery of local economic development activities and investment into community safety.

Conclusions

30. s 9(2)(f)(iv)

31. We still consider there is a case to remove exemptions if they are no longer fit for purpose. For some exemptions (such as the non-resident charity exemption) there may be a case for additional integrity measures rather than outright repeal. Submitters have raised several issues that we have not had sufficient time to consider and will address in the subsequent detailed report.

E. Tax simplification for volunteers and donation tax concessions.

Observations

32. Several suggested simplification ideas were proposed by submitters, including:

    32.1 *PAYE treatment for volunteers:* There was support for further work to extend the PAYE treatment of payments to volunteers for all in the NFP sector and to provide a simpler method of exempting volunteers from paying ACC levies. While most submitters considered this change would reduce compliance costs, further consultation may be required to confirm this.

    32.2 *Honoraria:* There was support for a review of the tax treatment of honoraria. Some submitters suggested introducing a tax-free threshold for honoraria, while others were more specific about simplification measures, such as a progressive rate and extended payment and filing dates.

    32.3 *Donation tax concessions:* There was specific support for:

        32.3.1 a proposal to refund donation tax credits (DTCs) prior to year-end and closer to the time donations are made;

        32.3.2 allowing Inland Revenue to collect data from donee organisations to pre-fill claims; and

        32.3.3 introducing a three-month grace period for deregistered charities.

        However, some submitters said any impact on charities, especially smaller charities, must be carefully assessed against the benefits. For example, assessing whether earlier DTC refunds would increase the compliance costs on charities due to the increased frequency of issuing compliant tax receipts to donors.

Conclusions

33. Although additional simplification ideas were proposed by submitters, we have not had sufficient time to consider the merits of those ideas in this report and will include them in the subsequent detailed report.

Fiscal impacts

34. If Ministers direct officials to do further policy work on the topics contained in the Issues Paper, there will not be any fiscal impacts for Budget 2025.

35. The current fiscal impacts associated with proposals in the Issues Paper are shown in Table A below. This is an update on fiscal impacts provided in prior reports (BN2025/047, BN2025/026 and IR2024/199 refer). These costings are preliminary.

Table A: Fiscal impacts of proposals subject to consultation

	Topic	Fiscal impact (pa)	Comment
A	Charity business income tax exemption	$50m	The costing is a range of $30m to $70m with a midpoint of $50m. It assumes the exemption will be removed for "unrelated" business income with a de minimis of $5m total expenditure and that there are no changes to distribution or donation policies. Until the policy is finalised there is a high level of uncertainty involved.
B	Accumulation within donor-controlled charities	$0	A policy change would impact on behaviour and would have no/minimal fiscal implications.
C	Removal of tax exemptions that are not fit for purpose:	s 9(2)(f)(iv)	
	s 9(2)(f)(iv)		
	(ii) Friendly societies and credit unions	*$7m*	
	s 9(2)(f)(iv)		
	(iv) Veterinary service bodies	*$2m*	
	(v) Herd improvement bodies	*$1m*	
	(vi) Bodies promoting scientific and industrial research	*$1m*	
	(vii) Non-resident charities	*Small unquantifiable gain*	Approximately 400 non-resident charities have approval for this exemption; however, no data is available.
D	NFP member transactions and related matters	Not costed	Depending on policy design, the changes for small-scale NFPs and related modifications could contain a range of revenue positive and revenue negative measures.
E	Simplifications (volunteers and donation tax credits)	Not costed	Fiscal implications are expected to be minimal, depending on design and behavioural response.

Next steps

36. Subject to your agreement, we will begin preparing detailed reports on the five topics covered in the Issues Paper, with the intention of providing these to you by 30 June 2025.

37. Our proposed future milestones are:

- ***April 2025:*** Inland Revenue begins consultation on its draft operational statement for NFPs and member transactions.
- ***May 2025:*** Budget announcements (if any).

- ***June 2025:*** Officials provide detailed reports to Ministers, recommending consultation on policy detail (where necessary).
- ***December 2025:*** Consultation ends; final reports to Ministers and Cabinet.

Recommended action

We recommend that you:

1. **agree** that officials will provide you with detailed reports on each of the five topics covered in the Issues Paper by 30 June 2025.

   Agreed/Not agreed Agreed/Not agreed

2. **note** that Inland Revenue will now publicly consult on operationalising its new interpretation of the law concerning the tax treatment of member transactions and membership subscriptions.

   Noted Noted

3. **refer** a copy of this report to the Minister for the Community and Voluntary Sector.

   Referred/Not referred Referred/Not referred

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
Policy

Hon Nicola Willis
Minister of Finance
/04/2025

Hon Simon Watts
Minister of Revenue
/04/2025

Appendix A: Notable points from large iwi submitters

Te Whakakitenga o Waikato Incorporated (Waikato-Tainui)

The Issues Paper fails to give any consideration to the unique nature of iwi and Maaori entities that have been established to receive, manage and deliver the benefits of the settlement of historical grievances under Te Tiriti o Waitangi (Te Tiriti).

…Put simply, the proposals in Chapter Two should not apply to post-settlement governance entities (PSGEs) and their related entities, including marae. In addition, we consider that there may be unintended implications for asset holding companies and mandated iwi organisations under the Maaori Fisheries Act 2004, iwi aquaculture organisations under the Maaori Commercial Aquaculture Claims Settlement Act 2004, and Maaori reservations under Te Ture Whenua Maaori Act 1993.

The Coalition Agreement between the parties who form the present Government included a clear commitment to uphold Treaty Settlements, recognising their significance in addressing historical injustices. However, the policies being implemented fail to honour this commitment, undermining the relationship and trust established as a result of Te Tiriti settlements…

The purpose of Te Tiriti settlements is to acknowledge, apologise for, and address, historical injustices of the Crown in breach of Te Tiriti o Waitangi. However, such settlements did not, and could never, fully compensate for the full extent of what was lost or for the associated intergenerational pain and suffering.

As such, the redress (by way of money and assets) provided under Te Tiriti settlements is necessarily only a "seed" fund, with the clear understanding and intention that this will be held, managed and used to restore and uplift the iwi through subsequent, intergenerational recovery and investment activity…Charitable status was granted to PSGEs as a redress mechanism to enhance that work, which ultimately benefits the wider community as well.

Te Rūnanga o Ngāi Tahu

Te Rūnanga o Ngāi Tahu does not support the removal of the tax exemption for charity business income that is unrelated to charitable purposes…

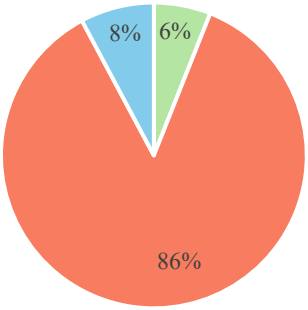
…removal of this exemption would: (i) be a tax on the most vulnerable in society; (ii) be a tax on economic growth; (iii) be a tax on the regions; (iv) be an attack on treaty settlements and mean they are no longer full and final; and (v) exponentially increase compliance costs in the charities sector.

Appendix B: Submission insights for specific topics

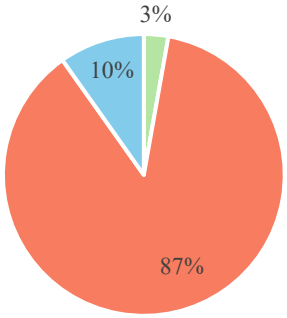
A total of **901** submissions were received by the due date. These pie charts show that the most significant opposition from submitters related to removing the exemption for charity business income and removing the FBT exemption.

Legend	
	Submitters that indicated support
	Submitters that indicated opposition
	Submitters with neutral or no clear position

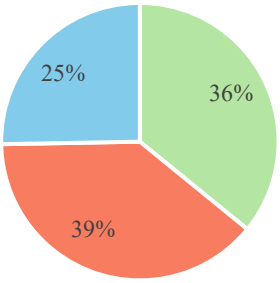
Remove exemption for charity business income unrelated to charitable purposes
(n=615)



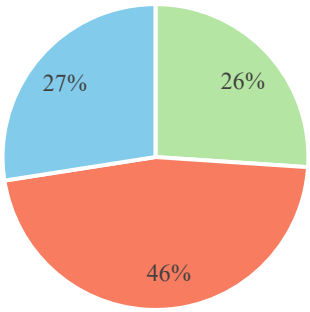
Remove/reduce FBT exemption for charities
(n=214)



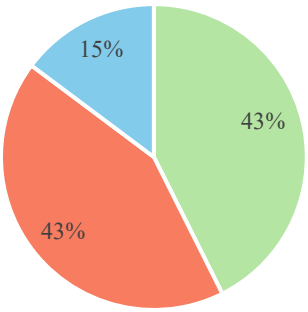
Distinguish between donor-controlled charities and other charitable organisations for tax purposes
(n=170)



Introduce mandatory minimum distribution for donor-controlled charities
(n=142)



Restrict investments for donor-controlled charities for tax purposes
(n=115)



The following Appendices are withheld in full under section 6(c) of the OIA:
Appendix: Large registered charities reporting business activity that is unrelated to charitable purpose
Appendix: Examples of large donor-controlled charities
The draft media statement and Q&As are withheld in full under section 9(2)(g)(i) of the OIA.

Item 40

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: Charities and NFPs tax issues announcements

Date:	17 April 2025	**Priority:**	High
Security level:	Sensitive - Budget	**Report number:**	IR2025/169

Action sought

	Action sought	**Deadline**
Minister of Finance Minister of Revenue	**Note** the contents of this report **Agree** to recommendations	23 April 2025

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**	**Suggested first contact**
Peter Frawley	Policy Lead	s 9(2)(a)	☒
Philip Marshall	Senior Policy Advisor		☐

17 April 2025

Minister of Finance
Minister of Revenue

Tax policy report: Charities and NFPs tax issues announcements

Purpose

1. As requested by Ministers, this report provides advice on the timing and content for a public announcement on the tax issues covered in the issues paper, *Taxation and the not-for-profit sector* (the Issues Paper). This report also attaches:

    1.1 a draft media statement and Q&As to support an announcement on the tax issues covered in the Issues Paper;

    1.2 a note that could be circulated to Budget Ministers setting out the practical difficulties of removing the charity business income tax exemption; and

    1.3 six information sheets on the topics covered in the Issues Paper.

Context

2. On 24 February 2025, Inland Revenue released the Issues Paper for five weeks of public consultation, closing on 31 March 2025. The Issues Paper covered the following five topics:

    1.4 the charity business income exemption;

    1.5 donor-controlled charities;

    1.6 not-for-profit member transactions and related matters;

    1.7 exemptions that may no longer be fit for purpose; and

    1.8 tax simplification for volunteers and donation tax concessions.

3. On 4 April 2025, officials reported to Ministers with high-level overview of the submissions received as part of consultation on Issues Paper [IR2025/146 refers].

4. In relation to the 4 April report, Ministers agreed that officials would provide detailed reports on each of the five topics covered in the Issues Paper by 30 June 2025, followed by further consultation where required, with a view to Ministers making final policy decisions in December 2025.

5. The 4 April report also noted that Inland Revenue would consult in April on its draft operational statement on the tax treatment of not-for-profit member transactions, including membership subscriptions (the Draft Operational Statement).

6. At the Joint Ministers meeting on 7 April 2025, you asked officials to prepare the present report setting out options for what announcements could be made on the topics covered in the Issues Paper, and when such an announcement could be made.

7. At the meeting of Budget Ministers on 9 April 2025, it was confirmed that none of the issues covered in the Issues Paper would be progressed through Budget 2025.

8. There was also a request at the Budget Ministers' meeting for officials to prepare a note that could be circulated to Budget Ministers setting out the practical difficulties of removing the charity business income tax exemption.

9. s 9(2)(g)(i)

Options for timing of announcement

10. Given the importance of providing the sector with certainty around how and when the issues covered in the Issues Paper will be progressed, officials recommend making a public announcement before Budget Day.

11. Officials recommend Ministers make an announcement on or around 28 April 2025 to align with the anticipated release date of the Draft Operational Statement. This would provide certainty in relation to the next steps for all the issues covered in the Issues Paper.

Content of public announcement

12. Attached to this report is a draft media statement and Q&As that Ministers may wish to use as part of their public announcement. The media statement:

    1.9 notes the significant response from submitters with over 900 submissions received;

    1.10 confirms that no changes relating to the issues covered in the Issues Paper will be included in Budget 2025;

    1.11 notes the complexity of the issues involved and that officials have been asked to do further work, including possible further consultation;

    1.12 notes that the Government wants to ensure the integrity of the tax system, and that the tax concessions provided remain fit for purpose and are not abused;

    1.13 notes that Inland Revenue will release the draft operational statement shortly; and

    1.14 notes that small not-for-profits should have minimal compliance costs and remain outside the tax base when possible.

Note on removing the charity business income tax exemption

13. As noted above, officials were asked to prepare a note setting out the practical difficulties of removing the charity business income tax exemption. It is understood that the intention is for this note to be circulated to Budget Ministers.

14. Officials have prepared this note and have attached it to this report.

Consultation

15. The Treasury and the Department of Internal Affairs have been informed of this report.

Next steps

16. Officials recommend that you note the contents of the attached:

    1.15 a draft media statement and Q&As to support an announcement on the tax issues covered in the Issues Paper;

    1.16 a note that could be circulated to Budget Ministers setting out the practical difficulties of removing the charity business income tax exemption; and

    1.17 six information sheets on the topics covered in the Issues Paper.

17. We are happy to discuss with you, or liaise with your office, if there is any additional material you require to support the announcement.

18. We recommend that you refer a copy of this report and attachments to the Minister for the Community and Voluntary Sector.

19. s 9(2)(g)(i)

Recommended action

We recommend that you:

1. **agree** to make a pre-Budget announcement on or around 28 April 2025 in relation to charities and not-for-profit tax issues covered in the officials' issues paper, *Taxation and the not-for-profit sector.*

Agreed/Not agreed	Agreed/Not agreed
Minister of Finance	*Minister of Revenue*

2. **note** that Inland Revenue intends to release its draft operational statement on the tax treatment of mutual associations and member transactions on or around 28 April 2025.

Noted	Noted
Minister of Finance	*Minister of Revenue*

20. **note** the content of the attached note on the practical difficulties of removing the charity business income tax exemption.

Noted	Noted
Minister of Finance	*Minister of Revenue*

21. **note** the contents of the six attached information sheets prepared on the topics covered in the officials' issues paper, *Taxation and the not-for-profit sector.*

Noted	Noted
Minister of Finance	*Minister of Revenue*

22. **refer** a copy of this report and attachments to the Minister for the Community and Voluntary Sector.

Referred/Not referred	Referred/Not referred
Minister of Finance	*Minister of Revenue*

s 9(2)(a)

Peter Frawley
Policy Lead
Policy

Hon Nicola Willis	**Hon Simon Watts**
Minister of Finance	Minister of Revenue
/ /2025	/ /2025

Practical difficulties of removing the charity business income tax exemption

Background

1. This note is provided in response to a request arising from Budget Ministers' 9 April meeting to provide a short why it is difficult to tax charity business income.

2. Inland Revenue's issues paper, *Taxation and the not-for-profit sector* raised the possibility of taxing charity business income that arose from activities unrelated to the relevant charity's charitable purposes. The issues paper also suggested ways to reduce compliance costs for smaller charities (for example, a de minimis) and reducing the tax liability to the extent that the business distributes the income to charity.

General themes from submissions

3. The general themes from submissions were:

   3.1 *Timeframe and process:* Many submitters said more time and further consultation was needed to deal with the various complex issues before any decisions are made to proceed.

   3.2 *Charities provide a net benefit, not a net cost, for the Government:* Many submitters said that the fiscal cost of the tax exemption is only one side of the equation and that charities save government expenditure and provide a net gain for the Government.

   3.3 *Insufficient problem definition:* Some submitters said there was a lack of clarity about what was the problem, especially since the paper stated that no competitive advantage is afforded to tax-exempt charitable businesses.

   3.4 *Better to focus on "bad actors":* Submitters said the focus should be on strengthening existing regulatory oversight for those abusing the current exemptions rather than introducing blanket tax measures including, potentially, narrowing the definition of "charitable purpose" in the Charities Act 2005.

   3.5 *Consideration of the Treaty of Waitangi:* Submitters, including iwi, said the consultation did not consider the unique circumstances of iwi and Māori entities, including those entities established to receive Treaty settlement assets.

   3.6 *Why charities have businesses*: Charities generally become involved in businesses because they see it as a less variable source of funding than donations.

Charity business tax specific issues

4. The themes from submissions made in relation to the charity business income tax exemption included:

   4.1 *Compliance costs:* Charities would face material compliance costs and a period of uncertainty if unrelated business income was taxed. This would divert resources away from their charitable activities. While the compliance costs could be ameliorated through a de minimis, larger charities would still incur those costs.

4.2 *Complexity:* There are technical issues that need to be worked through, including:

4.2.1 The tax base: Should it be income from unrelated sources or all business income. Even if it were just unrelated income, that could be wide enough to cover income on term deposits and rental income. This is an issue in overseas jurisdictions that tax some form of business income – in these cases the bases vary and there are various exemptions, which adds to the complexity. Education of taxpayers would be needed to minimise ongoing litigation in this area.

4.2.2 For example, a submission from BestStart stated its business activities are in early childhood education, which directly relates to the charitable purpose of advancing education; and Sanitarium considers that providing healthy food is part of its religious objective. Whatever the definition of "unrelated", it will have to be explained and enforced.

4.2.3 There would need to be apportionment of income and costs if business activity was not quarantined within a separate entity, and apportionment of distributions based on whether they were sourced from unrelated and related income.

4.2.4 If a deduction were allowed for distributions by a business to its parent charity, then absent other rules, the charity could simply recapitalise the business through equity injections. It would be very difficult to come up with sensible rules preventing such circularity. Making quick changes has a high risk of inadequate design, leading to a loss of efficiency for the sector.

4.3 *Investment bias*: There is no compelling case for distinguishing a charity's business income from its other forms of income. Applying different tax treatment to one form of income would distort investment decisions towards investments that remain tax-free, which may have lower returns.

4.4 s 9(2)(h)

4.5 *International investment implications:* Some of the iwi entities have arrangements with external investors that rely on the current tax arrangements. A change could more generally raise concerns among international investors. This aspect requires further consideration.

4.6 *Fiscal implications:* The fiscal estimates of taxing unrelated business income are now estimated to be in the range of $30 million to $70 million per annum, averaging $50 million per annum. The Government would need to consider how much of this revenue would be allocated to delivering replacement services to reduce any social costs.

Information sheet – Charity business income tax exemption

Overview of topic

- Registered charities are currently exempt from paying tax on their business income. This exemption applies regardless of whether the charity business is related to their charitable purposes.
- The fiscal cost of not taxing charity business income is material and is likely to increase.
- Tax concessions for unrelated charity businesses reduce government revenue, and shift the tax burden to other taxpayers. Whether charity business income should be taxed therefore depends on the level of support that the Government wants to provide charities through the tax system.
- New Zealand is an international outlier in providing charities with a tax exemption for unrelated charity business income. According to a 2020 OECD study, most countries have either restricted the commercial activities that a charitable entity can engage in, or they tax charity business income if the business income is unrelated to charitable purpose activities.

What was covered in the issues paper

- The issues paper explored the rationale for providing the charity business income tax exemption, and outlined a number of policy design issues that would need to be considered if charities were required to pay tax on their unrelated business income, including:
    - how "unrelated business" would be defined,
    - what an appropriate de minimis threshold would be to continue to provide an exemption for small-scale charity businesses, and
    - whether charity business income distributed for charitable purposes should remain tax exempt.

Issues raised in submissions

- Of all the topics covered in the issues paper, this topic is the most complex and was the primary focus for most submitters.
- While some submitters agreed with Inland Revenue's view outlined in the issues paper that the charity business tax exemption did not give charity businesses a competitive advantage, some other submitters disagreed on this point.
- Most submitters said New Zealand should not change its approach to business income, which follows a "destination of income" approach, recognising that what matters is where the money ultimately goes, not its original source.
- Some submitters thought it unlikely that any substantial revenue would be collected from the proposed change, and that it would likely result in the Government having to allocate further funding to deliver the essential services currently provided by charities to avoid social costs.
- Submitters highlighted the potential complexity of any rule changes, for example, around how an "unrelated business" would be defined.
- Submitters raised a range of exclusions that should be required under any proposed changes. This included various Treaty settlement entities that are charities, some of which have investment arrangements with external investors that rely on their current arrangements.

- Some iwi groups submitted that the reforms outlined in the issues paper would represent breaches of the Treaty of Waitangi.
- Concerns were raised that international investors attracted to New Zealand's stable investment environment could be dissuaded from investing and therefore undermine economic growth.
- Submitters stated that taxing unrelated business income would impose significant compliance costs and uncertainty on charities, adding a "deadweight" cost and distracting affected charities from carrying out their charitable purposes.
- Submitters said a change would also result in a reduction in the number of staff or charitable programmes.

Fiscals

- The fiscal estimates for taxing unrelated business income range from $30 million to $70 million per annum, averaging $50 million per annum.
- This estimate assumes the exemption will be removed for "unrelated" business income with a de minimis of $5 million total expenditure, and that there are no changes to distribution or donation policies. There is therefore a high level of uncertainty until the policy is finalised.
- Attached to this info sheet is a list of 15 large charities reporting business activity that is unrelated to charitable purpose. The cut-off we used to arrive at 15 was total assets of around $100 million or more.

Next steps

- At this point, officials consider that nothing raised in submissions changes their initial advice, which was not to progress this matter. Officials will report to Ministers on this topic by end of June 2025, followed by further consultation if required, with a view to Ministers making final decisions in December 2025.
- s 9(2)(h)

Information sheet – Donor-controlled charities

Overview of topic

- A donor-controlled charity (DCC) is a registered charitable entity that is controlled by a principal donor, their family, or their associates.
- Donors can claim donation tax credits on donations to their own DCC, in the same way as if they had donated to an unrelated charity.
- Unlike many countries, New Zealand does not distinguish DCCs from other charitable organisations.
- DCCs can enable tax avoidance and raise integrity concerns because of the control the donor or their associates can exercise over the use of charity funds. For example, DCCs can be used as part of circular arrangements, where the donor gifts money to a charity they control, claiming a donation tax credit, only for the charity to immediately invest the donated funds back into a business controlled by the donor or their associates.
- s 6(c)
- Data shows that between 2018 and 2021, donations made by donors to their DCCs, where donation tax credits had been claimed, exceeded $75 million. A table setting out 20 examples of large donor-controlled charities is attached as an appendix to this factsheet.

What was covered in the issues paper

- The Issues Paper explored DCC integrity issues and policy design questions including:
    - how a DCC could be defined
    - whether transactions between DCCs and their associates could be required to be on "arm's length" terms or prohibited outright, and
    - whether DCCs could be required to make a minimum distribution each year for charitable purposes.

Issues raised in submissions

- There was an acknowledgment from submitters that some integrity issues relating to DCC needed to be addressed.
- Some submitters said the existing charities legislation was already robust enough to deal with DCC integrity concerns, and that creating specific rules would impose unnecessary compliance costs for all DCCs. Other submitters said they had not observed integrity issues with DCCs and said they could not support adding specific integrity rules without detailed analysis of the scale of the problem.
- Submitters pointed to the challenges surrounding how DCCs would be defined. For example, an overly wide definition would run the risk of unintentionally extending any DCC rules to Māori post-settlement governance entities, and charities controlled by another organisation or charity.
- Submitters pointed to potential negative impacts of introducing DCC integrity rules, including:
    - discouraging and hindering private, proactive philanthropy

[1] This figure is indicative only and depends on how DCCs are defined.

  - minimum distribution rules increasing compliance costs and eroding a DDC's asset base, and
  - prohibiting related-party investments limiting the growth of DCCs.

Fiscals

- Any policy changes would impact on behaviour but would have no or minimal fiscal implications.

Next steps

- Submissions have not resulted in officials changing their initial advice that reform is necessary to improve the integrity of the tax rules for donor-controlled charities, and targeted consultation on the detailed design has been recommended to ensure there are workable definitions and rules.
- Officials will report to Ministers on this topic by end of June 2025, followed by consultation if required, with a view to Ministers making final decisions in December 2025.

Information sheet – Exemptions

What was covered in the issues paper

- The issues paper explores repealing tax exemptions that appear no longer fit for purpose and/or are inconsistent with New Zealand's broad-base, low-rate tax policy framework.
- The tax exemptions being reviewed are:
    - Fringe Benefit Tax (FBT) exemption for employees of charities
    - local and regional promotional bodies tax exemption (approximately 1,000 entities affected)
    - herd improvement bodies tax exemption (approximately 57 entities affected)
    - bodies promoting scientific and industrial research tax exemption (approximately 93 affected)
    - veterinary service bodies tax exemption (approximately 57 affected)
    - non-resident charities with no charitable purpose in New Zealand (approximately 300 to 400 entities affected), and
    - exemptions for member transactions made within friendly societies and credit unions (approximately 100 entities affected). s 6(c)

Issues raised in submissions

Overall, the FBT exemption attracted the most interest from submitters, while fewer submissions were received in relation to the other six income tax exemptions. Most submitters were against the removal of the exemptions, with only the veterinary service bodies exemption receiving more balanced feedback for and against its removal.

- *FBT exemption:* Submitters said this exemption goes some way to allow charities to compete for staff in the job market and removing it would hinder charities' ability to attract and retain staff. Removing it would also require reviewing remuneration policies. Some submitters instead called for changes to simplify the exemption and reduce compliance costs, which could be considered through the current FBT review.
- *Veterinary service bodies exemption:* Not-for-profit vet clubs (benefitting from the exemption) submitted that the removal of their exemption would lead to a reduction in the number of veterinary service providers in the market, therefore reducing competition. Private vet clinics supported removing the exemption saying that this would decrease vet clubs undercutting commercial vet clinics resulting in greater competition.
- *Non-resident charity tax exemption:* Some submitters supported reviewing the exemption to address perceived fairness and integrity concerns. Others noted its removal could discourage overseas charities from passively investing in New Zealand.
- *Local and regional promotional bodies exemption:* Those submitters that would be affected by the removal of this exemption submitted that the removal would reduce local economic development activities and investment into community safety.

- *Friendly societies and credit unions exemption:* Submitters almost universally expressed significant concerns that removing this exemption would undermine the core purpose of friendly societies and credit unions to support their members. The three credit unions said it would weaken their ability to compete in a concentrated financial market where they already have a disadvantage due to their smaller size and restrictions on raising capital.

Fiscals

	Fiscal impact (pa)
Removal of all tax exemptions considered	s 9(2)(f)(iv)
s 9(2)(f)(iv)	
Friendly societies and credit unions	$7m
s 9(2)(f)(iv)	
Veterinary service bodies	$2m
Herd improvement bodies	$1m
Bodies promoting scientific and industrial research	$1m
Non-resident charities	Small unquantifiable gain

Next steps

- Further policy analysis will be carried out on this topic, and officials will report to Ministers by end of June 2025, followed by further consultation if required, with a view to Ministers making final decisions in December 2025.

Information sheet – Key messages relating to charities and NFP tax issues.

Charities business income tax exemption

- It is clear from submissions that the issues are complex, and Ministers have asked officials to do more thinking on what was covered in the issues paper and the submissions.
- The fiscal estimates are not sufficiently high, and certainly not in the order of billions as had been reported and incorrectly attributed to the Minister of Finance. [With billions in 'profit' exempt from tax, changes to NZ's charity rules are long overdue - The Conversation].
- It is important to ensure the integrity of the tax system, and that the tax concessions provided to the sector remain fit for purpose and are not abused.
- Officials will report back at the end of June, followed by further consultation if required, with a view to Ministers making decisions by the end of the year.

Donor-controlled charities

- There has been some acknowledgement in the consultation that there are integrity issues relating to donor-controlled charities.
- After reading the submissions, officials still consider that reform is necessary to improve the integrity of the tax rules for donor-controlled charities, and further consultation on the detailed design has been recommended to ensure there are workable definitions and rules.
- Officials will report to Ministers by the end of June 2025, followed by further consultation if required, with a view to Ministers making final decisions in December 2025.

Not-for-Profits and member transactions

- This topic has generated a lot of interest from submitters, particularly around the extent to which membership subscriptions are taxable.
- Submitters have been clear about the negative impacts they foresee if membership subscriptions were to be taxed, and they have highlighted the contribution that NFPs make to the community.
- This topic doesn't affect registered charities or local sports clubs (amateur sports bodies) that have their own specific tax exemptions.
- Inland Revenue will be releasing its draft operational statement for consultation soon (on or about 28 April 2025).
- The statement will set out Inland Revenue's legal reasoning behind its updated view and will provide an opportunity for public submissions on the technical correctness of the updated view that member subscriptions may be taxable.
- Regardless of whether Inland Revenue then confirms or amends its view after consultation, officials have been asked to do further work on this topic.
- Officials will report to Ministers by the end of June 2025, followed by consultation if required, with a view to Ministers making final decisions in December 2025.

Specific exemptions and simplifications

- Submitters have told us that more time is required to work through these issues.
- Officials will report back at the end of June, followed by further consultation if required, with a view to Ministers making decisions by the end of the year.

Information sheet – Not-for-profits and member transactions

Overview of topic

- There are specific tax rules relating to transactions between not-for-profits (NFPs) and their members. (These rules are not relevant for entities with specific income tax exemptions, such as registered charities and amateur sports bodies.).
- Inland Revenue's website currently states that NFPs are liable for tax on income from member trading transactions but not on membership subscriptions.
- Inland Revenue has revised its interpretation of the current legislation and now considers that in some circumstances, NFPs may be liable for tax on membership subscriptions. This view is set out in a draft operational statement that Inland Revenue will release for consultation soon (28 April 2025).
- Inland Revenue estimates that 9,000 NFPs may not be paying tax in line with this updated view. Entities affected include, cosmopolitan clubs, RSAs, societies, trade associations, professional and regulatory bodies, industry councils.

What was covered in the issues paper

- The issues paper explored a number of options for mitigating the impact of the updated view for those NFPs not currently paying tax on member transactions, including subscriptions. These options included increasing the effective tax-free threshold for NFPs (currently $1,000) and simplifying the return filing requirements. Views were sought on an appropriate new threshold.

Issues raised in submissions

- This topic attracted a lot of interest, particularly in relation to the tax treatment of member subscriptions.
- There was broad support for the options raised for reducing compliance costs for NFPs.
- A number of submitters disagreed with the technical correctness of the updated view, particularly that member subscriptions might be taxable under the current legislation.
- Submitters stated that if Inland Revenue's updated view is confirmed, and member subscriptions were taxable, this would place a significant amount of financial pressure on NFPs, affecting the benefits provided and/or the price of membership subscriptions.
- Some submitters suggested a law change would be required to either provide NFPs with a full income tax exemption, as is the case for amateur sports bodies, or to confirm that member subscriptions should not be taxable.

Fiscals

- Fiscals have not been costed, but depending on policy design, the changes for NFPs and related matters could contain a range of revenue positive and revenue negative measures.

Next steps

- The draft operational statement will be released by Inland Revenue for consultation soon (on or about 28 April 2025). The statement will set out legal reasoning behind the updated view, and will provide an opportunity for public submissions on the technical correctness of the updated view.

- Once consultation on the draft operational statement has closed, Inland Revenue will consider the submissions received and either confirm or amend its updated view.
- Further policy analysis will then be carried out on this topic, officials will report to Ministers by end of June 2025, followed by consultation if required, with a view to Ministers making final decisions in December 2025.

Information sheet – Simplifications in the not-for-profit sector

Overview of topic

- Officials are reviewing ways to simplify the tax rules for the not-for-profit sector, particularly for donors under the donation tax credit (DTC) regime and volunteers receiving honoraria payments.

What was covered in the issues paper

- In relation to the DTC regime, changes were explored to reduce compliance costs and increase the claiming of DTCs, including:
    - real-time payments by delinking the regime from income tax
    - streamlining the claims process by collecting data from donee organisations
    - introducing a three-month grace period so donee status is retained if a deregistered charity is re-registered within three-months.
- In relation to volunteer honoraria payments, the issues paper considered treating these payments as salary or wages, rather than schedular payments, so that volunteers would not have to file a return or account for ACC levies themselves.

Issues raised in submissions

- Submitters were largely in favour of any measures to simplify the DTC regime and the tax treatment of volunteer payments.
- Some submitters raised concerns of potential compliance costs on the sector. For example, real-time payments would require charities to increase the frequency that they issue tax receipts to donors.
- Other volunteer payment simplification measures suggested by submitters included introducing a tax-free threshold for honoraria, a progressive rate, and extending payment and filing dates.
- Other DTC simplification ideas suggested by submitters included increasing the $5 minimum donation threshold to reduce the number of receipts charities would need to issue to donors.
- Submitters noted that the benefits of any proposed changes for volunteers and donors should be assessed against any potential compliance costs placed on not-for-profit entities.

Fiscals

- Fiscal implications are likely minimal but depends on design and behavioural response.
- Depending on the proposed changes to the DTC regime, there may be significant system and administration costs for Inland Revenue.

Next steps

- Officials will report to Ministers on these issues by end of June 2025, followed by consultation if required, with a view to Ministers making final decisions in December 2025.

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Te Tari Taake

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Briefing note

Reference: BN2025/213

Date: 6 May 2025

To: Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Helen Kuy
Revenue Advisor, Minister of Finance – Emma Grigg

From: Stewart Donaldson
Philip Marshall

Subject: **Not-for-profits: Inland Revenue advice to submitters and stakeholders**

Purpose

1. This briefing note outlines:

   - the generic responses officials are providing to submitters and stakeholders when asked about the next steps
   - the approach Inland Revenue is taking to Official Information Act (OIA) requests for submissions and advice relating to the February 2025 issues paper *"Taxation and the not-for-profit sector"*
   - more context about the $50 million fiscal estimate for taxing charity business income.

Generic responses provided to submitters and stakeholders

2. A number of submitters and stakeholders have contacted Inland Revenue asking what the next steps will be for the not-for-profit policy work. While we are tailoring our responses to the particular requestor, our responses generally cover the following six points.

Submissions received

3. Inland Revenue received over 900 submissions in response to its Issues Paper *Taxation and the not-for-profit sector*.

Announcement by the Minister of Finance

4. On 28 April 2025, the Minister of Finance announced that no changes relating to the charities and not-for-profits tax issues covered in the Issues Paper would be included in Budget 2025.

Detailed report to be provided in the coming months

5. The Minister of Finance said the consultation on the Issues Paper uncovered a lot of complexity about definitions and rules and how charities and not-for-profits would react in practice. She has asked officials to consider the submissions in detail and report to her again in the coming months.

Final policy decisions by year-end

6. For any issues the Government decides to progress after it has considered the detailed report on submissions, it is likely to make decisions by the end of the year. That will allow officials time to consult further before providing final advice.

Proactive release of submissions

7. Inland Revenue intends to proactively release the 900 submissions (apart from those that a submitter specifically requested be withheld) after the detailed report on submissions has been provided to Ministers.

Consultation by the Inland Revenue on mutual transactions of associations

8. The Issues Paper noted that after submissions on policy matters closed, Inland Revenue would release a draft operational statement relevant for not-for-profits that are not tax exempt. It noted that the draft operational statement would set out the Commissioner's view on how profits from certain not-for-profit member transactions, including subscriptions in certain circumstances, may be taxable. That draft operational statement has now been released (30 April 2025) for eight weeks of consultation ending on 25 June 2025.

9. The Minister of Finance has asked policy officials to report back to her after that consultation has taken place. It is possible that the Commissioner's view might change as a result of points raised by submitters. However, if applying the current legislation in line with the Commissioner's view would be impractical and unworkable, then the Government would look at taking a pragmatic approach and consider amending the legislation.

Approach taken to requests under the OIA

10. We are receiving ongoing requests for release of the submissions, and release of previous Inland Revenue advice, under the OIA.

11. We are refusing these requests in full, on the basis that the matters remain under active consideration.

12. We have indicated that once discussions have concluded with Ministers, the submissions will be published on Inland Revenue's Tax Policy website and previous advice will be released (subject to appropriate redactions under the OIA).

The $50 million per annum fiscal impact of amending the charity business income tax exemption

13. In respect of the $50 million per annum fiscal estimate for removing the charity business income tax exemption, we have previously advised:[1]

    - the fiscal impact is approximately $50 million per annum
    - the costing is a range of $30 million to $70 million with a midpoint of $50 million

[1] IR2025-146 refers

- the costing assumes the exemption will be removed for "unrelated" business income (income sourced from activities that are unrelated to a charity's charitable purpose) with a de minimis of $5 million total expenditure so that small-scale trading activity is not taxed, and that there are no changes to distribution or donation policies

- the costing is based on our estimate of profits retained by the business after distributions have been made to parent charities

- until the policy is finalised, there is a high level of uncertainty involved.

14. Ministers have been asked why the $50 million estimate is so low, given that in a published article in February 2025 AUT senior lecturer Ranjana Gupta stated there was about NZ$2 billion of "profit" in the charitable sector that was not subject to tax.

15. The figure quoted by Ms Gupta was taken directly from the Charities Services 2023/2024 Annual Review published in late 2024. That review stated the sector reported total income of $27.34 billion and total expenditure $25.28 billion, the difference being a surplus of $2.06 billion.

16. To provide Ministers with more context, our advice is that the $2.06 billion represents the aggregate surplus of all registered charities. This is not relevant for our fiscal estimate for taxing unrelated charity business income for the following reasons:

    - The majority of the surpluses reported by charities are not relevant for our unrelated business income estimate because they comprise passive investment income and income such as donations and grants that are directly relevant to carrying out charitable purposes.

    - The surpluses reported by charities that are relevant for the unrelated business income estimate are indicative only, as they are calculated using accounting standards and would need to be adjusted to reflect income taxable under the Income Tax Act. For example, the movement in the fair value of investments would be reported as accounting income but would generally not be taxable income.

    - The aggregate surplus reported by charities includes surpluses derived by entities that would be exempt from income tax even if they were not registered charities. For example, it includes surpluses reported by universities, which would be tax exempt under a separate exemption even if the universities did not register as a charity.

    - Some surpluses reported on the Charities Register are overstated due to reporting and transposition errors. Typically, this occurs because data is self-reported and therefore Charities Services has limited control over its quality and cannot verify its accuracy.

17. We have included a table in Appendix A summarising the nature of the largest surpluses reported by charities on the Charities Register in the most recent year.

Consultation with agencies

18. The Treasury was informed about this briefing note.

Stewart Donaldson
Principal Policy Advisor
s 9(2)(a)

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **Taxation and the not-for-profit sector: Recommendations from officials**

Date:	28 August 2025	**Priority:**	High
Security level:	Sensitive - Budget	**Report number:**	IR2025/257

Action sought

	Action sought	**Deadline**
Minister of Finance	**Agree** to recommendations	15 September 2025
Minister of Revenue	**Agree** to recommendations	15 September 2025

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**	**Suggested first contact**
Stewart Donaldson	Principal Policy Advisor	s 9(2)(a)	☒
Philip Marshall	Senior Policy Advisor		☐

28 August 2025

Minister of Finance
Minister of Revenue

Taxation and the not-for-profit sector: Recommendations from officials

Purpose

1. This report provides our recommendations for changes to the tax settings for the not-for-profit (NFP) sector. A supplementary report (IR2025/258) provides further details on the changes and feedback from public submissions.

2. We have split the issues into three packages reflecting the overall objectives of the tax policy work.

Integrity issues

- Charity business income tax exemption
- Tax treatment of donor-controlled charities and the donation tax credit

Simplification opportunities

- Tax treatment of subscriptions and member transactions
- Simplifying tax obligations for not-for-profit organisations including income tax return filing
- Simplifying tax obligations for donors and volunteers

Removal of tax exemptions that are no longer fit for purpose

- Income tax exemptions
- s 9(2)(f)(iv)

Background

3. This project is a priority on the Government's tax and social policy work programme. It is focused on improving the integrity and simplicity of the NFP tax rules while supporting the sector. Although some of these changes may result in a fiscal gain, this has not been the driver for these changes.

4. Our advice has been informed by submissions made on the February 2025 officials' issues paper, "Taxation and the not-for-profit sector". Over 900 submissions were received in response to that consultation, and they have been published on the Inland Revenue website.

5. Ministers have made public statements about this work. The key messages have been:

- The consultation uncovered a lot of complexity and Ministers do not want to rush any changes.

- The Government is committed to making sure we have a fair system with high integrity.
- In response to the Commissioner's updated view that some NFPs may need to pay tax on subscription income, Ministers have sought advice on how the legislation could be amended to ensure there is a fair and practical outcome in this area.

Context

NFP sector

6. NFPs make a significant contribution to the community and the economy. Many NFPs, particularly charities, contribute by reducing demand on government services, such as social welfare, mental health, and youth development programmes.

7. The NFP sector is complex from a tax perspective. It is made up of companies, trusts, incorporated and unincorporated societies, and joint ventures. NFPs range from large universities to churches, from iwi entities to small social clubs.

8. There is a range of income tax concessions and exemptions available for the sector and some NFPs move between them over their lifetime. At present most of the 81,000 NFPs recorded on Inland Revenue's system fall into the following tax categories:

   - 29,000 tax exempt charities registered under the Charities Act 2005
   - 26,000 taxable NFPs that can access a $1,000 tax-free threshold
   - 19,000 tax exempt amateur sports bodies (which are outside the scope of this work), and
   - 2,000 NFPs that claim other income tax exemptions, such as s 9(2)(f)(iv) , veterinary services bodies, herd improvement bodies, and bodies promoting scientific or industrial research.

9. In addition, 350,000 individuals claim donation tax credits (DTCs) on donations made to charities and schools each year. The main recipients of these donations are religious charities (63% of the total value of DTCs claimed), other charities (29%) and schools (8%).

10. This taxation review comes at a time when the NFP sector is navigating a major legislative transition, as all incorporated societies must re-register under the Incorporated Societies Act 2022 by April 2026 to retain their legal status. At the time of writing this report, approximately 16,000 societies incorporated under the previous Incorporated Societies Act are still to register under the new Incorporated Societies Act.

Māori sector

11. s 9(2)(g)(i)

12. s 9(2)(g)(i)

13. s 9(2)(h)

Department of Internal Affairs

14. We have worked closely with the Department of Internal Affairs (DIA) in preparing our advice. DIA is responsible for regulating over 29,000 charities registered under the Charities Act. It also advises the Minister for the Community and Voluntary Sector, so is interested in charities and NFPs more broadly. DIA is currently progressing an "enabling and growing philanthropic giving" policy initiative.

Package overview and recommendations

15. Each of the three packages has financial consequences, stakeholder impacts and risks you should be aware of. They are summarised below. The detailed supplementary report provides more analysis on these issues and feedback from submitters.

16. We recommend further consultation on matters you wish us to continue working on. Our specific consultation recommendations are provided at the end of this report. Consultation could be timed later in 2025 so that Cabinet could make final decisions as part of Budget 2026. You could then have the choice of Budget legislation or legislating in the 2026–27 annual rates Bill. The application dates could be the 2027–28 income year (generally commencing from 1 April 2027) or the 2028–29 income year (generally commencing from 1 April 2028), depending on how much lead-in time the sector and Inland Revenue need to implement change.

Integrity issues

17. Integrity of the tax system as it applies to NFPs was a key focus of the policy work. Two significant areas that we consulted on were the taxation of charity business income and the tax treatment of donor-controlled charities.

Charity business income tax exemption

18. We recommend that we cease work on developing proposals to tax the business income of a charity primarily because of the complexities, compliance costs and distortions that arise when taxing charity business income.

19. Instead, we recommend that Inland Revenue and DIA consider how to improve the reporting requirements for charities carrying on businesses, including details of the accumulation and distribution of their funds. This would improve public transparency and the information provided to DIA and Inland Revenue. This could also inform future changes to regulatory and tax settings and administration of the

rules. If a minimum distribution rule for donor-controlled charities is introduced (see below) we could also monitor the effectiveness of this specific minimum distribution rule before considering whether to apply it more widely across the sector.

20. We acknowledge that the current tax policy setting to exempt the income of all businesses owned by charities makes New Zealand (and Australia) an international outlier. Further, the extent of that exemption is largely uncapped so the amount of income tax forgone is unlimited. However, we consider the main problem is a broader issue of profit accumulation and the timing mismatch between when the tax exemption is provided and when the exempt income is used for charitable purposes. We take the view there is little competitive pricing advantage arising from the income tax exemption.

21. We have provided you with two other options. An option suggested in our issues paper, which was to tax accumulated net income of a charity business, would align with practice in many countries but would be complex to apply. There would be a number of key design issues to consider, such as whether to have an anti-avoidance rule to deter distributions that a business makes to its parent charity from being immediately recycled back into the business.

22. Some submitters suggested an alternative option to deal with accumulation through a minimum distribution rule. Under this option, charity businesses would need to distribute up to the amount of their theoretical tax liability, that is, the amount of tax they would have paid if they were taxable. They would only be taxed to the extent distributions fall short of this nominal tax amount. This alternative option would be more targeted than the option in our issues paper and impact on fewer charity businesses, so on balance it would be our preferred second option. However, it would also be complex to apply and there is little overseas experience to follow.

Donor-controlled charities and DTCs

23. Donor-controlled charities are organisations where the donor (or their associates) retain control over how charitable funds are spent. This poses a heightened risk of aggressive tax planning and can also lead to a delay between the time of tax concessions for the donor and the charity, and the distribution of funds for charitable purposes.

24. We recommend continuing work on integrity measures to address circular arrangements and non-arm's length transactions and to introduce a minimum distribution rule to ensure timely use of tax-exempt funds. These measures would draw on experience from the Australian and Canadian rules for donor-controlled charities.

25. We also recommend new integrity rules for donor-advised funds (which may be used as direct substitutes for donor-controlled charities) and for discretionary trusts that allocate income to tax-exempt beneficiaries such as charities but do not actually pay them (we propose a new "pay" rule). Both these matters help address, but are not limited to, integrity risks for donor-controlled charities. If the proposed work on donor-controlled charities does not go ahead, we still recommend advancing work on these two issues.

26. At the same time as developing new rules for donor-controlled charities we recommend that we provide you with further advice on a reduction in the ceiling for DTCs. This can be another option to address integrity concerns when fraud and tax avoidance could occur. It would also impact on many circular arrangements

involving donor-controlled charities which may reduce the need for donor-controlled charity rules. The advice would have a different focus compared to previous years when it was considered as an option to raise revenue. For example, if the ceiling was set at $15,000 for donations (a $5,000 DTC), we expect aggregate DTC claims could reduce by approximately $40 million per year, affecting about 2% of donors.

27. We and DIA recommend that, if you decide to progress this DTC option, it be part of the public consultation process to help identify any unintended consequences and to mitigate the risk of relationship challenges with key stakeholders. However, the decision whether to publicly consult is finely balanced and you have made the decision not to publicly consult on this issue in the past.

Fiscal impacts and affected stakeholders

28. Table 1A contains a summary of the fiscal impacts and affected stakeholders for these integrity issues. There are risks associated with these issues:

- s 9(2)(g)(i)
- We have previously reported to you that donor behaviour in response to DTC ceiling changes is difficult to forecast because limited research is available. If a change in the donation tax concession reduces charity donation income, some charities may reduce their services, resulting in an increase in demand for government support. (IR2024/359 refers).

Table 1A: Fiscal impacts and affected stakeholders

Proposal	Fiscals (pa)	Affected population
Remove income tax exemption for unrelated charity businesses	+$30m–$70m[1]	Could affect approximately 200 large charities. s 6(c)
Accumulation within donor-controlled charities	$0[2]	Could affect approximately 200 registered charities including private foundations controlled by high wealth individuals. A new rule would change behaviour going forward, so exactly who it would affect is unknown at this stage.
Reduce DTC ceiling	+$40m[3]	Could affect up to 2% of donors (approximately 8,000), depending on the level of the ceiling.

Recommendations

29. Table 1B contains our integrity issues recommendations.

[1] The option we recommend is not to remove the tax exemption, so there would be no fiscal gain. However, if Ministers prefer to tax accumulated business income, the costing is a range of $30 million to $70 million with a midpoint of $50 million. This costing assumes the exemption will be removed for unrelated business income with a de minimis of $5 million total expenditure.
[2] A policy change would affect behaviour and have no/minimal fiscal implications.
[3] Integrity issues for donor-controlled charities could be partly mitigated by lowering the DTC ceiling. For example, if the cap was set at $15,000 for donations (a $5,000 DTC) the fiscal saving would be approximately $40 million per year, affecting about 8,000 donors or 2% of the total 350,000 donors.

Table 1B: Recommendations – Integrity issues

Charity business income tax exemption *(Appendix 1)*
(a) No further work on the development of proposals to tax the business income of charities. Instead, **agree** to officials working with DIA to improve reporting requirements for accumulated funds and distributions, and monitor the effect that a minimum distribution rule for donor-controlled charities recommended below would have on accumulation behaviour. (*Officials' preferred option*) Agreed/Not agreed Agreed/Not agreed
(b) If you do not agree to recommendation (a), **agree** to officials working on a minimum distribution rule for charity businesses. *(Officials' preferred second option)* Agreed/Not agreed Agreed/Not agreed
(c) If you do not agree to recommendations (a) or (b), **agree** to officials continuing work to tax the net income of charity businesses that is not distributed to charitable purposes. Agreed/Not agreed Agreed/Not agreed
Donor-controlled charities and the donation tax credit *(Appendix 2)*
(a) Agree that officials continue work on the design of the following rules: i. A minimum distribution rule for donor-controlled charities along with integrity rules for transactions between donor-controlled charities and associated persons. Agreed/Not agreed Agreed/Not agreed ii. Integrity measures for donor-advised funds. Agreed/Not agreed Agreed/Not agreed iii. A "pay" rule for trust allocations to tax-exempt beneficiaries. Agreed/Not agreed Agreed/Not agreed
(b) Agree that officials provide further policy advice on donation tax concession settings for donors, with a view to reducing the donation tax concessions as a way to address integrity concerns. This would occur alongside the recommendations on changes to the treatment of donor-controlled entities, referred to above. Agreed/Not agreed Agreed/Not agreed

Simplifying tax obligations for NFPs

30. There are opportunities to simplify tax obligations for taxable NFPs, volunteers and donors.

Subscriptions and member transactions

31. We recommend consulting on a proposal to provide tax relief for NFP membership subscriptions and levies that have a non-commercial character. This will address sector concerns that, as a consequence of an updated Inland Revenue view,

thousands of taxable NFPs may need to start paying tax on subscription income under current law.

32. Under our proposal, membership subscriptions and levies paid in exchange for commercial goods or services would be taxable, as they would be under the updated Inland Revenue view. s 6(c) However, this does not mean all NFPs with subscriptions of a commercial nature would have a tax liability. Many would be able to deduct expenses incurred in earning subscription income, which they are unable to do at present, and some of these expenses may exceed their subscription income.

33. We recommend other simplification measures for taxable NFPs, which would benefit from consultation on detailed design. This includes simplifying filing requirements for small NFPs and increasing and better targeting the $1,000 tax-free threshold for NFPs. Based on previous consultation, we propose the tax-free threshold increases to $10,000 but is targeted at small NFPs, and the resident withholding tax (RWT) rules are amended to work more effectively.

34. As part of clarifying the rules for member transactions and subscriptions, and simplifying measures for taxable NFPs, we also recommend repealing the historic income tax exemption for approximately 100 friendly societies and s 6(c) . Currently, their member trading transactions, passive income and member subscriptions (if any) are tax exempt, and only their non-member trading transactions are taxable. Repealing the exemption will make their tax treatment consistent with other mutual associations.

35. s 9(2)(g)(i)

36.

Proposed simplifications for donors and volunteers

37. We propose specific simplifications for donors and volunteers. We have consulted sufficiently to make recommendations for volunteers, but we recommend further consultation on donor simplifications.

38. In respect of donors, we recommend two policy changes. The first would allow Inland Revenue to refund DTCs during the year instead of waiting until after year-end. The second would allow donors to allocate their DTC directly to the charity they donated to. These changes would support philanthropy and could be seen as a positive counterbalance to sector concerns if the DTC ceiling was to be reduced (see above).

39. The DTC changes have the advantage of being simple and would not incur fiscal costs. One-off implementation costs are likely to be able to be incorporated into

existing baselines. Overall, the costs would be low compared to more significant changes such as introducing the United Kingdom Gift Aid system into New Zealand or extending the scope of our existing DTC concessions.

40. In respect of volunteers, we recommend a policy change that would give NFPs the option of treating honoraria paid to volunteers as salary or wages. This simplification was supported by submitters and is already in place for Fire and Emergency New Zealand.

Fiscal impacts and affected stakeholders

41. Table 2A contains a summary of the fiscal impacts and affected stakeholders of simplifying NFP tax obligations. There are risks associated with these issues:

- If you do nothing in respect of subscriptions and levies, Inland Revenue would finalise its updated view that many subscriptions and levies would be taxable, which would impact on thousands of NFPs and is strongly opposed by the sector.
- If you decide to provide tax relief for NFP membership subscriptions and levies that have a non-commercial character (our preferred option), the fiscal cost would be approximately $3 million per annum. However, this fiscal cost would increase to approximately $7 million per annum if you decide to legislate the in-practice status quo and confirm all membership subscriptions and levies remain non-taxable.

Table 2A: Fiscal impacts and affected stakeholders

Proposal	Fiscals (pa)	Affected population
NFP tax-free threshold increase to $10,000	Less than −$1m	Could affect approximately 9,000 entities.
NFP subscriptions	−$3m	Fiscal impact assumes law change where only some subscriptions remain taxable.
Friendly societies and credit unions	+$7m	Could affect approximately 100 friendly societies such as s 6(c) and various working men's clubs. Could also affect s 6(c)
Simplifications (volunteers and DTCs)	$0m	Could affect entities that pay their volunteers honoraria (on an opt-in basis) and 350,000 individuals that claim DTC, but fiscal cost expected to be nil.

Recommendations

42. Table 2B contains our simplification recommendations.

Table 2B: Recommendations – Simplification opportunities

Subscriptions and member transactions *(Appendix 3)*	
(a) Agree officials continue work to provide tax relief for NFP membership subscriptions and levies that have a non-commercial character.	
Agreed/Not agreed	Agreed/Not agreed
(b) Agree officials continue work to simplify rules for taxable NFPs, including a review of the $1,000 tax-free threshold, the RWT exemption rules, and the income tax return filing requirements.	
Agreed/Not agreed	Agreed/Not agreed
(c) Agree officials continue work on repealing the income tax exemption for friendly societies and credit unions.	
Agreed/Not agreed	Agreed/Not Agreed
Donors and volunteers *(Appendix 4)*	
(a) Agree officials continue work on the proposals to simplify the rules for DTCs.	
Agreed/Not agreed	Agreed/Not agreed
(b) Agree officials continue work to provide NFPs with the option to treat honoraria as salary or wages.	
Agreed/Not agreed	Agreed/Not agreed

Removal of tax exemptions that are no longer fit for purpose

Income tax exemptions

43. We recommend that exemptions for non-resident charities with no charitable purpose in New Zealand, s 9(2)(f)(iv) , veterinary services bodies, herd improvement bodies, and bodies promoting scientific or industrial research should be repealed.

44. Our view is that the exemptions present various challenges to the integrity of the tax system. This includes limited oversight and public accountability, inconsistent treatment of similar entities and, in some cases, the exemptions confer a competitive advantage. The exemptions are also generally inconsistent with the Government's broad-base, low-rate tax policy framework.

45. While there is a strong justification to repeal all exemptions, in our view the exemptions for non-resident charities s 9(2)(f)(iv) are the highest priority because they have the greatest volume and raise the most integrity concerns. The veterinary services bodies exemption is also a priority because there are competitive advantage and equity concerns.

46. If you wish to maintain any of the exemptions, further policy work could be done to increase transparency about who is accessing them, which would improve the integrity of the exemptions compared to the status quo.

s 9(2)(f)(iv)

Fiscal impacts and affected stakeholders

50. Table 3A contains a summary of the fiscal impacts and affected stakeholders of removing outdated exemptions. There are risks associated with these issues:

- The tax exemption for non-resident charities applies to passive investments into New Zealand, exempting them from paying non-resident withholding tax or approved issuer levy. Some submitters noted that removal of the exemption could discourage overseas charities from passively investing in New Zealand, which could reduce foreign investment. However, we have no data to identify the amounts involved.
- s 6(c) could be impacted if the exemptions for herd improvement bodies and bodies promoting scientific or industrial research are repealed. Several submitters argued that removing the exemption could undermine these entities' independence from external and commercial pressures, and diminish policy innovation and long-term research capacity, potentially harming underfunded research areas.
- s 9(2)(f)(iv)

Table 3A: Fiscal impacts and affected stakeholders

Proposal	Fiscals (pa)	Affected population
s 9(2)(f)(iv)		
Veterinary services bodies	+$2m	Could affect approximately 50–60 entities. Entities potentially affected include s 6(c) .
Herd improvement bodies	+$1m	Could affect approximately 50–60 entities. Entities potentially affected include s 6(c) .

[4] s 9(2)(f)(iv)

Proposal	Fiscals (pa)	Affected population
Bodies promoting scientific or industrial research	+$1m	Could affect approximately 90–100 entities. Entities potentially affected include s 6(c) .
Non-resident charities	Small gain	Could affect up to approximately 350 entities, typically non-resident universities, religious organisations and private charitable foundations.

Recommendations

51. Table 3B contains our tax exemption recommendations.

Table 3B: Recommendations – Removal of tax exemptions that are no longer fit for purpose

Income tax exemptions that may no longer be fit for purpose *(Appendix 5)*	
(a) Agree to repeal the following income tax exemptions for NFPs *(officials' preferred option)*:	
i. non-resident charities non-business income *(officials' priority)*	
Agreed/Not agreed	Agreed/Not agreed
ii. s 9(2)(f)(iv)	
Agreed/Not agreed	Agreed/Not agreed
iii. veterinary services bodies *(officials' priority)*	
Agreed/Not agreed	Agreed/Not agreed
iv. herd improvement bodies	
Agreed/Not agreed	Agreed/Not agreed
v. bodies promoting scientific or industrial research.	
Agreed/Not agreed	Agreed/Not agreed
s 9(2)(f)(iv)	
Agreed/Not agreed	Agreed/Not agreed
s 9(2)(f)(iv)	
Agreed/Not agreed	Agreed/Not agreed

General recommendations

We recommend that you:

52. **Indicate** if you wish to discuss these reports with officials. If you do wish to discuss these reports, we recommend that you include the Minister for the Community and Voluntary Sector, the Hon Louise Upston, in those discussions.

Discuss/Do not discuss	Discuss/Do not discuss

53. **Refer** a copy of:

- both this report and the Supplementary Report to the Minister for the Community and Voluntary Sector
- both this report and Appendix 3 of the Supplementary Report (subscriptions and member transactions) to the Minister of Agriculture, Minister for Biosecurity and Food Safety, Minister for Rural Communities, Minister for Oceans and Fisheries (as requested by the Ministry for Primary Industries) and Minister of Commerce and Consumer Affairs (as requested by the Ministry of Business, Innovation and Employment)
- both this report and Appendix 4 of the Supplementary Report (proposed simplifications for donors and volunteers) to the Minister for Arts, Culture and Heritage
- both this report and Appendix 5 of the Supplementary Report (income tax exemptions that may no longer be fit for purpose) to the Minister of Agriculture, the Minister for Biosecurity and Food Safety, and the Minister for Rural Communities.

Referred/Not referred	Referred/Not referred

(a) **Agree** to officials consulting on the proposals made in this report, specifically:

- Donor-controlled charities, if you agree to recommendation (a) of the donor-controlled charities section.

Agreed/Not agreed	Agreed/Not agreed

- The donation tax concession, if you agree to recommendation (b) of the donor-controlled charities section (note that you have not agreed to consult on this proposal in the past).

Agreed/Not agreed	Agreed/Not agreed

- Simplification proposals for subscriptions and member transactions, if you agree to recommendations (a) to (c) of the subscriptions and member transactions section.

Agreed/Not agreed	Agreed/Not agreed

- Simplification proposals for donors, if you agree to recommendation (a) of the donors and volunteers section.

Agreed/Not agreed	Agreed/Not agreed

- s 9(2)(f)(iv)

Agreed/Not agreed

Agreed/Not agreed

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **Taxation and the not-for-profit sector: Supplementary report**

Date:	28 August 2025	**Priority:**	High
Security level:	Sensitive - Budget	**Report number:**	IR2025/258

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Stewart Donaldson	Principal Policy Advisor	s 9(2)(a)	☒
Philip Marshall	Senior Policy Advisor		☐
Geoff Leggett	Principal Policy Advisor		☐

28 August 2025

Minister of Finance
Minister of Revenue

Taxation and the not-for-profit sector: Supplementary report

1. In April 2025 we reported to you on the high-level themes from submissions received on our February 2025 issues paper, "Taxation and the not-for-profit sector" (the issues paper). We indicated that more detailed analysis of submissions on each of the topics covered in the issues paper would follow.

2. The appendices in this report contain that detailed analysis, which supplements the report "Taxation and the not-for-profit sector: Recommendations from officials" (IR2025/257).

3. There are six appendices:

    - Appendix 1: Charity business income tax exemption (pages 2–12)
    - Appendix 2: Donor-controlled charities and the donation tax credit (pages 13–23)
    - Appendix 3: Subscriptions and member transactions (pages 24–31)
    - Appendix 4: Proposed simplifications for donors and volunteers (pages 32–37)
    - Appendix 5: Income tax exemptions that may no longer be fit for purpose (pages 38–46)
    - Appendix 6: s 9(2)(f)(iv) (pages 47–52).

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
Inland Revenue

Appendix 1: Charity business income tax exemption

1. Appendix 1 details the tax policy concerns relating to charity business income.

2. Ministers earlier agreed that officials would report on submissions in response to the February 2025 officials' issues paper, "Taxation and the not-for-profit sector" (the issues paper) and Ministers would then decide what, if any, work should proceed.

3. The issues paper asked whether there was a compelling reason for taxing charity business income. The majority of submissions focused on this complex issue. Overall, submitters were concerned about the compliance costs and workability of any new requirements and the impact these would have on a charity's ability to provide services. Submitters also considered there should be more clarity on the problem needing to be addressed. Whether any changes would extend to Māori charitable entities (for example, post settlement governance entities) was also identified as needing consideration. Submitters also wanted to know more detail about how any taxation might work.

4. The issue of competitive advantage was contentious because of the Inland Revenue view expressed in the issues paper that there was little competitive pricing advantage arising from the income tax exemption. Submissions from tax/legal experts cited various reviews that had come to the same conclusion as the issues paper. Some submissions challenged our analysis, citing what they considered to be competitive advantages in specific sectors in which they are involved where charitable entities are major market participants.

5. Our conclusions following submissions are:

    - We still consider any competitive advantage distortions from the income tax exemption are much more minor than usually assumed and are not, in themselves, grounds for removing the income tax exemption.

    - To limit the compliance costs and complexity of any tax change, there is a need to focus change on the likely problem areas.

    - Accumulation is a potential issue because of the delay between the tax exemption and funds being spent on charitable purposes. We see scope for improving transparency in this area, to enhance integrity in the system.

    - There seems to be no standard tax policy grounds to exempt Māori charities from any policy changes but consultation with Māori on the detail is vital. There may be broader policy grounds for considering an exemption.

6. We recommend addressing accumulation concerns through a combination of:

    - Inland Revenue working with the Department of Internal Affairs (DIA) to determine if reporting requirements could be improved to gather better information about accumulated funds. Although charities are required to apply their funds to charitable purposes and provide information and explanation to Charities Services on accumulation, explanations are often vague. Longer term, increasing confidence in the sector could require enhancing the involvement of Charities Services.

    - The minimum distribution rule that we are recommending for donor-controlled charities (see Appendix 2). If you agree to that recommendation in relation to donor-controlled charities, we consider it preferable to see what impact that targeted initiative also has on accumulation behaviour before considering whether to apply more general income tax requirements, and therefore increased compliance costs, across the charitable sector.

7. This option (Option 1) is preferred by Inland Revenue, the Treasury and DIA. Even if the minimum distribution rule for donor-controlled charities does not proceed, we recommend progressing the work with DIA.

8. Alternatively, if Ministers wish work to proceed on a set of specific tax rules that, as a condition of an income tax exemption, require charities to ensure they are adequately distributing their surplus funds to charitable purposes, we suggest consulting publicly on the following options:

    8.1 Option 2: Tax the accumulated net income (that is, income less expenses and less distributions made for charitable purposes) of a charity business when it is unrelated to the charity's charitable purposes, subject to an expenditure de minimis. This option, which was suggested in the issues paper, would align with practice in many countries but would be complex to apply given the need to distinguish what is unrelated income. It would also be relatively untargeted because it would apply to any charity business above the threshold that had not fully distributed its surplus.

    8.2 Option 3: Introduce a minimum distribution rule for charity businesses, when the business activities are unrelated to charitable purposes, subject to a de minimis. Net income would be taxed only to the extent that distributions to charitable purposes fall below a minimum percentage threshold. The percentage could, for example, be based on the trustee tax rate of 39% to set an expectation that if tax is not paid to the Government, at least the same amount would be distributed to charitable purposes. This option, which was suggested by some submitters, would be more targeted than Option 2. It would also not affect as many charities as Option 2 because it is anticipated that the minimum percentage threshold for distributions would be met by many charities. However, it would still involve distinguishing between what is related and unrelated income.

9. We envisage that only around 200 of the 29,000 registered charities would be subject to these tax requirements, assuming a de minimis threshold of $5 million income or expenditure. As a result, the fiscal gain from taxing unrelated business income is estimated to be in a range of $30 million to $70 million per annum (midpoint of $50 million), based on Option 2. This estimate has a high level of uncertainty.

10. Ideally, any distribution requirement should be applied at the charity level where it would be more evident whether the funds are being used for charitable purposes. However, there are practical difficulties with this. Applying the requirement at the unrelated business level is, therefore, a compromise. The risk is then that the distribution from the business simply goes into a bank account at the charity level, but at least that may be more transparent than the status quo. Another risk is that focusing on the business income tax exemption could potentially create significant distortions if passive income remains untaxed.

11. If Ministers wish to explore Options 2 and 3 in more detail, we recommend public consultation occurs on those options.

12. s 9(2)(h)

Background

13. Charities are exempted from income tax, in relation to charitable purposes carried out in New Zealand, on the basis that they provide services that might otherwise be provided by the Government. Submitters noted that charities contribute significantly to the economy by reducing demand on government services such as social welfare, mental health, and youth development programmes. Taxing their income could, therefore, have unintended social costs through a reduction in the services they are able to provide, putting pressure on the Government to increase its own services.

14. Currently, under the destination of funds approach, the focus is on whether the funds are used for charitable purposes rather than what income sources they come from.

Problem definition

15. Submitters sought greater clarity from us on the underlying problem that needed to be resolved.

16. The issues paper had noted that government support through the exemption is largely uncapped. The Government would ordinarily have some control over the amount and mix of expenditure if it were itself providing the services. We are also aware of some businesses that are intending to restructure as charities, which would further reduce the corporate tax base.

17. There is a concern that some entities may be exploiting the exemption by nominally adopting a charitable purpose. Society as a whole is better off by ensuring that such entities are not exploiting the exemption. These aspects also have wider implications for the charities regulator.

18. Public commentary has also raised concerns about the exemption providing perceived competitive advantages to charity businesses that are competing with taxed businesses. This aspect is discussed in the following section.

19. However, notwithstanding the above issues, as previously reported to you, in our view the main problem in terms of system integrity is a broader issue of profit accumulation by a range of charitable entities including, but not limited to, charity businesses. In the tax context, accumulation creates a timing mismatch between the tax exemption and funding being spent on charitable purposes. In some instances, the mismatch can exist for decades (IR2024/199; T2024/2396 paragraphs 23 to 35 refer). Potential responses to this accumulation issue are discussed in subsequent sections.

Submitters' views on issues paper and officials' responses

20. This section summarises key submission areas and our responses. Submissions on charity business income were particularly focused on unrelated business income, that is, income that is earned from a business not directly related to a charity's charitable purpose, for example, an engineering business operated by a charity. As indicated in our report (IR2025/146) there was little support for removing the exemption although that may be expected given the majority of submissions were from charities or persons linked to charities. There was also some discussion on competitive advantage. Overall, the submissions have not led us to change our earlier advice on competitive advantage.

Competitive advantage

21. The issues paper noted that because the tax-exempt entity can generally earn tax-free returns from all forms of investment, the "after tax" return it expects from a trading activity is correspondingly higher than that of its taxed competitors.

Therefore, an income tax-exempt entity cannot rationally afford to lower its profit margins on a trading activity because alternative forms of investment would then become relatively more attractive. This means that the tax exemption simply translates to higher profits and higher potential distributions to charitable purposes.

22. While charities might sustain lower prices temporarily and make losses, taxable businesses can deduct losses against current or future taxable income. This idealised symmetry for the taxable business (profits are reduced by the tax system but so are losses) gives a taxable business the same incentive (if any) to carry out this strategy. However, there are some restrictions on the use of losses which might mute this incentive for a taxable business. For example, taxable businesses cannot immediately cash out losses when they are incurred.

23. The issues paper also noted more minor distortions and competitive advantages that could have an impact, such as:

    - charities not facing the income tax compliance costs faced by other businesses, and
    - given the difficulties and significant costs that can arise when charities endeavour to raise external capital, retained earnings are the most cost-effective form of financing for charities. Because the retained earnings of charities are higher, they may have lower costs in raising capital.

Submissions summary

24. Competitive advantage was a contentious point in submissions. The tax/legal experts cited various reviews that had come to the same conclusion as our issues paper that there should generally not be a competitive advantage as a result of the income tax exemption.

25. The few submitters that commented on the minor distortions agreed that such factors were relatively minor. More submitters noted what they considered to be disadvantages, such as more rigorous reporting requirements on charities. Others noted that dividends received by charities were subject to imputation and because the imputation credits were not refundable, charities were paying some tax.

26. Some submissions challenged our analysis by citing what they considered to be competitive advantages in specific sectors (industrial pump equipment, kiwifruit, construction) where charitable entities are major market participants. A healthcare products supplier made the point that a charity business with a single mission focus cannot realistically switch investments and may accept lower returns to fulfil their charitable purpose.

Officials' comment

27. Market dominance concerns do not, in and of themselves, justify removing the business income exemption. The underlying logic remains sound and is supported by extensive international analysis.[1] There are clearly genuine concerns in some concentrated sectors. From the examples provided, while the tax settings are one explanation for the success of those charitable businesses, another is that they have successful business strategies unrelated to the tax settings. The healthcare provider raises a new point, but it would still apply even if the businesses were taxed. A mission-focused trustee would presumably also over-invest in the particular mission even after tax, if they had a surplus to invest, to earn more income.

[1] For example, Australia's future tax system review (the Henry Tax Review), published in 2010, found that tax exempt entities are not incentivised to undercut the prices of their for-profit counterparts and thus the income tax concessions do not violate the principle of competitive neutrality and should be retained.

Accumulations

28. Various submitters suggested a need to require some charities to distribute more regularly. This led some to support taxing business income with an exemption for distributions to charitable purposes, while others were concerned that this would create significant compliance costs that would be disproportionately borne by smaller charities for little overall benefit, or even for a net social cost. There was greater support for a more focused approach, such as applying restrictions on donor-controlled charities/entities and several submissions provided examples of entities that they considered were not adequately distributing to charitable causes.

29. As noted earlier, faster relative growth, through tax-free returns that enable a charitable business to become more dominant in a market, does not of itself justify changing current tax settings.

30. We also accept that there can be valid reasons why charities and their businesses distribute funds only sporadically; for example, to assist recovery from a major national disaster. A charity may also have an inter-generational focus. However, there is an expectation that, as part of receiving an income tax exemption, charities should be endeavouring to distribute towards their charitable purposes.

31. DIA considered the issue of charities accumulating funds as part of its review of the Charities Act 2005 in 2021. In that review, DIA identified that accumulation of funds by charities can undermine public trust and confidence in the charitable sector. The review also identified that in some cases "fundraising charities" distribute very limited funds to their charitable purpose each year and it is often unclear how or when fundraising charities plan to distribute their funds to benefit the charitable purpose.

32. To increase transparency around the distribution of funds by charities, in 2024 DIA introduced requirements for large charities to report the reasons for accumulating funds in their annual return. This change was intended to provide the public with more accessible, easy to understand information on why funds have been accumulated, and to provide DIA, Charities Services and Inland Revenue with data that could be used to inform compliance activities. Some observations from this process are:

    - So far, the data indicates that large tier charities accumulate for the purpose of reinvestment to ensure the entity's purpose can be fulfilled in perpetuity (eg, universities, large foundations). Small charities seem to accumulate funds for contingency purposes and specific projects (eg, capital work).

    - In many cases, the information that charities are providing to Charities Services about accumulation is not meaningfully descriptive enough to provide an accurate and transparent picture of accumulation across the charitable sector. For example, a charity might simply note that the purpose of its accumulation is "to fund our charitable activities in the future" without further detail on when and how the accumulation might be used to benefit the charitable purpose.

    - Charities Services notes that it is not clear whether the accumulation question in its current state captures data about risks it cares about as a regulator, namely issues of appropriation of funds for private benefit and/or funds not being used for charitable purposes.

33. An option would be to consider whether improvements could be made to the reporting requirements on accumulations. This could be consulted on as part of Inland Revenue's broader consultation with the charitable and NFP sector. This option, along with options that involve taxing some level of business income that has not been distributed are discussed later in this appendix. We are also recommending a minimum distribution requirement, based on net assets, for donor-controlled charities. s 9(2)(g)(i)

Compliance costs and complexity

34. This theme was widespread across submissions. Submitters were particularly concerned about what would be defined as unrelated income and the likelihood of a period of prolonged uncertainty as charities came to grips with any new tax rules.

35. Compliance cost concerns were raised when Australia suggested a similar limitation on its income exemption for charity business income in 2011. That suggestion went through a period of design refinement and did not proceed following a change of Government. One factor for its failure to proceed was the likelihood that the ultimate outcome would not, once distributions and franking credit refunds were taken into account, be much different but charities would incur material compliance costs.

36. We note the limitations in Canada and the United Kingdom have been in place for decades and appear to be generally well understood. Guidance by Inland Revenue would be crucial if rules taxing charity business income were put in place in New Zealand, but there would clearly be upfront compliance costs. A de minimis exemption would remove this issue for smaller charities.

Raising revenue as an objective

37. Many submitters were of the view that the source of revenue should not matter, rather it was the application of that revenue to charitable purposes that was crucial.

38. Raising revenue is not a focus of this review of the exemption. Nevertheless, we note there is a fiscal opportunity cost associated with the exemption. The forgone tax from the non-taxation of charities' income (except for imputed dividends[2]), puts more pressure on those paying tax to make up the revenue difference. This implies a need to ensure that the entity is genuinely supporting a charitable purpose.

Māori charitable entities

39. Iwi have a wide variety of charitable entities, many of which were established as part of their Treaty settlements or as Māori Trust Boards. Most of the charities have become involved in businesses, some of which are substantial, particularly in the fisheries, forestry, farming and tourism sectors. Those businesses seek to operate on a sustainable basis and to provide long-term funding to support the charitable activities and inter-generational focus of iwi. Various iwi sought an exemption for their charity businesses from any new requirement based on their unique nature and, in the case of post-settlement governance entities, stated that they believed being income tax exempt was part of their Treaty settlement arrangements.

40. It is difficult to find grounds for an exemption from a tax policy perspective.

41. s 9(2)(h)

42. We are, however, mindful of the impact of any changes upon Māori and we will be including Māori entities in our consultation on any detailed options. Some Māori entities would be affected more than others because some make annual distributions while others fully retain surpluses to grow their asset base. If Option 3 is further explored, a lower distribution rate for Māori businesses could be discussed.[3]

[2] Many dividends received by charities from public companies have imputation credits attached, which means that they are already taxed to some degree.
[3] Māori authorities, for example, are taxed at 17.5% to reflect the likely tax rate of the ultimate beneficiaries.

43. s 9(2)(h) [redacted]

44. Following consultation, a decision on whether an exemption is appropriate could be made as part of Ministers' final decisions.

Decision on next steps

Option 1: Minimum distribution requirement on donor-controlled charities and Inland Revenue working with DIA on reporting requirements

45. This option would focus on bolstering the current income tax exemption for charity businesses with both the minimum distribution rule recommended for donor-controlled charities and by Inland Revenue working with DIA to determine if reporting requirements on accumulated funds could be improved.

46. This option has the key advantage of targeting the group most likely to be of concern and limiting the impact on the ability of most charities to carry out their existing functions. While we have noted potential concerns about accumulations, there is no evidence that accumulation issues are widespread enough to warrant an across-the-board change. This is consistent with our advice in previous reports about the uncertain benefits from a tax change relative to the compliance costs and complexity associated with applying it across a range of charities, even after allowing for a de minimis.

47. Further, changing the policy setting for taxing charity business income would have a negative impact on the coherence of the tax system because non-business income such as passive investment income would still be exempt.

48. DIA supports Option 1 because it considers this option best supports the charitable sector to deliver services for New Zealand and because it also encourages confidence and transparency in the sector.

49. Even if the minimum distribution rule for donor-controlled charities does not proceed, we would recommend proceeding with the work with DIA.

Options for taxing business income

50. If Ministers wish the work on wider charity business tax rules to proceed to the detailed design stage, we suggest including the following options for public consultation.

Option 2: Tax the accumulated net income of a charity business when it is unrelated to the charity's charitable purposes, subject to a de minimis

51. This option was suggested in the issues paper. Its advantages are that it would encourage the distribution of surpluses and is an approach applied by many overseas countries. Based on overseas experience, it has led to the placement of businesses in entities separate from the charity to simplify its application, and over time charities have come to understand the distinctions and apply them successfully when the revenue authorities provide adequate guidance.

52. The disadvantage of this option is that it would be complex to apply, particularly initially, given the need to distinguish business income from non-business income

and to distinguish unrelated business income from other income (and to apportion expenses and distributions accordingly).

Option 3: Introduce a minimum distribution rule for charity businesses when business activities are unrelated to charitable purposes, subject to a de minimis

53. This option, which was suggested by some submitters, would introduce a minimum distribution rule for charity businesses when the business activities are unrelated to charitable purposes, subject to a de minimis. Income would be taxed only to the extent that distributions to charitable purposes fall below a minimum percentage threshold. The percentage could, for example, be based on the trust tax rate (39%) to set an expectation that if tax is not paid to the Government, at least the same amount should be distributed for charitable purposes.

54. The advantages of this option are that it would discourage ongoing accumulation, it would not impact on as many charities as Option 2 because it is anticipated that the threshold would be met by many charities, and it has the appeal that the distribution requirement is in effect equivalent to their being taxed. On balance it would be our preferred second option.

55. A disadvantage of this option is that like Option 2 it would be complex to apply given the need to distinguish what is business income and what is unrelated income. There is also little overseas experience to follow.

56. A minimum distribution rule is likely to be problematic for many Māori entities because of their focus on growing assets through accumulation for inter-generational purposes.

57. Applying the distribution requirement at the unrelated business level would be second best to applying it at the charity level where it would be more evident whether the funds are being used for charitable purposes. However, there are difficulties in measuring distributions for businesses that are also charities, such as a zoo or charity hospital, where much of the annual surplus is, by necessity, channelled back into the funding of buildings and equipment. The risk with applying the requirement at the business level is that the distribution from the business simply goes into a bank account at the charity level rather than being distributed to charity beneficiaries.

Other options considered

58. We also considered and dismissed:

- Taxing all business net income, subject to a de minimis and deductions for distributions to charitable purposes. This option would generally be less complex to apply given there would be no need to distinguish what is unrelated income. The disadvantages of this option are that it would likely still distort charity investment decisions given other income would still be untaxed, it would apply to more charities than Options 2 or 3, and there is little international precedent because few countries go beyond targeting unrelated business income.

- Taxing all charity income that was not distributed. In principle, that approach would be less distortionary than taxing just one source of charity income. Only a few countries adopt this approach.

Number of charities affected

59. There are around 29,000 registered tax charities. Assuming a de minimis of $5 million income or expenditure, Options 2 and 3 would likely affect around 200 charities,

whereas taxing either all business income or all income would likely affect 1,300. We are continuing to analyse data to confirm these numbers.

Example comparing Options 2 and 3

60. The following examples show the difference in outcome between Options 2 and 3.

Minimum distribution rate set at 39%, to align with the trust tax rate. ***Example 1***: The unrelated business generates a surplus of $100, of which 50% is distributed: • Under Option 2, the remaining 50% (ie, $50) would be taxable income. Applying a tax rate of 39% to that income, the tax payable would then be $20. • Under Option 3, none of the surplus would be taxable because the minimum distribution rate has been exceeded. ***Example 2***: The unrelated business generates a surplus of $100, of which 30% is distributed: • Under Option 2, the remaining 70% (ie, $70) would be taxable income. Applying a tax rate of 39% to that income, the tax payable would then be $27. • Under Option 3, because the actual distribution rate (30%) is less than the minimum distribution rate (39%), the difference is tax payable, that is, 9% ($9) would be the tax.

Detailed design issues

61. If work on either Option 2 or 3 were to continue towards potential legislative amendments, Appendix 2A lists the key policy design issues to be worked through and consulted on to shape draft legislation.

Financial implications

62. The options are still being explored so attributing any revenue implications would be premature. As noted in our report of 4 April 2025 (IR2025/146), Option 2 was estimated to raise revenue in a range of $30 million to $70 million per annum (with a midpoint of $50 million). That estimate was subject to a range of assumptions and disclaimers and would require updating if further detailed work is undertaken on any of the options.

Administrative implications

63. There would be additional administrative costs for Inland Revenue if you agree to tax unrelated business income. This would arise from providing information and interacting with charities on the new requirements. The additional costs would be incurred particularly over the first few years of operation. More details on those additional costs can be provided as part of our final recommendations.

Consultation

64. We have undertaken wide consultation both through the issues paper and a significant number of meetings with key stakeholder groups, including several overseas jurisdictions and New Zealand government departments such as DIA and

the Treasury, since February 2025. The views of those consulted are summarised in this appendix.

Next steps

65. If you prefer work to progress to detailed design, public consultation could occur on the options. We would recommend that any consultation be public given the earlier criticism that submitters needed to know more detail before they could meaningfully comment, and to meet consultation obligations under the Treaty of Waitangi.

Appendix 1A: International comparisons of charity income

Australia	Fully exempt from paying income tax on both commercial and non-commercial income. If dividends are received from a trading business that has paid tax in Australia, the parent charity can claim a franking credit refund, effectively reducing the net tax liability to nil. Competitive advantage is not an issue.
Canada	Not permitted to undertake commercial activities unless they are related to the charitable purpose the entity is undertaking or if the entity is run almost entirely with volunteer labour. Regime introduced in 1976, partly because of concerns about taking focus away from charitable activities and competitive advantage arguments.
Germany	Related income exempt, unrelated income taxed above €35,000.
Switzerland	Exempt from income and wealth taxes. Commercial activities are allowed if they support the non-profit purpose and do not dominate the organisation's operations.
United Kingdom	Trading activity is taxable unless they support a charity's purposes. However, small-scale trading activity unrelated to a charitable purpose remains tax exempt when trading income is less than 25% of total income, subject to an overall upper limit of £80,000. Regime has been in place for many years. Trading activity seen as riskier than investment activity, and concerns about competitive advantage.
United States	The US has an unrelated business income tax, which means if a charity's business activities are not substantially related to furthering the charitable purpose, the income from such activities will be taxable. The unrelated business income tax was introduced in 1950 in response to claims of unfair competition.

Carve-outs include certain fundraising activities (US, UK), most forms of passive investment income (US, UK, Canada), businesses that are run entirely by volunteers (US, Canada) or beneficiaries (UK), businesses that sell donated goods (US), and "ancillary" trading, which compliments a charitable purpose (UK).

Appendix 1B: Key detailed design issues to consider for Options 2 and 3

- What would qualify as "unrelated income", including whether interest, dividends, royalties and rental income would be included.
- The level and base used for the de minimis and number of charities that would be covered.
- Distributional issues:
    - what qualifies as a distribution for charitable purposes
    - whether distributions would be calculated on a simple annual basis or over a longer period to enable short-term accumulation, and
    - the merits of an anti-avoidance rule to deter distributions being recycled back into the business.

- Allocation of distributions and expenses when charity business is not separate from the charity.
- Treatment of income and distributions from entities that are look-through for tax purposes (a partnership, limited partnership, and a look-through company).
- Interaction with the income tax applicable on deregistration of a charity.

Appendix 2: Donor-controlled charities and the donation tax credit

1. Appendix 2 details the tax policy concerns relating to donor-controlled charities and how these could be addressed, including by reducing the donation tax credit (DTC) ceiling.

2. The term "donor-controlled charity" refers to a registered charitable organisation in which the donor (or their associates) retain control over how charitable funds are spent. This control poses a heightened risk of donor-controlled charities engaging in aggressive tax planning, such as engaging in circular or non-arm's length transactions that yield private benefits for the donor or their associates. It can also lead to a delay between the time of tax concessions for the donor and the charity, and the distribution of funds for charitable purposes.

3. The February 2025 officials' issues paper, "Taxation and the not-for-profit sector" (the issues paper), consulted on whether the policy concerns outlined above warrant a policy response, including explicit tax rules relating to how donor-controlled charities invest their funds and when they should distribute their funds.

4. Submitters generally agreed that tax planning strategies should be addressed. However, some submitters were of the view that the proposals were unnecessary for various reasons outlined in this appendix.

5. We remain of the view that the tax policy concerns relating to donor-controlled charities should be addressed through reform of the tax rules.

6. Any policy changes to reduce the value of donation tax concessions for donors would impact on the proposed work above. For example, a reduction in the donation tax credit (DTC) ceiling would reduce the financial benefit of circular arrangements in donor-controlled charities. It would also mitigate concerns around donors receiving tax concessions and then accumulating funds while making minimal distributions to charitable purposes going forward, because fewer tax concessions would be provided.

7. We have previously reported on options to reduce donation tax concessions. We recommend that you agree to reconsider donation tax concessions (such as the DTC) to address integrity concerns alongside progressing donor-controlled charity rules. Reducing the DTC ceiling would reduce the need for donor-controlled charity rules, so we recommend that final policy decisions on the DTC ceiling or rate be considered at the same time as the proposed work above.

8. There are other related tax issues that could be addressed as part of the proposed donor-controlled charities work. These issues relate to integrity concerns with donor-advised funds and trustees allocating beneficiary income to charities without actually paying it. These issues are often a feature of donor-controlled charities but they do affect other charities. If the proposed work on donor-controlled charities does not go ahead, we still recommend advancing work on these two issues.

9. The Department of Internal Affairs (DIA) has been consulted, and its view is set out in paragraphs 55–57. DIA prefers a more targeted approach to addressing donor-controlled charities. It has concerns with a broader option like lowering the DTC ceiling for reasons outlined in our previous advice.[4] DIA also has a strong preference for public consultation on any changes to donation tax concessions.

10. If you wish to progress work on the donor-controlled charity rules and other related issues, we recommend public consultation on the detailed policy design. This is because the proposals are complex, and submitters have highlighted the potential

[4] (IR2024/482; T2024/3292, dated 11 December 2024, IR2025/079; T2025/635, dated 13 March 2025 refers).

for unintended consequences. Following consultation, we would report to you with final policy recommendations.

11. If you agree to reconsider the policy settings for tax benefits for donations, we recommend that this be subject to public consultation. However, we recognise the decision whether or not to publicly consult is finely balanced and you have made the decision not to publicly consult on this in the past.[5] We could report to you later in the year on policy options, and then final policy decisions could be made alongside donor-controlled charity rules.

Background

12. In September 2024, we reported to you on tax policy options to address accumulation and integrity concerns in donor-controlled charities (IR2024/360 refers). This work culminated in Cabinet agreeing to Inland Revenue releasing an officials' issues paper on 24 February 2025 for public consultation. One chapter of the issues paper sought feedback on whether New Zealand should introduce targeted rules for donor-controlled charities.

13. The term "donor-controlled charity", although not currently defined in legislation, refers to a charity registered under the Charities Act 2005 that is controlled by the donor, the donor's family, or their associates. Donor-controlled charities can access the same tax concessions as other publicly supported registered charities. They are exempt from income tax, have donee status so their donors can claim DTCs or gift deductions, and are exempt from fringe benefit tax in some circumstances.

14. The tax policy framework provides targeted tax concessions to charities that are registered under the Charities Act 2005. This framework relies on tax-exempt charities being appropriately regulated and publicly accountable. The objectives of this review are to improve revenue integrity and minimise opportunities for tax avoidance.

Problem definition

15. Two key issues with the current tax rules as they apply to donor-controlled charities are discussed below.

Aggressive tax planning

16. Donor-controlled charities pose a heightened risk of aggressive tax planning and tax compliance concerns because of the control the donor and/or their associates has over when and how charitable funds are spent.

17. Some examples Inland Revenue is aware of include:

    17.1 **Circular arrangements:** The donor donates money to a charity they control, claims a DTC or gift deduction, and the charity immediately loans the money back to the donor or invests it into businesses controlled by the donor or their associates. While the loan or investment may pay a market rate of return, typically it is accrued and no cash is actually paid to the charity for many years.

    17.2 **Non-arm's length transactions:** The donor-controlled charity purchases assets or regularly acquires goods or services from the donor or their associates at above-market rates.

[5] IR2024/359; T2024/2572, dated 20 September 2024 refers

18. Such arrangements can result in significant private benefits for the donor or their associates, particularly when a DTC has been claimed. While the instances of these arrangements are low, the amounts involved are often significant. It is important for the overall integrity and fairness of the tax system that such arrangements are effectively countered.

19. Inland Revenue is better placed than the charities regulator to address these integrity concerns from a compliance perspective. Inland Revenue has visibility over all entities involved in circular arrangements and can monitor donation tax concessions claimed by donors, whereas the charities regulator only has access to the financial information of the charity itself and has no oversight over donation tax concessions. Inland Revenue also has greater information gathering powers than the charities regulator.

20. We consider that effective tools to address these integrity concerns should be developed. This is because the anti-avoidance provisions are difficult to apply to these arrangements in practice, and it is resource intensive to attempt to do so. Specific rules may also deter donor-controlled charities from entering into tax avoidance arrangements.

Accumulation

21. The accumulation of tax-exempt funds by donor-controlled charities can raise concerns.

22. Currently, all registered charities can accumulate tax-exempt surpluses and grow their net assets over time. Donors can also claim DTCs on qualifying donations or a gift deduction at the end of the tax year in which the donation is made. One of the primary concerns with unrestricted accumulation is the delay between the time of tax concessions for the donor and the charity, and the funds being distributed to their charitable purpose. In some cases, it takes many years before the value of charitable distributions exceeds the value of the DTC claimed by the donor.

23. The tax policy concern with unrestricted accumulation is heightened for donor-controlled charities because without an independent board, the donor who provides the funds and benefits from tax concessions retains control over when and how charitable funds are spent. The donor-controlled charity may have no immediate desire to distribute charitable funds and could instead accumulate so the charity can be self-sustaining in the future, or to retain funds for use in rollover loan-back arrangements.

24. There can be valid reasons for charities to accumulate funds (for example, to save for the acquisition or construction of capital assets). However, there is an expectation that, as part of receiving an income tax exemption, charities should be endeavouring to distribute towards their charitable purposes.

25. DIA considered the issue of charities accumulating funds as part of its review of the Charities Act in 2021. In that review DIA identified that in some cases "fundraising charities" (which includes many donor-controlled charities) distribute very limited funds to their charitable purpose each year and it is often unclear how or when fundraising charities plan to distribute their funds to benefit the charitable purpose. The charity business income tax material has more information about DIA's review of the Charities Act and whether reporting requirements could be improved (see Appendix 1).

Submitters' views on issues paper and officials' responses

26. The issues paper asked whether the integrity and accumulation concerns associated with donor-controlled charities warrant a policy response, including:

26.1 requiring transactions between donor-controlled charities and their associates to be on arm's length terms or prohibited outright, to reduce integrity issues with aggressive tax planning

26.2 requiring donor-controlled charities to distribute at least a minimum of their funds towards their charitable purpose over a certain period (a minimum distribution rule), to mitigate unrestricted accumulation.

27. This received both support and opposition from submitters. However, we note that the donor-controlled charities proposals are complex, and there was general uncertainty over who would be affected.

28. Submitters generally agreed that circular or non-arm's length transactions should be addressed. Typical observations and concerns raised by submitters are covered in the following table.

Theme	**Submitters' suggestions and concerns**	**Officials' comment**
Follow international precedent	Any new rules should align with established guidelines in other jurisdictions.	We agree.
Specific rules are not warranted	The legislative framework for registered charities is robust enough to deal with integrity issues officials have observed, and these rules should be better enforced. Some submitters have not observed circular, non-arm's length arrangements and felt they could not support specific rules without further analysis of the scale of the problem.	We do not agree that the existing rules are enough to deal with integrity issues. The anti-avoidance rules are difficult to apply and resource intensive. It is important for the integrity of the tax system that these arrangements are effectively countered.
Charities regulator is better placed	Those opposed to the proposals took the view that the charities regulator is better placed to deal with the misuse of charities than to fix those issues by changing tax settings.	As mentioned in paragraph 19, we consider that Inland Revenue is better placed than the charities regulator to monitor and regulate aggressive tax planning arrangements.

There are legitimate reasons to accumulate	There are legitimate reasons for long-term accumulation, such as building a corpus for greater distributions in the future or for intergenerational purposes. They noted that Charities Services recently introduced additional disclosure requirements on the reasons that charities are accumulating funds.	Some concerns raised by submitters can be mitigated by policy design. For example, a minimum distribution rule could be set at a level that would, on average, allow for some capital accumulation. Exceptions to a minimum distribution rule could also be permitted to allow for long-term accumulation when the accumulation meets certain criteria. Also, as noted in the business income material (Appendix 1), there are limitations to the information that charities are providing as part of the new disclosure requirements.
Additional rules would be complex and discourage philanthropy	Additional rules would pose unnecessary compliance costs on charities and discourage private philanthropy from high-wealth individuals. For example, some donors would want conditions attached to a donation to their private foundation, such as requiring it to be spent on their own construction firm that they trust. It was submitted that some may not donate if these conditions were prohibited.	Any new tax rules should balance addressing integrity, fairness and coherency concerns with not distorting genuine philanthropy in New Zealand and incentivising donors to move their donor-controlled charity offshore to countries with more favourable tax rules.
Review imputation credit refundability	Many submitters, including some donor-controlled charities, called for a review of the policy settings preventing registered charities from accessing imputation credit refunds. They noted that this results in some charities effectively paying millions of dollars in tax, limiting their ability to make charitable distributions. They also noted that Australia allows for franking (imputation) credit refunds for registered charities.	You have previously ruled out including imputation credit refundability in the scope of the charities/NFPs work (IR2024/237 refers). A policy change would have a fiscal cost (based on 2020 estimates the cost could be $70 million to $100 million per annum) and would need to be carefully worked through to prevent a range of tax avoidance arrangements.

29. Overall, we remain of the view that the tax policy concerns relating to donor-controlled charities should be addressed through legislative reform to improve the integrity and fairness of the tax rules for donor-controlled charities.

Relationship with other work: Reducing expenditure on donation tax concessions

30. We have previously reported to you on a number of options that would reduce the Government's expenditure on donation tax concessions.[6] A copy of the first report to recommend change, IR2024/359; T2024/2572, is in Appendix 2B.

[6] IR2024/359; T2024/2572 (20 September 2024); IR2024/482; T2024/3292 (11 December 2024), IR2025/079; T2025/635 (13 March 2025) refer.

31. In addition to reducing expenditure, the option to lower the DTC threshold ceiling would reduce integrity concerns when fraud and tax avoidance could occur and address research into elasticity that indicates DTCs are not "treasury efficient".

32. However, reducing the DTC ceiling is also likely to result in a reduction in charitable donations because it may make donating less attractive, particularly for wealthier donors. If a change in the donation tax concession reduces charity donation income, some charities may reduce their services, resulting in an increase in demand for government support.

33. This work was not included in the scope of the February 2025 issues paper because it was considered for Budget 2025. A decision was eventually made not to progress this work for Budget 2025.

34. If the Government were to progress work on reducing the DTC threshold ceiling, it would mitigate some of the integrity concerns outlined in this appendix by reducing the financial benefit of circular arrangements (which are a common feature of tax aggressive arrangements involving donor-controlled charities). Going forward, the tax policy concern with the accumulation of tax-exempt funds would be reduced because fewer tax concessions would be provided.

Conclusions and recommendations

35. The status quo does not address integrity concerns associated with aggressive tax planning, such as circular or non-arm's length transactions. It also does not address donors and their related charities accessing tax concessions and then not providing any distributions or only very small distributions for charitable purposes. Inland Revenue anticipates that, without targeted rules to address these issues, these arrangements will continue and may increase in frequency.

36. We recommend progressing policy work to address these integrity issues. This would include:

- defining a donor-controlled charity in legislation
- introducing integrity measures to address circular or non-arm's length transactions between donor-controlled charities and associated persons, and
- requiring donor-controlled charities to make a minimum distribution over a certain period to address the delay between tax concessions and funds being distributed to support charitable purposes.

37. We consider that these reforms are necessary to strengthen the integrity and fairness of tax concessions provided to donor-controlled charities and the donor or associated persons, and to enhance public trust and confidence in the tax exemption for charities.

38. Any new tax rules should balance addressing integrity, fairness and coherency concerns with not distorting genuine philanthropy in New Zealand and incentivising donors to move their donor-controlled charity offshore to countries with more favourable tax rules.

39. The starting point for any reform should be to align with Australia's rules for private ancillary funds.[7] If New Zealand's regulations were significantly tighter, this would create a risk of donors shifting philanthropic activities to Australia, where donors may perceive the rules to be more favourable.

[7] We have reported previously on Australia's rules for private ancillary funds (IR2024/360 refers).

40. Appendix 2A outlines the high-level policy design consulted on in the issues paper. It also summarises submitters' views and our current view on key policy design options that could be considered in future consultation.

Reducing tax concessions for donations

41. We also recommend that you agree to a reconsideration of the donation tax concessions for donors (such as the DTC). This is because reducing the DTC ceiling would have a material impact on tax integrity concerns, particularly with donor-controlled charities, and may reduce the need for donor-controlled charity rules.

42. Reducing the DTC ceiling would, in principle, be simpler to implement than donor-controlled charity rules, but would be a blunt instrument. For example, there are 350,000 individual taxpayers claiming DTCs. We can provide further advice on options that reduce the number of taxpayers who could be affected by a reduction in the DTC ceiling. We also note that reducing the value of donation tax concessions does not address all the integrity concerns we have with donor-controlled charities, for example, with accumulated funds that have already benefited from the high DTC ceiling. Some integrity issues may remain after reducing the DTC ceiling, so further policy work may still be required.

43. Because there is a close connection between the DTC ceiling and donor-controlled charity rules, we recommend that you consider final policy decisions on any changes to the DTC ceiling before or at the same time as any decisions on donor-controlled charity rules.

Other integrity issues

44. This section outlines other related tax issues that should be addressed as part of the proposed donor-controlled charities work. These issues are more prevalent in donor-controlled charities, but they affect all charities and should be progressed even if you choose to stop work on donor-controlled charities.

Donor-advised funds

45. Donor-advised funds are charitable giving accounts established within a specific fundholding charity. Donors can contribute to their individual giving account, receive a donation tax concession at the end of the year of the donation, and then retain some control over how and when their funds are distributed.

46. We are concerned that these funds may be used as substitutes for donor-controlled charities. If rules such as a minimum distribution requirement or other integrity measures were imposed on donor-controlled charities, donors could instead use donor-advised funds to avoid those rules. For this reason, we consider there is a strong case for applying the same integrity measures to donor-advised funds.

47. There are also broader policy issues that need to be considered for donor-advised funds. For example, there is an existing requirement that a donee organisation must apply at least 75% of its funds to charitable, benevolent, philanthropic, or cultural purposes within New Zealand to qualify for donee status. Under current legislation, it is likely this test applies to the fundholding charity, instead of each individual giving account. Our view from a policy perspective is that this test should be applied to each giving account instead.

Trust allocations to tax-exempt entities

48. Currently, it is possible for trustees to allocate income to a beneficiary while not actually paying it to them. This poses integrity risks when the beneficiary is a charity

because the income receives a tax exemption despite not actually being paid to the charity and used for charitable purposes.

49. We recommend progressing work to explore a "pay" rule, so trustees are required to distribute income allocated to a tax-exempt beneficiary within a certain period up to the date they are required to file their tax return. If the income is not distributed within the required time, it would be taxed at the trustee rate of 39%.[8]

50. This policy would be similar to Australia's "pay or notify" rule, where trustees must either pay or notify the beneficiary of their allocation. However, we believe a "pay" rule would better address integrity concerns and would be consistent with our general rule that donations must be paid to qualify for a tax concession.

Financial implications

51. Any reform for donor-controlled charities would have the policy objective of changing behaviour to ensure donations made to donor-controlled charities are used for charitable purposes in a timely manner. The proposals outlined in this report are expected to be fiscally neutral or have only a small fiscal gain, depending on the policy design.

52. The proposed rule for trust allocations to tax-exempt beneficiaries would seek to change behaviour to ensure funds allocated to charities are actually distributed. The proposal is expected to have a small fiscal gain. Any potential changes will be costed in a later report on final policy decisions.

53. Reducing the DTC ceiling would be fiscally positive. If you agree to expand the scope of this work to include reducing the DTC ceiling, we will include the fiscal impacts of different options in future advice.

Consultation

54. DIA and the Treasury were consulted in the preparation of this appendix.

Department of Internal Affairs

55. DIA prefers a more targeted approach to addressing donor-controlled charities, such as a minimum distribution to charitable purposes for such charities. It has concerns with a broader option like lowering the DTC ceiling for reasons outlined in our previous advice.[9]

56. DIA note that reducing the DTC ceiling is likely to have a detrimental effect on the value of donations made to charities and reduce their ability to deliver services. It could also result in stakeholders questioning the Government's commitment to growing philanthropic giving, particularly if this is combined with other tax changes to concessions for businesses owned by charities.

57. DIA also notes that there has been some public consultation on donor-controlled charity rules, but not on the donation tax concession proposals. This presents certain risks, including uncertainty regarding how these changes could affect the sector and the potential for relationship challenges with key stakeholders. DIA's view is that there should be public consultation on any changes to donation tax concessions to better understand the impacts on the sector. We agree with DIA that there should be public consultation to help identify any unanticipated consequences,

[8] Unless the trustee income is below $10,000, then it would be taxed at 33%. However, this is unlikely to be the case.
[9] (IR2024/482; T2024/3292, dated 11 December 2024, IR2025/079; T2025/635, dated 13 March 2025 refers).

but we also note that public consultation may not be consistent with Ministers' priorities for Budget 2026.

Next steps

58. If you agree to progress work on donor-controlled charity rules and other integrity issues, consultation could be later this year. We would then report back to you with final policy recommendations that could then be made by Cabinet. We are recommending that consultation be public because the proposals are complex, and submitters have highlighted the potential for unintended consequences.

59. If you agree to progress policy options to reduce the DTC ceiling, then we would provide a further report on policy options later this year. If you agree to public consultation, we recommend that this occurs at the same time as consultation on donor-controlled charity rules.

Appendix 2A: Detailed policy design and submitters' comments

Definition of "donor-controlled charity"

60. The issues paper asked submitters what criteria could be used to determine if a charity is "donor-controlled" and outlined other countries' approaches.

61. Submitters raised concerns that adopting other countries' definitions could unintentionally capture certain charities, including some Māori organisations established through Treaty settlements, as well as charities controlled by another charity or organisation. We agree that Māori organisations created as a result of Treaty settlements should not be considered donor-controlled because the primary donor is the Crown, which does not retain control over how funds are used. Charities controlled by another charity should not be considered donor-controlled, unless that charity itself is donor-controlled.

62. Our current view is that a charity should be considered donor-controlled if it is directly or indirectly controlled by a person or group of associated persons who contribute more than 50% of the charity's funds or if a charity does not have an independent board of trustees.

Minimum distribution rule

63. The issues paper sought feedback on introducing a minimum distribution requirement for donor-controlled charities and outlined international approaches.

64. Typical comments made by submitters were:

    64.1 Minimum distribution would erode asset base: It was submitted that some charities would not be able to meet a minimum distribution requirement without selling assets. This would undermine their long-term sustainability and ability to provide future charitable donations.

    64.2 Minimum distribution should be a percentage of surplus: Some submitters suggested that the minimum distribution should be based on surplus income, instead of net assets, to better reflect a charity's ability to give.

    64.3 Inefficient use of charity resources: Submitters raised concerns that a minimum distribution rule could result in inefficient use of charity resources when no suitable projects are identified in a given year.

64.4 Risk that distribution rate becomes a target: Some submitters cautioned that a minimum distribution could encourage charities to distribute the minimum amount, even if they have the ability to distribute more. It could also encourage riskier investments that generate higher returns.

64.5 Minimum distribution would pose compliance costs: Submitters opposed to a minimum distribution requirement noted that it could pose significant compliance costs, for example in determining what counts as a distribution. However, submitters broadly agreed that compliance costs and unintended consequences could be reduced if a minimum distribution were averaged over a three-year period, and if exceptions were permitted in certain circumstances.

65. Our current view is that donor-controlled charities should be required to distribute a percentage of the market value of their net assets over a certain period to support their charitable purpose, subject to certain adjustments.[10] We think many of the concerns highlighted by submitters can be addressed through policy design. For example, the minimum distribution could be averaged over a three-year period to provide flexibility, and exceptions to the rule could be allowed in certain circumstances to allow for long-term accumulation.

66. We do not support the suggestion that the minimum distribution should be based on net income because this could incentivise charities to invest in non-income-generating assets to minimise their distribution obligations and would require different treatment of various income sources.

Integrity rules for related party transactions

67. The issues paper sought feedback on whether transactions between donor-controlled charities and the donor or their associates should be required to be on arm's length terms or prohibited outright to address the risk of tax abuse.

68. Typical comments made by submitters were:

68.1 Prohibiting related-party investments limits growth of charities: Some submitters pointed out that many related-party investments are on terms favourable to the charity involved and this supports the long-term financial growth of the charity. Those who supported the proposals preferred requiring investments to be on arm's length terms.

68.2 Inland Revenue should explore other measures: Some submitters suggested that Inland Revenue should put out clearer guidance over what is acceptable from a tax avoidance perspective.

68.3 Compliance costs: Concerns were raised that an arm's length rule could impose compliance costs that could divert funds from charitable purposes.

69. We agree with submitters that related-party investments should not be prohibited. However, to address integrity concerns with transactions between donor-controlled charities and the donor or associated persons, our current view is that the following policy options are worth exploring:

69.1 requiring donor-controlled charities to demonstrate that transactions with the donor or their associates are conducted on arm's length terms

69.2 requiring interest on loans to associated persons be regularly paid, rather than accrued

[10] For example, assets that are used to carry out a charitable programme, such as a church building, could be excluded.

69.3 introducing a prescribed interest rate in legislation that must be paid on loans made to associated persons

69.4 reducing the value of a DTC when funds are loaned back to an associated person or invested in a business linked to the donor after a period of time, and

69.5 restrictions on the value of "in-house assets"[11] that a donor-controlled charity can hold.

Appendix 2B: Tax policy report – Donation tax concession caps

70. The report *Donation tax concession caps,* IR2024/359; T2024/2572 (20 September 2024), is attached for reference.

[11] This may include loans to or investments in related parties of the charity.

Appendix 3: Subscriptions and member transactions

1. Appendix 3 details the tax policy concerns relating to subscriptions, member transactions and related matters.

2. To support your decision-making, this advice addresses a number of related matters affecting taxable not-for-profit (NFP) entities. The advice focuses on equity and simplification of the rules. The most significant issue is the draft change of view (the updated view) of Inland Revenue that membership subscriptions and levies are taxable income for many NFPs.

3. We have specifically considered the following issues:

   3.1 possible policy responses to Inland Revenue's updated view that membership subscriptions and levies will be taxable for many NFPs

   3.2 repealing the friendly society and credit union exemption for member transactions and investment income

   3.3 increasing and/or redesigning the current $1,000 tax-free threshold to remove small-scale NFPs from the tax system

   3.4 whether the resident withholding tax (RWT) exemption rules for NFPs should be retained or modified, and

   3.5 simplifying the income tax return filing requirements for smaller NFPs.

4. If you wish to progress work on membership subscriptions, the tax-free threshold, the RWT exemption and return filing requirements, we recommend public consultation on the detailed policy design. Following consultation, we would report back with final policy recommendations. We recommend targeted consultation on the impact of repealing the friendly society and credit union exemption.

5. The fiscal cost of legislating to confirm the current position that all membership subscriptions and levies are non-taxable is estimated to be $7 million per annum. However, this would reduce to $3 million if a targeted approach was taken. This figure is provisional and will be affected by where the line is drawn between taxable and non-taxable subscriptions. The fiscal cost of increasing the current tax-free threshold from $1,000 to $5,000 would be $60,000 per annum and a change to $10,000 would be $300,000 per annum.

Background

6. Appendix 3 provides more information to support your decision on whether work on member subscriptions, transactions and related matters should cease or continue. If it were to progress, we recommend consulting on the detail of possible changes later this year.

7. The advice in Appendix 3 is also informed by submissions received on the officials' issues paper, "Taxation and the not-for-profit sector", (the issues paper) and in response to draft operational statement "Mutual transactions of associations (including clubs and societies)".

8. We have previously reported to you on our work on member transactions, subscriptions and levies, and related matters in July 2024 (IR2024/238 refers).

9. As noted in IR2025/257, the objectives of this review are to protect and strengthen the integrity of the tax system while minimising any unintended social costs. There are 26,000 taxable NFPs that will be affected by the proposals in this appendix and our primary focus is to balance integrity and simplicity, particularly for smaller NFPs.

Membership subscriptions and levies

10. In our previous advice, we outlined Inland Revenue's updated view that confirms that membership subscriptions and levies will likely be taxable for many NFPs, a change from Inland Revenue's long-standing position that these amounts are non-taxable under the mutuality principle. The common law mutuality principle provides that an association of people does not derive taxable income from transactions within its circle of membership, based on the idea that persons cannot make a profit from trading with themselves. We recommended that you commission policy work on possible ways to mitigate some of the impacts of the updated view for small NFPs and address related policy issues. At that time, we did not recommend changing the law to make membership subscriptions and levies non-taxable because:

    - it would come at a fiscal cost
    - would not be consistent with a broad-base, low-rate tax framework, and
    - any inconsistency between the tax treatment of member trading transactions and membership subscriptions would provide an opportunity for NFPs to structure transactions with members to reduce their tax liability.

11. Inland Revenue has recently publicly consulted on the updated view set out in the draft operational statement. In addition to concluding that membership subscriptions and levies may be taxable, the draft operational statement also reiterates Inland Revenue's current position that member trading transactions (eg, food and drinks at a club) are taxable. Inland Revenue will not be finalising its updated view and the draft operational statement while these policy issues are being considered. The updated view, if confirmed, would then be applied prospectively from a date to be decided (unlikely to be before 1 April 2027).

12. Following strong opposition from submitters in relation to taxing membership subscriptions, you have asked us to consider the circumstances in which subscriptions and levies could remain non-taxable.

Draft operational statement: Submissions summary

13. Submitters strongly opposed imposing tax on membership subscriptions. Many submitters stated that if the updated view is confirmed, it would:

    - place a significant amount of financial pressure on NFPs
    - cause smaller NFPs to close on the basis that they would no longer be financially viable
    - result in NFPs increasing their membership subscriptions and/or reducing the benefits provided to members, and
    - require NFPs to restructure.

14. Most submitters said that a law change should be considered to ensure that member subscriptions remain non-taxable in recognition of the significant role NFPs provide to their communities.

15. On a related note, several submitters suggested introducing exempt entity categories for public-facing NFPs delivering advocacy and/or education services similar to overseas jurisdictions such as Australia, the United Kingdom, and the Republic of Ireland.

16. Some submitters made a distinction between those membership subscriptions that provide benefits of a non-commercial nature, which should remain non-taxable, and

those that were linked to commercial goods and services, that should continue to be taxable.

17. It was also submitted that if the updated view is confirmed, the law should be changed so that only subscriptions paid to NFPs clearly carrying on a commercial activity (which can be seen as profit-making in nature, under which valuable benefits are provided to members) would be taxable (perhaps also with a de minimis threshold).

Officials' comments and recommendations

18. We support the updated view from a policy perspective because it aligns with normal income tax principles and a broad-base, low-rate tax framework. However, it raises legitimate questions about the appropriate level of compliance costs imposed on small NFPs for little to no fiscal gain.

19. As previously reported in July 2024, we do not recommend changing the law to make membership subscriptions and levies non-taxable in all circumstances. Instead, we recommend considering the consequences of the updated view and to provide relief in appropriate circumstances, particularly for smaller NFPs.

20. If Ministers wish to maintain some or all of the current non-taxable position for membership subscriptions and levies, we recommend that consultation be undertaken later this year. This consultation could include:

- making all membership subscriptions and levies non-taxable
- placing a dollar threshold on the amount of membership subscriptions and levies that would be non-taxable, or
- apportioning membership subscriptions and levies into commercial/non-commercial categories.

21. Our preferred option at this time is the third option above, or some variant of it. This option is more consistent with the broad-base, low-rate tax framework, and with principles of equity. It also better addresses integrity issues. However, there is potential for this option to impose higher compliance costs and could be less simple to apply.

22. The Ministry of Business, Innovation and Employment reflected comments from submitters that taxing membership subscriptions may have a significant impact on incorporated societies (not otherwise covered by a tax exemption, such as registered charities). It also noted that incorporated societies are currently required to re-register, and adding additional tax burdens will add to their compliance costs.

23. The Ministry of Primary Industries raised concerns that taxing membership subscriptions and levies could negatively impact a range of primary sector NFPs that rely on these amounts to operate, for example NFPs that participate in biosecurity activities under the Government Industry Agreements.

24. The fiscal cost of legislating to confirm the current position that all membership subscriptions and levies are non-taxable is estimated to be $7 million per annum. However, this would reduce to $3 million if a targeted approach was taken. For example, apportioning membership subscriptions and levies into commercial/non-commercial categories and/or introducing a de minimis over which subscriptions would be taxable under ordinary concepts.

Member transactions

25. Some submitters said NFPs should receive a full income tax exemption, including for commercial sales transactions, as is the case, for example, for amateur sports bodies, on the basis that they also provide important benefits to the community. This approach would cover not just subscription income but also other member trading income, which has always been subject to tax.

26. We do not support providing such a wide exemption. The nature of trading transactions undertaken in the course of business or trade by NFPs strongly suggests that they be treated for tax purposes in the same way as other business activities.

Related matters

Friendly societies and credit unions

27. There are approximately 100 friendly societies, which vary in size s 6(c)

28. Friendly societies and credit unions have a specific tax exemption for their member trading transactions, passive income and member subscriptions (if any). Only their non-member trading transactions are taxable.

Submissions summary

29. The issues paper asked for comment on the implications of removing this exemption. In the context of credit unions, submitters said the implications of removing the exemptions include reduced accessibility and competition in the financial sector. Another submitter noted that the existing regulatory framework for credit unions already ensures sufficient transparency.

30. In the context of friendly societies, Southern Cross Medical Care Society submitted that removing the exemption could result in premium increases or benefit decreases, which could add to pressure on the public health system.

Officials' comments and recommendation

31. The income tax exemption has existed since the 1800s when friendly societies and credit unions operated as community-based mutual aid groups, pooling resources to offer support and small loans. In the early 1900s, before the introduction of the welfare state, these entities were widespread across New Zealand, providing essential welfare services. Since then, some of these entities have evolved into health insurance providers and regulated financial institutions.

32. While, as noted in submissions, credit unions and friendly societies still serve a clear purpose, we consider that the context in which these income tax exemptions were originally introduced has since altered. Whether the public policy objective of this exemption remains current and relevant depends on the extent to which the Government wishes to continue supporting these entities.

33. In addition, this exemption is inconsistent with the tax treatment for other taxable NFPs and if retained, would impact on the equity and coherency of the tax system.

34. We therefore recommend repealing the income tax exemption for friendly societies and credit unions. The priority is to repeal the exemption for friendly societies because they are substitutable for other mutual NFPs. If you choose to keep the income tax exemption for both entities, we recommend reducing it to only apply to member trading transactions. There is no clear rationale for providing an exemption for investment income.

35. If the exemption is repealed, the tax settings for friendly societies and credit unions would align with other taxable NPFs and may still be able to access the tax-free threshold for NFPs (currently $1,000).

36. s 9(2)(g)(i)

37.

NFP $1,000 tax-free threshold

38. Currently, NFPs with constitutions that prohibit distributions to members (for example, incorporated societies) are entitled to a tax-free threshold of $1,000 (that is, they can deduct up to $1,000 against their income). The threshold has not changed since 1979 and in our view is poorly designed.

39. To reduce compliance costs for NFPs, especially those small NFPs that may not have paid tax on member transactions in the past, the issues paper raised the question of increasing and/or redesigning the current $1,000 tax-free threshold to continue to remove small-scale NFPs from the tax system.

Submissions summary

40. There was near-universal support from those that submitted on this topic that the $1,000 tax-free threshold was too low and should be increased. Proposed options ranged from $2,000 to $100,000 with most supporting a threshold of around $10,000. Other submitters suggested linking the threshold to the tiered approach used for charity reporting.

41. Several submitters considered that the tax-free threshold applies to NFPs that cannot distribute to members and therefore the deduction does not assist with NFPs that can distribute to members. Some submitters suggested that NFPs such as amateur sports clubs should have an income tax exemption.

Officials' comments and recommendation

42. We agree with submitters' concerns. We support further work on the tax-free threshold, including who it should apply to, whether it should be available to shelter

investment income, the interaction with the other mutuality issues outlined in this appendix and how to provide clear guidance. There is no policy rationale for providing a large NFP with a tax-free threshold to offset against their income. However, there may be a rationale for providing a concession to smaller NFPs – recognising that the additional revenue collected from taxing these smaller NFPs may not offset the additional compliance costs incurred by them.

43. Increasing the tax-free threshold would be consistent with the policy principle of keeping the rules simple and compliance costs low.

44. The fiscal cost of increasing the current tax-free threshold from $1,000 to $5,000 would be $60,000 per annum and a change to $10,000 (our preferred threshold) would be $300,000 per annum.

Resident withholding tax

45. Currently, NFPs with taxable income under $1,000 are entitled to a resident withholding tax (RWT) exemption so that RWT is not deducted at source from interest and dividends paid to them. However, it does not exempt them from paying tax on that income in their final return. NFPs are required to advise Inland Revenue when they no longer meet the criteria for the RWT exemption (this is an annual test). However, we are aware that there is widespread non-compliance in this area and that some NFPs consider that the RWT exemption means they do not pay tax on interest income.

46. The issues paper raised the question of whether the RWT exemption rules for NFPs should be modified.

Submission summary

47. This topic received very few responses. Those that submitted on this issue suggested that the exemption be modified and simplified particularly in relation to the process for obtaining an exemption.

Officials' comments and recommendation

48. We support further work in relation to the RWT exemption. The $1,000 tax-free threshold was introduced to reduce the compliance costs of paying tax on small amounts of interest and dividends. However, with the introduction of RWT in 1989, these compliance costs were removed, reducing the rationale for the tax-free threshold.

49. We recommend reviewing the requirements for accessing the RWT exemption and whether the exemption is still needed. This work would also look at the interaction of this issue, the other member transaction issues, and how to provide clear guidance.

50. If the RWT exemption was removed, the fiscal implications will be dependent on the changes to the NFP deduction and is unquantifiable at this time.

Filing requirements

51. Currently, Inland Revenue does not require taxable NFPs to file tax returns if they qualify for the $1,000 tax-free threshold and have net taxable income of $1,000 or less. However, this approach is not supported by the current legislation, which requires all taxable NFPs to file income tax returns even if they have no taxable income.

52. Of the approximately 26,000 taxable NFPs on Inland Revenue's system, currently only 4,000 file income tax returns. If the current legislation were enforced, these remaining 22,000 non-filing NFPs would be required to file tax returns.

Submission summary

53. There was unanimous support for reduced filing requirements, particularly for smaller NFPs. Some submitters suggested that small NFPs should not be required to file at all.

Officials' comments and recommendation

54. Conceptually, filing requirements for NFPs should balance the objective of reducing compliance costs with the need for appropriate integrity measures, particularly when a significant tax concession is being provided.

55. We agree with submitters that filing requirements for smaller NFPs should be reduced. However, we do not support maintaining the current operational practice of exempting smaller NFPs from filing tax returns because this limits Inland Revenue's ability to maintain oversight of the NFP sector. Instead, we would support scaling back full tax returns to essentially be an annual confirmation that an NFP qualifies for the income tax deduction, and that it has income under the relevant threshold. Our initial view is that the threshold for reduced filing requirements should be aligned with the effective tax-free threshold for the sake of simplicity.

56. Changes in filing requirements in this way can be made without the need for a legislative amendment. Inland Revenue can use its existing ability to prescribe the form of a tax return so that the information smaller NFPs are required to provide annually is not onerous.

57. We recommend progressing this regardless of whether changes are made in relation to membership subscriptions and levies, the effective tax-free threshold level, and the RWT exemption.

58. There would be no fiscal impact associated with reducing filing requirements for smaller NFPs.

Financial implications

59. The financial implications of each proposal are set out above.

Consultation

60. The Department of Internal Affairs, Financial Markets Authority, Ministry for Primary Industries, Ministry of Business, Innovation and Employment, Ministry of Health, and the Treasury were consulted in preparing this appendix. Agency comments have been reflected in this appendix.

Next steps

61. If you wish to progress work on membership subscriptions, the tax-free threshold, the RWT exemption and return filing requirements, we recommend public consultation on the detailed policy design. Following consultation, we would report with final policy recommendations. We recommend targeted consultation on the impact of repealing the friendly society and credit union exemption.

62. We recommend that a copy of this appendix is referred to the Minister of Agriculture, the Hon Todd McClay; Minister for Biosecurity and Food Safety, the Hon Andrew Hoggard; Minister for Rural Communities, the Hon Mark Patterson; Minister for Oceans and Fisheries, the Hon Shane Jones (as requested by the Ministry for Primary Industries); and Minister of Commerce and Consumer Affairs, the Hon Scott Simpson (as requested by the Ministry of Business, Innovation and Employment).

Appendix 4: Proposed simplifications for donors and volunteers

1. Appendix 4 details specific simplifications for donors and volunteers. It is informed by submissions received on the officials' issues paper, "Taxation and the not-for-profit sector" (the issues paper), and stakeholder suggestions made in the 2024 "Donations Tax Credit Regime Regulatory Stewardship Review" undertaken by Inland Revenue.

2. In respect of donors, we recommend two policy changes. The first would allow Inland Revenue to refund donation tax credits (DTCs) during the year instead of waiting until after year-end. The second would allow donors to allocate their DTC directly to the charity they donated to. Both changes would take advantage of new capabilities in the Inland Revenue computer system. These changes would support philanthropic giving and could be seen as a positive counterbalance to sector concerns if the DTC ceiling was to be reduced (see Appendix 2: Donor-controlled charities and the donation tax credit). We recommend that you consult on these proposals.

3. In respect of volunteers, we recommend a policy change that will give NFPs the option of treating honoraria paid to volunteers as salary and wages. This simplification was supported by submitters and has already been put in place for Fire and Emergency New Zealand.

4. Initial advice indicates that there are no fiscal costs associated with either of these proposed changes.

5. In respect of administrative costs, the volunteer simplification proposal is not expected to require additional resourcing and can be managed within existing baselines. The cost of implementing the donor simplification proposal could be a one-off cost of up to $4.3 million.

6. We consider sufficient feedback has been given by stakeholders regarding the proposal to treat honoraria as salary and wages. No further public consultation is necessary for this proposal.

Background

7. On 27 March 2024, the Minister for the Community and Voluntary Sector raised concerns that current tax rules for honoraria may impose undue compliance costs and hinder volunteer participation. Inland Revenue subsequently reported on 14 April 2024 (IR2024/161), outlining potential issues with the tax treatment of honoraria and proposing options for further exploration, including an "opt-in to PAYE" regime.

8. On 20 September 2024, we reported on the draft findings from the DTC regulatory stewardship review concluding that while the regime performs adequately, there are significant opportunities for improvement and reform. In line with these findings, Inland Revenue recommended exploring simplifications for donors, including allowing DTC refunds to be released before year-end (IR2024/359 refers).

9. The proposals in this appendix seek to achieve the following policy objectives:

    9.1 **Simplicity with low compliance costs:** Keep the tax rules simple and compliance costs low, particularly for volunteers.

    9.2 **Encourage philanthropy:** Reinforce and encourage giving to support the charitable, community, and voluntary sectors.

Improvements to the DTC

10. The DTC is a longstanding policy mechanism designed to encourage philanthropy by allowing individuals to claim a 33⅓% tax credit on donations made to approved donee organisations.

11. Inland Revenue's DTC regulatory stewardship review findings, published in 2025, explored ways to improve the DTC to encourage greater philanthropy, and in some cases lower compliance costs, including:

    11.1 delinking DTCs from income tax to allow for more real-time payments, for example when DTCs are refunded before year-end and closer to the time a donation is made

    11.2 allowing donors to allocate their DTC back to the charity, and

    11.3 allowing Inland Revenue to collect data from donee organisations to pre-fill DTC claims and streamline the DTC claiming process.

Submitters' views on issues paper and officials' responses

12. The issues paper asked submitters for their views on the policy initiatives proposed in the DTC regulatory stewardship review.

13. A significant majority (74%) of submissions on this issue supported the proposal to delink DTCs from income tax to allow for more real-time payments.

14. A smaller majority (55%) of the submissions on this issue supported the proposal to allow Inland Revenue to collect data from donee organisations to pre-fill DTC claims and streamline the DTC claiming process.

15. Typical suggestions and concerns raised by submitters are summarised below.

Theme	Submitters' views	Officials' comments
Allocation of DTC directly to donee organisations	Inland Revenue should reinstate the ability for donors to allocate their DTC to the donee organisation.	This is explored further in paragraphs 19–25.
Public awareness	Greater public awareness of the DTC is required.	We agree. Inland Revenue recently undertook a campaign to increase customer awareness of the DTC credit.
Compliance costs of pre-filling DTC claims	Pre-filling DTC claims will shift compliance costs from the donor to the charity because new systems would be needed to gather and store information.	We agree. Inland Revenue would also have greater administration costs.
Compliance costs of real-time payments	Real-time payments could significantly increase compliance costs, especially for charities that operate on a monthly subscription model and issue a single receipt to donors at the end of the financial year. Charities are concerned that they may be expected to provide frequent or even immediate receipts.	Charities will not be *required* to provide receipts to donors more frequently, but they may face *pressure* to do so.

Officials' recommendations

16. Given the compliance and administration costs for stakeholders and Inland Revenue, and non-alignment with our policy objectives set out in paragraph 9, we

do not recommend progressing the proposal to allow Inland Revenue to collect data from donee organisations to pre-fill DTC claims.

17. We recommend undertaking further consultation on the proposal to allow in-year payments of the DTC. The objective of the consultation is to finalise a proposal that ensures what Inland Revenue systems can deliver will have sufficient integrity measures, will positively impact on donor behaviour, and will not put undue pressure on donee organisations to provide receipts more frequently.

18. If you agree to progress work on the proposal to allow in-year payments of the DTC, consultation could be later this year. We would report to you with final policy recommendations. We are recommending that consultation be public because the proposal would have widespread impact and submitters have highlighted the potential for unintended consequences.

Allocation of DTC directly to donee organisation

Policy options and submitters' views on issues paper

19. As noted in the previous table, many submissions proposed that we reinstate the ability for donors to allocate their DTC to the charity. This aligns with findings from the DTC regulatory stewardship review.

20. Currently, when a donation is made the donor is the only eligible recipient of the DTC. This means that if the donor wants the charity to receive the DTC, they must manually donate it back to the charity.

Officials' comments

21. This proposal aligns with our objective to encourage philanthropy through the tax system and reduce compliance costs for those giving to NFPs.

22. The Minister for Arts, Culture and Heritage has been asked to support a Gift Aid scheme,[12] and has shown interest in exploring options to stimulate philanthropic investment through the tax system.

23. Combining the proposal for allowing individuals to allocate their DTC back to the charity with the proposal for in-year DTC payments, provides a simpler alternative to the United Kingdom's Gift Aid system, where donors can donate part of their tax credit to the charity.

24. This proposal could involve both operational and policy change. For example, as an integrity measure and to minimise administration costs, the Inland Revenue payment may need to be excluded from being eligible for a further DTC claim.

Officials' conclusions and recommendations

25. Therefore, we recommend progressing work, including public consultation, to determine the feasibility of allowing donors to allocate their DTC directly to the donee organisation.

[12] Gift Aid is a United Kingdom government scheme that allows charities to claim an extra 25% on the donations they receive. High-rate taxpayers with a 40% or 45% tax rate can also claim a 15% or 20% tax credit on this donation.

Option to treat honoraria as salary and wages

26. Honoraria are treated as schedular payments for tax purposes. Honoraria payments are given as a token of appreciation for voluntary services or contributions. They are not a contractual obligation but rather a gesture of gratitude, and the amount is not necessarily tied to the market value of the service provided.

27. Schedular payments are most commonly made from businesses to contractors, allowing contractors to choose their own tax rate and claim business expenses. This flexibility is often unnecessary for some volunteers.

28. Treating income as schedular payments creates similar compliance costs to treating income as salary and wages, neither is significantly more complex than the other. Both treatments:

    - do not require end of year filing
    - receive automatic refunds for over-payments
    - obligations, such as KiwiSaver and student loan payments, are deducted at source, and
    - require the individuals to fill in a form when they start work.

29. However, ACC levies are not withheld with taxes on schedular payments, meaning volunteers need to pay ACC separately at the end of the year. This often causes confusion and adds to compliance costs. This differs to income treated as salary and wages where the ACC levy is withheld alongside PAYE throughout the year.

Tax treatment for honoraria received by volunteers working for Fire and Emergency New Zealand (FENZ)

30. In 2019 a legislative change was made allowing FENZ to treat honoraria paid to volunteers as salary and wages.

31. FENZ provide their volunteers with an honoraria payment for their loss of income when they attend a mandated training course. This meant before the policy change was made, FENZ volunteers were receiving an ACC levy invoice (sometimes months after their course) creating confusion and compliance costs.

32. Now that FENZ honoraria payments are treated as salary and wages this confusion and extra compliance cost is substantially reduced for volunteers.

Policy option

33. To encourage philanthropy and maintain low compliance costs for volunteers, the FENZ approach could be extended to all NFPs. This would allow NFPs to treat honoraria payments as salary and wages on an opt-in basis, as an alternative to treating them as schedular payments.

Submitters' views on issues paper

34. The issues paper asked submitters for their views on extending the FENZ simplification as an option for all NFPs. The majority of submitters expressed support for this option. Typical suggestions and concerns raised by submitters are covered in the following table.

Theme	Submitters' suggestions and concerns	Officials' comments
Increased compliance costs	The change could lead to higher compliance costs. This concern was primarily raised by those who assumed the approach would be mandatory rather than optional.	It is intended that entities can decide whether to opt in. That is, they can continue to treat honoraria payments as schedular payments.
Implementation caution	Treating honoraria as salary and wages could inadvertently trigger employment-related obligations, such as leave entitlements, so caution should be taken.	We agree, however, this can be managed through legislative clarification.
Optional participation	The initiative should be optional, rather than compulsory.	We agree.
Introduce tax-free threshold	There should be a tax-free threshold for honoraria payments. Views varied on how this threshold should be structured and applied.	A tax-free threshold could be explored further. However, we note there is an existing mechanism for Inland Revenue to make determinations exempting certain types of honoraria.[13]
Introduce full tax exemption	There should be an income tax exemption for honoraria.	We disagree, this would raise a number of integrity issues.

Officials' conclusions and recommendations

35. We consider that allowing NFPs to opt in to treating honoraria as salary and wages will reduce compliance costs and confusion for volunteers. This aligns with our two policy objectives referenced in paragraph 9.

36. We consider sufficient feedback has been given by stakeholders regarding the proposal to treat honoraria as salary and wages. Therefore, we do not consider it necessary to undertake further consultation on this proposal. If you agree to this change, we recommend that Cabinet make final decisions as part of Budget 2026. You could then have the choice of Budget legislation or legislating in the 2026–27 annual rates Bill.

Relationship with other work: Reducing expenditure on donation tax concessions

37. In Appendix 2: Donor-controlled charities and the donation tax credit, we have recommended that you reconsider the policy settings for donation tax concessions (including the DTC). If the Government were to consider this for Budget 2026, this could provide an opportunity to announce the two proposed DTC simplification measures as part of a wider package of DTC reforms.

Financial and administrative implications

38. Initial advice indicates that there are no fiscal costs associated with these proposed changes.

39. Inland Revenue has confirmed the changes to honoraria payments are not expected to require additional resourcing and that they can be managed within existing baselines with no additional funding required.

[13] Inland Revenue can make determinations exempting certain types of schedular payments including honoraria.

40. Inland Revenue has undertaken a high-level high contingency cost assessment. The cost of implementing DTC in-year payments is estimated to be a one-off cost of approximately $0.8 million. The cost of implementing the proposal to refund DTCs back to the charity is estimated to be a one-off cost of approximately $3.5 million. Both implementation costs are likely to be able to be incorporated into existing baselines.

Consultation

41. The Department of Internal Affairs, the Ministry for Culture and Heritage, and the Treasury, were consulted as part of preparing this appendix; agency comments have been reflected in this appendix.

Next steps

42. If you agree to progress work on the DTC proposals, consultation could be later this year. We would then report to you with final policy recommendations. We are recommending that consultation be public because the proposal would have widespread impact and submitters have highlighted the potential for unintended consequences.

43. We consider sufficient feedback has been given by stakeholders regarding the proposal to treat honoraria as salary and wages. No further public consultation is necessary for this proposal.

44. We recommend that a copy of this appendix be referred to the Minister for Arts, Culture and Heritage, the Hon Paul Goldsmith, for his information.

Appendix 5: Income tax exemptions that may no longer be fit for purpose

1. Appendix 5 details tax policy concerns relating to exemptions for non-resident charities with no charitable purpose in New Zealand, s 9(2)(f)(iv) , veterinary services bodies, herd improvement bodies, and bodies promoting scientific or industrial research.

2. Our view is that the exemptions present various challenges to the integrity of the tax system. This includes limited oversight and public accountability, inconsistent treatment of similar entities and, in some cases, the exemptions confer a competitive advantage. Additionally, alternative tax concessions could support some of these NFPs.

3. While we have considered submissions on the February 2025 officials' issues paper, "Taxation and the not-for-profit sector" (the issues paper), they have not changed our view that the exemptions should be repealed. When considering changes to the wider NFP landscape, and the principles of tax policy design, maintaining these activity-specific exemptions is difficult to justify.

4. While there is a strong justification to repeal all exemptions, we consider the exemptions for non-resident charities s 9(2)(f)(iv) the highest priority because they have the greatest volume and raise integrity concerns. The veterinary services bodies exemption is also a priority because there are competitive advantage and equity concerns.

5. If you agree with the recommendations, the changes could be enacted alongside other final decisions on taxation and the NFP sector. If you wish to maintain any of the exemptions, further policy work could increase transparency about who is accessing them, which could include targeted consultation.

Background

6. In July 2024, we reported to you on several tax concessions for NFPs that may be out of date and no longer fit for purpose (IR2024/237 refers).

7. The Government supports a broad-base, low-rate tax system that minimises economic distortions and ensures the system is coherent and predictable.

8. Income tax exemptions can distort resource allocation to tax-favourable activities and give certain entities tax advantages not enjoyed by other similar entities. These exemptions affect the coherence of the tax system, and perceptions of its fairness and equity.

9. However, income tax exemptions are afforded in rare circumstances to achieve a wider public policy objective. In the case of NFPs, the exemption should be limited to entities prohibited from providing private pecuniary benefits and subject to sufficient public accountability and transparency measures. These measures may be relaxed when there is a well-justified rationale, such as to avoid imposing excessive compliance or administrative costs.

10. The objectives of this review are to protect and strengthen the integrity of the tax system while minimising any unintended social costs. The following standard principles of policy design are used to evaluate income tax exemptions:

    10.1 **Coherency:** Exemptions should support the delivery of a public policy objective and fit within the wider NFP framework.

    10.2 **Revenue integrity:** Exemptions should be accompanied by transparency measures to ensure public accountability.

10.3 **Equity and fairness:** Exemptions should avoid treating similar entities inconsistently.

10.4 **Simplicity and low compliance costs:** Exemptions should seek to minimise compliance and administrative costs.

10.5 **Economic efficiency:** Exemptions should avoid distorting behaviour.

Problem definition

11. Most of these exemptions date back to the 1950s. Specific tax concessions are generally inconsistent with New Zealand's broad-base, low-rate tax policy framework. If the Government wishes to encourage a particular economic activity, it is preferable this is done in a transparent way by direct funding, or alternatively through more general provisions, such as the exemption for registered charities.

12. The existence of these exemptions results in unnecessary complexity and inconsistent tax outcomes for NFPs that are factually similar. Following the introduction of the Charities Act 2005, some entities claiming the exemptions may qualify to instead register as tax-exempt charities. This results in similar entities using different tax concessions with inconsistent reporting requirements.

13. Approximately 1,000 to 2,000 entities claim these exemptions. It is unclear how many are incorporated societies and report publicly, compared with unincorporated societies, trusts and companies that do not report publicly. Furthermore, some entities may have merged over time or may no longer operate. This poses oversight and transparency concerns.

14. These income tax exemptions challenge the tax system's equity and fairness, revenue integrity, and economic efficiency. The exemptions result in inconsistent treatment of similar entities, pose integrity concerns from limited oversight and public accountability and, in some cases, confer a competitive advantage.

15. Furthermore, changes to the framework, nature, and operating context of these entities mean that the exemptions may no longer fulfil their original public policy objectives. As such, supporting these entities through specific income tax exemptions is difficult to justify under the principles of tax policy design.

Submitters' views on issues paper

16. Most submitters were against removing the exemptions. The only exemption most submitters supported removing was the non-resident charities exemption. The veterinary services bodies exemption received strong views both for and against.

17. Some submitters said the exemptions are not justified due to integrity and fairness concerns. However, other submitters said the exemptions support the delivery of public services and provide a net gain for the Government. They said to remove the exemptions would impose significant compliance, restructuring, and administrative costs without raising significant revenue.

18. The background, submissions summary, and our comments and recommendation for each exemption are discussed below.

Exemptions that may no longer be fit for purpose

Exemption for non-resident charities with no charitable purpose in New Zealand

Background

19. Non-resident charities operating entirely outside New Zealand can apply for a tax exemption on their non-business income earned here. This includes rental, dividend, or interest income. This exemption results in New Zealand supporting charitable purposes overseas.

20. These entities are typically universities, religious organisations and private charitable foundations that are tax-exempt in their own jurisdiction. Most are located in the USA, the UK and Australia. Approximately 350 entities have sought approval; however, limited data means it is unclear how many still hold investments in New Zealand.

21. These entities are not required to report regularly to Inland Revenue or appear on any public register, raising integrity concerns. Inland Revenue is unaware if an entity still exists or remains eligible. There have also been cases of charities misapplying the exemption to business income.

Submissions summary

22. Most submitters supported reviewing the exemption due to perceived fairness and integrity concerns linked to the lack of reporting requirements. It was stated that charities providing no charitable purpose in New Zealand should be taxed on any accumulated funds.

23. However, others considered its removal could reduce the flow of international aid into New Zealand charities or discourage overseas charities from passively investing in New Zealand. This could impact foreign investment.

Officials' comments and recommendation

24. Our view is that the public policy rationale for the charitable exemption for non-business income derived by non-resident charities who have no charitable purposes in New Zealand has not been established. There are weak grounds for providing this tax exemption, when other non-resident entities are taxed on their New Zealand non-business income.

25. If Ministers choose to maintain this exemption to support overseas charitable purposes or foreign investment into New Zealand, there may be a public policy rationale to keep the exemption.

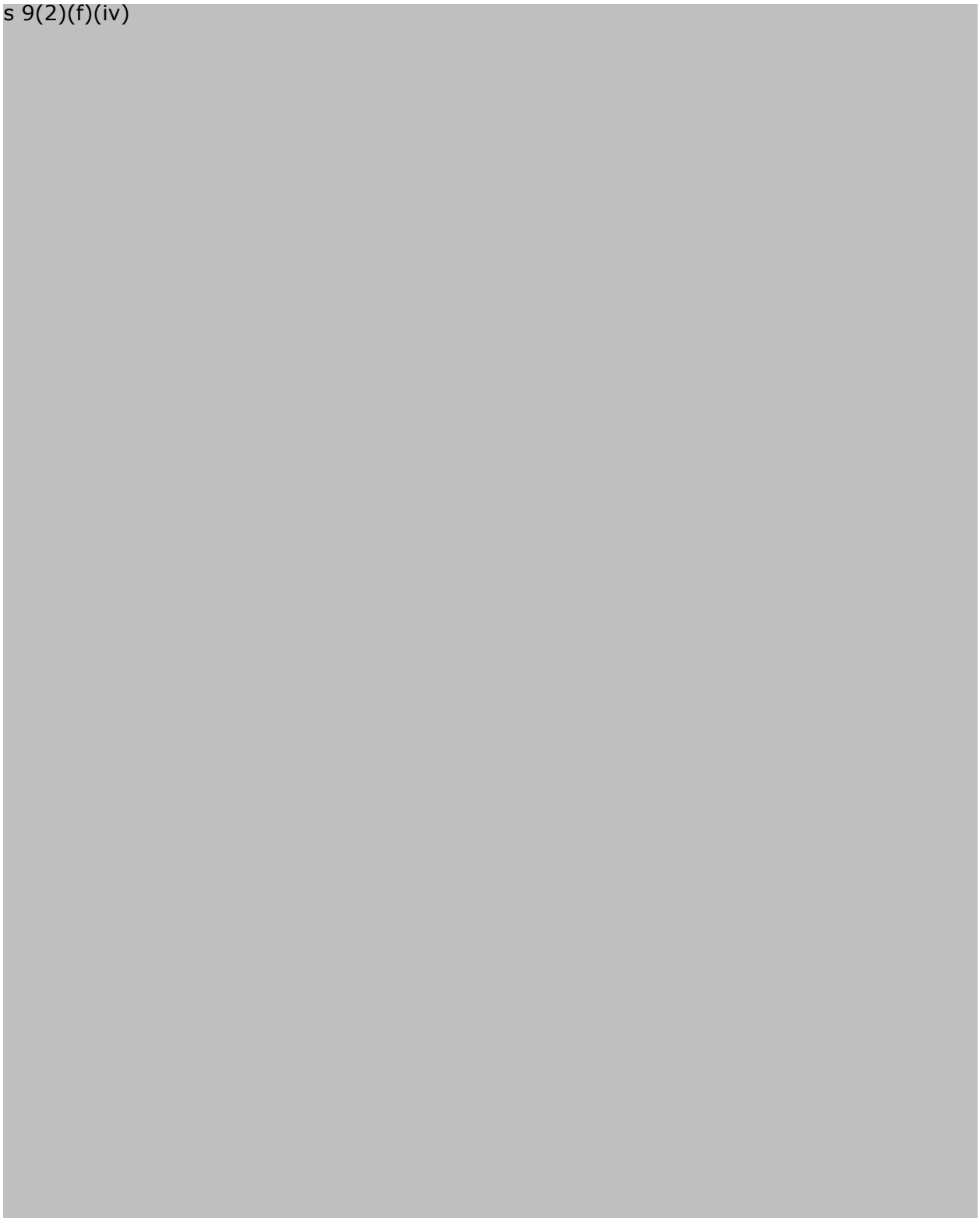
26. We consider that the inconsistent tax treatment of different types of non-resident entities and the inconsistent reporting by non-resident and domestic charities pose equity concerns. We are also concerned about the integrity challenges outlined above.

27. We recommend repealing the exemption for non-resident charities with no charitable purpose in New Zealand.

28. Alternatively, if Ministers do not support repeal, we recommend increasing transparency over who is claiming the exemption. For example, by publishing these entities' names on Inland Revenue's website, or requiring periodic re-application. Strengthening integrity measures was supported by a number of submitters.

29. Repealing this exemption would result in a small gain when withholding tax is applied to foreign investment. This would affect up to approximately 350 entities. We note this may be affected by behaviour change (see paragraph 23).

s 9(2)(f)(iv)



Exemption for veterinary services bodies

Background

38. The Veterinary Council of New Zealand has advised us that there are approximately 3,700 individual veterinarians and 500 to 600 veterinary clinics in New Zealand. The sector is split between tax exempt veterinary clubs and many more for-profit corporations. There are approximately 50 to 60 veterinary services bodies claiming the exemption (according to Inland Revenue records), which applies to entities like s 6(c)

39. Tax exempt veterinary services bodies were established mainly to promote efficient veterinary services in New Zealand. They are mostly governed by boards made up of their farmer members. This exemption was introduced in 1955 when New Zealand had no veterinary college. It aimed to encourage overseas trained veterinarians to set up practices in New Zealand to support the growing agricultural sector.

40. These entities are now more established, undertake commercial trading activities outside their immediate services, and compete directly with tax-paying private veterinary practices. Consequently, the exemption raises competitive advantage and international trade law concerns.

41. While we do not see evidence of a competitive advantage in the charity business income area (see Appendix 1), the veterinary services bodies exemption may distort behaviour. In comparison to entity-based exemptions, activity-specific exemptions can create distortions. The veterinary services bodies exemption favours veterinary work over other activities, so this may draw excessive resources into the veterinary sector, adversely impacting taxpaying businesses.

42. s 6(a)

Submissions summary

43. Private veterinary clinics supported removing the exemption arguing it disadvantages tax-paying private clinics. They said that removing the exemption could prevent veterinary clubs undercutting commercial veterinary clinics, resulting in a fairer environment. They provided examples of tax-exempt veterinary bodies purchasing private clinics to become some of the largest veterinary practices in the country. These submitters also argued that the exemption's original justification was no longer relevant and that veterinary services bodies were operating in more urban areas, servicing companion animals, and undermining the staff retention and renumeration abilities of private veterinary clinics.

44. Conversely, veterinary services bodies submitted that the removal of their exemption would lead to a reduction in the number of veterinary service providers. They argued that the exemption allows for greater competition in an industry that is becoming increasingly consolidated, and ensures New Zealand-owned practices are maintained.

45. These submitters also said veterinary services bodies ensure access to veterinary care in rural areas and provide various community benefits. It was considered that removing the exemption would disadvantage veterinary services bodies that are unable to access equity funding and imputation credits or make distributions to shareholders.

Officials' comments and recommendation

46. Since 1955, the veterinary industry has evolved significantly, reflected in the establishment of domestic veterinary training and the convergence of practices between non-profit and for-profit entities. These developments mean the exemption no longer fulfils the original public policy objective.

47. s 6(a)

48. The Ministry for Primary Industries noted that removing the exemption may have an impact on veterinary shortages in rural areas, which could affect the production animal sector, animal welfare, and biosecurity, with potential flow on implications for trade. Nevertheless, they also agreed with submitters that the industry and ownership have evolved.

49. On balance, we recommend repealing the exemption for veterinary services bodies.

50. If Ministers would like more detailed advice on the broader impacts of repealing this exemption before making a final decision, we can work with other government agencies and the New Zealand Veterinary Council to provide further advice.

51. Based on our data, repealing this exemption would result in a fiscal gain of approximately $2 million per annum and affect approximately 50 to 60 entities. The fiscal gain may be affected by behaviour change (see paragraphs 71–72).

Exemption for herd improvement bodies

Background

52. Herd improvement bodies were established mainly to promote the improvement of dairy cattle standards in New Zealand. Herd improvement bodies support pastoral farming and the dairy economy (for example, by facilitating information-sharing between farmers and providing advice about breeds). They were exempted from income tax in 1955 on the basis that such entities were of national significance.

53. This exemption was originally intended to apply to smaller less financially robust organisations but now applies to some larger well-funded organisations.

Submissions summary

54. This exemption received few responses and no submissions from directly affected entities. Those against its removal considered that its repeal could harm the efficiency and productivity of the dairy farming sector and increase costs for farmers. However, those supporting its removal argued that herd improvement services are part of the cost of specific commercial interests and should not be subsidised.

Officials' comments and recommendation

55. Our view is that this exemption creates inconsistent treatment with similar industries or other levy bodies in New Zealand, which could be seen as a risk to the tax system's fairness and coherency. Additionally, there is limited oversight or public accountability regarding these entities' activities.

56. Whether the public policy objective of this exemption remains relevant and current depends on the extent to which the Government wishes to continue supporting

these entities. The public policy rationale to support these specific entities may be unclear or difficult to justify.

57. We recommend repealing the exemption for herd improvement bodies.

58. Repealing this exemption would result in a fiscal gain of approximately $1 million per annum and affect approximately 50 to 60 entities, including s 6(c) , as reported in its public accounts. The fiscal gain may be affected by behaviour change (see paragraphs 71–72).

Exemption for bodies promoting scientific or industrial research

Background

59. Bodies promoting scientific or industrial research are tax exempt provided they are NFP organisations dedicated solely to research that benefits the public. This exemption was introduced in 1957 on the basis that the activities of these bodies were in line with national interests.

60. However, the tax context for bodies promoting scientific or industrial research has changed significantly since the introduction of the 1957 exemption. Before its introduction, it was unclear whether entities promoting scientific or industrial research were necessarily covered by the charitable exemption. That is not the case today. Since 2005 many organisations conducting research register under the Charities Act 2005. They are regulated by the Department of Internal Affairs (DIA) and access the tax exemption for registered charities.

61. In contrast, while applications under the 1957 exemption are approved by the Royal Society of New Zealand, there are no oversight or reporting mechanisms to monitor these entities' ongoing activities.

Submissions summary

62. One submitter supported the exemption's removal, saying if these bodies have a charitable purpose, they could register as charities.

63. However, other submitters opposed the removal, arguing that removing the exemption could undermine these entities' independence from external and commercial pressures, and diminish policy innovation and long-term research capacity, potentially harming underfunded research areas. Others argued that not all areas of research have become commercialised. Accordingly, the exemption should be retained for research serving the public.

Officials' comments and recommendation

64. Given that since 2005 many research entities have registered as charities and are subject to greater accountability measures, this exemption results in similar entities being treated differently, presenting risks to revenue integrity and tax system fairness. These developments may mean the exemption no longer fulfils the original public policy objective.

65. We recommend repealing the exemption for bodies promoting scientific or industrial research.

66. Repealing this exemption would result in a fiscal gain of approximately $1 million per annum and affect approximately 90 to 100 entities including some s 6(c) , as reported in its public accounts. The fiscal gain may be affected by behaviour change (see paragraphs 71–72).

Conclusions and recommendations

Option 1: Repeal all exemptions

67. Our preferred option is to repeal all these income tax exemptions for NFPs.

68. Removing the exemptions would increase the revenue system's integrity by reducing risks linked to limited public accountability, potential competitive advantage, and trade law obligations.

69. This option would also improve the coherency, equity, and fairness of the tax system because similar entities would more likely be subject to consistent tax treatment and reporting requirements.

70. While we recommend repealing all exemptions, the strongest grounds are for removing the exemptions for non-resident charities s 9(2)(f)(iv) because these pose the highest integrity concerns.

Alternative tax concessions

71. If the exemptions are repealed, it is possible that some of these NFPs may be able to register as charities. Exempting these entities through registration with Charities Services would promote more integrity in the tax system because similar entities would be subject to the same public reporting requirements.

72. Alternatively, other entities may still be able to access the tax-free threshold for small NFPs (currently $1,000). Accordingly, the impact of repealing these exemptions may depend on the outcome of changes to simplify the law for NFPs (see Appendix 3). If Ministers agree to review the size and design of the current $1,000 tax-free threshold for NFPs, this would reduce compliance costs for smaller NFPs that can no longer access specific income tax exemptions.

73. Entities that do not qualify as charities or that are above the NFP tax-free threshold may have tax liabilities or, alternatively, tax losses.

Option 2: Enhance transparency, particularly for non-resident charities

74. If Ministers do not wish to repeal these exemptions, we recommend considering increasing transparency for entities claiming the exemptions, particularly non-resident charities. These pose a higher integrity risk because they are outside our jurisdiction, meaning it is harder to obtain information on their income and the location of their activities.

75. As outlined above, income tax exemptions should be supported by public accountability measures. However, accountability measures may be relaxed when there is a well-justified rationale.

76. In principle, we do not support introducing reporting requirements for other exempt NFPs unless there are integrity concerns because that would likely impose undue compliance and administrative costs. This is consistent with the March 2025 legislative change, which confirmed that tax exempt entities do not need to file income tax returns.

77. For all entities, repealing the exemptions remains our preferred approach.

Financial implications

78. The financial implications of each proposal are set out above.

Administrative implications

79. While removing these exemptions would not result in major administrative costs for Inland Revenue, this may lead to more NFPs seeking registration with Charities Services, imposing administrative costs for DIA. However, given the low volumes, we do not anticipate these would be significant.

Consultation

80. DIA, Ministry of Business, Innovation and Employment, Ministry of Foreign Affairs and Trade, Ministry for Primary Industries, and the Treasury, were consulted in preparing this appendix. Agency comments have been reflected in this appendix.

Next steps

81. If you agree with the recommendations, changes could be enacted alongside other final decisions on taxation and the NFP sector.

82. If you wish to maintain any of the exemptions and agree for officials to explore options to enhance transparency for these entities, we will report to you in early 2026.

83. If you decide to maintain the status quo and maintain all exemptions without further work, we will cease policy work in this area.

84. We recommend that a copy of this appendix be referred to the Minister of Agriculture, the Hon Todd McClay; the Minister for Biosecurity and Food Safety, the Hon Andrew Hoggard; and the Minister for Rural Communities, the Hon Mark Patterson (as requested by the Ministry for Primary Industries).

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Briefing note

Reference: BN2025/385

Date: 16 October 2025

To: Private Secretary, Minister of Finance (Revenue) – Carl Harris
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Melissa Zhen

From: Stewart Donaldson
Andrew Pillay

Subject: **Taxation and the not-for-profit sector: Draft media statement, Q&A and proactive release**

Purpose

1. The Minister of Finance's office has asked for a draft media statement and related questions and answers.

2. This briefing note is accompanied by BN2025/411 "Taxation and the not-for-profit sector: Timelines and consultation".

Draft media statement and Q&A

3. A draft media statement is in Appendix A and a draft Q&A is in Appendix B.

Proactive release

4. Now that Ministers have decided to cease work on five policy matters, in late October/early November 2025 we will proactively release advice that we have provided on these matters. The detail will be in a separate briefing note. We expect it to draw on the briefing notes and reports listed in Appendix C.

Consultation with the Treasury

5. The Treasury was informed about this briefing note.

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
s 9(2)(a)

APPENDIX C: Proactive release

Now that Ministers have decided to cease work on five policy matters,[1] in late October/early November 2025 we will proactively release advice that we have provided on these matters. The detail will be in a separate briefing note. We expect it to draw on the following briefing notes and reports.

1. **IR2024/237** "Tax policy options for the NFP sector"

2. **T2024/2396, IR2024/199** "Charity business income tax exemption"

3. **IR2024/454** "Charities and not-for-profits: Proposed 2025 public consultation"

4. **BN2024/504** "Charities and not-for-profits consultation: Potential changes to scope and timing"

5. **BN2025/032** "Summary of the 'charity business income tax exemption' issue"

6. **BN2025/035** "Taxation and the not-for-profit sector: Proposed officials issues paper and timeline"

7. **BN2025/042** "Taxation and the not-for-profit sector: Updated officials' issues paper and timeline"

8. **BN2025/047** "Revenue impact of charity business income and other not-for-profit income tax exemption proposals"

9. **IR2025/039** "Cabinet paper – Release of Issues Paper – Taxation and the not-for-profit sector"

10. **IR2025/135** "Taxation of not-for-profits: possible in principle decisions"

11. **IR2025/146** "Taxation and the not-for-profit sector – submission summary and next steps"

12. **IR2025/169** "Charities and NFPs tax issues announcements"

13. **BN2025/213** "Not-for-profits: Inland Revenue advice to submitters and stakeholders"

14. **IR2025/257** "Taxation and the not-for-profit sector: Recommendations from officials"

15. **IR2025/258** "Taxation and the not-for-profit sector: Supplementary Report"

[1] Charity business income tax exemption, veterinary services bodies, herd improvement bodies, bodies promoting scientific or industrial research, friendly societies and credit unions.

Appendix A is withheld in full under section 9(2)(g)(i) of the OIA
Appendix B is withheld in full under section 6(c) of the OIA

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Briefing note

Reference: BN2025/411

Date: 16 October 2025

To: Private Secretary Minister of Finance (Revenue) – Carl Harris
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Melissa Zhen

From: Stewart Donaldson

Subject: **Taxation and the not-for-profit sector: Timelines and consultation**

Purpose

1. The Minister of Finance's office has asked for:

   - an outline of timelines for consultation, with options for amendments to be included in a Budget Bill or an omnibus taxation Bill, and
   - what questions are planned to be covered in targeted consultation and who would be consulted.

2. This briefing note is accompanied by BN2025/385 "Taxation and the not-for-profit sector: Draft media statement, Q&A and proactive release".

Discussion

3. To assist with the detailed design of amendments, Ministers have agreed that officials undertake consultation (IR2025/257, paras 16, 52(b) refer).

4. We initially considered the option of undertaking targeted consultation in November 2025 with the option of subsequently undertaking public consultation. However, we are now of the view that there will be insufficient time following targeted consultation to complete a round of public consultation before Budget 2026 decisions are required.

5. This briefing note provides a timeline for either a targeted consultation option in November 2025 (with no subsequent public consultation) or for a public consultation option in December 2025 to Waitangi Day 2026 (with no prior targeted consultation). The difference in timing reflects the need to take the public consultation paper through the Cabinet process.

6. s 9(2)(g)(i)

7. If targeted consultation is undertaken, it would be done on a confidential basis. However, there is a risk that the content could be disclosed to the public. One of the most controversial matters that we have not raised publicly is the option to introduce a donation tax credit ceiling. To mitigate any reputational risk if targeted consultation on this matter becomes public, the Minister's media statement (BN2025/385 refers) could pre-empt this by stating a donation tax credit ceiling is being considered for donor-controlled charities.

8. **We recommend the public consultation option** because of the broad public interest, the risk that targeted consultation could be disclosed to the public, s 9(2)(f)(iv)

Timeline

9. If targeted consultation alone were to be undertaken, a possible timeline is:

Date	Milestone
Late October to end of November 2025	Undertake targeted consultation
December 2025	Report to Ministers on submissions and recommended next steps
February 2026	Report to Ministers with final recommendations and Budget bid

10. If public consultation were to be undertaken (our recommended option), a possible timeline is:

Date	Milestone
30 October 2025	Report to Ministers with draft issues paper
3 to 11 November 2025	Ministerial consultation
13 November 2025	Lodge paper
19 November 2025	ECO
24 November 2025	Cabinet
December 2025 to Waitangi Day 2026	Undertake public consultation
February/March 2026	Report to Ministers with final recommendations and Budget bid

11. Under both timelines, resulting amendments could then be included in a Budget Bill or an omnibus taxation Bill. We recommend that whichever legislative vehicle is used, that the Bill be referred to Select Committee so there is a further round of public consultation.

Draft consultation questions

12. The proposed draft consultation questions are set out in Appendix A. These questions would be provided as part of a more comprehensive document, so we have provided them to you for context only. There are questions relating to:

    - donor-controlled charities
    - membership subscriptions and related matters, and
    - donation tax credit simplifications.

13. The draft questions could be asked in either a targeted consultation document or in a public consultation document.

Stakeholders who would be part of targeted consultation

14. Attached as Appendix B is a list of the stakeholders we propose consulting with as part of a targeted consultation process (if Ministers prefer that we do not undertake public consultation).

15. These stakeholders reflect a cross-section of those we have previously consulted with and/or those that could be impacted by the proposals.

16. s 6(c)

Consultation with the Treasury

17. The Treasury was informed about this briefing note.

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
s 9(2)(a)

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Briefing note

Reference: BN2025/443

Date: 30 October 2025

To: Private Secretary Minister of Finance (Revenue) – Carl Harris
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Melissa Zhen

From: Stewart Donaldson
Philip Marshall

Subject: **Not-for-profits: Inland Revenue advice to the sector during targeted consultation**

Purpose

1. On 28 October 2025 the Minister of Finance indicated she is comfortable with officials communicating Ministers' decisions about the not-for-profits tax policy work.

2. This briefing note outlines the generic update officials intend to provide during targeted tax policy consultation and in response to requests from other stakeholders when they ask about the next steps for the not-for-profits tax policy work.

Generic responses provided to submitters and stakeholders

3. From Friday 31 October 2025 we will start to proactively contact a number of sector representatives as part of targeted tax policy consultation. The consultation questions will be sent in the week beginning 10 November 2025. We anticipate that some submitters and stakeholders will also contact Inland Revenue asking what the next steps will be for the not-for-profits tax policy work, following the Minister of Revenue's announcement yesterday about the refreshed tax and social policy work programme.

4. We will tailor our responses to the specific stakeholder and provide updates on the topics that are relevant to them. Our responses will generally draw on/contain the following narrative.

Announcement by Minister of Revenue

5. Officials received comprehensive feedback from over 900 submitters during consultation in February/March 2025. The consultation document, submissions and a summary of the submissions are published on the tax policy website (the link is here). The submissions informed decision-making and helped Ministers decide where best to focus attention.

6. The Minister of Revenue released the Government's refreshed tax and social policy work programme on 29 October 2025 (the link is here). The Minister said that the Government will continue to focus on simplifying the tax system and improving integrity, and this includes ongoing policy work looking at the taxation of charities and not-for-profits.

7. When the Minister spoke about the work programme on 29 October 2025, he said the Government has stopped work on taxing charity business income. He was concerned the complexities, compliance costs and distortions associated with a change would impose significant costs on charitable organisations and distract them from their core purposes. However, the Minister said he expects Inland Revenue to increase its enforcement efforts to make sure charity businesses are complying with the existing rules.

8. The Minister said that Inland Revenue will continue to work on donor-controlled charities as the main focus because these types of charities receive generous tax concessions, and it is vital that the rules governing them are clear, fair, and robust.

9. The Minister said Inland Revenue will also work with the Department of Internal Affairs on improving transparency for charitable funds that are accumulated.

10. The Minister said final policy decisions will be made in early 2026.

Donor-controlled charities

11. Officials will undertake targeted tax policy consultation on the following matters affecting donor-controlled charities:

    - a proposed definition for donor-controlled charities
    - a proposed minimum distribution rule
    - proposed integrity measures, including whether a donation tax concession ceiling should apply to donations made to donor-controlled charities
    - a proposal to subject donor-advised funds to the same rules as donor-controlled charities, as well as other integrity rules, and
    - a proposed "pay in money" rule for private trust income allocations to tax-exempt beneficiaries.

Taxable associations: subscriptions, mutual transactions and related matters

12. A draft operational statement, ED0265 "Mutual transactions of associations (including clubs and societies)" was released in April 2025. The statement reiterated Inland Revenue's current position that member trading transactions (for example, food and drinks at a club) are taxable. It also outlined Inland Revenue's updated view that membership subscriptions and levies may be taxable.

13. Officials will undertake targeted tax policy consultation on the following matters affecting taxable associations:

    - a proposal to clarify the circumstances when membership subscriptions and levies could be exempt
    - a proposal to raise the annual tax-free threshold[1] from $1,000 to $10,000 based on advice from submitters

[1] Refer to section DV 8 of the Income Tax Act 2007.

- a proposal to require taxable not-for-profits to have simplified income tax return filing requirements, and

- a proposal to require financial institutions to provide Inland Revenue with financial information for all not-for-profits that rely on the section DV 8 tax-free threshold.

Simplifications for volunteers and donors

14. Officials will progress work to simplify tax rules for volunteers, as discussed in the issues paper.

15. The Government supports providing more options to claim donation tax credits to encourage philanthropic giving. Officials will undertake targeted tax policy consultation on the following matters affecting donor simplifications:

    - proposals that will allow donors to claim in-year donation tax credits, and

    - proposals that will allow donors to allocate donation tax credits to the charity they donated to.

Exemptions

16. Officials consulted on whether to remove several not-for-profits tax exemptions in the 2025 officials' issues paper.

17. The Government decided not to progress further policy work on the income tax exemptions for friendly societies and credit unions, veterinary services bodies, herd improvement bodies, and bodies promoting scientific or industrial research.

18. Officials will continue work to remove income tax exemptions for certain non-resident charities s 9(2)(f)(iv)

s 9(2)(f)(iv)

Targeted consultation

20. Ministers have asked officials to undertake targeted consultation on the policy design of matters that will be progressed, so that final decisions can be made in early 2026. Consultation will occur over the period November 2025 to early February 2026, starting in the week beginning 10 November 2025.

21. Targeted consultation will draw from the pool of people who submitted on the 2025 issues paper.

Consultation with agencies

22. The Treasury and the Department of Internal Affairs were informed about this briefing note.

Stewart Donaldson
Principal Policy Advisor
s 9(2)(a)

Briefing note

Inland Revenue
Te Tari Taake

Reference	BN2026/060
Date	25/02/2026
To	Private Secretary Minister of Finance (Revenue) – Carl Harris Revenue Advisor, Minister of Revenue – Angela Graham Private Secretary, Minister of Revenue – Melissa Zhen
From	Stewart Donaldson
Subject	**Taxation and the not-for-profit sector: Virtual meetings with submitters**

Purpose

1 This briefing note provides an overview of our upcoming virtual meetings with submitters and the content we are sharing with them.

Virtual meetings

2 On 27 February 2026 we are holding two virtual meetings with all submitters on our targeted consultation document, "*Taxation and the not-for-profit sector: Targeted consultation on detailed design*". The meetings will cover:

- Donor-controlled charities and donation tax credit simplifications
- Membership subscriptions and related matters for taxable not-for-profits.

3 The purpose of the meetings is for us to share the main themes we heard from submitters and confirm whether anything substantial has been overlooked before we report to Ministers in March. The meetings will not be confidential, and attendees could release content or their views with the media afterwards.

4 We received approximately 140 submissions on our targeted consultation and are expecting over 100 attendees at each virtual meeting.

Pre-reading material

5 On Tuesday 24 February, we sent out slideshow presentations covering pre-reading material for the two meetings. A copy of the material we have sent out is attached.

6 Given that these slideshows could be distributed widely, we have only included factual information we heard from submitters. While we may give an indication of our current thinking verbally at the meetings, we have not included anything about our likely recommendations in the pre-reading.

Next steps

7 We will provide you with an update if anything substantial is raised.

Stewart Donaldson

Principal Policy Advisor | s 9(2)(a)

Tax policy report

Inland Revenue
Te Tari Taake

Taxation and the not-for-profit sector: Interim update and possible lines of communication

Date	13 March 2026	**Priority**	High
Security level	Budget sensitive	**Report number**	IR2026/083

Action sought		**Deadline**
Minister of Finance	**Note** the main recommendations to be included in our report to you on 19 March 2026 **Note** our proposed lines of communication for the Minister of Revenue, which could be used at the upcoming CTG meeting and for other public communications and responses to sector enquiries.	16 March 2026
Minister of Revenue	**Note** the main recommendations to be included in our report to you on 19 March 2026 **Note** our proposed lines of communication for the Minister of Revenue, which could be used at the upcoming CTG meeting and for other public communications and responses to sector enquiries.	16 March 2026

Purpose
The Minister of Revenue requested an interim report outlining our main recommendations for taxation and the not-for-profit sector. This interim report provides context for your Joint Ministers meeting on 16 March 2026. It also sets out possible lines of communication if the Minister of Revenue decides to share the direction of travel at a Corporate Taxpayers Group meeting on 17 March 2026.

Contact for phone discussion, if required			
Name	**Position**	**Phone number**	**First contact**
Stewart Donaldson	Principal Policy Advisor	s 9(2)(a)	✓
Philip Marshall	Senior Policy Advisor		☐

Taxation and the not-for-profit sector: Interim update and possible lines of communication

Background

1 In August 2025, we reported to you with a package of tax changes for the not-for-profit (NFP) sector to address significant tax integrity issues and simplify current rules and processes. That report was informed by over 900 public submissions.

2 Between November 2025 and February 2026, we undertook targeted consultation with affected entities. We sought feedback on detailed design options for three topics:

- tax policy settings for taxable NFPs (including membership subscriptions, member trading transactions and simplification measures)
- donor-controlled charities
- donation tax credit (DTC) refund simplifications.

3 This targeted consultation resulted in a further 140 submissions. In late February, we invited all 140 submitters to meet, hear the feedback and share what our recommendations were likely to be. In total we have had more than 100 meetings with stakeholders over the last 12 months.

4 This interim report outlines our main recommendations for tax policy settings for taxable NFPs and donor-controlled charities. Simplification for DTC refunds were broadly supported by the sector and are not controversial, so have been excluded from this report. All our formal analysis and recommendations will be provided to you on 19 March 2026 (reports IR2026/062 and IR2026/063).

5 This report does not discuss our analysis or recommendations about the broad tax policy settings for the DTC. That work is Budget sensitive and has not been mentioned to any external stakeholders. However, it is part of our package of tax changes for the NFP sector and there are inter-dependencies between the recommendations below and your decision about whether to change the DTC policy settings.

Tax policy settings for taxable NFPs

6 Our policy work for taxable NFPs would impact on approximately 26,000 clubs and societies. The main issues involve the taxation of membership subscriptions and levies, the taxation of member trading transactions, and simplifications for small NFPs. You indicated your objective is to simplify the rules for NFPs, and we anticipate that our recommendations will be well-received by most of the sector. However, there may be push-back on specific matters. There will also be fiscal implications, which we have summarised below.

Membership subscriptions and levies

7 The Commissioner is about to formally change his interpretative view and announce that many membership subscriptions and levies charged by clubs and societies are taxable. This change in view will result in significant compliance costs for the sector for an estimated revenue gain of only $20.6 million over the forecast period. We consulted on what we considered was a pragmatic policy solution – to define components of subscriptions that would remain non-taxable. Submitters made it clear that breaking down subscriptions into taxable and non-taxable components is impractical and will result in significant compliance costs. We have taken on board their concerns and suggestions and recommend a simpler policy approach that will make virtually all subscriptions and levies non-taxable. We expect this to be well-received by the sector.

Taxable member transactions

8 Although membership subscriptions and levies would remain non-taxable under the above revised approach, the current legislation taxes profits when members purchase trading stock and pay for the supply of services. For example, when members pay for food and drinks at a cosmopolitan club eatery and bar.

9 Some NFPs are not paying tax on these transactions and Inland Revenue intends to publish an operational statement confirming these transactions are taxable. However, there are interpretative issues with the scope of the current rules for taxable member transactions, particularly when goods and services are sold to members on a non-commercial basis. For example, small scale fundraising when members buy snacks, t-shirts or calendars from their club, or when they pay fees to attend an annual conference when there is no intention to make a profit.

10 In our view, the policy setting should tax NFP profits on the provision of commercial goods and services to members when they are provided in the course of doing business. Most submitters support legislative amendment to confirm this approach as long as Inland Revenue provides appropriate guidance on when an NFP will be considered to be in business. It will mean non-commercial fundraising activities with members, and profits from non-commercial member activities such as annual member conferences, will not be taxable.

11 We note that some submitters suggested that member transactions should not be taxable at all, as is the case in Australia. However, we do not support this view and we note that many submitters were comfortable with NFPs paying tax on commercial member transactions. The rules taxing certain member transactions have existed since the 1950s and, despite some non-compliance in the sector, the large NFPs typically pay tax on member trading transactions. Accordingly, a change to this approach would come at a fiscal cost. We also note that based on our discussions s 6(a) , the Australian approach is not without its own difficulties, particularly around the member/non-member distinction.

Simplifications for small NFPs

12 To reduce compliance costs for smaller NFPs, particularly those that are run by volunteers, our 19 March 2026 report will recommend simplification measures that increase the tax-free threshold for NFPs from $1,000 to $10,000 and provide income tax return filing exemptions for NFPs earning under this tax-free threshold. These proposed changes were generally well-received, however, submitters did not support our recommendation to target the higher tax-free threshold using a cliff-edge approach.

Donor-controlled charities

13 Our policy work for donor-controlled charities will impact on approximately 200 charities that control assets exceeding $2 billion. We propose to address integrity issues inherent in charities where the donor (or their associates) retain control over how charitable funds are spent. For these charities, there is a heightened risk of aggressive tax planning. There can also be a significant delay between the time of tax concessions for the donor and the charity and the distribution of funds for charitable purposes.

14 Our advice takes on board lessons from Australia, Canada and the United States where there are specific tax rules for these types of charities. We have followed the principle that New Zealand should not have stricter rules than those countries without a strong reason, given that our philanthropic sector is growing but is much smaller. We note that Australia, Canada and the UK have recently announced or implemented changes that strengthen their rules.

15 We considered how to define a donor-controlled charity, whether there should be:

- a minimum distribution rule

- specific integrity measures (such as clawing back or disallowing donation tax concessions when there are circular arrangements between the donor, the donor-controlled charity and entities controlled by the donor or their associates)
- any rules that also apply to donor-advised funds, and/or
- a limit to donation tax concessions for all donations to these charities.

16 While there is mixed public support for specific tax rules for these charities, most submitters who participated in targeted consultation were not supportive of our proposals because they believed the problem definition should be clarified, and that charity fiduciary duties and behaviour should be addressed by the regulator, Charities Services, instead of Inland Revenue. Submitters were also concerned that any tax-specific minimum distribution rules could discourage philanthropy.

17 In respect of our policy design proposals, submitters advised us to be careful when defining what a donor-controlled charity is so there is no overreach. They pushed-back on our proposal for a 5% net asset minimum distribution rule because it could undermine the long-term sustainability of charities and could pose high compliance costs. Submitters were concerned about complex integrity rules. They also said a limit to donation tax concessions would be a blunt tool to address integrity issues and reduce the scale of philanthropic giving in New Zealand.

18 There was support for some proposed design features, such as averaging a minimum distribution requirement over three years and allowing an exemption from a minimum distribution rule in certain circumstances.

19 We have considered this feedback. While we still believe it is important to introduce tax rules for these charities, we have softened our recommendations. For example, we propose:

- a narrow definition of a donor-controlled charity so that fewer are impacted
- a deferred implementation date
- a lower minimum distribution rate (we will recommend 3.5% of net assets)
- a de minimis, so that small donor-controlled charities will not be affected.

20 A limit on tax concessions for donations to donor-controlled charities would address our integrity concerns while raising revenue at the same time. However, we agree with submitters that it is a blunt tool and it would be difficult to design an effective rule without further consultation. Therefore, we do not recommend this option.

Financial implications and interaction with Budget process

21 The detailed fiscal implications of policy options in relation to the NFP sector will be set out in our 19 March 2026 report.

22 All decisions remain subject to final Budget 2026 decisions, to be made by Budget Ministers and Cabinet.

23 We consider it important that final decisions are taken together, given the interdependencies between the various policy options. In particular, if a decision to update broad tax policy settings for the DTC is progressed, we recommend that you do not progress any specific policy changes in relation to donor-controlled charities.[1] Therefore, we would not recommend communicating decisions in relation to donor-controlled charities in advance of any decision in relation to DTC settings.

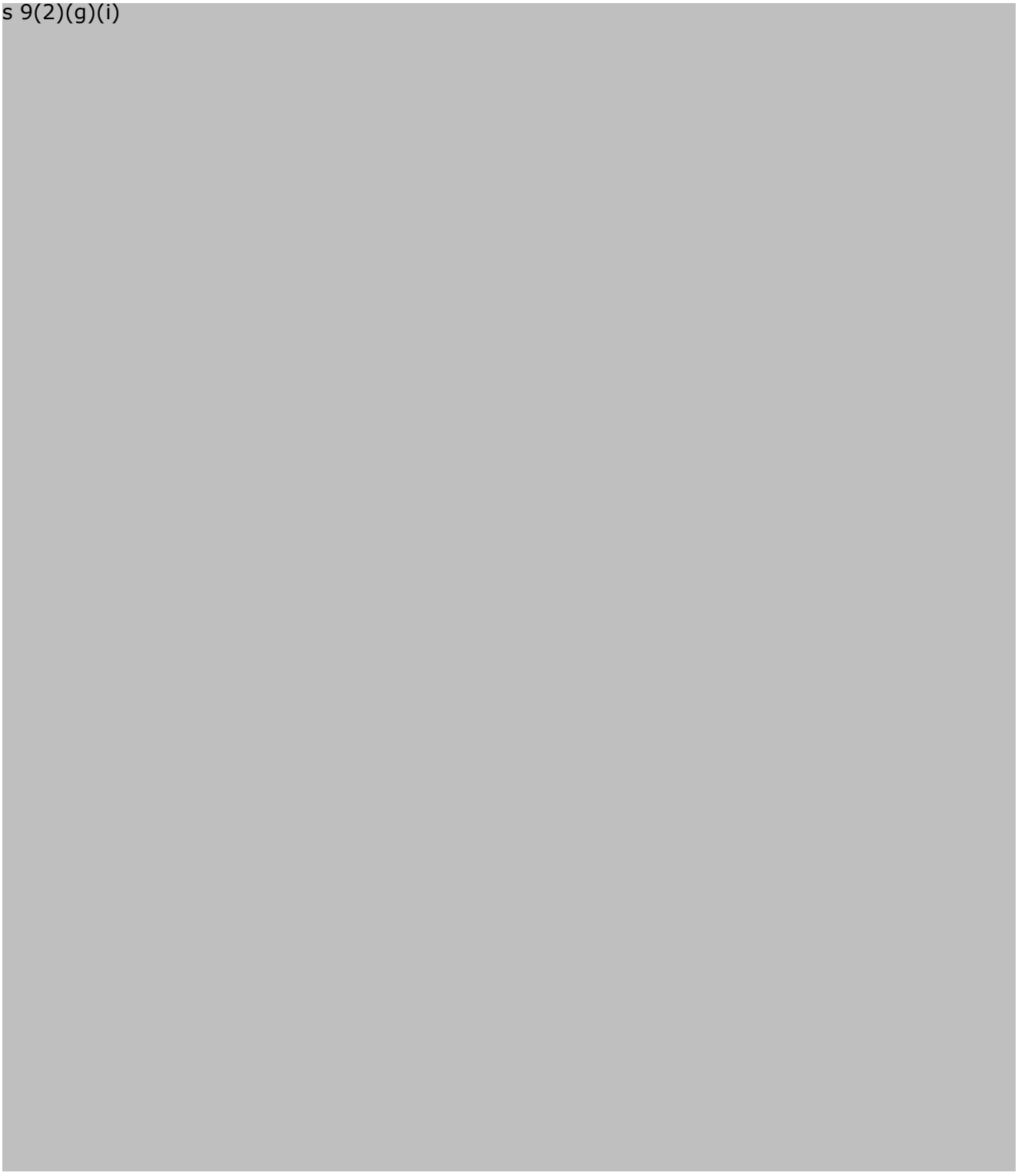
[1] A capped DTC would effectively address the existing concern that donor-controlled charities may be used as vehicles for favourable tax arrangements. For this reason, a donation tax concession cap specific to donor-controlled charities is a viable policy option, although our 19 March 2026 report to you will recommend more targeted measures, more directed at the specific policy problem, instead of this blunt tool.

24 Depending on the net impact of your decisions, the fiscal impact of the policy change(s) may be managed against the tax and social policy Scorecard and/or the Budget 2026 operating allowance.

Possible lines of communication

25 If you agree with our policy recommendations outlined above, noting that formal decisions have not been made and that the decisions will have fiscal implications, here are some proposed lines of communication for the Minister of Revenue. These could be used at the upcoming Corporate Taxpayers Group meeting and other events.

s 9(2)(g)(i)



s 9(2)(g)(i)

Consultation

29 We have consulted with the Treasury in the preparation of this report.

Recommendations

We recommend you:

1	**Note** the main recommendations to be included in our report to you on 19 March 2026.	
	Noted	Noted
	Minister of Finance	*Minister of Revenue*

2	**Note** our proposed lines of communication for the Minister of Revenue, which could be used at the upcoming Corporate Taxpayers Group meeting and for other public communications and responses to sector enquiries.	
	Noted	Noted
	Minister of Finance	*Minister of Revenue*

s 9(2)(a)

Stewart Donaldson
Principal Policy Advisor
Policy | Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2026

Hon Simon Watts
Minister of Revenue
/ /2026

Briefing note

Inland Revenue
Te Tari Taake

Reference	BN2026/119
Date	9/04/2026
To	Revenue Advisor, Carl Harris Revenue Advisor, Minister of Revenue – Angela Graham Private Secretary, Minister of Revenue – Melissa Zhen
From	Alison Wright
Subject	**Taxation and not-for-profit sector draft Regulatory Impact Statements**

Purpose

1 Please find attached the Taxation and not-for-profit sector draft Regulatory Impact Statements for:

- Donor-controlled charities
- Changing donation tax credit policy settings
- Tax policy settings for not-for-profits, and
- s 9(2)(f)(iv)

2 Also attached is a document summarising the Regulatory Impact Statements.

3 The Minister of Finance and the Minister of Revenue recently agreed that work on donor-controlled charities is to stop. We are not doing further work on this issue. s 9(2)(f)(iv)

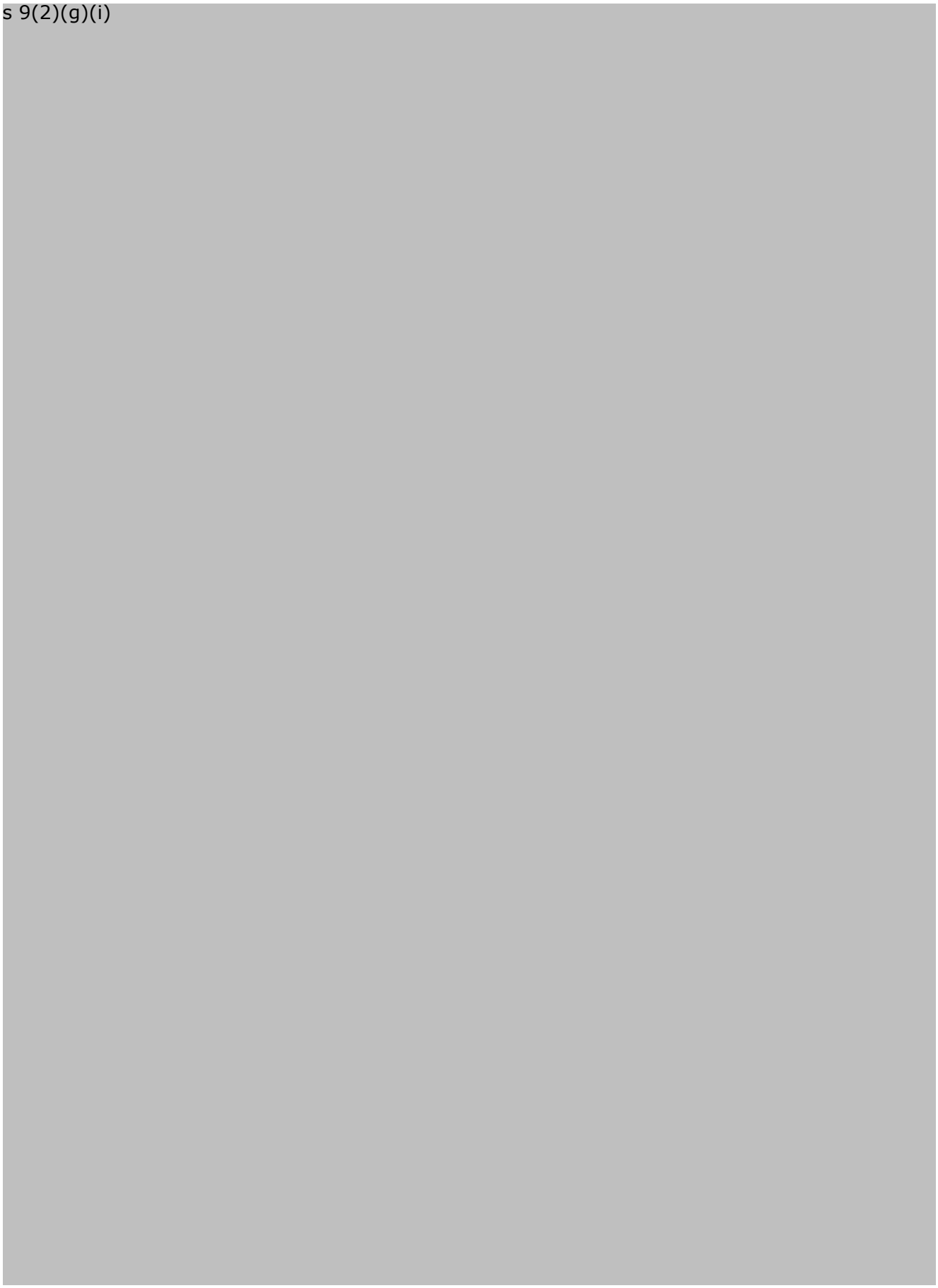
4 The Regulatory Impact Statements reflect the decisions to date of the Minister of Finance and the Minister of Revenue.

5 Final versions of the Regulatory Impact Statements will be provided with the Cabinet Legislation Committee paper for the 2026–27 annual rates taxation Bill, which is scheduled for introduction in September 2026.

Alison Wright
Principal Policy Advisor
s 9(2)(a)

FACT SHEETS

s 9(2)(g)(i)



s 9(2)(g)(i)



Changing donation tax credit policy settings

Problem definition

The existing donation tax credit settings result in Crown expenditure of around $350 million per year. The empirical evidence is mixed on whether such a tax credit is cost effective in encouraging socially valuable charitable giving. Ministers asked for advice on whether changes could be made to donation tax credit settings (currently 33⅓%, capped at taxable income) to improve value for money, address tax integrity concerns, and support fiscal sustainability. The proposals in the RIS could also buttress the integrity concerns identified with donor-controlled charities.

Options and recommendation

1. Status quo.
2. Reduce maximum entitlement to a lower ceiling with sub-options of $4,500, $15,000, and $100,000 **(officials' preferred sub-option $100,000)**.
3. Reduce the rate of the tax credit from 33$^{1}/_{3}$% to 25%.

The options would continue to support charitable giving across a broad donor base, while advancing value-for-money and fiscal sustainability objectives. We consider there is merit in a maximum entitlement ceiling of $100,000 as it best balances the above objectives. This option targets high value giving but leaves unaffected 99.9% of individuals who currently engage with the donation tax credit system. Ministers have not yet indicated a preferred option.

Key points

Officials' views

- The stated objectives for these proposals may not easily reconcile with the Government's other stated objectives of growing donations to the charitable, voluntary and community sector. Before final decisions are made, the Minister for the Community and Voluntary Sector and the Minister for Culture and Heritage should be consulted.

Data and evidence

- Over the last decade the number of individuals claiming the donation tax credit has declined, but the average value of the tax credit paid has increased.

Consultation

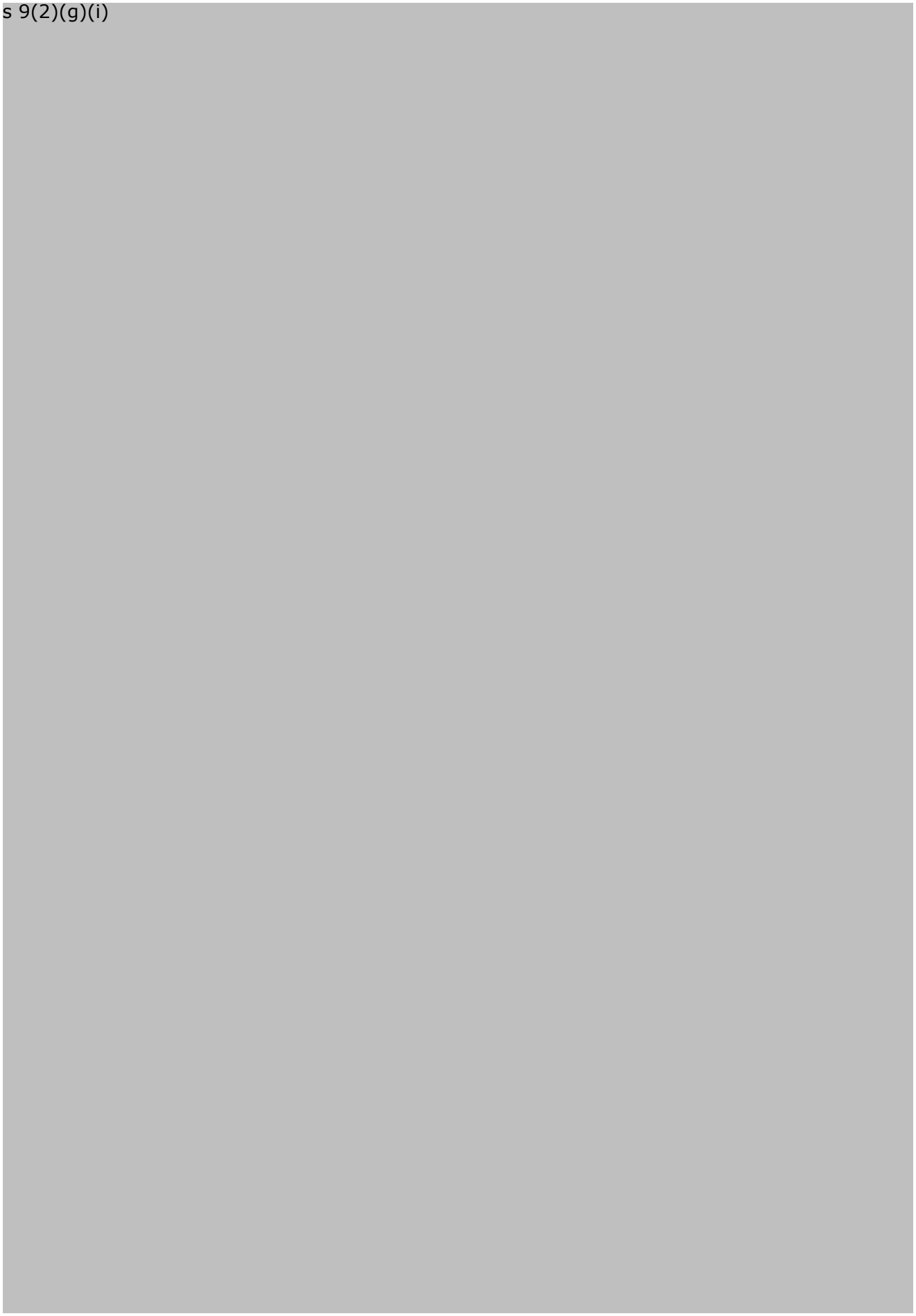
- There has been no direct consultation on this proposal. However, officials have considered: (1) external commentary received through Inland Revenue's stewardship review of the donation tax credit (published 2025); and (2) broader feedback on tax settings for the not-for-profit sector from tax practitioners, iwi groups, industry representatives, individuals, and donee organisations.
- The sector would consider that they are not supported enough by Government, so this proposal could be seen as unnecessarily reducing support and discourage donations. The Department of Internal Affairs and Ministry for Culture and Heritage note that the current tax policy settings are an important platform for supporting Government initiatives for promoting philanthropy to further social and community outcomes and facilities.

Fiscal impact and outcomes

- Depending on Ministers' preferred option, adjusting the donation tax credit settings could provide fiscal savings of between $13 million and $107 million a year. Officials' recommended option of setting the maximum entitlement threshold to $100,000 is expected to provide fiscal savings of $19 million a year when fully implemented.
- It is currently unclear to what extent donors would change their behaviour in response to this proposal. There could be uneven impacts. It is difficult to estimate the value of

positive externalities provided by the sector and how that might change under the proposal.

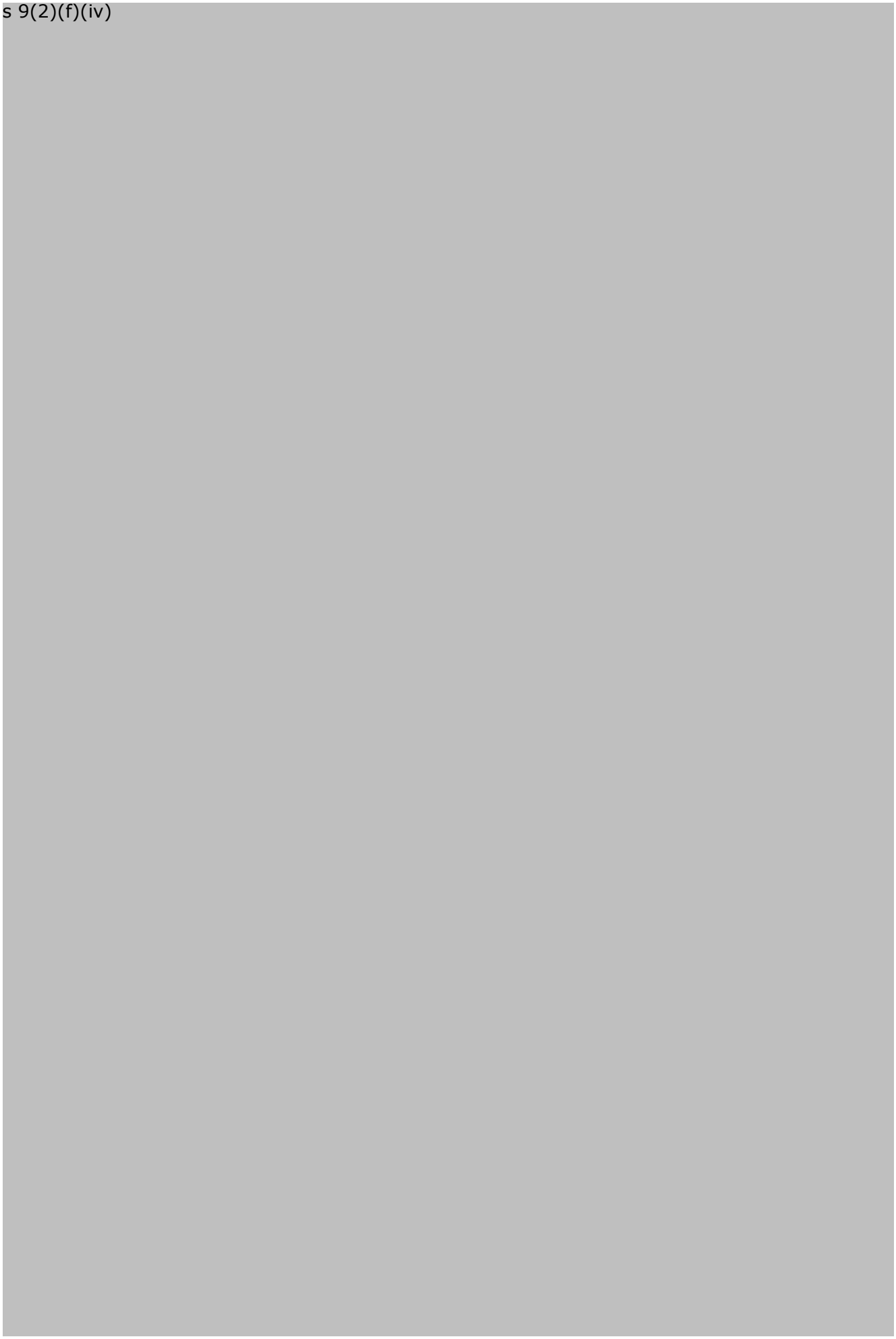
s 9(2)(g)(i)



s 9(2)(g)(i)



s 9(2)(f)(iv)



s 9(2)(f)(iv)

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: Non-resident contractors' tax: asset leasing

Date:	24 September 2025	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2025/364

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to recommendations **Note** the contents of this report	15 October 2025
Minister of Revenue	**Agree** to recommendations **Note** the contents of this report	15 October 2025

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Sam Rowe	Policy Lead	s 9(2)(a)	☒
Pamela Law	Principal Policy Advisor		☐
Hamish Dick	Senior Policy Advisor		☐

24 September 2025

Minister of Finance
Minister of Revenue

Non-resident contractors' tax: asset leasing

Executive summary

1. Stakeholders have raised an issue regarding the adverse impact of non-resident contractors' tax (NRCT)[1] on asset leasing, particularly in the airline industry. Non-resident lessors often do not wish to engage with the New Zealand tax system, meaning that either the New Zealand lessee pays the NRCT due (unduly increasing the tax cost of the lease) or the lease does not proceed. Current NRCT settings therefore present a barrier to the leasing of capital assets to New Zealand. Addressing this barrier may improve the inflow of capital assets, with commensurate flow-on benefits to economic activity and growth.

2. This issue has particularly affected New Zealand lessees in the airline industry owing to the current global constraints on the supply of aircraft and parts. Where supply of a good or service is limited, relative tax and administrative settings become all the more consequential for those determining where to do business.

3. We recommend that we explore a solution to this issue that would provide for a final tax to be paid by the New Zealand lessee at an appropriate rate. We seek your direction and agreement to progress this work. Further advice will consider whether any policy option should apply to commercial asset leasing generally or be specific to the airline industry.

Background

Purpose

4. The purpose of this report is to provide you with initial advice regarding the impact of NRCT on asset leasing. In particular, this report responds to the issues and options raised by s 9(2)(a) of Grant Thornton New Zealand in his letter of 15 August 2025 (the letter) concerning the airline industry. We seek your agreement to undertake further work on NRCT and asset leasing.

Context and background

5. NRCT is intended to operate as an interim withholding tax on a gross payment. It is withheld by New Zealand payers from payments to non-resident contractors in relation to their activities in New Zealand. The non-resident's final tax position should be settled via self-assessment with any NRCT withheld in excess of the non-resident's substantive tax liability being refunded.

6. NRCT's function is to protect the New Zealand tax base by mitigating flight risk – contractors who leave New Zealand without paying the tax ultimately due on their income.

[1] A non-resident contractor is a non-resident person, company or entity contracted to provide services, the use of another person's services, or the use of equipment in New Zealand.

7. In addition to the specific asset leasing issue set out in this report, businesses have raised a number of other issues with NRCT, which we are approaching in stages. Some have been addressed in the current omnibus taxation Bill or a previous Bill. We will report to you in a few weeks regarding the issues which we would like to address in next year's Bill.

NRCT and asset leasing

8. The letter particularly focuses on the impact of NRCT on the airline industry. However, based on previous consultation with private sector stakeholders about NRCT, we think that the concerns identified in the letter about the rate and incidence of the tax will be common to commercial asset leasing generally. Our next advice to you will consider whether any policy solution should be specific to the airline industry or apply in relation to commercial asset leasing generally.

9. In relation to the airline industry, NRCT is generally payable on short-term leases of aircraft and aircraft parts from non-residents (provided they are taxable domestically and in accordance with an applicable double taxation agreement). Long term leases (referred to as finance leases) are treated as the sale of an asset for tax purposes, so are not subject to NRCT. Broadly speaking, we understand that overseas lessors respond to NRCT in one of two ways:

    9.1 They require the New Zealand lessee pay the NRCT due to Inland Revenue on a grossed-up basis. This means that NRCT is in effect a final tax borne by the lessee (probably passed on in turn as a higher cost to their customers), which does not operate as originally intended; or

    9.2 They decline to lease the asset to a New Zealand lessee at all, opting for markets that are already more competitive and less costly (e.g., those with a geographic advantage).

The problem with NRCT and New Zealand airlines

10. For the airline industry, NRCT issues have become more pressing in recent years due to the global difficulty in obtaining aeroplanes and parts. The lack of supply has increased lessors' market power.[2] Further, this lack of supply has meant that, in recent years, finance leases of planes and parts (which are not subject to NRCT) have become less common and short-term operating leases (which are subject to NRCT) have become more common.

11. The problem is that the NRCT currently charged on airline leasing (and other leasing of substantial equipment) is much greater than the potential tax liability of the non-resident lessor.

12. Where the non-resident lessor does not have an IRD number, NRCT is paid by the lessee at a grossed-up rate of 25% on the gross lease payments. However, aircraft leasing arrangements are highly structured and are closer to a financial arrangement than an ordinary business. Proft margins of s 9(2)(b)(ii) are typical, with New Zealand tax on these payable at 28%. This implies that a gross withholding rate of 2-3% could be more appropriate (rather than 25%), though further work is necessary to interrogate these assumptions and determine an appropriate rate. Nonetheless, we are confident that the current regime results in the significant over-taxation of aircraft lessors which is borne by New Zealand lessees and their customers.

[2] Lessors dominate - Aviation Leaders Report 2024 - KPMG Ireland

13. This over-taxation is contrary to our broad-base low-rate framework and is providing a significant disincentive to lease aircraft (and other substantial assets) to New Zealand lessees. The requirement to interact with the New Zealand tax system may result in leases not progressing. In other scenarios the contract(s) may be structured in commercially undesirable ways so that payments are not subject to NRCT.

14. The letter states that the current NRCT tax settings are a barrier to cross-border large capital asset lease negotiations and are a blockage and barrier to New Zealand capital asset growth. It notes the writer has firsthand examples where offshore asset owners simply refuse to look at New Zealand lease market opportunities because of New Zealand's tax and administrative settings. We consider a law change is warranted to address this problem.

15. It is notable that where a foreign-owned airline enters into leases offshore, there is no immediate NRCT implication for the lessee. This creates a competitive disadvantage and an incentive to relocate to another jurisdiction, such as Australia.

Options raised in the letter

16. The following options were raised in the letter:

16.1 *A 10-year NRCT exemption for significant commercial asset leases*.

This option is a poor fit from a tax policy perspective, as it would undermine the purpose of NRCT. It would mean that non-resident lessors would lack an incentive to pay their tax liability and so would function more like a broad income tax exemption. We do not recommend tax exemptions under our broad-base low-rate framework. It also has the potential to create further demand for exemptions from NRCT.

s 6(c) non-tax options may be more appropriate. We note that the Government has developed an Aviation Action Plan and has stated it is prepared to make loans to at risk regional air routes from the Regional Infrastructure Fund.[3]

16.2 *Introduction of an "as agent" system for New Zealand lessors or alternatively deeming a portion of the fee to be New Zealand source income (similar to non-resident insurers and shippers rules)*.

We think these suggestions or a similar approach, have merit and recommend exploring options of this nature as a solution to the issues raised (see *Inland Revenue preferred option* below).

New Zealand's tax rules deem a small portion of non-resident shippers' and general insurers' income to be New Zealand source income (5% and 10% respectively).[4] The letter indicates that the profit margin for non-resident airline industry assets is approximately s 9(2)(b)(ii), meaning the effective rate of tax could be around 2%–3% of the gross income. Further information is required to establish an approximate tax rate, which we will consider as part of any further advice to you. Grant Thornton New Zealand has requested further information on average leasing profit margin for this purpose, but this information is not yet available.

[3] Government backing vital regional connectivity | Beehive.govt.nz
[4] This is to reflect the fact that much of the activity involved in these industries takes place outside New Zealand, and so only a small percentage of the income should be taxed here.

16.3 *Expansion of double taxation agreement (DTA) concessions.*

As the letter notes, to achieve these changes would be complex and time-consuming. Further, DTAs are reciprocal. Changes to agreements would depend on a negotiated outcome meaning that the overall result will reflect the interests of both parties. We prefer domestic solutions to the issues raised in the letter as they are administratively simpler, faster to make, and more certain.

16.4 *Change New Zealand's tax settings to support the growth of a Pacific regional aircraft leasing hub*.

This proposal would involve targeted tax exemptions or other concessions to attract lessors. From a tax policy perspective this approach would be contrary to New Zealand's broad-base, low-rate tax settings. There would also be non-tax implications that would require exploration if the Government wanted to pursue this option.

Although we understand that Zealand airlines struggle to lease aircraft and parts, this solution does not appear commensurate to the problem. Further, we are not aware of evidence that there is international appetite to move away from the current well-established global leasing hubs: Ireland, Japan and the USA.

Inland Revenue's preferred option

17. Inland Revenue prefers an option similar to the deemed source income approach set out in paragraph 16.2 above. We think that a potential approach would be to adapt the approved issuer levy mechanism[5] for NRCT purposes. This means that the New Zealand lessee would pay a levy on the lease payment at a low rate (which would need to be determined), and the non-resident lessor would have no further New Zealand tax or filing obligations. Future advice to you will consider whether any solution should be available for all asset leases, rather than being confined to a single industry (subject to fiscal constraints).

18. Changing NRCT to optionally allow it to be a final tax on the payer, at an appropriate, lower rate, could reduce the cost of capital and compliance costs. This approach would recognise that the lessor does not wish to consider New Zealand tax in its decision to engage with a New Zealand business. Although the revenue raised by NRCT would decrease, it would result in a tax payable commensurate with the profits earned by the non-resident lessor from New Zealand leasing. It would also mean that the non-resident would have no New Zealand tax or tax compliance obligations, making New Zealand a more attractive place to do business. Making this mechanism optional would still allow the parties to apply the NRCT rules and seek exemption or self-assess the amount of tax due under the ordinary rules if they preferred.

19. As the issue with NRCT applies in respect of all asset classes, future advice will consider whether any policy solution should apply to all asset classes, not just aircraft and parts. Changing NRCT settings for asset leasing more generally would provide an opportunity to improve New Zealand's capital stock and productivity and enhance the Government's growth agenda, but would come at a greater fiscal cost. We think that measures to change NRCT to simplify and lower the cost of asset leasing would be well-received by businesses.

[5] New Zealand borrowers can elect to pay approved issuer levy at the rate of 2% on interest payments to non-resident lenders. This is instead of withholding non-resident withholding tax at the rate of 10% or 15%. The approved issuer levy was introduced to reduce the cost of capital for New Zealand borrowers as, similarly to NRCT for aircraft leases, the cost of non-resident withholding tax was simply being passed on to the New Zealand borrower by the offshore lender.

20. This could also be a good alternative to any further, non-infrastructure related thin capitalisation reform at this point in time. While changing thin capitalisation settings should in theory be expected to reduce foreign firms' effective tax rates, our data suggests that most foreign owned businesses operating here (outside of infrastructure) are not sensitive to thin capitalisation settings. Only 13% of foreign owned businesses currently have a thin capitalisation ratio of between 40% and the current 60% threshold, while 65% of businesses have a ratio of less than 20%. This suggests that more general changes to thin capitalisation settings are unlikely to have a significant effect on investment.

Consultation on the problem

21. We have consulted with s 9(2)(a) of Grant Thornton New Zealand, s 6(c) . We approached two other domestic airlines but they did not respond

22. The Treasury has been informed of this report.

Financial implications

23. The financial implications of any change will be ascertained when the proposal for reform is clearer. Contextually, and using data that has limitations, we estimate that NRCT from asset leasing collects up to $22 million per year across all industries. The airline industry segment represents less than a quarter of this figure, although it is growing.

24. The limitations arise as NRCT is reported via the pay-as-you-earn system, where it mingles with other schedular payments and can be hard to identify. We also suspect that some NRCT payments may be put through the non-resident withholding tax system in error. The data also cannot indicate the fiscal impact of lost opportunities to enter into a lease arrangement arising from the current system.

25. If the Government agrees to progress this item as part of the Tax and Social Policy Work Programme, we note that changes to NRCT are likely to be revenue negative and will require a budget bid. Alternately, you could consider using some of the tagged contingency allocated to the thin capitalisation infrastructure project in Budget 2025 to fund the NRCT changes, as the thin capitalisation project is likely to cost less than forecast due to the selection of the narrower option.[6]

Administrative implications

26. Administrative costs would also depend on the scope and design of a potential solution to this issue and costing would be included in future reporting.

Next steps

27. We are already seeking approval to retain general NRCT reforms on the Tax and Social Policy Work Programme. If you agree, a potential solution for asset leasing would be included as part of that wider work and more detailed reporting would follow.

[6] Note that this would require broadening the original scope of the tagged contingency, with the appropriate joint Minister or Cabinet approvals.

28. NRCT changes are likely to require a Budget bid to account for the fiscal cost (but, as noted above, costs could be met through the money allocated to the thin capitalisation infrastructure project at Budget 2025). The policy changes could be implemented via an omnibus tax Bill.

29. Subject to your directions, we will respond to the letter confirming next steps.

Recommended action

We recommend that you:

1. **agree** that we should continue to work on non-resident contractors' tax impact on commercial asset leasing with a view to a solution that:

   1.1 mitigates New Zealand tax compliance obligations for non-resident asset lessors and New Zealand lessees;

   Agreed/Not agreed Agreed/Not agreed

   1.2 provides for a final tax to be paid by the New Zealand lessee at an appropriate rate;

   Agreed/Not agreed Agreed/Not agreed

   1.3 allows the parties to choose whether to pay the final tax or to engage with the non-resident contractors' tax withholding rules;

   Agreed/Not agreed Agreed/Not agreed

2. **note** that, subject to your agreement to progress this work, future advice will consider whether any policy solution should apply to commercial asset leasing generally or be specific to the airline industry (and/or any other industry).

   Noted Noted

3. **note** that we will report to you on proposals to simplify and modernise non-resident contractors' tax settings in a future report.

   Noted Noted

s 9(2)(a)

Sam Rowe
Policy Lead
Policy

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

Tax policy report

Inland Revenue
Te Tari Taake

Non-resident contractors' tax: Budget 2026 policy options for aircraft asset leasing

Date	28 January 2026	**Priority**	Medium
Security level	Budget sensitive	**Report number**	IR2026/001
Bill name	TBC		

Action sought		**Deadline**
Minister of Finance	**Agree** to recommendations	11 February 2026
Minister of Revenue	**Agree** to recommendations	11 February 2026

Purpose
This report sets out policy options for the Budget 2026 submission in relation to improving non-resident contractors' tax (NRCT) settings for the airline industry. It seeks Ministers' agreement to an exemption from NRCT for aircraft asset leasing, subject to confirmation by Budget Ministers and Cabinet.

Contact for phone discussion, if required			
Name	**Position**	**Phone number**	**First contact**
Sam Rowe	Policy Lead	s 9(2)(a)	✓
Hamish Dick	Senior Policy Advisor		☐

Non-resident contractors' tax: Budget 2026 policy options for aircraft asset leasing

Executive summary

1 This report sets out policy options for the Budget 2026 submission in relation to improving non-resident contractors' tax (NRCT) settings for the airline industry. It seeks Ministers' agreement to an exemption from NRCT for aircraft asset leasing, subject to confirmation by Budget Ministers and Cabinet. This workstream is incorporated within the submitted Budget 2026 Tax and Social Policy Work Programme placeholder initiative.

Policy problem

2 In September, we reported to you in relation to NRCT and asset leasing [IR2025/364 refers]. This report highlighted a distortionary impact of NRCT on asset leasing arrangements, particularly in relation to aircraft operating leases.

3 Current NRCT settings present a barrier to the leasing of capital assets to New Zealand. Specifically, non-resident lessors often do not wish to engage with the New Zealand tax system, meaning that either the New Zealand lessee pays the NRCT due (unduly increasing the cost of the lease) or the lease does not proceed.

4 The issue is particularly acute for the airline industry, owing to global supply constraints and the lack of market power for New Zealand lessees. NRCT is also levied at a much higher rate than is justifiable by the profits earned from aircraft leasing, meaning that airline leases are significantly over-taxed when NRCT is paid.

5 In September, the Minister of Revenue indicated a preference for a simple solution that minimises compliance costs and has a quick impact. In order to achieve this, the Minister of Revenue also indicated that any such solution should be limited to the airline industry and not, at least in the first instance, be extended to commercial asset leasing more generally. We agree with this approach.

Policy options

6 A policy solution could take one of two forms:

- an **exemption from NRCT** for aircraft asset leasing, on either a time-limited or permanent basis (automatically or by application), or
- an **opt-in final tax** for aircraft asset leasing at a low rate (which could be similar to, or incorporated within, the approved issuer levy (AIL) regime).

Table 1: Summary of Policy Options

Option	Design choices	Timing	Tax burden	Compliance costs	Revenue cost	Overall assessment
NRCT exemption (officials' recommendation)	• Time limited or permanent • Automatic or by application • Removal of overseas lessors' tax liability	• Simplest, quickest (minimal legislative change required)	• Nil	• Nil to low	• Moderate ($4.463m avg pa), but could be costly if exemption extended to other asset classes in future	Simplest, quickest solution
By application, opt-in final levy or tax	• Inclusion within AIL or unique regime for asset leasing (tax deductible) or non-deductible final rate • Opt-in low rate • Information collection	• 4–6 months to create new AIL-type account for aircraft leasing, quicker if no need to register a security	• Fair relative to profitability	• Moderate, falls on NZ-resident lessee	• Moderate (depending on rate and design; $3.496m avg pa for a 2% final tax)	Appropriate if settings may be extended in future to other classes of leased assets

Recommendation

7 We recommend that you agree to progress an exemption from NRCT for aircraft asset leasing, at a fiscal cost of $17.850 million operating (forecast period total).

8 An exemption is an appropriate solution on the basis that New Zealand-resident lessees of aircraft can, under "good" market conditions, structure out of NRCT. NRCT already does not apply to leases from some countries under our double tax agreements (DTAs), nor does it apply to longer-term "finance leases" (whereas it does apply to shorter-term operating leases). We note that New Zealand is also somewhat unusual internationally in taxing lessors of assets in these circumstances; no tax would be payable by lessors under the standard OECD model tax treaty, for example. This solution is also supported by the stakeholders we consulted.

9 In the airline industry, operating leases have become more common owing to global supply constraints and increasing global demand, and lessors of aircraft are often resident in countries ineligible for relief from NRCT under a DTA. When it is payable, NRCT is functioning as a punitive tax on leasing arrangements, inhibiting the competitiveness of New Zealand-resident companies.

10 We agree with the submissions of stakeholders that improving tax settings for aircraft leasing will be beneficial for the economy. An exemption represents the near-immediate removal of tax constraints, tackling New Zealand's currently limited ability to compete for aircraft in a globally constrained market, it is welcoming to offshore lessors, it is quick and easy to promote, and it is easy for industry to understand.

11 We note that while NRCT issues with asset leasing are felt most acutely in the airline industry, they also likely exist for other asset classes, such as those in the oil industry. You could, on a longer timeframe, extend the NRCT improvements proposed here to other leased assets.

12 If this is your intention, a low, opt-in final tax (for example, 2%) may be preferable.

13 For aircraft leasing, a 2% final tax option would cost $13.983 million operating (forecast period total). This option would be more consistent in principle with our current tax settings. It would preserve New Zealand's current taxing right over airline leases, while ensuring that a more appropriate amount of tax is withheld to reflect the actual profits from airline leasing. Administrative costs could be minimised by adopting a low-compliance solution, and we would not recommend introducing a new AIL-like regime unless this is to become a template for commercial asset leasing more generally.

14 The revenue at stake between the two options is $0.910 million operating per annum in outyears. While this may not be sufficient to justify a 2% tax over the larger economic benefits of an NRCT exemption for aircraft leasing, the same might not be true if expanded to other leased assets. A full tax exemption for airline leasing may create an expectation of similar treatment for other asset classes, when it may be inappropriate. One way to mitigate this issue would be to signal that the airline exemption is an interim measure pending a full review of NRCT settings for asset leasing generally.

15 Operationally, either option is achievable on a Budget 2026 timeline, although we consider an exemption to be a more pragmatic solution for airline leasing from a tax administration perspective. From the perspective of the taxpayer, an exemption from NRCT is similarly the most effective, low-compliance option.

16 As part of this initiative, we would also amend the law (under either option) so that overseas lessors would have no remaining tax liability in New Zealand in relation to the leased aircraft and parts, reflecting how NRCT has been functioning in practice in relation to aircraft leasing contracts (that is, as a final tax borne by the lessee). This would ensure that the non-resident is not discouraged from leasing aircraft here by the need to engage with our tax system.

17 We recommend that any policy solution apply from 1 April 2026 (we recommend retrospective application in the Budget Bill).

Financial implications

Tax Revenue impact

Table 2: Fiscal impact of a permanent exemption of aircraft leasing from NRCT

	$m – increase / (decrease)				
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Crown Revenue and Receipts: Tax Revenue – PAYE	(1.050)	(4.200)	(4.200)	(4.200)	(4.200)
Total Operating	**1.050**	**4.200**	**4.200**	**4.200**	**4.200**

Table 3: Fiscal impact of replacing NRCT with a 2% final tax for aircraft leasing

	$m – increase / (decrease)				
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Crown Revenue and Receipts: Tax Revenue – PAYE Final Tax (tbc)	(1.050) 0.228	(4.200) 0.910	(4.200) 0.910	(4.200) 0.910	(4.200) 0.910

Total Operating	**0.823**	**3.290**	**3.290**	**3.290**	**3.290**

Administrative impact

Table 4: Administrative cost of a permanent exemption for aircraft leasing from NRCT

	$m – increase / (decrease)				
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
One-off implementation	-	0.100	-	-	-
Ongoing operating costs	-	-	0.050	0.050	0.050
Total Operating	**-**	**0.100**	**0.050**	**0.050**	**0.050**

18 Inland Revenue has included a placeholder initiative in the 19 December Budget 2026 submission that included the departmental administration costs above. Once the scope, scale and timing of all Budget 2026 initiatives become clearer, Inland Revenue will adjust the funding sought for all initiatives and report on its ability to deliver them.

19 If agreed, this initiative will be funded through the Budget 2026 operating allowance.

Consultation

20 In late 2025, we undertook targeted consultation with stakeholders on the policy options. We received submissions from Chartered Accountants Australia and New Zealand (CA ANZ), the New Zealand Law Society, Air New Zealand, Grant Thornton (s 9(2)(a)), Deloitte and the Corporate Taxpayers Group (CTG).

21 Feedback from stakeholders is reflected in this advice. Stakeholders agree with the merits of an exemption from NRCT for aircraft asset leasing and, if an exemption is not viable, stakeholders have indicated support for the introduction of a low-rate final tax for lessees (at a rate of around 2%). Stakeholders noted cases where the need for non-residents to engage with our tax system meant that aircraft leases did not proceed.

22 A number of stakeholders argued in favour of extending the NRCT improvements proposed here to other classes of leased assets in the future.

23 The Treasury has been consulted and agrees that the policy options outlined would contribute to the Government's objectives to simplify the tax system and reduce compliance costs.

Next steps

24 Your decisions will be reflected in the existing Budget 2026 placeholder submission in relation to NRCT and aircraft asset leasing, which will then be subject to confirmation by Budget Ministers and Cabinet.

25 If you agree, the necessary legislative changes could be included in Budget Night legislation with retrospective application from 1 April 2026.

26 The decision sought in relation to NRCT and aircraft asset leasing can be taken in isolation from your decisions in relation to other options for NRCT reform, though some of the decisions sought from you in the forthcoming advice may be complementary (for example, limiting the scope of entities to whom NRCT applies and introducing a standalone tax code for NRCT).

Recommendations

We recommend that you:

1. **Agree** to:

   a. **Introduce** a permanent, by application exemption from non-resident contractors' tax (NRCT) for the leasing of aircraft (excluding aircraft charters) and parts at a total operating cost of $17.850 million across the forecast period. (*Recommended*)

   Agree / Disagree — Agree / Disagree

   Minister of Finance — *Minister of Revenue*

   and

   b. **Note** the following changes to Crown revenue and receipts to give effect to the policy decision in recommendation 1(a) above, with a corresponding impact on the operating balance and net core Crown debt.

	$m – increase / (decrease)				
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Crown Revenue and Receipts: Tax Revenue – PAYE	(1.050)	(4.200)	(4.200)	(4.200)	(4.200)
Total Operating	**1.050**	**4.200**	**4.200**	**4.200**	**4.200**

OR

   c. **Introduce** an opt-in, final tax at a rate of 2% for the leasing of aircraft and parts replacing the need for a lessee to withhold NRCT from contract payments, at a total operating cost of $13.983 million across the forecast period.

   Agree / Disagree — Agree / Disagree

   Minister of Finance — *Minister of Revenue*

   and

   d. **Note** the following changes to Crown revenue and receipts to give effect to the policy decision in recommendation 1(c) above, with a corresponding impact on the operating balance and net core Crown debt.

	$m – increase / (decrease)				
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Crown Revenue and Receipts: Tax Revenue - PAYE Final Tax (tbc)	(1.050) 0.228	(4.200) 0.910	(4.200) 0.910	(4.200) 0.910	(4.200) 0.910
Total Operating	**0.823**	**3.290**	**3.290**	**3.290**	**3.290**

2. **Agree** that under your preferred option in relation to recommendation 1 there will be no tax or filing obligations for the non-resident lessor in relation to the leased aircraft and parts.	
Agree / Disagree *Minister of Finance*	Agree / Disagree *Minister of Revenue*
3. **Agree** that the net reduction in Crown tax revenue in recommendation 1 above be charged against the Budget operating allowance, subject to confirmation by Budget Ministers and Cabinet.	
Agree / Disagree *Minister of Finance*	Agree / Disagree *Minister of Revenue*
4. **Agree** that the initiative should have an application date of 1 April 2026, to be given effect through Budget Night tax legislation.	
Agree / Disagree *Minister of Finance*	Agree / Disagree *Minister of Revenue*
5. **Note** that the departmental operating and capital costs of this initiative will be considered as part of Budget 2026.	
Agree / Disagree *Minister of Finance*	Agree / Disagree *Minister of Revenue*

s 9(2)(a)

Sam Rowe
Policy Lead, International
Policy | Inland Revenue

28 January 2026

Hon Nicola Willis
Minister of Finance
/ /2026

Hon Simon Watts
Minister of Revenue
/ /2026

Inland Revenue
Te Tari Taake

POLICY

TE TAI ŌHANGA
THE TREASURY

Tax policy report: Integrity measures (making imputation work)

Date:	9 October 2024	**Priority:**	Medium
Security level:	Budget Sensitive	**Report number:**	IR2024/383 T2024/2730

Action sought

	Action sought	**Deadline**
Minister of Finance	**Agree** to the recommendations	24 October 2024
Minister of Revenue	**Agree** to the recommendations	24 October 2024

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**	**1st Contact**
Jean Le Roux	Manager, Tax Strategy, The Treasury	s 9(2)(a)	
Claire McLellan	Acting Policy Lead Inland Revenue		
Pawel Borowski	Analyst, Tax Strategy, The Treasury		✓
Casey Plunket	Special Policy Advisor, Inland Revenue		✓

Minister's Office actions (if required)

Return the signed report to Treasury and Inland Revenue.

Note any feedback on	

the quality of the report	

Enclosure: No

Integrity measures (making imputation work)

Purpose

1. At the 15 August 2024 Joint Ministers' meeting, you commissioned further advice on integrity measures. This report explains at a high level the proposed measures and their impact.

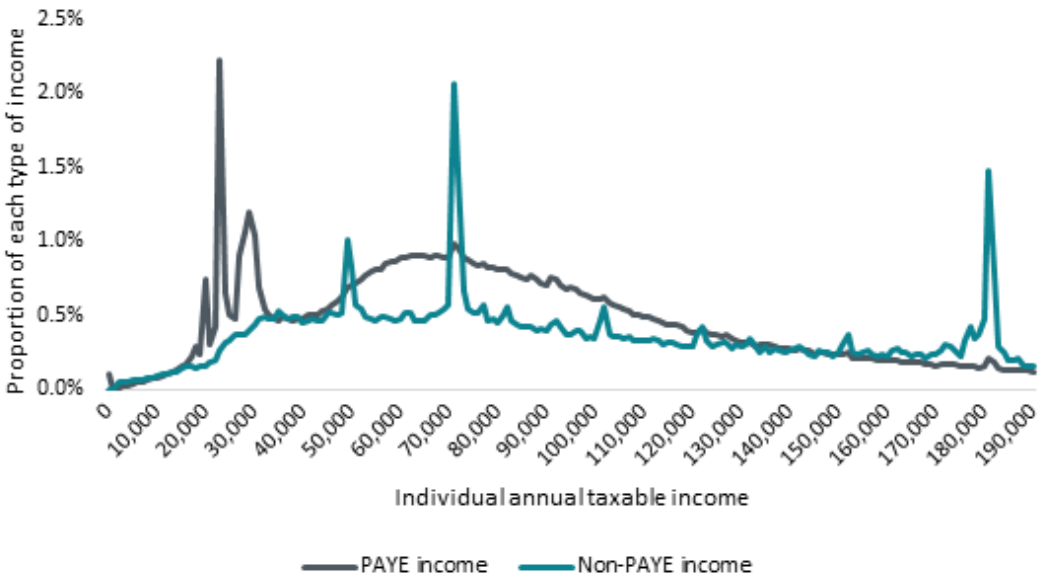
2. We recommend you direct officials to report back in late October 2024 with more detailed advice, including the fiscal implications, economic impacts, compliance costs and administrative implications of such policy.

3. We also seek your agreement to conduct targeted consultation on this issue with a few trusted external stakeholders as soon as possible (October/November 2024).

Problem definition

4. The misalignment between the 28% corporate tax rate and the higher personal rates (up to 39%) creates an incentive for people to earn and retain income in companies. Figure 1 below provides evidence showing how high-income earners have been using companies and trusts to take advantage of lower tax rates.[1]

Figure 1: Taxable income distribution for PAYE and non-PAYE income (2022-23)



Note: This figure compares the distribution of income for people earning PAYE income (mainly employees and those receiving main benefits or New Zealand Superannuation) with other (non-PAYE) income earners. The "spikes" of income at $48,000, $70,000, and $180,000 (the personal tax thresholds at the time) demonstrate that individuals whose income is predominantly non-PAYE have been retaining income in companies and trusts so that the higher personal tax rates do not apply. The increase in the trustee rate to 39% from 1 April 2024 means trusts can no longer be used in this way.

[1] We have previously provided this evidence in T2024/1331, IR2024/248. Please note this graph is based on the personal threshold in place before 31 July 2024. We don't have an updated version of that graph with new thresholds yet.

5. Under current law, corporate income is only taxed at the shareholder's marginal rate when it is distributed as a dividend. On distribution, the imputation credit system ensures that the shareholder pays further tax on income earned through a company equal to the difference between the corporate tax rate and their marginal rate. Taxing the shareholder's income at their marginal rate occurs only on distribution so the shareholder's income can be subject to a final tax of 28% when they sell their shares. This means a shareholder with a marginal tax rate of 30% or above can effectively receive income that is only ever taxed at 28%. This reduces the effectiveness of the personal tax rate scale and has negative impacts on efficiency and horizontal equity. It also makes it difficult to reduce the company tax rate if that is thought desirable to increase foreign investment.

6. Broadly speaking, this project aims to tax more corporate income at the marginal tax rate of the shareholder by taxing some undistributed corporate income at the shareholder rate. This would be a policy shift from the current law outlined above, which only taxes at the shareholder rate when corporate income is distributed as a dividend. As set out above, the reason for the shift is that the current law often does not tax income earned through a company at the shareholder's marginal tax rate at all. We illustrate this problem with an example below.

Table 1: Example of sale of company by shareholder

A company owned by a shareholder with a 39% marginal rate earns $1 million in profits annually and distributes this as dividends to the shareholder. The total annual tax paid is $390,000 per annum: $280,000 by the company (company tax rate of 28%) and $110,000 by the shareholder.

If the owner had run the business directly (as a sole trader, partner or trust) instead of a company, they would pay $390,000 yearly in tax.

Company profits retained and business sale

Instead of paying dividends, the company retains its after-tax profits ($720,000 yearly) for four years, adding up to $2.88 million. The profits may be reinvested in the business or used to acquire passive investments. The company is then sold for $10 million.

The buyer uses a new holding company, funding it with $1 million in equity and a $9 million loan, to buy the operating company.

Tax implications of the business sale

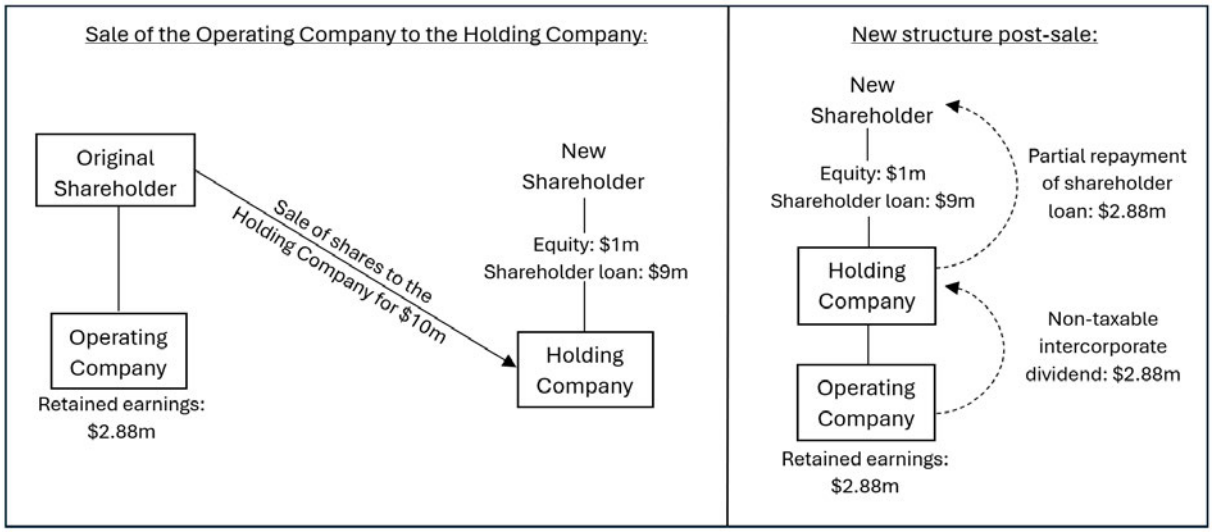
After being sold, the operating company distributes $2.88 million as untaxed (due to the exemption for dividends paid within a wholly-owned group) dividends to the new holding company.

The holding company uses these dividends to repay part of the $9 million loan to the new shareholder.

As a result, no additional tax is paid on the $4 million of income the company made over the four years before the sale. This leads to a $440,000 tax saving compared to the scenario when the company regularly paid dividends to the shareholder, or the shareholder ran the business itself.

Our proposal would involve imposing $440,000 additional tax on the retained earnings in the operating company at the time of sale. This tax could be payable by the shareholder or the operating company.

Figure 2: Illustration of above example



Overview of options

7. We recommend the following options to address the under-taxation of income earned through companies:

   7.1 **Ensuring imputation applies when ownership changes:** We propose an "imputation credit flushing" rule. Under the existing imputation rules, imputation credits are cancelled if a company's ownership changes by 34% or more. The proposed reform would replace this cancellation with a deemed distribution of fully imputed dividends to the company's shareholders. This deemed dividend would be taxed at their marginal rate with a credit for the imputation credits.

   7.2 **Ensuring tax can't be deferred or circumvented through loans to shareholders:** We propose to treat a loan by a company to a shareholder as a dividend, subject to limited exceptions to be determined.

   7.3 **Better information reporting to improve compliance with existing and proposed rules:** New requirements for companies to report information on capital contributed by their shareholders and net capital gains to Inland Revenue.

8. The package of measures could be collectively described as "making imputation work", which is more descriptive than "integrity measures" and signals that these options are about improving the effectiveness of the imputation system rather than being narrowly targeted at tax avoidance.

9. Appendix 1 outlines the specific issues that each of these options is trying to address and describes how and when companies would need to apply the proposed new rules.

These measures can form an efficient and fair source of revenue

10. The proposed measures could raise material tax revenue. We are currently preparing fiscal estimates for the proposed options and will include these in our next report.

11. The proposed measures will improve horizontal and vertical equity by taxing income earned through companies more consistently. They will also improve the tax system's responsiveness to personal and corporate tax rate changes.

These measures have costs and are likely to be opposed by submitters

12. The proposed measures are likely to increase compliance costs. These proposals will also increase the tax paid by the affected companies (mainly companies with a small number of shareholders) or their shareholders. These stakeholders are likely to argue that this runs counter to goals to encourage investment. We propose to advise further on this in a subsequent report. We outline further below the likely opposition by stakeholders.

Consultation

Previous consultation

13. The previous Government consulted in 2022 on similar proposals to ensure imputation applies when ownership changes and improve information reporting. The previous Government ultimately decided to defer the work due to concerns raised by submitters in relation to the ownership changes proposal.[2]

14. Submitters opposed the 2022 proposal on ownership changes. Criticisms included:

    - it was overly broad and unnecessary
    - it was "effectively a capital gains tax" because it would have created a tax bill when shares were sold
    - it could create barriers to succession planning, and
    - practical concerns about the detailed design of the proposal.

15. We have adjusted our proposed approach to the issue to address some of these concerns, particularly around the detailed design of the proposal. In some respects, the new proposal is broader than the 2022 proposal because it applies to all shareholders once a 34% shareholding change has occurred, not just the controlling shareholders. This would mean some shareholders who have not sold their shares would be allocated and pay tax on income that they have not yet realised.

16. We expect stakeholders will oppose our new proposal, however as outlined above we still recommend further consideration of this option, our initial view is that it would improve the fairness and efficiency of the tax system.

17. Stakeholders were generally supportive of the 2022 proposal for more information sharing.

18. We have not previously consulted on our proposal to address issues with loans to shareholders. We expect many stakeholders will oppose the proposal and will argue it is unnecessary or an overreach.

We recommend further external consultation

19. We recommend you agree to officials conducting limited targeted external consultation to test both the problem definition and the options we are developing.

20. We anticipate complex design questions will arise as we continue to work through the proposal. We believe consultation is necessary to identify any fundamental issues with the proposal. External consultation could also allow officials to better understand

[2] The reports to the previous Government following the 2022 submissions are publicly available here: https://www.taxpolicy.ird.govt.nz/publications/2022/2022-ir-dividend-integrity-psa-reports

the potential effectiveness, feasibility and compliance costs of the proposed measures.

21. We recommend any initial consultation be with a few trusted external tax practitioners in October and November 2024. This would be on a strict in-confidence basis and aim to test our problem definition and check the options are workable. We would emphasise that officials are exploring the issue and a range of options, but no decisions have been made yet. While this consultation is likely to occur too late to inform the detailed advice due in October, to the extent it exposes any fundamental issues, we will report back to you, likely in late November or early December. If you prefer the next piece of advice to be informed by the consultation, please note this would mean the next advice would be provided to you mid-November at the earliest.

22. Following this, we recommend wider external consultation. We believe wider consultation is necessary to finalise the design of the measures before the proposal could be legislated. There would also be value in consulting more widely on the problem definition, however this would be challenging on Budget 2025 timelines because a well-developed and fully costed proposal will be required prior to Budget Day announcements.

23. We will provide further information on options for consulting on this project. These would include a discussion document in 2025 consulting on the detailed design to enable revenue to be recognised for Budget 2025 or a discussion document that allows for broader consultation and work to progress for Budget 2026. There are also options to conduct in-confidence consultation with a broader group of stakeholders ahead of Budget 2025.

Next steps

24. We recommend you direct officials to report back to you in late October 2024 including updated fiscal estimates, analysis of economic impacts, compliance costs and administrative implications. Subject to your agreement, officials will also begin consulting a few trusted external tax practitioners in October and November 2024.

25. Our late October report will seek your decisions on whether to proceed with developing a proposal that could be announced as part of Budget 2025, externally consulted on in 2025, and implemented from April 2027.

Recommended action

a. **Agree** to officials providing further advice on ensuring imputation applies when ownership changes.

Agreed/Not agreed	Agreed/Not agreed
Minister of Finance	*Minister of Revenue*

b. **Agree** to officials providing further advice on ensuring tax cannot be deferred or circumvented through loans to shareholders.

Agreed/Not agreed	Agreed/Not agreed
Minister of Finance	*Minister of Revenue*

c. **Agree** to officials providing further advice on better information reporting to improve compliance with tax law relating to corporate distributions.

Agreed/Not agreed
Minister of Finance

Agreed/Not agreed
Minister of Revenue

d. **Agree** to officials conducting limited, targeted external consultation on the issue and potential options with a few trusted external tax practitioners on an in-confidence basis in October/November 2024.

Agreed/Not agreed
Minister of Finance

Agreed/Not agreed
Minister of Revenue

e. **Indicate** whether you prefer detailed advice to be provided in late October 2024 without input from targeted consultation or to be provided in mid-November 2024 with input from targeted consultation.

October 2024/November 2024
Minister of Finance

October 2024/November 2024
Minister of Revenue

s 9(2)(a)

s 9(2)(a)

Jean Le Roux
Manager, Tax Strategy
The Treasury

Claire McLellan
Acting Policy Lead
Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2024

Hon Simon Watts
Minister of Revenue
/ /2024

Appendix 1: Details of main policy options

Ensuring imputation applies when ownership changes

26. If a company has earned taxable income, it can distribute the income to its shareholders as an imputed dividend (cash plus an imputation credit). The cash and the imputation credit are both taxable, but the imputation credit also gives the shareholder a tax credit that is used to ensure that the shareholder only pays further tax on that income equal to the difference between the corporate tax rate and their marginal rate.

27. Companies can also accumulate profits instead of distributing them as dividends. Their shareholders can realise the value of these retained earnings by selling their shares. Unlike dividends, the proceeds of a share sale are generally not taxable income. Furthermore, the buyer of the shares can often structure its acquisition so that unlike the seller, it does not recognise taxable income when the company distributes its retained earnings.

28. Under the existing imputation rules, imputation credits are cancelled if a company's ownership changes by 34% or more, for example because there has been a sale of shares or the company has issued further equity to enable further investment. The proposed reform would replace this cancellation with a deemed distribution of fully imputed dividends to the company's shareholders. This would distribute the imputation credits before they are lost. As with ordinary dividends, these deemed dividends would be income for the shareholders, with a credit for the imputation credits.

Ensuring tax can't be deferred or circumvented through loans to shareholders

29. As an alternative to paying a dividend, some closely held companies may instead lend funds to their major shareholders. This allows a shareholder to access company funds while deferring the additional tax that would arise when a dividend is paid to the shareholder (although some tax is collected on the loan interest paid to the company).

30. In addition, if the loan is not repaid, the forgiveness of the loan is not always correctly recognised as taxable income to the shareholder because the processes around the wind up of closely held companies without other unrelated creditors can lack transparency. In this case, the tax is permanently avoided. In other cases, any additional tax may be reduced by the time the loan is eventually forgiven because the shareholder may have moved offshore and become non-resident or moved onto a lower rate tax bracket because they now earn less income or have retired. Lastly, the tax treatment of shareholder loans makes shareholder-level tax easier to eliminate by way of a share sale, since it enables the shareholder to have use of excess company funds without paying the top-up tax.

31. There are several options that could attempt to deal with these issues. These include:

    - treating the loan as a deemed dividend unless it is repayable within a certain timeframe, or properly documented and on commercial terms
    - ensuring the forgiveness of the loan results in taxable income being correctly reported
    - requiring additional information to be reported to Inland Revenue on shareholder loan accounts.

Better information reporting to improve compliance

32. Distributions by a company are not taxable to the extent they are either returns of capital contributed by their shareholders (referred to as "available subscribed capital") or because they represent the distribution of net capital gains at the time the company is liquidated.

33. In practice, measuring these amounts can be difficult because the calculation of the amounts involved is complicated and requires the maintenance of records over a long period of time.

34. The information reporting proposal requires entities to maintain, and potentially submit to Inland Revenue, tracking accounts of the relevant amounts on an annual basis. This would improve compliance with existing rules, although it would impose compliance costs and administrative costs to implement.

Inland Revenue
Te Tari Taake

POLICY

TE TAI ŌHANGA
THE TREASURY

Tax policy report: Advice on integrity measures

Date:	11 December 2024	**Priority:**	Medium
Security level:	Budget Sensitive	**Report number:**	IR2024/423 T2024/3336

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to the recommendations	21 January 2025
Minister of Revenue	**Agree** to the recommendations	21 January 2025

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Jean Le Roux	Manager, Tax Strategy, The Treasury	s 9(2)(a)	
Claire McLellan	Acting Policy Lead, Inland Revenue		
Paul Quirke	Senior Analyst, Tax Strategy The Treasury		✓
Gordon Witte	Principal Policy Advisor, Inland Revenue		✓

Advice on integrity measures

Executive summary

Purpose and policy objectives

1. This report seeks decisions on proposals which aim to improve the integrity of the tax system and raise revenue in an efficient manner by ensuring more income earned through companies is taxed at the shareholders' marginal tax rates. It follows a previous report on the policy problem (IR2024/383, T2024/2730 refers).

2. Shareholders of closely held companies often borrow from their company or sell their shares to new owners. These arrangements are more "tax efficient" than paying dividends, as they allow the shareholder to receive funds without being taxed at their marginal tax rate (typically 39% for high-income individuals and trusts). However, they are common commercial practices (particularly share sales) and so cannot be said to have a main purpose of minimising tax.

3. That said, our data indicates there is a very large and growing use of loans by companies to their shareholders which we believe is significantly influenced by the fact that loans allow the shareholders to access cash without paying tax. The UK, Canada, Australia and US address this issue by deeming unpaid loans be taxed as dividends in certain circumstances. We propose developing similar rules to ensure tax cannot be deferred or circumvented through loans to shareholders.

4. We also propose an 'imputation credit flushing' rule to ensure retained earnings are taxed at the shareholder's tax rate when company ownership changes. This would replace the current rule which cancels imputation credits when ownership of the company has changed by 34% or more, with a new rule which would require the imputation credits to be attached to a deemed distribution of dividends to the company's shareholders.

Policy impacts

5. The proposals would improve horizontal and vertical equity, and they improve the Government's ability to effectively adjust personal and corporate tax rates.

6. The proposals would reduce some tax motivated behaviours, thereby improving efficiency. But they would also create new incentives for tax planning behaviour, especially if alternative avenues to minimise tax remain available.

7. The impact of these proposals on investment incentives is unclear. International comparisons are inconclusive and difficult to apply to these proposals. To some extent these proposals can discourage some investments, especially for equity-dependent businesses, but less so than a headline increase to a dividend tax would.

8. The number of affected taxpayers and their tax liabilities are highly uncertain due to potentially strong behavioural responses.

9. The loans to shareholders proposal could affect up to 23,000 shareholders. The additional tax is highly concentrated, with 700 shareholders facing potential tax liabilities of over $500,000 contributing to almost half of the total tax revenues. However, we expect that many affected shareholders would try to repay their loans rather than pay additional tax if they have funds available to do so.

10. The imputation credit flushing proposal could apply to 1,500 companies per year. 1,200 of these companies would pay less than $10,000 of additional tax under the proposal, but 70 companies may face a significant tax liability of more than

$500,000 each. We expect many of these company owners will respond to the proposal by setting up holding companies to own their shares, which would defer the tax liability that would otherwise arise when the shares are sold.

Fiscal implications

11. The revenue raised by these proposals is potentially significant but also highly uncertain. We expect strong behavioural responses to these proposals which can significantly reduce the revenue raised.

12. Due to the complexity of the proposals, it would be necessary to consult on the policy in 2025 and legislate using a full Bill process in 2026. Officials consider they could not be implemented until April 2027 as earlier implementation would have a significant risk of unintended consequences. This means the additional tax revenue would be collected from the 2028/29 fiscal year.

Problem and policy objectives

13. Shareholder salaries and dividends are taxed at the shareholder's tax rate (typically 39% for high-income individuals and trusts). However, the use of drawings and other types of company loans to shareholders or a sale of shares in a company with retained earnings allow shareholders to receive amounts without being taxed at their marginal tax rate.

14. These arrangements are common commercial practices and do not necessarily aim to minimise tax. As such, they are not seen as a problem by external stakeholders. They do however result in lower revenue raised and create horizontal and vertical inequities, as well as some economic inefficiencies.

15. The policy objective of these proposals is to ensure more income earned through companies is taxed at the shareholders' marginal tax rates by limiting any tax advantage that can be gained for shareholders through loans or the sale of a company relative to the payment of a dividend.

Ensuring tax is not deferred or circumvented through loans to shareholders

16. Shareholders of closely held companies often borrow funds from their company. This includes formal loan contracts and informal drawings where the owner simply keeps an accounting record of the amounts they have withdrawn from the company. If the loan is not repaid within a short period, it can be a tax efficient substitute for a dividend.

17. The shareholder can use the cash from the loan while the company will pay only a small amount of tax each year on the interest income it receives. The company may later forgive the loan, which generates a taxable dividend for the shareholder, but this can be timed to occur years later when the shareholder has moved to a lower tax rate or moved overseas (non-residents are not subject to New Zealand tax on fully imputed dividends).

18. Tax can be eliminated altogether if the loan is repaid at the time the company is sold, using the proceeds of the sale to fund the repayment. In some cases, the company will be wound-up without the loan being repaid. This eventually leads to any loans being forgiven, but the existence or tax consequences of the loans is easily overlooked, making it difficult to collect the tax.

19. The very large and growing amount of loans made by companies to shareholders suggests that at least some of these loans are made to minimise tax liabilities. The reported stock of outstanding loan balances was about $8 billion in 2022/23 and had grown by $940 million compared to 2021/22. About 23,000 shareholders owed these amounts to their companies and over 3,500 of these shareholders owed more than $1 million each to their companies.

20. New Zealand has few tax rules applying to loans to shareholders which makes it easier to minimise tax through loans than in other OECD countries. Loans become taxable dividends only if the loan is forgiven.

21. In contrast, the UK, Canada and Australia deem a dividend to arise for a shareholder loan if it has not been repaid within a certain time period. Their rules offer, however, various exceptions. Norway immediately taxes all shareholder loans as dividends. The OECD has recently recommended countries adopt stricter rules for shareholder loans.[1]

22. At this early stage, officials consider the most effective way to address the problems would be to treat any loan provided by a company to a shareholder as a dividend if the shareholder has not repaid the loan within a short time period, for example, by the end of the year following the year the loan is made. A time limit recognises that while the use of shareholder loans is an accepted commercial practice for managing cashflow, after a certain period of time there is a stronger case that the loan is being used as a substitute for a dividend. This approach would be similar to the UK and Canada's comprehensive rules. Based on current taxpayer behaviour, this could impose tax on a very large amount of New Zealand loans, if applied to the full historic loan balance.

23. As an alternative to the comprehensive option, a narrower option could be to deem loans as dividends unless they are properly documented and are made on commercial terms. This approach is adopted by the Australian and the US tax systems, but their rules allow for a longer period of repayment (such as 7 years in Australia). Compared to a more comprehensive reform, we consider this approach to be much less effective at reducing the opportunities for tax minimisation. It would also create more compliance issues for taxpayers and administrative issues for Inland Revenue, due to the need for significant documentation and information collection.

Ensuring income earned through companies is taxed when ownership changes

24. Instead of distributing company profits as taxable dividends, the shareholders may choose to retain the funds in the company. The shareholder will eventually realise the value of these retained earnings when selling the company to new shareholders.

25. The sale of the company by the original shareholders will be an untaxed capital gain. Tax will usually not apply when company's retained earnings are distributed to the new owners because typical acquisition structuring allows for the profits to be considered a non-taxable return of capital invested by the purchaser.

26. To address this issue, we propose an "imputation credit flushing" rule. This would apply the shareholder's tax rate to a company's undistributed earnings when ownership of the company changes by 34% or more. Under the existing imputation rules, imputation credits are cancelled if a company's ownership changes by 34% or more. The proposed reform would replace this cancellation with a deemed distribution of fully imputed dividends to the company's shareholders. This would achieve the same tax outcomes as cases where a company distributes its profits as imputed dividends to its shareholders.

27. The purpose of imputation credits is to allow shareholders a credit for the income tax the company has already paid, so that company profits are not taxed twice. When company profits are distributed as a dividend, imputation credits are attached, and the receiving shareholder pays a top-up of tax to their marginal rate (e.g. 11% for a shareholder with a 39% tax rate receiving a fully imputed dividend). Deeming a dividend to the extent there are imputation credits that would have otherwise been cancelled serves the purpose of making the imputation system more

[1] OECD Working Paper *Tax arbitrage through closely held businesses: implications for OECD tax systems* 7 October 2024, paragraph 71.

effective at ultimately taxing corporate income at the marginal rate of its shareholders. In this context, imputation credits can be considered a proxy for the otherwise difficult task of separating taxable income from capital and other aspects of the company's value on sale. Because imputation credits are only held by a company to the extent there has been taxable income, they do not arise where value is shareholder capital or capital gains.

28. The proposal is similar to a proposal consulted on by the previous Government in 2022 which would have applied tax to share sales by controlling shareholders to the extent the company had retained earnings. Submitters opposed the 2022 proposal because they considered it was unnecessary and "effectively a capital gains tax" on share sales and could create barriers to succession planning. They also had practical concerns about the design of the proposal.

29. In some respects, the new proposal is more practical. It only applies to the extent the company has imputation credits (rather than where it has retained earnings, which is difficult to measure) and only once there has been an ownership change of at least 34% (companies are already required to monitor this threshold). However, it would also apply more broadly because shareholders who have not sold their shares would be required to pay tax on a deemed amount of income that they have not yet realised. In most cases, all the shareholders would be selling their shares (as the affected company will usually have a few shareholders who are selling all or most of their shares). In cases where there are non-selling shareholders any tax obligations could be met by a pre-sale dividend. Any deemed dividend will enable them to receive earnings from the company tax free in the future. In effect, a deemed divided would work as if shareholders got a distribution and reinvested it into the company.

30. We note that while Australia has an imputation system, they do not cancel imputation credits when a company is sold. However, their capital gains tax reduces the tax advantages from selling shares instead of paying dividends.

Improved information reporting to support compliance

31. Better information reporting to Inland Revenue could be used to improve compliance with existing dividend rules and the proposed new rules. However, on its own, this would not result in any change to the taxation of income earnt through companies.

32. For example, capital contributed by a company's shareholders and net capital gains can be distributed to shareholders without being considered a taxable dividend. However, there is no requirement to report these amounts to Inland Revenue, so compliance is difficult to verify. As part of their annual imputation account returns, there could be new requirements for companies to report to Inland Revenue information on these amounts. If the relevant amounts are not reported and the company then distributes funds to its shareholders, the payments could be assessed to be a taxable dividend.

Economic impacts

The proposals would reduce some current biases in the tax system

33. The proposals would improve the horizontal equity of the tax system. They would tax income earned through companies more consistently with income which has been distributed as dividends or earned by natural persons (such as employees) or through other types of businesses (such as sole traders, partnerships or trusts).

34. Similarly, vertical equity would be improved. Under current rules, the owner of a closely held company may face tax on earnings of over $180,000 at 28% which may be a lower tax rate than someone earning less income directly.

35. The proposals would reduce the economic and fiscal costs of future tax reforms. The current policy settings make it more costly to reduce the corporate tax rate because it would incentivise the New Zealand resident owners of closely held companies to recharacterize their labour income as company income or retain profits in the company. These proposals would reduce, though not eliminate, these incentives.

36. At the same time, whenever specific measures are brought in to reduce income shifting or similar tax planning, we can expect new methods of tax planning to emerge which would reduce the overall effectiveness of the proposals.

Impacts on investment are unclear but can be negative for some businesses

37. The proposals would not represent an increase to headline dividend taxation, but they would, at a high level, increase the taxation of dividends by broadening the base of amounts which are deemed as dividends. As such, the proposed measures will embed the impact of higher top personal tax rate on cost of capital for business investment by closely held companies. This would have some negative impacts on business investment in New Zealand.

38. Based on international literature, we expect the proposals to have some negative impact on investment, though these are unclear and would depend on the type of businesses they affect. The international literature on the impacts of increasing headline tax rates on dividends is not particularly conclusive, and its implications cannot be easily applied to the proposals.

39. Some recent empirical studies suggest that dividend taxes do not reduce investment in aggregate.[2] This is especially true for 'cash-rich' companies which do not rely on domestic shareholders. 'Cash-constrained' companies may still be negatively impacted due to the higher costs of capital.

40. The literature also suggests that changing the tax rate on dividends could distort the allocation of capital as it has a larger impact on cash-constrained firms compared to those which can fund investment out of their retained earnings.[3]

41. Evidence from the UK on owner-managed businesses found that while these companies respond to dividend tax increases by retaining more earnings, they tend to hold more current assets (e.g. bank deposits), rather than invest the funds into the company's capital stock.[4] In such cases, the overall amount that the company invests back into their business is unchanged. This suggests that whether the proposals decrease or increase retained earnings, businesses investment decisions may remain unchanged.

42. Comparisons with other countries are, however, difficult because, unlike the countries studied, New Zealand has an imputation system which encourages the use of dividends and allows Portfolio Investment Entities (PIEs) to distribute income without any top-up tax.

43. Because PIEs currently face a final tax rate of 28% (with no further tax on distributions), the proposals would make investing through PIEs relatively more attractive than investing into the affected closely held companies. s 9(2)(f)(iv)

[2] Sobeck, K., Breunig, R., and Evans, A. (2022), Corporate income taxation in Australia: Theory, current practice and future policy directions, Tax and Transfer Policy Institute (TTPI) Policy Report No. 01-2022, Canberra, Australia pp 15-20
Koivisto A. (2023), Tax planning and investment responses to dividend taxation, FIT working Paper 15, pp 37
[3] Alstadsæter A., Jacob M., Michaely R. (2017), *Do dividend taxes affect corporate investment?* Journal of Public Economics, Volume 151, Pages 74-78
[4] Miller, H., Pope, T., and Smith, K (2021), *Intertemporal income shifting and the taxation of owner-managed businesses*, IFS working Paper W19/25

Furthermore, investment in companies and PIEs are not perfect alternatives because PIEs can only be used for passive portfolio investment which is a different type of investment to the active, owner managed companies that the proposals would impact. s 9(2)(f)(iv)

Specific impacts of shareholder loans proposal

44. The shareholder loan rule would incentivise shareholders to repay the loans within the prescribed time limit to avoid triggering a tax liability. This could lead to more cash being retained in the company.

45. Some shareholders will experience cashflow difficulties if they have already spent the cash they originally borrowed but will now need to repay the remaining balance or incur a tax liability. This may disproportionately affect a subset of 700 shareholders who will face potential tax liabilities exceeding $500,000 per shareholder and who are expected to contribute nearly half of the additional tax revenue.

46. Some shareholders would not repay their loans, but this would not necessarily directly reduce investment. For some companies, the alternative to repaying the loan would be a distribution of earnings as dividends, in which case there would be no adverse effect on investment. For others, the alternative would have been to eventually invest the earnings into capital stock, but due to temporary cashflow difficulties, the shareholders were unable to repay their loans. To address this and reduce the potential for the tax to impact investment, the proposal would offer a tax refund for shareholders who repay the loan eventually as this would allow them to invest the total borrowed amount.

Specific impacts of imputation credit flushing proposal

47. The imputation credit flushing rule would remove an incentive for owners to sell their companies in order to receive value from the retained earnings without additional tax. However, in so doing, it may also distort other behaviours. For example, small shareholders may wish to exit companies before imputation flushing provisions are breached which would prompt some shareholders to negotiate new shareholder agreements to protect themselves from the actions of other shareholders. It may also introduce inefficient "lock in" effects where businesses that would usually be sold or passed on to the next generation are retained to avoid triggering the tax liability.

48. The imputation credit flushing proposal would deem a taxable dividend which was not paid in cash. This can create cashflow issues for companies which may not have the funds to pay a withholding tax at the time the dividend is deemed. Similarly, shareholders would be deemed to receive taxable income, even if they have not sold their shares and would therefore not have cash.

49. The imputation credit flushing rule would decrease the retained earnings in a company. However, given that these earnings are currently realised at sale rather than invested, we do not anticipate the rule to directly decrease companies' investment. It would however lower the amount of the affected company's savings, which in turn can reduce its financial stability, especially for smaller firms which rely more heavily on corporate savings during downturns.

The proposals increase tax and compliance costs for owners of closely held companies

50. The proposed measures would mainly apply to closely held companies (with less than 5 shareholders) owned by New Zealanders, for example, larger family-owned or controlled businesses. They are unlikely to affect widely held businesses such as

NZX-listed companies which distribute a larger percentage of their profits as imputed dividends, which for tax purposes are generally treated as not subject to ownership changes, and which do not make loans to their shareholders.

51. The proposals would have no direct impact on shareholders who are non-residents or PIEs (such as managed funds or KiwiSaver) because they do not pay any top-up tax on fully imputed dividends.

52. The impact on small businesses differs depending on the proposed measure. For example, providing a loan to a shareholder may be more common among small companies but selling shares may be rare as most small businesses are sold to new owners by selling the business assets rather than company shares.

53. The shareholder loans and imputation credit flushing proposals would impose new compliance costs on companies as they would need to seek tax advice and closely monitor changes in ownership and their loans balances to their shareholders. These compliance costs are likely to be large in the aggregate, because the proposals can potentially apply to a large number of companies and shareholders (as described in the fiscal implications section below). However, for an individual company the incremental increase in compliance costs is expected to be low.

54. The information reporting proposal would impose additional compliance costs on companies with imputation credit accounts (about 450,000 companies) because they would need to report on changes to available subscribed capital and net capital gains as part of their annual imputation credit account returns. For most companies, the amounts may not ever become relevant to determining their tax liabilities. Therefore, there would be an option to not the report the amounts to forego incurring these compliance costs.

Consultation is required to develop the proposals

55. These proposals are complex and require consultation to identify and mitigate practical issues before the new rules can be finalised and announced. We recommend consulting on these proposals during 2025 with the aim to announce the proposals at Budget 2026 and implement on 1 April 2027.

56. Stakeholders are likely to strongly oppose the proposals. We expect pushback on the proposals since they would increase both compliance costs and the tax paid by the affected companies (mainly companies with a small number of shareholders). Furthermore, reclassifying share sales and loans as taxable dividends may be perceived as penalising taxpayers engaged in common and legal practices which are not necessarily aiming to minimise tax.

Fiscal implications

Loans to shareholders

57. The loans to shareholders proposal would involve treating loans to shareholders as dividends in some circumstances. There are a range of design options. We have produced an indicative fiscal estimate for the most comprehensive option which is similar to the UK's rules.[5] The costing also assumes that there will be a deemed dividend arising for the existing stock of loans. Changes such as excluding the historic stock or phasing the deemed divided in for historic loans, would significantly reduce the upfront fiscal impact of the proposal. Narrower options such as developing rules similar to Australia's are expected to apply to far fewer loans and would therefore collect much less additional tax revenue. The costing should be

[5] We have assumed the proposal would apply to loans made by companies with outstanding loan balances to their shareholders that exceed $50,000 for two consecutive years.

used indicatively, and we will need to re-cost the proposal based on design decisions that would need to be made if the work is to be progressed.

58. With a commencement date of 1 April 2027, we would expect that both reporting companies and the relevant shareholders would be filing their income tax returns during the 2028/29 fiscal year. We have estimated this could result in additional tax revenue of $1,180 million in 2028/29 as shown in the following table:

	$ million increase / (decrease)				
Vote Revenue **Minister of Revenue**	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29**
Tax Revenue: Other persons tax	0.000	0.000	0.000	0.000	1,180.000
Total operating	**0.000**	**0.000**	**0.000**	**0.000**	**(1,180.000)**

NB: The 2028/29 revenue is one-off; the forecast revenues are $155 million per year from 2029/30 and outyears.

59. The forecast additional tax revenues would decrease to $155 million per year from 2029/30 and subsequent outyears. The reason why the first-year estimate for 2028/29 is much higher than later years is the proposed rule would effectively apply to the total accumulated stock of unpaid loan balances for such companies in 2028/29. From 2029/30 and future years, the rules would then apply to the annual net flow of loans (i.e. new lending less shareholder repayments).

60. These fiscal impacts are highly uncertain and there is a downside risk that this measure collects much less revenue than these estimates.

61. We expect many taxpayers are likely to change their behaviour (such as repaying loans earlier or choosing to retain the funds in the company) to not trigger an additional tax liability. The concentration of the forecast additional tax in a relatively small number of companies with high-value loans to their shareholders could increase the risk of potential behavioural changes.

62. Although we have assumed there could be a 50% reduction in the value of outstanding loan balances compared to the current data, the potential behavioural response is very uncertain. For example, if all the shareholders were to repay the loans within the prescribed time limit, no additional tax revenue would be collected.

63. We have estimated that about 23,000 shareholders could potentially face additional tax. The additional tax is highly concentrated, with 700 shareholders facing potential tax liabilities of over $500,000 contributing to almost half of the total tax revenues.

Estimated additional tax that the shareholder may need to pay in 2028/29	**Number of shareholders**	**Percent of total additional tax**
Less than $10,000 of additional tax	5,200	1%
$10,000 to 50,000	10,300	11%
$50,000 to 100,000	3,400	10%
$100,000 to 500,000	3,500	30%
More than $500,000 of additional tax	700	47%
All shareholders	**23,100**	**100%**

64. The industries most impacted would be property and real estate services (27.4% of the total additional tax), agriculture (16.4%), finance[6] (9.1%), professional services (5.9%) and construction services (5.2%).

65. There will be different outcomes for shareholders who have the financial means to repay their loans and those that do not. Shareholders who are able to repay their loans would not face additional tax. However, other shareholders who are unable to repay their loans within the prescribed time period will incur additional tax which they may not have the ability to pay (for example, if they have already spent the cash they originally received from the loan). This would lead to an increased level of tax debt which will add to the current levels of debt and might mean that the received tax receipts will be significantly lower than those forecasted.

66. Some of the amounts loaned by companies to shareholders may have been funded from capital gains previously made by the company. Some of these companies could respond to the proposed tax on loans by choosing to wind up the company instead, as capital gains can be distributed with no additional tax if the company is wound up. This behaviour would further reduce the number of shareholders who ultimately pay any additional tax.

Imputation credit flushing

67. We have estimated the imputation credit flushing proposal could generate additional revenue of $55 million per year from 2028/29 and outyears as displayed in the following table:

	$ million increase / (decrease)				
Vote Revenue **Minister of Revenue**	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29 & Outyears**
Tax Revenue: Other persons tax	0.000	0.000	0.000	0.000	55.000
Total operating	**0.000**	**0.000**	**0.000**	**0.000**	**(55.000)**

68. We have estimated that about 1,500 companies could potentially pay additional tax under this proposal. About 1,200 companies would face additional tax of less than $10,000. However, about 70 companies could pay additional tax of over $500,000, and these 70 companies would contribute to 80% of all the additional tax revenues.

69. There is a risk that the proposal collects much less revenue as these estimates are based on current data and assume that the companies and shareholders do not change their behaviour to try to minimise the impact of the proposal.

70. For example, a likely behavioural response would be for company owners who are natural persons or trusts to hold their shares through personal holding companies, which they own 100%. This would mean that the deemed dividend arising from changes of ownership would be derived by the personal holding company, and not subject to any additional tax. While this arrangement would defer the payment of additional tax, the tax would eventually arise if the natural person or trust received a dividend from the personal holding company or sold it.

Information reporting

71. The information reporting measures are mainly intended to improve compliance with the existing rules for taxing dividends. They would not directly increase tax revenue.

[6] Finance may include holding companies for corporate groups operating in other industries.

Administrative implications

72. Inland Revenue considers that it can successfully implement the initiatives discussed in this report assuming a 1 April 2027 start date.

73. All three measures combined would require medium implementation effort (approx. $1 million - 2 million one-off cost) and medium ongoing effort (approx. $1 million - 2 million per year cost). The company loans to shareholders proposal would require medium implementation effort. However, depending on system decisions such as increased automation/pre-population, the quality of the data which is collected in the proposed returns should improve, which should decrease the ongoing administration effort over time. The imputation credit flushing and information reporting proposals would require a small implementation effort.

74. If this workstream was progressed as part of Budget 2025, Inland Revenue would seek funding as part of the Budget process to fund this initiative. Inland Revenue has limited capacity to implement Budget 2025 initiatives and maintain the current system. Once the scope, scale and timing of all Budget 2025 initiatives is clearer, Inland Revenue will report on its ability to deliver them. Inland Revenue will submit a placeholder bid for this initiative into the Treasury CFISnet on 23 December 2024. The placeholder will be contingent on the Minister of Finance inviting this initiative into the Budget 2025 process. Inland Revenue will update this placeholder bid, including revenue impacts and administration costings, as policy decisions are made.

Next steps

75. We recommend progressing work on the proposed measures. If you wish to progress policy work on these proposals, we recommend doing so on a timeline that would allow revenue to be included in the Budget Economic and Fiscal Update 2026. This would provide more time for further analysis and consultation before a final decision would need to be made. Particularly for shareholder loans, we would recommend consulting on the problem highlighted by the data we are analysing. We want to better understand the nature and size of the problem and whether the approaches taken in other countries would be an effective way of addressing it. Working with external stakeholders on this would, in our view, give the project a greater chance of success.

76. If you want to progress policy work on a timeline that would allow revenue to be included in the Budget Economic and Fiscal Update 2025, we still recommend conducting consultation on policy design details prior to announcement. This would be on a confidential basis with a group of targeted stakeholders. There would be very little time available for consultation before the deadline for Budget decisions. Therefore, this option carries a higher risk and significant downside risk to the revenue raised by the measures.

77. Both timelines would mean implementing the proposals from 1 April 2027, with the resulting revenue arising from the 2028/29 fiscal year onwards. The difference is whether this future revenue is included in the Budget forecasts produced in 2025 or in 2026.

78. Whichever timeline you choose, if you wish to progress work on the proposed measures, we will prepare consultation materials and a Cabinet paper and regulatory impact statement for inclusion of the proposals in the omnibus taxation bill introduced in 2026. This would commit tax policy resource to developing the proposals which may reduce our ability to progress other tax policy work.

79. If we are working to a Budget 2026 timeline, the consultation material will be more open so that we can better engage with stakeholders on the problem and development of the proposals. If we are working to a Budget 2025 timeline the

consultation material will necessarily be more restrictive in scope and will focus on detailed design of pre-determined proposals.

80. Future reporting would occur in March 2025 and focus on the development of the detailed design and any consultation materials.

Recommended action

81. We recommend that you:

Agree to one of these options for company **loans to shareholders**:	**Minister of Finance**	**Minister of Revenue**
Option 1 – Progress the policy work on a timeline that would allow revenue to be included in the Budget Economic and Fiscal Update 2026 (**Inland Revenue and the Treasury's preferred option**).	Agreed Not agreed	Agreed Not agreed
Option 2 – Progress the policy work on a timeline that would allow revenue to be included in the Budget Economic and Fiscal Update 2025.	Agreed Not agreed	Agreed Not agreed
Option 3 – Stop further policy work on this issue and reallocate the resource to other tax policy priorities.	Agreed Not agreed	Agreed Not agreed
Agree to one of these options for **imputation credit flushing:**		
Option 1 – Progress the policy work on a timeline that would allow revenue to be included in the Budget Economic and Fiscal Update 2026 (**Inland Revenue and the Treasury's preferred option**).	Agreed Not agreed	Agreed Not agreed
Option 2 – Progress the policy work on a timeline that would allow revenue to be included in the Budget Economic and Fiscal Update 2025.	Agreed Not agreed	Agreed Not agreed
Option 3 – Stop further policy work on this issue and reallocate the resource to other tax policy priorities.	Agreed Not agreed	Agreed Not agreed
Agree to progress work on improved **information reporting** to support compliance.	Agreed Not agreed	Agreed Not agreed

s 9(2)(a)

Jean Le Roux
Manager – Tax Strategy
The Treasury

s 9(2)(a)

Claire McLellan
Acting Policy Lead
Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2024

Hon Simon Watts
Minister of Revenue
/ /2024

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **Loans to shareholders – case studies and data from company liquidations**

Date:	14 May 2025	**Priority:**	Low
Security level:	Sensitive	**Report number:**	IR2025/165

Action sought

	Action sought	Deadline
Hon Nicola Willis Minister of Finance	**Note** the contents of this report	5 June 2025
Hon Simon Watts Minister of Revenue	**Note** the contents of this report	5 June 2025

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Claire McLellan	Acting Policy Lead, Inland Revenue	s 9(2)(a)	
Gordon Witte	Principal Policy Advisor, Inland Revenue		✓

14 May 2025

Minister of Finance
Minister of Revenue

Loans to shareholders – case studies and data from company liquidations

Purpose

1. This report provides case studies and data from liquidations, in response to your request. This relates to a consultation document that officials are drafting on proposals to improve the taxation of company loans to shareholders and distributions on liquidation.

Background

2. A company can be liquidated when it is unable to pay Inland Revenue or other creditors. In some cases, the company will have made loans to its shareholders, either formally or by taking drawings from the company's current account (including payments to third parties for the owner's private expenses). Non-repayment of these loans is often the reason a company is unable to pay its creditors.

3. Ministers asked officials to work with MBIE to provide case studies and data from company liquidations which illustrate this problem. We consulted with MBIE and the Treasury to prepare this report.

4. Officials are currently preparing a draft consultation paper to publicly consult on proposed new tax rules to ensure tax cannot be deferred or circumvented through companies providing loans to their shareholders instead of paying dividends. We will provide you the draft paper in June alongside a Cabinet paper seeking approval to release the paper for public consultation in July 2025.

5. The proposals are intended to address an integrity risk that arises because shareholders can borrow money from their companies tax-free. The proposals would treat the loan as a taxable dividend in cases where the shareholder has borrowed a material amount of money from a company and has not paid the money back by the end of the following tax year (or prior to the company being liquidated or removed from the companies register). This would be similar to Canadian and UK rules.

6. Although their main purpose is removing this integrity risk, the proposals would also partially address concerns (highlighted by the case studies and data below) that the use of shareholder loans is reducing the likelihood of creditor recovery on liquidation. The proposals would mitigate this problem by:

    6.1 discouraging companies from lending funds to their shareholders in the first place, and

    6.2 where there are outstanding loans on liquidation, enabling a recovery of tax from the borrower (up to 39% of the loan, subject to ability to pay).

Case studies

7. We have found seven publicly available news articles from the last 12 months about companies which lent funds to their shareholders before going into liquidation. This has contributed to the liquidated companies being unable to pay their creditors. These details are summarised below:

    7.1 John S. MacDonald Builders Ltd was liquidated owing $1.6m to creditors. The owner and director had allocated his company's funds for his personal interests including renovations on his own home, paying interest on personal loans and funding an interest in a racehorse. The High Court found the director was liable to creditors for allowing the company to trade while insolvent.[1]

    7.2 Kitchens Direct (NZ) Ltd and three other linked companies were put into liquidation owing creditors more than $350,000. $685,000 was taken from the shareholders account prior to the liquidation.[2]

    7.3 BF7 Trading, a labour hire company, went into liquidation with debts of $1.5m. BF7 Trading had lent $314,900 to its shareholders prior to liquidating. It had also set-up a family trust which these loans were transferred to, and the trust had borrowed the full value of the company's year-end balances before on-lending these amounts to shareholders and a brother of one shareholder.[3]

    7.4 A different labour hire company, Prolink NZ was liquidated owing about $4 million to creditors. One of the directors of this company withdrew about $80,000 out of the company's bank account without justification, about two weeks prior to the company going into liquidation.[4]

    7.5 Hanmer Building Solutions Ltd was liquidated owing $1.2m to unsecured creditors, including claims for uncompleted building projects. The liquidators identified an overdrawn current account in respect to one shareholder/director who was paid by way of loans in lieu of salary.[5]

    7.6 Tui Terraces went into liquidation owing nearly $4.6 million in taxes to Inland Revenue. Their assets comprised $6.7m in loans made to Du Val entities, a related property group, prior to liquidation.[6]

    7.7 Auckland Restaurant SPQR went into liquidation owing more than $2m to Inland Revenue and other creditors. Prior to liquidating, they lent nearly $1.4 million to the company that owns it and $1.2m to other related companies. [7]

8. We note that the last two cases (in paras 7.6 and 7.7) involve loans to other related party New Zealand companies. The proposed tax reforms would not apply to loans made to other New Zealand companies as there is typically no tax advantage from such loans. However, these related party companies can on-lend to their own

[1] Builder spent clients' deposits on his own house and race horses, Stuff, 11 May 2025
[2] Liquidator of Kitchens Direct still chasing owner over overdrawn account, The Press, 1 April 2025
[3] Troubled businessmen ordered to co-operate with liquidators, Stuff, 25 November 2024
[4] Labour hire company at centre of immigration probe estimated to owe creditors $4.01 million, RNZ News, 18 January 2025
[5] Hanmer builder's unsecured creditor debt up almost 50%, The Press, April 8, 2025
[6] Du Val entity liquidation complicated by parent group's statutory management – receivers, RNZ News, 20 January 2025
[7] SPQR shareholder withdrew $1.4m from the business, restaurant lent $1.2m to related companies, NZ Herald, 21 July 2024

shareholders and the proposed reforms would apply to funds which were on-lent to shareholders who were natural persons or trusts.

9. The reforms could also potentially apply when a New Zealand company lends funds to a non-resident parent company.

10. A historic and well-known case study is Mainzeal, a large construction company which provided loans totalling around $44m to its foreign parent companies, despite making losses for most of 2008 to 2012. It was liquidated in 2013 owing $110m to unsecured creditors.

11. In 2023, the Supreme Court ruled that Mainzeal's directors were liable to pay $39.8m plus interest to the creditors. This was because the loans to Mainzeal's foreign parents were not recoverable and meant it was trading while it was insolvent.[8]

Data from liquidations

12. MBIE has provided us with Companies Office data on liquidations completed since September 2020 where money was obtained in the liquidation from a shareholder or director. The data shows liquidators have collected $5.687m from shareholders and $6.978m from directors in 417 liquidations since September 2020. This data includes liquidations by the Official Assignee and private sector liquidators.

13. MBIE's Insolvency and Trustee Service began collating information on the debt owed by shareholders under liquidations they administer as the Official Assignee this year. Since 15 January 2025, they have identified 18 companies that were owed money by their shareholders, totalling $2.958m. There are 16 other companies with no amount entered yet, which may indicate there is likely to be an amount owed but it has not been quantified yet. This data excludes private sector liquidators.

Liquidations are a small part of the overall problem

14. Based on discussions we have had with MBIE and private sector liquidators we understand that formal liquidations are a small part of the overall problem of companies lending funds to shareholders before they fail.

15. A significant proportion of companies never go into liquidation. Instead, the Companies Office removes them from the companies register when they cease filing annual Companies Office returns. In the last 6 years, 123,000 companies were removed from the register this way compared to about 10,000 liquidations. We understand many of these companies will have related party current accounts (loans to / drawings by their shareholders).

16. In addition, the problem is often not observable to liquidators due to poor record-keeping by the company prior to its failure. More specifically:

    16.1 In many cases, liquidators are unable to access the company records, and any records they do receive are often out of date. Company accounts are rarely completed in the two years prior to liquidation.

    16.2 Particularly in the case of closely held companies, rather than the owners withdrawing cash from their company, it is more common to use the company's bank account to pay third parties for the owner's private

[8] Mainzeal directors lose appeal, ordered to pay nearly $40m in damages, RNZ News, 25 August 2023

expenses. These private expenses should be coded to the owners' current account. However, on many occasions these payments by the company to third parties may not be correctly coded to the current account.

16.3 As the company starts to fail, these problems become worse as the company owners often use the company's current account as the main way they pay for their own personal expenses and stop coding these transactions.

17. Accordingly, when a company has lent funds to its shareholders prior to being liquidated, it is difficult for liquidators to identify and recover these loans. This reduces the amounts that liquidators can recover for the company's creditors.

18. The tax proposals would aim to discourage companies from lending funds to their shareholders to begin with, as it is difficult to recover these funds once a company begins to fail. The proposals would treat a loan to shareholder as a taxable dividend if it has not been repaid by the end of the following tax year or at the time the company is liquidated or removed from the companies register. They would also improve annual reporting by companies on the balances of their loans to shareholders, which will help liquidators and Inland Revenue to identify and recover these loans.

Next steps

19. Officials will report back in June with a draft consultation document and a Cabinet paper seeking approval to release the consultation document for public consultation in July 2025.

Recommended action

We recommend that you:

1. **note** the contents of this report

Noted

Noted

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Claire McLellan
Acting Policy Lead
Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

Inland Revenue
Te Tari Taake

Briefing note

Reference: BN2025/378

Date: 9/9/2025

To: Revenue Advisor, Minister of Finance – Carl Harris
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Helen Kuy

From: Gordon Witte, Principal Policy Advisor, Inland Revenue

Subject: **Timeframes and smoothing options for company loans to shareholders**

1. This note provides information on possible timeframes for implementing and beginning to collect tax from reforms to the taxation of company loans to shareholders. It also provides more information on options which could mitigate the initial impact of the proposal to tax shareholder loans as dividends, particularly for taxpayers with existing loans.

2. This note also sets out our proposal for targeted consultation.

Timeframes for potential reform and tax impact of main reform option

3. We note the current design of the main reform option would tax as dividends shareholder loan balances that have exceeded a de minimis (such as $50,000 per company) at the end of two consecutive tax years.

4. This could provide about 22 months between the reform being announced (May 2026) and the relevant tax liability arising (typically 31 March 2028 for companies with standard balance dates and longer for other companies). There would be a further 10 or 12 months before the tax would need to be paid to Inland Revenue (7 February 2029 or 7 April 2029 for shareholders with tax agents).

5. The following tables provide an indicative timeline of key events:

Potential date	**Event (Consultation and legislation)**
Sept 2025	Targeted consultation (in-confidence with members of Minister of Revenue's Tax System Forum)
October 2025	Cabinet decisions to publish issues paper
Oct-Nov 2025	Public consultation on issues paper
November 2025	Submissions close
February 2026	Report back to Ministers with advice on policy options following submissions
March-April 2026	Cabinet decisions on policy reform to allow fiscal benefits to be recognised in B26
May 2026 (near Budget day 2026)	Announce final policy decisions

Potential date	Event (Consultation and legislation)
Aug 2026	Tax Bill introduced with required amendments
Sept 2026-Jan 2027	FEC consideration of Tax Bill
March 2027	Legislation enacted

Potential date	Event (Impact of potential new rules on taxpayers)
1 April 2027	Rules apply to tax years beginning on or after 1 April 2027
During the 2027/28 tax year	Many of the affected taxpayers will respond to the reforms so they do not incur additional tax. This includes if the shareholder repays the loan out of their own resources or if they liquidate their company and pay a dividend which is tax-free because it is funded out of Available Subscribed Capital or a capital gain. Examples 1 and 2 in the appendix illustrate these behavioural responses. In other cases where the company has imputation credits there will be incentives to declare an imputed dividend and use this dividend to repay the loan. This is illustrated by example 3 in the appendix.
31 March 2028	End of first tax year for taxpayers with standard balance dates. If the company has had more than $50,000 of outstanding loans for 2026/27 and 2027/28, the loan could be taxed as a dividend. Example 4 of the appendix illustrates a loan being taxed as a dividend.
7 February 2029	Tax payment due for shareholders without tax agents
Until 31 March 2029	A company with a standard balance can declare a shareholder salary if the shareholder is an employee of the company in which case this salary will be taxed / used to offset the loan, rather than being treated as a taxable dividend
7 April 2029	Tax payment due for shareholders with tax agents

Longer transitional and smoothing options

6. During the consultation we expect stakeholders will seek a longer transition period or smoothing options for applying the reforms to existing, pre-reform loans. Some potential smoothing options that may be raised could include:

    a) Providing an additional tax year before the rules applied to existing loans (31 March 2029 for companies with standard balance dates, which means the corresponding tax payments would not be due until 7 April 2030 for shareholders with tax agents).

    b) Applying the reform to a percentage of the total loan balance in the initial years, for example, treat 50% for the loan balance as a dividend at the end of the 2028/29 tax year with the remaining 50% being taxed at the end of 2029/30 tax year.

    c) Allowing the initial tax liability to be paid using a few annual instalments. For example, if a shareholder had a $60,000 tax liability at the end of their 2028/29

tax year, a transitional rule could require $30,000 of this tax to be paid in April 2029 and $30,000 to be paid in April 2030.

d) A higher *de minimis*. Because companies with smaller loan balances below the de minimis would only have these loans taxed as dividends if they were wound-up and removed from the Companies Register, this would reduce the number of companies who face additional tax. This option is analysed further below.

Higher de minimis

7. While nearly 120,000 companies have loans to shareholders, 70% of the total value of shareholder loans is concentrated in about 12,000 companies that have loans exceeding $500,000. This represents 10% of the total number of companies.

8. As shown by the following table the $50,000 *de minimis* that is currently suggested in the issues paper could remove about 50% of all companies with shareholder loans from having a tax liability (if the value of their loans hasn't increased since 2024/25), while still applying the rules to 97% of the total value of loans.

9. Increasing the *de minimis* to $100,000 could remove 65% of companies while still applying the rules to 92% of the value of loans.

10. Increasing the *de minimis* to $500,000 could remove about 90% of companies while still applying the rules to about 70% of the value of loans. However, a very high de minimis would be less effective at addressing the policy concerns as it would encourage close companies to maintain loan balances just below the de minimis. Other amounts between $100,000 and $500,000 could be considered.

Value of de minimis	Number of companies below de minimis in 2024/25	Number of companies above de minimis in 2024/25	% of total companies with shareholder loans above de minimis	% of total value of shareholder loans above de minimis
No de minimis	0	118,938	100%	100%
$50,000	59,977	58,961	49.6%	96.6%
$100,000	77,703	41,235	34.7%	92.2%
$500,000	107,228	11,710	9.8%	69.4%

Targeted consultation prior to release of issues paper

11. We think there would be value in a short round of targeted consultation to test our approach with a small number of stakeholders prior to publishing the issues paper. If the Minister of Revenue and the Minister of Finance agree, we propose engaging with the Minister of Revenue's Tax System Forum as soon as possible. We would provide them with a brief summary and the draft issues paper and seek their initial comments. Due to budget timeframes, we recommend progressing this in tandem with Cabinet processes.

Consultation

12. The Treasury were consulted on this briefing note.

Gordon Witte
Principal Policy Advisor, Inland Revenue
s 9(2)(a)

Appendix: Examples of taxpayer responses and when the tax could apply

Example 1: Repayment of loan by shareholder out of their own funds

Summer Co has outstanding loans of $150,000 owed to it by its shareholder Julia, at its balance date of 31 March 2027.

In early March 2028 Julia repays $101,000 of the loans to Summer Co by withdrawing funds from her personal bank savings / term deposits and by selling other investment assets. Accordingly, Summer Co's outstanding loans are $49,000 on 31 March 2028. Because this amount is below the $50,000 de minimis, the loans will not be treated as a taxable dividend.

Example 2: Repayment of loan out of ASC and capital gains by liquidating the company

Winter Co has outstanding loans of $500,000 owed to it by its sole shareholder Diane, at its balance date of 31 March 2027.

Diane decides to close Winter Co and begins selling its assets which generates $200,000 of capital gains for Winter Co. In February 2028, Diane liquidates Winter Co and Winter Co distributes Available Subscribed Capital of $300,000 and net capital gain amounts of $200,000 to Diane. These amounts are tax-free distributions because Winter Co has been liquidated. The $500,000 of distributions are used to repay the loan that Diane owed Winter Co.

In March 2028, Diane applies to have Winter Co removed from the Companies Register. When Winter Co is removed, it does not have any outstanding shareholder loans so the new rules will not apply to deem a dividend.

Example 3: Using an imputed dividend to repay the loan

Spring Co has outstanding loans of $100,000 owed to it by its shareholder Sam, at 31 March 2027.

In early March 2028 Spring Co declares a fully imputed dividend of $164,000 which includes $45,920 of imputation credits. Because Sam is on a 39% marginal tax rate, he has a $63,960 tax liability on the dividend income, but $45,920 of this is offset by the imputation credits, which means the remaining tax to pay will be $18,040. The after-tax dividend is $100,040 which Sam uses to repay the debt he owes Spring Co.

Accordingly, Spring Co's outstanding loans are nil on 31 March 2028 so the new rules will not apply to deem a taxable dividend. Instead, Sam has already paid tax on an actual, imputed dividend.

Example 4: Payment of tax on shareholder loan (main reform option in issues paper)

Mario is the sole shareholder in M Ltd. M Ltd has a standard balance date.

Starting in June 2026, Mario uses the company credit card to pay for his house renovations. At the end of the income year (31 March 2027), the total cost of the renovations (and the amount Mario owes to the company) is $65,000.

Mario does not repay any of the amount, and the balance is still outstanding at the end of the following income year (31 March 2028). Mario will be treated as having derived a dividend of $65,000 on 31 March 2028. This will be subject to tax at his marginal tax rate.

Mario uses a tax agent so will have until 7 April 2029 to pay the tax on the dividend.

Fiscal implications

1. Publishing a consultation paper would have no direct fiscal implications. However, the proposed reform could generate significant, though highly uncertain, tax revenue depending on the final design. If the main proposal was legislated in 2026 and implemented from April 2027 there could be a one-off additional tax revenue of about $3 billion to $5 billion in 2028/29. Due to this uncertainty, we have taken a conservative approach in recent Budget and tax policy work programme reporting by reflecting the positive impact as at least $1 billion over the forecast period.

2. Importantly, this one-off fiscal gain would only arise if policy decisions are made to tax the existing stock of loans (which we recommend). Even if this policy decision is taken, our estimated range is uncertain because it depends on behavioural assumptions (repaid loans would not be taxed) that are highly uncertain.

3. The ongoing fiscal impacts from 2029/30 onwards are also highly uncertain as the net tax collected each year would depend on the values of newly taxed loans minus tax deductions for previously taxed loans that the shareholder has subsequently repaid to their company. The ongoing revenues could be in the range of $200 million to $500 million per year but could potentially be negative for a few years if lots of the loans that were taxed in 2028/29 were subsequently repaid in future years.

4. We expect strong pressure from submitters to amend the proposals to provide more exemptions or relief for the affected loans (including for the stock of existing loans) as well as strong behavioural responses to repay loans. Both issues could greatly reduce the additional tax revenue which could be generated if the proposals were implemented.

5. We will report back with further advice on the design of the proposals and the fiscal implications of proceeding with them, following public consultation.

Inland Revenue
Te Tari Taake

Briefing note

Reference: BN2025/406

Date: 6/10/2025

To: Revenue Advisor, Minister of Finance – Carl Harris
Revenue Advisor, Minister of Revenue – Angela Graham

From: Gordon Witte, Principal Policy Advisor, Inland Revenue

Subject: **Taxation of loans made by companies to shareholders - revised Cabinet paper and issues paper**

1. In August, we provided Ministers with a draft Cabinet paper to seek Cabinet decisions to publish an officials' issues paper to publicly consult on improving the taxation of company loans to shareholders (IR 2025-219 refers)

2. Following the Minister of Finance's meeting with officials on 29 September we have revised the Cabinet paper and officials' issues paper to reflect her comments on the documents and policy design decisions including:

   - addressing transitional issues by only applying the proposed new time limit to new loans (existing loans would be exempt); and
   - seeking submissions on the appropriate amount for a *de minimis;* and
   - removing the policy option of increasing the prescribed interest rate

3. We have also updated some material in the Cabinet paper about the expected submissions based on the feedback we received from the targeted consultation that officials conducted in September. This feedback supported for taxing loans when company is removed from register, but expressed issues with the time limit and transitional concerns.

4. Some other minor changes have been made to the Officials' issues paper to address some design features which were raised with us during our targeted consultation.

5. We have attached the revised documents for Ministers' consideration.

Next steps

6. In order to allow the public consultation to begin in late October so submissions can be received before the Christmas break, we recommend the following timeline for seeking Cabinet decisions:

Deliverable	**Date**
Ministerial consultation on Cabinet paper	9 October
Lodgement of attached papers with the Cabinet Office	16 October
ECO considers Cabinet paper	22 October
Cabinet approval to release consultation paper	28 October
Publication of consultation paper	29 October
Submissions due	10 December

7. This timeline will allow us consider submissions and report back to you in early 2026 to seek final policy decisions. If you wanted to recognise revenue in Budget 2026, Cabinet decisions on the final policy design of the reforms would be required by early April 2026.

8. An alternative timeline of seeking Cabinet decisions in November (e.g. ECO 12 November, Cabinet on 17 November) would either require extending the deadline for submissions to late January 2026, or shortening the submission period to only 4 or 5 weeks.

Consultation

9. The Treasury were informed of this briefing note.

Gordon Witte
Principal Policy Advisor, Inland Revenue
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Inland Revenue
Te Tari Taake

Briefing note

Reference: BN2025/425

Date: 21/10/2025

To: Revenue Advisor, Minister of Finance – Carl Harris
Revenue Advisor, Minister of Revenue – Angela Graham

From: Gordon Witte, Principal Policy Advisor, Inland Revenue

Subject: **Shareholder loans - information for joint Ministers' meeting on 23 October**

1. Ministers have been considering a draft officials' issues paper which could be used to publicly consult on improving the taxation of company loans to shareholders (IR 2025-219 and BN2025-406 refer).

2. The Ministers of Finance and Revenue are meeting on Thursday 23 October to discuss this tax policy project. This briefing note provides further information to support their discussion. In summary:

Topic	Key points
Main points from targeted consultation	- Strong support for taxing shareholders when the company is wound up / liquidated. - Some tax advisors did agree there is a broader problem which should be addressed and aligning our rules with UK/Canada is a reasonable approach. - Most tax advisors opposed the main reform of requiring loans to be repaid within a time limit, mainly because the existing rules should be sufficient and new rules would be disruptive. - All advisors raised the importance of transitional rules for existing loans to mitigate the impact on taxpayers who may be cash constrained.
Other potential design options to mitigate impact on taxpayers	- Increase de minimis, for example a $100,000 de minimis reduces impacted companies to about 30,000 and a $200,000 de minimis reduces impacted companies to about 20,000. - Exclude capital gains that are lent to shareholders.

Revised fiscal estimates based on consultation feedback and Ministers' decision to exclude existing loans from time limit proposal	- Most likely fiscal estimates based on current policy design (including Ministers' decision to exclude existing loans) and assumptions are estimated to raise $1.1 billion over forecast. - An example of a more generous policy design is estimated to raise $960m over forecast. - Progressing just the change to tax shareholders when the company is would up / liquidated is estimated to raise $170m over forecast.
Information on the distribution of company loans to shareholders	- Distributional analysis is based on existing stock. The time limit rule is proposed to apply only to new lending, that means taxpayers will have a choice of whether to continue to this practice. We expect many of the affected companies will change to paying more dividends or salaries instead of issuing new loans. - We have provided data on the distribution of existing loans by the size of the loan balance. About 10% of companies with loans over $500,000 represented around 70% of the total existing loan balance. - Expected to mainly apply to businesses with a small number of shareholders (1.4 on average). - The main industries which use shareholder loans are property, real estate, agriculture, and construction.

Main points from targeted consultation

3. In September, officials conducted targeted consultation on the draft issues paper on a strict in-confidence basis and received feedback from 14 tax advisors.[1] The main points from this targeted consultation are summarised below.

Strong support for taxing shareholders when the company was wound up / liquidated

4. Nearly everyone supported taxing loans when a company is removed from Company Register and considered this should be addressed even if the other reform options did not proceed.

Some tax advisors did agree there is a broader problem which should be addressed

5. Some of the tax advisors agreed there was an issue which was illustrated by both the issues paper chapter which provided IRD data on large loans and their own observations of liquidator's reports which identified large loans prior to the company's failure. They considered it was reasonable to require the loans to be repaid within a certain time limit. They noted the proposal would align New Zealand's tax rules with the UK and Canada.

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6. One stakeholder said that public messaging was critical and suggested a clear fact sheet be produced to support the issues paper. We have started to draft a fact sheet which could be used for this purpose (see appendix one).

Most tax advisors opposed the main reform of requiring loans to be repaid within a time limit

7. Most of the tax advisors did **not** support the main reform of requiring loans to be repaid within a time limit (loans which were not repaid within 12 months of the end of the tax year they were made would become taxed as dividends).

8. The main issues these advisors raised about the proposed time limit were:

   - Existing rules to pay tax on a prescribed rate of interest are adequate.
   - Better monitoring and enforcement of the existing tax rules and company law should be used to address large loan balances, instead of applying new general tax rules.
   - Reform would disrupt longstanding practices of thousands of companies.
   - The legal form is a loan and so there should be a high bar, such as tax avoidance to reclassify them as dividends.
   - Some also noted the new rules would be complex and would encourage affected taxpayers to restructure or change their behaviours to ensure they would not be taxed on a deemed dividend.

Concerns about taxing existing loans when businesses may be struggling

9. All the tax advisors raised concerns about the potential impact of imposing a time limit to repay existing loans. Some considered it would hit companies and shareholders who were already struggling and that had intended to repay the loans (rather than defer or avoid tax) but now could not repay them in the current business environment.

10. Some advisors expressed concern that in many cases the company would be unable to pay an actual imputed dividend to clear the shareholder loan balance, and the shareholder may not be able to repay the loan out of their own funds. This could lead to some shareholders being forced to sell their house to pay the tax. On the other hand, one advisor considered many shareholder loans existed because it was easier than applying for a bank loan, and that the affected shareholders may respond by simply obtaining a bank loan which they would use to repay the loan from their company.

Transitional rules need to be more generous for existing loans

11. Everyone considered there would need to be generous transitional rules for existing loans. The main option suggested were to provide a longer time period of between 24 to 48 months after enactment before any existing loans were taxed. Some advisors mentioned we could consider exempting existing loans but monitoring these could make the rules more complex. Other smoothing options raised included using a higher de minimis that gradually reduces each year, or spreading the amount of the loan or the payment of any resulting tax liability over a few years.

12. Ministers have decided to address this concern by excluding existing loans[2] from the proposed time limit rule so it would only apply to new lending after the date the

[2] Existing loans would still be considered when measuring whether a company's total loan balance exceeded the *de minimis*. Therefore, if an existing loan balance increased due to additional borrowing or interest being capitalised into the loan value owing, and the total balance was above the *de minimis,* the increased amount would become subject to the time limit rule. Also, existing shareholder loans would still be required to return

issues paper was published. This would put reasonable limits on new lending while ensuring it would not create a new cashflow pressure on shareholders who have previously borrowed from their companies. We have revised the fiscal estimates to account for this decision to exclude existing loans.

Other suggestions on the design of new rules

13. Several tax advisors also considered any new rules should exclude loans which were funded by capital gains. They noted that companies may sell land or other assets on capital account and then lend the proceeds out to shareholders as they do not currently need to utilise or reinvest the funds. The current tax rules also allow capital gains to be distributed tax-free if the company is liquidated. Advisors considered the requirement to liquidate a company was inefficient, and loans should be able to be used to distribute these gains before the company is liquidated.

14. Some advisors considered that the company should be able to attach imputation credits to a deemed dividend. We noted that if the deemed dividend had been imputed it would be difficult to provide a tax deduction for the shareholder if they decided to subsequently repay the loan, but the advisors considered this would be less important than allowing the imputation credits to be used.

15. A few advisors commented that a $50,000 de minimis seemed a reasonable amount which would exclude ordinary business practices. One advisor noted that a dollar-based de minimis will become effectively lower over time due to inflation.

16. On the policy design for companies removed from the Companies Register, some advisors suggested it may be simpler to tax such loans under the financial arrangement rules rather than as a deemed dividend. Two advisors also suggested a grace period of 3 months be provided before the shareholder became taxed to accommodate situations where a company was inadvertently removed and then reinstated to the register.

17. We have updated the issues paper to consult on the above design suggestions, and the revised fiscal estimates have considered how these design parameters may affect the estimates.

Other design features to mitigate the potential impact on taxpayers

18. As noted above, by far the largest concern raised during the targeted consultation was the potential impact on existing loans. The decision to exclude existing loans from the time limit rule is the most effective way to address this concern.

19. While other policy changes could be considered to further mitigate the potential impact on taxpayers, they would have a smaller impact. The issues paper is currently drafted to invite feedback on these points.

20. These other design features include:

    a) A higher de minimis value. Because companies with smaller loan balances below the de minimis would only have their loans taxed as dividends if they were wound-up and removed from the Companies Register, this would reduce the number of companies who could be negatively impacted:

tax on interest income and would be subject to tax if the loan was forgiven or if the company was removed from the Companies Register.

- With a $50,000 de minimis we estimate around 40,000 companies could be impacted by the time limit rule.[3]
- This reduces to about 30,000 companies with a $100,000 de minimis and about 20,000 companies with a $200,000 de minimis.
- Regardless of the de minimis value, about another 4,500 companies per year are removed from the Companies Register reporting loans to their shareholders in their last filed tax return, so could be taxed under that proposed rule.

b) Excluding loans which are funded from capital gains. We understand some companies may sell land or other assets on capital account and then lend the proceeds out to shareholders as they do not currently need to utilise or reinvest the funds. We do not have data to gauge how significant this may be. However, because current tax rules already allow companies to distribute capital gains tax-free if they are liquidated, not providing an exclusion for loans funded from capital gains would likely lead to the affected taxpayers adopting arrangements whereby they liquidate the company instead.

Fiscal estimates

21. We have revised the fiscal estimates to reflect Ministers' recent policy decision to only apply the time limit rule to new lending after the date the issues paper is published (assuming a November 2025 publication date).

22. The estimates depend on assumptions about taxpayers' behavioural responses, assumptions about the relevant marginal tax rates of the shareholders, and policy design features which are still subject to consultation. On 9 October, we provided a Tax and Social Policy Work Programme update, which indicated a $800 million - $1.4 billion range over the forecast period.

23. Changing some of these assumptions leads to substantial changes in the fiscal estimates. For these reasons we have produced a range of fiscal estimates that use different assumptions and potential policy designs.

24. All the following tables have assumed 2/3rds of the taxed loans belong to natural persons on 33% marginal tax rates and 1/3rd of the shareholders are trustees or high income belong to trustees or natural persons on 39% tax rates.[4] Assuming a greater proportion of 39% shareholders significantly increases the estimated revenues.[5]

25. Based on the feedback received from targeted consultation we consider the most likely policy design could be a $50,000 de minimis, allowing imputation credits to be attached to the deemed dividends and not allowing tax deductions if the shareholder subsequently repays a taxed loan. This is illustrated in table 1 below:

[3] Based on the number of companies with loans above this de minimis value at the end of the 2023/24 tax year and their loan balance had increased compared to the previous tax year (2022/23).

[4] This assumption means the average marginal tax rate for all taxed loans would be 35%. This assumption is considered more realistic than assuming higher tax rates as the proposal would only apply to new loans and would no longer generate large amounts of income in the first year for shareholders with large existing loans.

[5] For example, assuming all shareholders were on 39% marginal tax rates would increase the total amount of tax collected over the forecast period by about $500m.

Table 1: Most likely fiscal estimates based on current policy design and assumptions

	$m - increase					
	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	**Total for forecast period**
Time limit on new loans: $50k de minimis, allow imputation credits, no deductions for repayment	70	250	220	200	200	940
Tax all loans when company removed from Companies Register	24	30	40	38	38	170
Total for both measures	94	280	260	238	238	1,110

26. If the policy settings for a time limit rule were made more generous (a $200,000 de minimis), fewer loans would be taxed, and this could reduce the estimated tax revenues as shown in Table 2:

Table 2: Fiscal estimates with fewer loans taxed under time limit because of more generous policy design ($200k de minimis)

	$m - increase					
	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	**Total for forecast period**
Time limit on new loans: $200k de minimis allow imputation credits, no deductions for repayment	60	210	180	170	170	790
Tax all loans when company removed from Companies Register	24	30	40	38	38	170
Total for both measures	84	240	220	208	208	960

27. In contrast, table 3 shows the high-end of estimated tax revenues if the policy design for time limit on new loans had tight policy settings (not allowing imputation credits to be attached to the deemed dividends, providing no deductions for subsequent repayments, and a $50,000 de minimis).

Table 3: High fiscal estimates due to tight policy design (no imputation credits, no deductions for repayment, $50,000 de minimis)

	$m - increase					
	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	**Total for forecast period**
Time limit on new loans: $50k de minimis, no imputation credits, no deductions for repayment	80	360	300	270	280	1,290
Tax all loans when company removed from Companies Register	24	30	40	38	38	170
Total for both measures	104	390	340	308	318	1,460

28. Because there was much greater acceptance that loans should be taxed when a company was removed from the Companies Register, one option would be to only proceed with that measure and not impose a time limit rule. This is estimated to raise $170 million over the forecast period as shown in the tables above.

Information on the distribution of company loans to shareholders

29. The Minister of Revenue has asked for data on the distribution of company loans to shareholders.

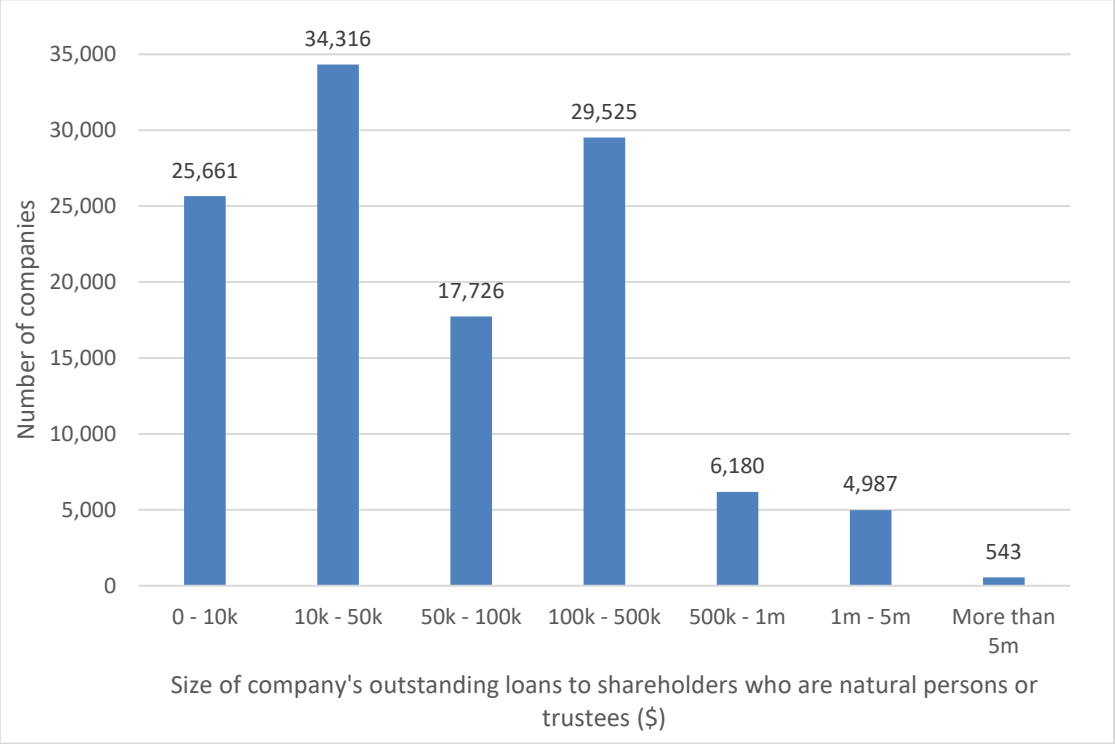
30. The distributional data is useful for illustrating the type of taxpayers who make use of loans under current settings. The time limit rule will only apply to new lending which taxpayers have a choice over. We expect this rule would lead to the affected taxpayers changing behaviours from taking new loans from their companies to receiving income via dividends or salary payments.

31. It is our expectation that the proposed rule would mainly apply to companies with a small number of shareholders that are New Zealand resident natural persons or trustees. Based on our data, the average number of shareholders with a loan for each lending company was 1.4 shareholders. We anticipate the proposed rule would primarily apply to family-owned or controlled businesses, many of which will be SMEs, especially where the shareholders are on a 39% personal marginal tax rate.

32. The rule would apply to some larger companies, especially ones owned by high-net worth individuals. However, we do not expect the proposed rule would apply to widely-held companies such as NZX-listed companies, or companies with foreign ownership, as those companies do not typically distribute their profits by way of loan.

33. About 10% of companies with loans over $500,000 represented around 70% of the total existing loan balance. While we do not currently have data on the size of the companies by revenue or number of employees, the ability for these companies to loan out large sums to their shareholders suggest that the company is generating substantial revenue.

Chart 1: Number of companies with loans to shareholders, by size of existing loans at end of 2023-24 tax year



34. As shown in the following table, the main industries that currently use shareholder loans are property and real estate services, agriculture, construction, finance, and professional services.

Table 4: Number of companies with loans to shareholders, by main industry, 2023-24 tax year

Industry	Number of companies	Existing loans at end of 2023-24 tax year ($m)	% of total loan values
Rental, Hiring and Real Estate Services	14,274	7,638	26.1%
Agriculture, Forestry and Fishing	9,647	5,330	18.2%
Construction	21,261	3,093	10.6%
Financial and Insurance Services	3,474	2,414	8.2%
Professional, Scientific and Technical Services	19,277	2,030	6.9%
Other industries	51,005	8,767	30.0%
Total for all industries	118,938	29,272	100.0%

Consultation

35. The Treasury were consulted on this briefing note.

Gordon Witte
Principal Policy Advisor, Inland Revenue
s 9(2)(a)

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: Shareholder loans design features

Date:	6 November 2025	**Priority:**	Medium
Security level:	BUDGET SENSITIVE	**Report number:**	IR2025/440

Action sought

	Action sought	**Deadline**
Minister of Finance	**Agree** to recommendations	13 November 2025
Minister of Revenue	**Agree** to recommendations	13 November 2025

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**	**Suggested first contact**
Claire McLellan	Acting Policy Lead, Inland Revenue	s 9(2)(a)	
Gordon Witte	Principal Policy Advisor, Inland Revenue		✓

6 November 2025

Minister of Finance
Minister of Revenue

Shareholder loans design features

Purpose

1 Ministers have been considering a draft officials' issues paper that could be used to publicly consult on improving the taxation of company loans to shareholders (IR 2025/219, BN2025/406 and BN2025/425 refer).

2 The Ministers of Finance and Revenue are meeting on Thursday 13 November 2025 to discuss this tax policy project. This report provides further information to support this discussion.

3 The report also provides advice on design features of the consultation proposal. Officials have modified the design of the proposal based on Minister's decisions and feedback from our targeted consultation.

4 We will update the officials' issues paper to reflect your decisions on design features.

Executive summary

5 The main proposal discussed in the draft officials' issues paper would be to tax new shareholder loans as a dividend if they are not repaid within two years of being made. This report provides additional information and seeks decisions on two design features of this main proposal.

6 **Level of de minimis.** The de minimis would allow companies to continue to lend small amounts to their shareholders as part of their usual business operations. Officials recommend that the de minimis be set at $50,000 per company. This level is generous compared to other countries with similar rules. During our targeted consultation, some tax advisors commented that the level seemed reasonable and would exclude most ordinary business practices.

7 We recommend against a higher de minimis because we consider that it would reduce the effectiveness of the proposed rule. There is a risk that a higher de minimis could result in some companies lending more than they otherwise would, simply due to the existence of the de minimis.

8 To support your decision on the level of de minimis, we provide additional information on the expected fiscal effect of different de minimis levels.

9 **Interaction between grandparenting and de minimis**. You have previously decided that the proposed time limit rule would not apply to any existing shareholder loan balances at the date of publication of the issues paper. However, we propose that existing loan balances would still be taken into account when determining whether a company exceeds the de minimis. This is because the de minimis is intended to remove companies with small loan balances from the scope of the new rule, rather than allowing all companies an additional tax-free threshold

before the rule applies. An example of this is included in the report to assist you in deciding whether you agree with this approach.

10 If you decide not to proceed with consultation on the issues paper, we consider that the proposal to tax shareholder loans when a company is removed from the Companies Office should still proceed.

Advice on design features

Proposed time limit on new loans

11 The main proposal in the issues paper is to tax a new loan as a dividend if it is not repaid within a time limit. There are some exceptions when this rule would not apply, the main one being if the company's total loan balances to shareholders is below a de minimis amount.

12 We seek direction on the following design features:

- level of de minimis, and
- interaction between grandparenting and de minimis.

Level of de minimis

13 The purpose of the de minimis is to allow companies to continue to lend small amounts to their shareholders as part of their usual business operations (such as using drawings to manage temporary cashflow pressures).

14 There are a large number of small value loans from companies to shareholders. The de minimis would exclude these smaller loans, significantly reducing compliance costs for those companies and administrative costs for Inland Revenue.

15 The draft officials' issues paper proposes a de minimis of $50,000 of outstanding loan balances per lending company and asks for submissions on the value for the de minimis.

16 Officials do not recommend increasing the de minimis at this stage. We can provide further advice on this following any public consultation.

17 Increasing the de minimis would reduce the effectiveness of the rule in encouraging loans to be repaid, which would reduce the fairness and integrity benefits of the reform. The current rules make the tax system less fair and efficient because owners of close companies can benefit from an unintended tax advantage. In contrast, other types of businesses such as widely-held companies, partnerships and sole traders cannot use shareholder loans and will be fully taxed (typically at 33% or 39% tax rates) when their owners receive dividends or other types of income.

18 Increasing the de minimis could even result in undesirable behavioural responses from some companies and shareholders. For example, it may create a perverse incentive by setting a higher target that encourages companies to bunch just below de minimis (as is the case for other tax thresholds), when they may have otherwise made smaller loans.

19 During the targeted consultation in September 2025, a few advisors commented that a $50,000 de minimis seemed a reasonable amount that would exclude ordinary business practices.

20 Among countries that set a de minimis, a $50,000 amount is generous:

- Australia has no de minimis. However, we note that the Commissioner has discretion not to treat a loan as a dividend in a variety of situations.
- Canada has no de minimis.
- Norway has a de minimis of NOK100,000 (approximately NZ$16,000).
- The United Kingdom has a de minimis of £15,000 (approximately NZ$34,000) for loans to a director or employee.

21 A higher de minimis would allow companies to lend more before they had to consider the time limit rule. It would mean fewer companies would become subject to the rule, meaning fewer companies incur compliance or tax costs:

- About 120,000 companies reported loans to shareholders at the end of the 2024–25 tax year.
- With a $50,000 de minimis we estimate about 44,000 companies could initially be impacted by the time limit rule.[1]
- This may reduce to about 32,000 companies with a $100,000 de minimis, about 21,000 companies with a $200,000 de minimis, about 16,000 companies with a $300,000 de minimis and about 10,000 companies with a $500,000 de minimis.
- Regardless of the de minimis value, about another 4,500 companies per year are removed from the Companies Register reporting loans to their shareholders in their last filed tax return, so could be taxed under that proposed rule.

22 An increased de minimis would generate less tax revenue because fewer companies would need to replace their loans with taxable dividends or shareholder salaries. This is shown in the table below. Further fiscal impacts of other potential policy design options are shown in the appendix.

	$m - increase					
Time limit on new loans: **allow** imputation credits, **no** deductions for repayment	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	**Total for forecast period**
$50,000 de minimis	60	240	220	200	200	920
$100,000 de minimis	50	230	200	190	190	860
$200,000 de minimis	50	210	180	170	170	780
$300,000 de minimis	40	190	170	160	160	720
$500,000 de minimis	40	170	150	140	140	640

[1] To be impacted, the company's loans must be above the de minimis at the end of two consecutive tax years and their loan balance has grown since the date the issues paper was published (due to a new loan or capitalised interest).

23 We recommend that the level of de minimis in the issues paper remains at $50,000. If you consider that the de minimis should be increased, we seek your decision on the appropriate level.

Interaction between grandparenting and de minimis

24 You have previously decided that the significant existing stock of loans should be excluded from the new time limit rule. This ensures the reform would not create a new cashflow pressure on shareholders who have previously borrowed from their companies.

25 The issues paper describes this grandparenting as meaning that the rule would not apply to any shareholder loan balances at the date of publication of the issues paper, unless there is a material variation to the terms of the loan after introduction of the rules.

26 The proposed rule would, however, apply to any new lending that occurs on or after the date of publication of the issues paper. This would include increases to existing shareholder current accounts, any interest accruing to existing loans that is capitalised to the loan balance, and if there is a material variation to the terms of the loan.

27 Despite the exclusion of existing loan balances from the scope of the rule, we propose that existing loans would be taken into account when determining whether a company exceeds the de minimis. The de minimis is intended to remove companies with small loan balances from the scope of the new rule, rather than allowing all companies an additional tax-free threshold before the rule applies.

28 The following example (based on an example in the issues paper) shows the proposed interaction between the de minimis and existing loans.

Example 1: Interaction between de minimis and existing loans

Welby is the sole shareholder in W Co, which has a standard balance date of 31 March. Welby borrowed $500,000 from W Co in 2020 to fund the purchase of his family home. He pays interest on that loan. The principal is only repayable once the family home is sold, but Welby pays regular interest on the loan at a market rate.

The new rule will not apply to this loan because it was entered into before the date of this issues paper.

On 16 October 2026, Welby borrows $10,000 from W Co to travel overseas for a family emergency. The balance remains outstanding on 31 March 2027. The new rule will apply to the new $10,000 loan because the total lending by W Co exceeds the de minimis of $50,000. If Welby has not repaid the new $10,000 loan by 31 March 2028, he will be treated as deriving a dividend of $10,000 on that date.

If the existing balance was not taken into account in determining the de minimis, Welby would be able to borrow an additional $50,000 before any amount would be treated as a dividend.

29 Taking into account the existing loan balance for the purpose of the de minimis could mean that for a shareholder with a significant loan balance who capitalises

the interest, the interest could be subject to the new rule almost immediately. This may result in desirable behavioural changes because it may encourage shareholders with large existing loan balances to either begin paying interest rather than continuing to capitalise those amounts or to repay their loans to ensure they do not have to consider the new rules.

30 We seek your confirmation of the decision to grandparent existing loans, and we recommend that existing balances should be taken into account in determining the de minimis. If the existing balances are not taken into account in determining the de minimis, the proposal would become complex to administer which would increase compliance costs and make it more difficult for Inland Revenue to enforce. Shareholders would also be able to borrow more before the rule applied. We expect that this would significantly reduce the fiscal estimates, but due to the additional complexity are not able to quantify that reduction at this stage.

Proposal to tax all loans when company removed from Companies Register

31 The second proposal in the issues paper is to ensure that any outstanding shareholder loan amount (that is, the amount owed by a shareholder to the company) would result in taxable income for the shareholder when the company is removed from the Companies Register.

32 All the company's loans to shareholders would be taxed under this proposal, including existing loan balances and loan balances that would be below the de minimis for the time limit. This is appropriate because once the company ceases to exist, the shareholder will not repay the loan so it should be treated as income for the shareholder.

33 Under the current law, once a loan becomes unenforceable, the borrower will have income under the financial arrangements rules. However, the exact timing of this income arising is unclear because the mere removal of a company from the Companies Register does not give rise to income. The proposal would ensure that it is clear the amount is income to the borrower, and that the timing of income arising is clear.

34 If you decide not to proceed with consultation on the issues paper, we will report to you separately to seek approval to proceed with a change to tax loans when a company is removed from the Companies Register. This change could be introduced as part of Budget 2026. While this change would be less effective without the main proposal, we consider that it is an important change to provide certainty and improve compliance. The proposal simply clarifies when income arises so we do not consider that extensive consultation is necessary and the feedback from targeted consultation supported this proposal.

35 The proposal is estimated to generate $167 million over the forecast period (2025/26 to 2029/30) if it applied from December 2025 (date it was announced in an issues paper) or $146 million over the forecast period if it applied from late May 2026 (as a Budget 26 measure).

Consultation

36 The Treasury was consulted on this report and supports the current design features (as reflected in the officials' issues paper). Treasury anticipates that the design would improve fairness and integrity of the tax system over the long term. In the short term, the design would mitigate any cashflow pressures on companies with large existing loans, avoiding any potential negative economic effects from limiting

their ability to reinvest or manage short-term liquidity. Treasury also acknowledges the added benefits of minimising compliance costs for companies with smaller loans by maintaining a de minimis threshold.

Next steps

37 The following table provides some indicative timelines for publishing the officials' issues paper.

Deliverable	Date (Option 1)	Date (Option 2)
Joint Ministers' discussion	13 November	13 November
Lodgement of Cabinet paper and officials' issues paper with Cabinet Office	13 November (late lodgement)	20 November
Cabinet Committee considers Cabinet paper	19 November (ECO)	24 November (CBC)
Cabinet approval to release consultation paper	24 November	1 December
Publication of consultation paper	25 November	2 December
Submissions close	30 January 2026	30 January 2026

38 If you wanted to recognise revenue in Budget 2026, Cabinet decisions on the final policy design of the reforms would be required by early April 2026. A timeline for this and legislating the proposals is shown below.

Deliverable	Date
Report back to Ministers with advice following submissions	Late February 2026
Cabinet decisions on policy reform to allow fiscal benefits to be recognised in Budget 2026	March and April 2026
Announcement of final policy decisions	May 2026 (on or near Budget day)
Taxation Bill introduced with required amendments	August 2026
FEC consideration of taxation Bill	September 2026 to February 2027
Legislation enacted	March 2027

Recommended action

We recommend that you:

1 **Agree** to one of the following:

1.1 Inland Revenue publicly consulting on the officials' issues paper in its current form (subject to Cabinet approval). This includes the following design features as the starting points for consultation:

- New loan balances taxed as dividends if outstanding at the end of two consecutive tax years.
- A $50,000 de minimis.

- Loan balances from the date of the issues paper would be grandparented.
- The de minimis would take account of any existing loan balances.
- Taxing loans as dividends when the company is removed from the Companies Register (no de minimis applies).

Agreed/Not agreed Agreed/Not agreed

OR

1.2 Inland Revenue publicly consulting on an officials' issues paper that is amended in accordance with the following directions (subject to Cabinet approval):

Design feature	**Tick if change required**	**Detail of change required**
De minimis level	☐	
Grandparenting start date	☐	
Interaction between grandparenting and de minimis	☐	
Other change	☐	

Agreed/Not agreed Agreed/Not agreed

2 **Note** that if you do not agree to public consultation on the officials' issues paper, we will report to you separately to seek approval to introduce the proposed reform to tax shareholder loans when a company is removed from the Companies Register.

Noted Noted

s 9(2)(a)

Claire McLellan
Acting Policy Lead
Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

Appendix: Fiscal estimates of different design features

Fiscal estimate of taxing loans to shareholders when the lending company is removed from Companies Register

	$m - increase					
	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	**Total for forecast period**
Tax **all** loans when company removed from Companies Register	21	30	40	38	38	167

We note that this reform measure could be progressed independently, or alongside any of the time limit options outlined below. If both measures were implemented, the total revenues collected would be the sum of the above table and the relevant row for the time limit option in the following tables (e.g. $167 million + $920 million = $1,087 million). All the estimates in this appendix assume the measures apply from December 2025 (the date the proposals could be announced in the officials' issues paper).

Officials' recommended policy design ($50,000 de minimis, allow imputation credits, no deductions for repayment)

	$m - increase					
	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	**Total for forecast period**
Time limit on new loans: **$50,000** de minimis, **allow** imputation credits, **no** deductions for repayment	60	240	220	200	200	920

All the estimates are uncertain, and due to this uncertainty, any specific design option could potentially collect a similar amount of revenue as any other design option. The estimates are based on data of previous lending growth and required assumptions about the amount of loans in future periods and about how taxpayers may respond to the new rules.

Potential fiscal impact of increasing the de minimis (allow imputation credits, no deductions for repayment)

An increased de minimis would generate less tax revenue because fewer companies would need to replace their loans with taxable dividends or shareholder salaries.

	$m - increase					
Time limit on new loans: **allow** imputation credits, **no** deductions for repayment	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	**Total for forecast period**
$100,000 de minimis	50	230	200	190	190	860
$200,000 de minimis	50	210	180	170	170	780
$300,000 de minimis	40	190	170	160	160	720
$500,000 de minimis	40	170	150	140	140	640

Potential fiscal impact of other design changes

Some other design features that may impact the overall costings are whether to **allow** imputation credits to be attached to the deemed dividends and whether to **provide** tax deductions in a future tax year if a shareholder repaid a loan that had previously been taxed as a deemed dividend. It would be complex to provide both features (complexity would increase compliance costs). During targeted consultation, some tax advisors considered it was more important to allow imputation credits to be attached to the deemed dividend, rather than providing a deduction for repaying the loan.

No imputation credits, but **provide** deductions for repayment:

	$m - increase					
Time limit on new loans: **no** imputation credits, **provide** deductions for repayment	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	**Total for forecast period**
$50,000 de minimis	70	350	270	240	230	1,160
$100,000 de minimis	60	330	260	220	210	1,080
$200,000 de minimis	60	300	230	200	190	980
$300,000 de minimis	50	270	210	190	180	900
$500,000 de minimis	40	240	190	160	150	780

No imputation credits, **no** deductions for repayment (maximises tax collection):

	$m - increase					
Time limit on new loans: **no** imputation credits, **no** deductions for repayment	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	**Total for forecast period**
$50,000 de minimis	70	350	300	280	280	1,280
$100,000 de minimis	60	330	280	260	260	1,190
$200,000 de minimis	60	300	250	230	240	1,080
$300,000 de minimis	50	270	230	220	220	990
$500,000 de minimis	40	240	200	190	190	860

Allow imputation credits, and **provide** deductions for repayment (complex policy design):

	$m - increase					
Time limit on new loans: **allow** imputation credits, **provide** deductions for repayment	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	**Total for forecast period**
$50,000 de minimis	60	240	200	160	130	790
$100,000 de minimis	50	230	190	150	120	740
$200,000 de minimis	50	210	170	140	110	680
$300,000 de minimis	40	190	160	130	100	620
$500,000 de minimis	40	170	140	110	90	550

BUDGET SENSITIVE

Office of the Minister of Finance

Office of the Minister of Revenue

Cabinet Business Committee

Consulting on the taxation of loans made by companies to shareholders

Proposal

1 This paper seeks agreement to release a consultation paper to publicly consult on potential policy reforms to improve the efficiency and fairness of the tax system by improving the effectiveness of the rules for taxing loans provided by companies to shareholders.

Relation to government priorities

2 The proposal supports the Government's focus on simplifying and strengthening the fairness and integrity of the tax system, as outlined in the Tax and Social Policy Work Programme. This workstream advances integrity measures which maintain a simple, stable, and predictable tax system.

Executive Summary

3 Shareholders of close companies (companies controlled by a few shareholders who are natural persons or trustees) often borrow from their company. This ranges from formal loans to simply using the company's bank account as if it were their own money.

4 This behaviour is common and shareholder loans are a well established commercial mechanism. However, it can lead to large loans. Approximately 165,000 shareholders who are natural persons or trustees owed $29 billion to 119,000 companies in 2024 (about 16% of the 730,000 total companies in New Zealand). About 5,550 companies had outstanding loan balances of more than $1 million.

5 The consultation paper proposes excluding existing loans from the potential tax reforms (unless the lending company is wound up). This is intended to put reasonable limits on new lending while ensuring it would not create a new cashflow pressure on shareholders who have previously borrowed from their companies.

6 If the loans were treated as dividends they would be taxed at the shareholder's marginal tax rate (up to 39%), because they are a form of income.

7 The current rules for taxing shareholder loans can result in an unintended tax advantage for shareholders that borrow funds from the company instead of the company paying dividends. A lack of clarity in the current rules also means that they often fail to collect tax on the funds left in the hands of the shareholder when a company is wound up.

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8 This makes the tax system less fair and efficient. Shareholder loans can result in an unintended tax advantage for owners of close companies that is not available to other types of businesses such as widely-held companies, partnerships, or sole traders.

9 Other countries recognise the concerns associated with the use of shareholder loans and address them with stronger rules that tax loans as dividends if they are not repaid within certain time periods.

10 Inland Revenue has prepared the attached officials' issues paper to publicly consult on tax issues with shareholder loans. The issues paper would consult on the nature and size of the problem (including data and examples to illustrate the problem), international approaches, and a package of potential reform options.

11 Public consultation is required to ensure a full and accurate understanding of the issue, estimate the fiscal impact, and address practical issues and unintended consequences of the reform options and their design features.

12 The main policy option discussed in the consultation paper is based on the tax rules used in Canada and the United Kingdom. It would involve taxing certain company loans to shareholders that are made after the date of the issues paper as dividends if they exceed a de minimis and are not repaid at the end of two consecutive tax years.

13 To ensure tax is collected if a company is wound up, the consultation paper proposes to tax shareholders on outstanding loans when their company is removed from the Companies Register.

14 Finally, the consultation paper includes proposals for companies to report information to Inland Revenue to improve compliance with the proposed new rules for shareholder loans as well as the existing rules that determine taxable dividends when a company is wound up.

15 We expect submissions will support taxing loans when a company is removed from the Companies Register but there will be some opposition to the main reform option of introducing a time limit for repaying new loans. However, other countries use similar time limits. Also, because the proposed time limit would only apply to new loans and to large loan balances, it would have limited impact on existing arrangements or ordinary practices where small amounts are lent to company owners. The consultation paper seeks feedback on how the options could be improved.

16 If, following consultation, we decide to progress the proposed reforms we will report back to Cabinet with recommendations on the final policy design and its fiscal implications.

Background

17 Shareholders of close companies often borrow from their company to manage cashflow and fund their private expenses. Given the close relationship between the shareholder and the company, shareholder loans are often made on very informal and borrower-friendly terms.

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18 When shareholders receive dividends and other payments from their companies, the funds are fully taxed at the shareholder's marginal rate (up to 39%). In contrast, when a shareholder receives funds from their company in the form of a loan, only a small amount of tax is due on the loan interest each year (often at the 28% company tax rate, and the interest can be capitalised into the outstanding loan balance). The tax rules therefore result in an unintended tax advantage when shareholder loans are used instead of dividends and provide little incentive for shareholders to repay these loans so large amounts can remain owing indefinitely.

19 The current rules also fail to collect further tax if the company is wound up, which makes the tax advantage permanent. Media reports on company liquidations often mention shareholder loans, and have included some companies who owe debts of over a million dollars to creditors but have lent hundreds of thousands to their shareholders.

20 These problems make the tax system less fair and efficient. Owners of close companies can benefit from an unintended tax advantage. In contrast, other types of businesses such as widely-held companies, partnerships and sole traders cannot use shareholder loans and will be fully taxed (typically at 33% or 39% tax rates) when their owners receive dividends or other types of income.

21 Inland Revenue's data indicates there is a large and widespread use of loans by companies to their shareholders. Approximately 165,000 shareholders who are natural persons or trustees owed nearly $29 billion to 119,000 companies in 2024 (about 16% of the 730,000 total companies in New Zealand). For context, these companies reported $8 billion of taxable income in 2024, so the loan balances were over 3.5 times their annual income.

22 While half of these companies had outstanding loan balances of less than $50,000, some companies had made very large loans, which represented a high proportion of the total value of shareholder loans:

- About 5,550 companies had outstanding loan balances of more than $1 million (55% of the total value of all loans compared to being about 5% of all companies with shareholder loans).
- About 540 companies had outstanding loan balances of more than $5 million (22% of the value of all loans compared to being about 0.5% of all companies with shareholder loans).

Analysis

23 A recent OECD working paper on the taxation of closely held businesses recommends that countries have strict rules and monitoring to ensure company loans to shareholders are truly loans rather than artificial reductions to the shareholder's taxable income.[1]

[1] Zawisza, T. et al. (2024), "Tax arbitrage through closely held businesses: Implications for OECD tax systems", OECD Taxation Working Papers, No. 70, OECD Publishing, Paris, para 71, https://doi.org/10.1787/24b4ed4d-en

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24 New Zealand's current rules appear to be inadequate compared to the rules that are used in other countries, which tax loans as dividends if they are not repaid within certain time periods.

25 A tax policy reform is expected to improve the fairness and efficiency of the tax system by limiting the tax advantage from shareholder loans compared to paying dividends, a shareholder salary or using another type of business structure (widely-held companies, look-through companies, partnerships, trusts and sole traders).

26 We recommend publicly consulting on the problem and policy reform options to ensure a full and accurate understanding of the issue, and to identify and mitigate practical issues with any tax reform proposals. Inland Revenue has prepared the attached consultation paper for this purpose. (See Appendix One: Officials' issues paper: Improving the taxation of loans made by companies to shareholders).

27 Because the main reform option would only apply to new loans and larger loan balances above a *de minimis*, it would have limited impact on existing arrangements or ordinary practices where small amounts are lent to company owners. However, it is expected to lead to more robust accounting and tax practices by reducing the use of large, long-term lending by close companies to their shareholders.

28 The consultation paper also proposes to tax shareholders on outstanding loans when their company is removed from the Companies Register. This will improve tax collection by ensuring tax is collected at the time the company ceases to exist.

29 Both proposals are expected to reduce the integrity risk of unpaid tax on shareholder loans. They could also reduce insolvency risks because if the loan is repaid, the company would have more funds available to pay its creditors (including tax debt owed to Inland Revenue).

Main proposal: require large loans to be repaid within certain time period

30 The main proposal that would be consulted on in the consultation paper is based on the approach used in Canada and the United Kingdom to tax company loans to shareholders if they are not repaid within a certain time period.

31 Under the proposed reform, if a company had outstanding loan balances above a *de minimis* (such as $50,000) at the end of two consecutive tax years to shareholders who are natural persons or trustees, the loans would be taxed as dividends. This means the loan amount will be income to the shareholder and tax would be paid at the shareholder's marginal rate (up to 39%).

32 This proposed reform would only apply to new loans, so loans made prior to the consultation document being published would generally be excluded from the time limit.[2] This ensures the reform would not create a new cashflow pressure on shareholders who have previously borrowed from their companies. Norway and Australia similarly only applied their tax rules to new loans made by companies to

[2] If an existing loan balance increased due to additional borrowing or interest being capitalised into the loan value owing, the increased amount would become subject to the time limit rule. Also, existing shareholder loans would still be required to return tax on interest income and would be subject to tax if the loan was forgiven or if the company was removed from the Companies Register.

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shareholders after the date their reforms were first introduced. Consulting on potential tax reforms is expected to increase awareness and improve compliance with the current tax rules, which will continue to apply to existing loans.

33 The proposed value and time limits would allow shareholders to continue to borrow a limited amount from their companies to manage their cashflow without that amount being treated as a dividend. The proposal would encourage affected shareholders to repay their loans, in which case they would not face additional tax. It accommodates a common practice where short-term loans are often repaid by declaring a dividend or a shareholder salary within the 12 months following the end of the company's tax year.

34 The consultation paper also discusses the approach Australia takes, which requires the shareholder loans (including informal drawings) to be properly documented in written agreements with minimum interest rates and repayments (undocumented and non-complying loans are taxed as dividends). It notes that officials consider this would increase compliance and administration costs but is unlikely to be effective at addressing the tax issues.

Taxing shareholder loans when company removed from Companies Register

35 The use of company loans to shareholders often increases as a company begins to fail or is expected to be wound up. The existence of shareholder loans is a common feature in media reports of individual company failures. This can undermine public confidence in the tax system and the perceived fairness of limited liability companies, particularly in the more high-profile cases where the reporting often describes large shareholder loan balances, significant tax debt and debts to other creditors.

36 This problem is relatively large. Inland Revenue has analysed a dataset of about 182,000 companies that were removed from the Companies Register over a nearly six-year period between 1 April 2019 and early 2025. Nearly 15% of these companies (about 27,000) had reported they had loans to natural person or trustee shareholders in their last filed tax return prior to being removed from the Register. The total amount that they were owed by these shareholders was approximately $2.3 billion, with an average amount per company of nearly $85,000. Because the current tax rules do not deem these loans to be treated as taxable dividends before the company is removed from the Register, no tax is collected from the shareholder.

37 To address this problem, the consultation paper proposes shareholder loans would be taxable income for the shareholder when the lending company is removed from the Companies Register. This would impose clear tax obligations on the company and shareholder, and improve Inland Revenue's ability to collect the tax, including on existing loans.

Reporting information to Inland Revenue

38 The consultation paper also consults on proposals for companies to report information to Inland Revenue to improve compliance with the proposed new rules for shareholder loans as well as the existing rules that determine taxable dividends when a company is wound up.

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Next steps

39 The new rules would be complex and therefore require consultation to identify and mitigate unintended consequences and practical issues. We recommend publishing the attached public consultation paper for this purpose.

40 Subject to Cabinet agreeing to publish the attached consultation paper, the public consultation would occur from early December 2025 to late January 2026.

41 We plan to report back to Cabinet with final policy recommendations in early 2026. If Cabinet decided to proceed with a tax reform, we would aim to announce final Cabinet decisions as part of Budget 2026, introduce legislation in mid-2026 and implement the new rules from 1 April 2027.

Cost-of-living Implications

42 The proposed reform would not have specific cost-of-living implications because it would not affect the cost of everyday expenses.

Financial Implications

43 Releasing the attached consultation paper for consultation has no fiscal implications. If, following consultation, we decide to progress and implement stronger tax rules for company loans to shareholders it will increase tax revenue. Accordingly, we will report back to Cabinet with recommendations on the final policy design and its fiscal implications.

Legislative Implications

44 If, following consultation, Cabinet decides to proceed with new tax rules, changes to the Income Tax Act 2007 and Tax Administration Act 1994 will be necessary. Any new tax measures could be included in the 2026–27 annual rates omnibus taxation Bill, which does not yet have a slot or priority category on the Legislation Programme but is expected to be enacted in March 2027.

Impact Analysis

45 As required by the Ministry for Regulation, Inland Revenue’s Quality Assurance panel has reviewed the consultation paper and determined that it will lead to effective consultation and enable the development of future impact analysis. Therefore, a separate regulatory impact statement (RIS) is not required at this stage. A full RIS will be completed at a later stage to inform Cabinet's final decisions on this proposal.

Population Implications

46 The proposal does not have any specific impacts for population groups.

Human Rights

47 The proposal is consistent with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

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Consultation

48 The Treasury, Inland Revenue, the Ministry of Business, Innovation and Employment, and the Ministry for Regulation were consulted on this Cabinet paper.

49 The design of improved tax rules for loans to shareholders is complex and requires public consultation to identify and mitigate practical issues and unintended consequences of the potential reforms. We recommend publishing the attached public consultation paper to support the consultation process.

50 Officials conducted targeted consultation on a strict in-confidence basis with 14 trusted private sector tax advisors. Based on the targeted consultation feedback, we expect submissions will support taxing loans when a company is removed from the Companies Register but there will be some opposition to the main reform option of a time limit for repaying new loans. This is because they may consider the current rules which require tax to be paid on an annual amount of interest income are adequate and loans should only be reclassified as taxable dividends in egregious cases (such as deliberate tax avoidance).

51 However, other countries use similar time limits. Also, because the proposed time limit would only apply to new loans and to large loan balances above a *de minimis,* it would have limited impact on existing arrangements or ordinary practices where small amounts are lent to company owners. The consultation paper seeks feedback on how the options could be improved.

Communications

52 Inland Revenue could issue a press release or factsheet when the proposed officials' issues paper is published for public consultation.

Proactive Release

53 The Ministers of Finance and Revenue propose to delay the proactive release of this Cabinet paper, associated minutes and key advice papers with appropriate redactions until after Budget 2026.

Recommendations

The Ministers of Finance and Revenue recommend that the Committee:

1 Note that close companies with only a few shareholders often lend funds to their shareholders and Inland Revenue's data indicates there is large and widespread use of these shareholder loans.

2 Note New Zealand's current tax rules result in an unintended tax advantage when close companies loan funds to their shareholders instead of paying taxable dividends and other countries have stronger rules to address this by taxing loans as dividends if they are not repaid within certain time periods.

3 Authorise Inland Revenue to publicly consult on the nature and size of the problem, international approaches, and a package of potential reforms to the tax rules that apply to company loans to shareholders.

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4 Note the attached draft consultation paper "Officials' issues paper: Improving taxation of loans made by companies to shareholders".

5 Authorise the Ministers of Finance and Revenue to approve editorial and other minor changes to the consultation paper before its release.

6 Agree to releasing the attached consultation paper for public consultation.

7 Invite the Ministers of Finance and Revenue to report back to Cabinet on the outcome of consultation and final recommendations in early 2026.

Hon Nicola Willis

Minister of Finance

Hon Simon Watts

Minister of Revenue

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Appendix

Officials' issues paper: Improving taxation of loans made by companies to shareholders.

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Cabinet Business Committee

Minute of Decision

This document contains information for the New Zealand Cabinet. It must be treated in confidence and handled in accordance with any security classification, or other endorsement. The information can only be released, including under the Official Information Act 1982, by persons with the appropriate authority.

Taxation of Loans Made by Companies to Shareholders: Release of Consultation Paper

Portfolios **Finance / Revenue**

On 24 November 2025, the Cabinet Business Committee:

1 **noted** that close companies with only a few shareholders often lend funds to their shareholders, and that Inland Revenue's data indicates there is large and widespread use of these shareholder loans;

2 **noted** that:

2.1 New Zealand's current tax rules result in an unintended tax advantage when close companies loan funds to their shareholders instead of paying taxable dividends;

2.2 other countries have stronger rules to address this by taxing loans as dividends if they are not repaid within certain time periods;

3 **authorised** Inland Revenue to publicly consult on the nature and size of the problem, international approaches, and a package of potential reforms to the tax rules that apply to company loans to shareholders;

4 **noted** the draft consultation paper *Officials' Issues Paper: Improving Taxation of Loans Made by Companies to Shareholders* (the consultation paper), attached to the paper under CBC-25-SUB-0064;

5 **agreed** to the release of the consultation paper, subject to any editorial and other minor changes that may be authorised by the Minister of Finance and the Minister of Revenue before its release;

6 **invited** the Minister of Finance and the Minister of Revenue to report back to Cabinet on the outcome of the consultation and with final recommendations in early 2026.

Jenny Vickers
Committee Secretary

Attendance: (see over)

Present:
Rt Hon Christopher Luxon (Chair)
Hon David Seymour
Rt Hon Winston Peters
Hon Nicola Willis
Hon Chris Bishop
Hon Simeon Brown
Hon Brooke van Velden
Hon Shane Jones
Hon Erica Stanford
Hon Louise Upston
Hon Judith Collins KC
Hon Todd McClay
Hon Simon Watts
Simon Court MP

CAB-25-MIN-0428

Cabinet

Minute of Decision

This document contains information for the New Zealand Cabinet. It must be treated in confidence and handled in accordance with any security classification, or other endorsement. The information can only be released, including under the Official Information Act 1982, by persons with the appropriate authority.

Report of the Cabinet Business Committee: Period Ended 28 November 2025

On 1 December 2025, Cabinet made the following decisions on the work of the Cabinet Business Committee for the period ended 28 November 2025:

Not in scope

CBC-25-MIN-0064	**Taxation of Loans Made by Companies to Shareholders: Release of Consultation Paper** Portfolios: Finance / Revenue	CONFIRMED

Not in scope

Rachel Hayward
Secretary of the Cabinet

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Briefing note

Reference	BN2026/055
Date	19/02/2026
To	Revenue Advisor, Minister of Finance – Carl Harris Revenue Advisor, Minister of Revenue – Angela Graham Private Secretary, Minister of Revenue – Melissa Zhen
From	Gordon Witte, Principal Policy Advisor
Subject	**Shareholder loans – consultation feedback and next steps**

Purpose

1 Public consultation on the proposed tax reforms for company loans to shareholders has closed. We received 38 submissions and met 9 submitters.[1]

2 This note summarises the consultation feedback and outlines potential next steps for communicating with stakeholders and briefing Ministers.

Background and overview of current thinking

3 The package of proposed reforms in the December 2025 officials' issues paper was:

- *Time limit for repaying new loans*: If a new loan is not repaid within 12 months after the income year in which it was made then it could be taxed as a dividend. To reduce the impact on small businesses and ordinary business practices, the proposed time limit would only apply to companies whose total lending to shareholders was more than $50,000.
- *Taxing loans when a company ceases*: A new rule would ensure that any outstanding loans are taxed when a company is removed from the Companies Register.
- *Improved reporting:* Companies would be required to provide additional information to Inland Revenue to ensure compliance.

4 Consultation has helped us to refocus the problem to loans which are not ultimately repaid and to understand why companies lend funds to shareholders and how the proposed reforms could impact the affected companies. Officials acknowledge feedback from submitters that, while the company cessation proposal is clearly linked to the policy problem, the time limit would have a significant impact on loans which are being appropriately used and managed.

5 Officials are now considering a more targeted alternative to the time limit and will report to Ministers with further advice on this and other potential changes in response to submissions on 5 March. We consider it useful to be able to communicate this thinking with stakeholders sooner rather than later to provide some assurance that submissions are being taken into account.

[1] ATAINZ, CA ANZ, CPA, Deloitte, EY, NZLS, OliverShaw, PwC, Tax Justice Aotearoa

6 Compared to the initial proposals, a more targeted option would collect much less tax revenue than a broad time limit.

Submission themes

Problem occurs when loans are not repaid, rather than an inherent tax advantage

7 Submissions considered the problem was unclear and generally disagreed that there was an unintended tax advantage or unfairness from using shareholder loans. Submitters raised concerns that the proposals in the issues paper treated all shareholders loans as being a problem. In their experience, nearly all shareholder loans were for legitimate commercial or practical reasons and were compliant with paying the required interest on the loan and with the loan being eventually repaid (including by the company paying dividends or salary to the shareholder to clear the loan balance).

8 We have reflected on the problem and consider the focus of this work should be situations whereloan balances become unmanageable and ultimately leave amounts not able to be repaid.

Current rules are adequate in most cases

9 Submissions noted examples of commercial and practical reasons why shareholder loans arise which are not motivated by any potential tax benefit. There are a wide variety of loans, including some which arise unintentionally and may only be recognised later (e.g. as part of an accounting audit or due diligence when selling the business).

10 Some submitters explain that because loans incur additional tax costs on interest income, more tax could be paid after about 6 years compared to a salary or imputed dividend being paid in the first year.

11 Submissions generally consider New Zealand's current rules provide a sufficient incentive to repay the loans. In their experience as accountants and tax advisors, shareholders are motivated to repay their loans as that is best practice and minimises overall costs. Some consider the failure to repay loans may be due to poor compliance capability / understanding of the tax costs and that guidance, education and compliance activity would better address this problem (Business NZ, CA ANZ, Deloitte, EY).

Support for taxing loans when the company ceases

12 Submissions support the proposal to ensure shareholders pay tax on loans if the lending company ceases (is removed from the Companies Register). This proposal could proceed as a standalone reform, ahead of any wider reform to shareholder loans. It is estimated to generate $167m over the forecast period.

13 Submissions suggested some improvements to the proposed design (e.g. using the financial arrangement rules rather than deeming a dividend and applying the rules 6 months after the company is removed) which officials are likely to recommend.

Concerns proposed time limit would be too broad / disruptive

14 Only three submissions[2] supported the proposed time limit for repaying new loans. Other submissions were opposed as they consider it would be significant overreach, unduly impacting ordinary practices and compliant shareholders who will eventually repay the loan. They consider it would significantly increase the complexity of the tax

[2] Tax Justice Aotearoa, Booster, s 9(2)(a)

rules and impose high compliance and tax costs on close companies, disproportionate to the problem of loans which are never repaid.

15 Many submissions noted other countries have differences in their tax systems (e.g. they don't have imputation, have larger gaps between company and dividend tax rates, and have capital gains taxes) which could increase any potential tax risks from using shareholder loans. They therefore considered the time limit rules in other countries are not appropriate for New Zealand. One submitter noted that US tax rules for shareholder loans were similar to NZ's current rules.

16 Submitters have provided examples where the proposed time limit would impose larger disruption and costs on ordinary commercial practices than we initially thought. It could deem dividends in cases where the loan was used for valid commercial reasons, exceeded the de minimis, was likely to be repaid (but could not be repaid during the next tax year) and is unlikely to be providing the shareholder with a significant tax advantage.

17 Officials are mainly concerned about taxpayers who draw down loans, often over time, which are never repaid. Requiring new loans to be repaid during the following tax year would impact a much wider range of loans which are likely to be repaid in subsequent years under the current rules. Furthermore, a time limit would not apply to some high-risk cases such as loans made in the last few months before a company closes (the company cessation proposal would apply instead).

Higher de minimis and longer time limit

18 Although most submitters consider a strict time limit rule was the wrong approach due to its broad impacts, some submitted that if it did proceed it should have a higher de minimis value[3] and a longer time limit.[4]

19 Some submitters considered the de minimis should be per shareholder rather than per company (Buddle Findlay, Deloitte). ATAINZ and Deloitte consider the de minimis should only apply to new loans.

20 While officials can provide further advice on higher de minimis amounts and longer time limits, we think they are unlikely to address submitters' overall concerns with the time limit applying too broadly and being poorly targeted at the problem of loans which are ultimately not repaid.

Mixed views on Australia's rules

21 Some submitters[5] suggested New Zealand should adopt Australia's rules, although submissions also cautioned that Australia's rules were complex. Australia's rules effectively provide a 7-year time limit for loans which have been properly documented with a minimum interest rate and repayment terms, increasing to 25 years if the loan is secured over land.

[3] $100k (s 9(2)(a) , Accountants Studio, Hargreen Accountants), $150k (EY), $100k-$250k (ATAINZ), $500k (s 9(2)(a)), $750k (BVO), $1m (CA ANZ and Federated Farmers), $2m (OliverShaw), $2.5m (s 9(2)(a))

[4] 2 years (s 9(2)(a)), 3 (Russell McVeagh), 5 (Federated Farmers, s 9(2)(a)) or 7 years (CA ANZ, Deloitte)

[5] CPA Australia, s 9(2)(a) , EY, s 9(2)(a) , Russell McVeagh, Sharpe Tudhope

Develop a targeted rule instead of a broad time limit

22 Some submissions suggest a targeted rule should be developed instead.[6] CA ANZ noted that the rule could include some high value and time limits (e.g. $1m and 7 years) for certainty but should include a rebuttable presumption so the taxpayer could provide evidence to Inland Revenue to explain why their loan doesn't meet the criteria for being taxed as a dividend. OliverShaw suggested reconsidering a 2018-19 Tax Working Group recommendation that if IRD had reasonable concerns that the loan might not be repaid it could require the loan to be formally documented with the shareholder providing adequate security.

23 Officials consider a more targeted policy option is worth exploring. We are currently considering the potential parameters for more targeted rule and will prepare further advice on the effectiveness of this approach at addressing the problem and mitigating unintended impacts.

24 Rather than applying to all companies which lend funds to their shareholders (based on the most recent IR data, 119,000 companies), it could apply to a much smaller group of companies where there appears to be a significant risk of the shareholder never repaying the loan (e.g. company owes old tax debt, doesn't meet solvency criteria for paying a dividend etc).

25 A targeted rule could effectively expand the scope of the removal from the Companies Register proposal. It could address a weakness of that proposal as rather than waiting for the company to be removed from the Register or liquidated (by which time the shareholder may no longer have the financial means to pay the tax), it could allow Inland Revenue to assess tax on the shareholder loan earlier.

26 Because a targeted option would represent a new policy option, officials would recommend conducting further consultation with submitters to test and refine the new option before finalising its design.

Application date should be delayed / reconsidered

27 Some submitters considered any new rules should apply from date of enactment to ensure certainty (s 9(2)(a) , Deloitte, EY, Taxpayer's Union), with limited anti-avoidance rules to guard against any transitional integrity risks. Others (Buddle Findlay) noted transitional measures may be required if there was a significant gap between 4 December 2025 and the date the legislation is enacted.

28 If a more targeted rule was progressed, it would likely apply to existing loan balances, which would allow the application date of the targeted rule to be prospective from enactment. Officials are still likely to recommend that companies removed from the Companies Register on or after 4 December 2025 be subject to the removal from the Register proposal.

Qualified support for information reporting proposals

29 Submitters were generally supportive of the need for improved information reporting for available subscribed capital (ASC) and available capital distribution amount (ACDA). Despite this support, some submitters cautioned that mandatory reporting could impose disproportionate compliance costs on SMEs, as the amounts may not ever become relevant for some companies.[7]

[6] Business NZ, CA ANZ, Corporate Taxpayer's Group, Co-operative Business NZ, Deloitte, OliverShaw

[7] CAANZ, s 9(2)(a) , BVO, s 9(2)(a) , CPA Australia.

Next steps

30 Officials plan to report to Ministers by 5 March with advice on the proposals in the issues paper and alternative policy options such as a targeted alternative to a broad and strict time limit. This advice could be discussed at the joint Ministers meeting on 9 March.

31 As we develop more targeted options, we will prepare fiscal estimates for any new policy options. Compared to the broad time limit which IRD consulted on in the issues paper, a targeted option would collect much less tax revenue as far fewer shareholder loans would be subject to additional tax.[8]

32 As noted earlier, the company cessation proposal could be progressed as a standalone reform and was estimated to generate $167m of additional tax over the forecast period. This could be supplemented by a targeted measure that would apply prior to the lending company ceasing and could therefore collect additional tax revenue.

33 We're aware that some stakeholders are particularly concerned about the uncertainty of the proposals, especially the impact of the proposed time limit potentially applying to loans made from 4 December 2025. As officials consider a more targeted measure, it would be useful to consult stakeholders to develop and refine this. To reduce uncertainty, we could communicate our intentions to develop a more targeted alternative to the time limit that was proposed in the issues paper. Subject to Ministers' comfort, this could be informally as part of ongoing consultation with submitters or more widely via an update to the tax policy website.

Gordon Witte

Principal Policy Advisor

s 9(2)(a)

[8] Either directly from a deemed dividend, or indirectly as taxable dividends and salaries are paid to clear loan balances earlier than the status quo.

Inland Revenue
Te Tari Taake

MINISTRY OF SOCIAL DEVELOPMENT
TE MANATŪ WHAKAHIATO ORA

TE TAI ŌHANGA
THE TREASURY

Tax policy report: Working for Families: Changes to residency requirements, information sharing and definition of income

Date:	29 October 2025	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2025/379 T2025/2673 REP/25/10/818

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to recommendations	12 November 2025
Minister for Social Development and Employment/Minister for Child Poverty Reduction	**Agree** to recommendations	12 November 2025
Minister of Revenue	**Agree** to recommendations	12 November 2025

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Paul Young	Acting Policy Lead, Inland Revenue	s 9(2)(a)	☒
Melissa Siegel	Principal Policy Advisor, Inland Revenue		☐
Alex Harrington	Principal Advisor, Welfare and Oranga Tamariki, The Treasury		☒
Alana Roughan	Principal Analyst, Ministry of Social Development (Social Development and Employment)		☒
Deborah Tucker	Principal Analyst, Ministry of Social Development (Child Wellbeing and Poverty Reduction)		☐

29 October 2025

Minister of Finance
Minister for Social Development and Employment
Minister for Child Poverty Reduction
Minister of Revenue

Working for Families: Changes to residency requirements, information sharing and definition of income

Executive summary

Purpose and background

1. The policy proposals outlined in this report are to simplify the residency requirements for Working for Families tax credits, progress improved information sharing with the New Zealand Customs Service (Customs), and simplify the definition of family scheme income.

2. These proposals have merit on their own but would also support changes to s 9(2)(f)(iv) a shorter assessment period, should Ministers agree to these on the basis of future advice.

Problem definition and proposals

3. The Working for Families scheme is complex, making it difficult for recipients to understand what they need to do to comply and how changes will impact their payments. It also results in a large administrative burden for Inland Revenue.

4. The proposals in this report would simplify Working for Families and help to prevent overpayments, meaning less debt would be generated and families would find it easier to interact with the scheme. The proposals also lay the groundwork for more fundamental changes in the future (such as changes to s 9(2)(f)(iv) a shorter period of assessment).

Next steps

5. If Ministers agree to proceed, work on simplifying family scheme income, changes to residency requirements, and the Approved Information Sharing Agreement with Customs will continue.

6. Officials will provide further advice on changes to s 9(2)(f)(iv) a shorter period of assessment, and the Minimum Family Tax Credit before the end of 2025.

Background and purpose

7. This report is the first in a series of reports which outline policy options to simplify the Working for Families scheme, address debt issues, and improve integrity. It seeks your agreement to continue detailed policy design work on three smaller proposals which could be included in Budget 2026.

8. On 29 September, Ministers met to discuss the role that Working for Families changes could play in a potential welfare reform package for Budget 2026 and beyond. Ministers confirmed the key objectives were incentivising people to enter work or work more hours, keeping fiscal targets in mind. They also indicated interest in progressing specific changes to improve information sharing and simplify the

definition of family scheme income for Working for Families purposes. The Government publicly consulted on these proposals in consultation following the release of the discussion document *Empowering families: increasing certainty and preventing debt in the Working for Families scheme* ("the discussion document"), at Budget 2025. We have previously provided you with a summary of submissions on the discussion document [*IR2025-221, T2025/2105, REP/25/8/616 refers*].

Problem definition and objectives

9. The Working for Families scheme is highly complex. Families struggle to understand the information they are required to provide, and the ways in which their working hours, care levels, types and amounts of income can impact their Working for Families entitlements. These issues have led to persistent under- and over-payments, uncertainty and debt at an additional cost to Government, and can disincentivise paid work for some customers. They also create administrative burden and inefficiency for Inland Revenue and the Ministry of Social Development.

10. The recommendations for a Working for Families work programme in this report series aim to simplify the scheme, improve integrity and payment accuracy, and reduce the risk of overpayments while maintaining fiscal sustainability and reducing administrative burden.

Simplifying residence requirements

11. To qualify for Working for Families, recipients must meet specific residence requirements on an ongoing basis. These must all be met by either the person caring for a dependent child (the principal caregiver), or the child themself. The requirements are not the same for the principal caregiver test and the dependent child test. While there is some commonality, some requirements are unique to either the principal caregiver or the dependent child as shown in the table below:

	Principal caregiver	**Dependent child**
Living in New Zealand	Ordinarily resident in New Zealand	
Visa status	Lawfully resident in New Zealand, not on a temporary entry class visa	
Physical presence	Have been physically present in New Zealand for a continuous period of 12 months at any time	Physically present in New Zealand for the entitlement period
Tax residence	Tax resident in New Zealand	N/A

12. The current residency rules can be difficult for families to understand. Families who leave New Zealand and no longer qualify are required to inform Inland Revenue to stop payments. However, families do not always advise of their departure. In this case they will continue to be paid until Inland Revenue systems or staff raise an issue. Inland Revenue then requests information from Customs about the border movements of that family before their payments can be stopped. The family's account is reassessed, and a debt is created. Debt recovery is uncertain and expected to be low in these situations. While it is difficult to determine the true cost of this issue, we estimate that in the 2022-23 tax year, between $12 and $25 million in payments were made to Working for Families recipients who had relocated permanently from New Zealand.

13. We recommend simplifying the residence requirements for Working for Families so that both the principal caregiver and the dependent child must meet all requirements. The test should consider their legal authority to be in New Zealand

and physical presence here, as well as whether they are "ordinarily resident" to ensure that visitors cannot qualify for Working for Families when they are in New Zealand for a limited time and do not intend to reside in the country permanently.[1] However, the link to tax residence and a minimum 12-month period in the country would be removed.

14. This should be accompanied by a tolerance for short periods of physical absence to enable families to go overseas on holiday or to visit family, for example. In the discussion document, a period of six weeks was suggested. If a family is out of the country for longer than this period, their Working for Families payments would stop.

15. During consultation, the proposed period of six weeks was broadly viewed as an appropriate length for someone to be physically absent from New Zealand before losing their eligibility for Working for Families, although this sentiment was not universal. Written submitters did raise the importance of this period being consistent with other residence requirements. Submitters emphasised the importance that any period should allow for consideration of life events that require people to travel overseas.

16. We recommend including a limited range of exceptions where individuals would continue to be treated as though they were present in New Zealand, for example, if they are overseas in the service of the New Zealand Government, for death or illness of a close family member, or certain global or national events that restrict air travel (such as a pandemic or volcanic eruption).

17. Changes could be included in the next omnibus taxation bill, likely introduced in August 2026, and apply from 1 April 2027.[2] Alternatively, changes could be included in a Budget 2026 bill with the same application date.

Sharing border movement information

18. The Ministry of Social Development has an information sharing agreement with Customs which allows it to receive information on beneficiaries leaving the country. This enables the Ministry of Social Development to stop payments in a timely manner, even if a recipient has not notified it that they are leaving New Zealand.

19. We recommend expanding Inland Revenue's information sharing with Customs to include border movements of customers who receive Working for Families payments. In combination with simplifying the residency requirements, this would enable Inland Revenue to automatically stop payments when a principal caregiver has been out of the country for a specified period and is no longer entitled to receive Working for Families. This information sharing is a necessary step to ensure the proposed residence requirements work effectively in practice and should be implemented at the same time (by 1 April 2027).

20. The discussion document included two options to implement an information sharing agreement. Further discussions between Inland Revenue and Customs have indicated that the only viable option is an Approved Information Sharing Agreement. The Office of the Privacy Commissioner previously noted that this is its preferred option to enable this information sharing under the Privacy Act 2020. The standard timeframe for putting an Approved Information Sharing Agreement in place is around 18 months. This means an application date of 1 April 2027 to align with the proposed start date of the new residence requirements is feasible. If the Approved Information Sharing Agreement is effective before then, information received could be used to better understand trends and impacts and allow Inland Revenue to prepare to support impacted customers.

[1] For example, Australian citizens are automatically granted a resident visa on arrival and without an ordinarily resident test, they would qualify for Working for Families while in New Zealand on holiday.
[2] Changes to the residence rules for Working for Families should apply from the start of a tax year.

21. There was support in public consultation for targeted information sharing and clearer residency rules to ensure payments are accurate without being overly punitive or complex, with appropriate safeguards in place for information sharing.

Definition of family scheme income

22. Working for Families entitlements are calculated based on family scheme income, which includes the income of the principal caregiver, their partner and children. The definition of family scheme income is broad to ensure targeting of support and to reduce the risk of fraudulent behaviour through income structuring. It is based on net income for tax purposes plus or minus adjustments outlined in legislation. Most adjustments increase family scheme income.

23. The current definition of family scheme income is complex and can be confusing for customers. All customers are asked to verify whether these income adjustments apply to them even though for most customers, family scheme income is the same as their net income for tax purposes.[3] In the 2021–22 tax year, only 2% of Working for Families customers had income adjustments included in their calculation.[4]

24. We recommend simplifying the definition of family scheme income by removing some income adjustments based on how commonly they are used and the level of risk they present to the integrity of the Working for Families scheme. For those adjustments that remain, administration would be improved by making better use of the information Inland Revenue holds.

25. Inland Revenue officials consider some income types to be low risk because they are not an effective way of minimising family income. Some of the less frequently used income types, such as requiring families to declare some pensions and annuities for Working for Families purposes, could be removed without substantially increasing the risk to the integrity of the scheme.

26. Simplifying family scheme income would help address complexity, resolve some of the customer compliance, payment accuracy and debt issues, and reduce administrative burden. It would also allow Inland Revenue to better allocate resources to maintain the integrity of the tax system.

27. As part of this simplification, increased legislative flexibility could be introduced to provide a mechanism for the inclusion of new income types in the future should they become an integrity risk. This would future-proof and further protect the integrity of Working for Families.

28. Most submissions on the recent discussion document did not comment on the proposal to simplify family scheme income. Those that did were generally supportive of simplification based on analysis of usage and risk for each adjustment type, with the caveat that any changes needed to be clearly communicated.

29. The Ministry of Social Development and the Ministry of Health[5] also use family scheme income to calculate certain entitlements. The Ministry of Social Development uses family scheme income as part of assessing eligibility for three sources of financial assistance: as part of the Parental Income Test for Student Allowance, the income test for a Community Services Card for low-income earners with dependent children, and as part of the Parental Income Test of the Young Parent Payment. The Ministry of Social Development will need to update guidance, forms, and web content to reflect the updated definition and communicate the changes to clients.

[3] This excludes child support, as many Working for Families customers have child support amounts either paid or received, which also adjusts family scheme income.
[4] Other than adjustments for child support.
[5] For community services card purposes

30. The Ministry of Social Development considered whether by changing the definition of family scheme income, it would be required to reassess entitlements based on the revised definition. Their initial view is that there is no requirement to reassess entitlements for Student Allowance, Community Services Card or the Young Parent Payment based on the revised legislative definition of income.

s 9(2)(f)(iv)

Moving to a shorter period of assessment

35. A high number of under- and over-payments during the tax year are due to incorrect income estimates; it can be very challenging for families to get this right, particularly over a long period. On the other hand, an annual period of assessment is the internationally accepted norm for payments delivered via the tax system, and provides individuals with the ability to 'smooth' their income over a longer period.

36. Officials are considering options to move from an annual period of assessment based on estimated income and current circumstances with potentially significant end of year square-ups, to a shorter (quarterly) period based on lagged income, as

s 9(2)(f)(iv)

well as either lagged or current circumstances. These options could increase the certainty of payments and reduce debt for many families. This could involve some negative trade-offs for those families with variable income due to the misalignment between the timing of the payments a person receives and the period of income used to determine those payments, however, it would be more accurate during the year and wouldn't require end of year adjustments.

37. Submitters had a mixed response to the proposal on a shorter period of assessment. While many agreed that the current model does not work for many families, the complexity of the issue and potential trade-offs for low-income families with variable income meant there was no consensus on what a better approach would look like. We will provide further advice on shorter periods of assessment by the end of the year.

Intermediaries

38. Public consultation highlighted that stakeholders struggle with the complexity of Working for Families and saw potential for intermediaries to help. However, barriers such as cost and privacy concerns mean intermediaries are prevented from helping or are reluctant to get involved in Working for Families. Officials recommend that Inland Revenue should continue to assess opportunities for intermediation and develop a wider intermediary strategy for Working for Families.

Sequencing and dependencies

39. We recommend that implementation is sequenced, with changes to residency requirements, information sharing and family scheme income implemented prior to the more complex changes to s 9(2)(f)(iv) the period of assessment noted in this report. This report seeks agreement to work on detailed design for these options to include them as part of the package put forward for Budget 2026 and implemented by 1 April 2027. These initiatives collectively are expected to result in fiscal savings of $48.4 million over the forecast period.

40. Even if changes to s 9(2)(f)(iv) moving to a shorter assessment period do not progress, changes to residency and information sharing of border movements of Working for Families recipients with Customs have merit, as does simplifying the definition of family scheme income.

Administrative implications

41. Inland Revenue has completed initial administrative costings for Vote Revenue for the three proposals. These costings are based on high-level assumptions for the changes being considered and are conservative estimates given the lack of certainty at this time. Inland Revenue will refine these costs as part of subsequent work on detailed policy design. Cost estimates may change based on policy settings and implementation timing.

Simplifying residence requirements and sharing border movement information

42. We estimate the one-off cost to Inland Revenue for implementing an information share with Customs and changing the residence rules to be around $1 million. The residency changes would be built to automate the facilitation of border movements and the end dating of Working for Families entitlements. Although this change would introduce new processes to administer the proposed exemptions and permit changes to who is the principal caregiver within a family, this would also reduce follow-up work that occurs as a result of overpayments. Therefore, while Inland Revenue would incur increased ongoing costs over the forecast period 2025/26 to 2029/30, we anticipate these costs to balance out with benefits of reducing current

administrative work. These achieved savings would help fund the aforementioned ongoing cost.

43. The administrative costings have been completed on the assumption that the system solution will enable significant automation of the end dating of Working for Families payments based on data received from Customs and any exemptions will be able to be self-serviced by the customers.

44. Cost impacts of implementing information sharing with Customs are subject to completion of confirmed costings. Customs will provide further information on the cost and any further operational impacts of implementing an Approved Information Sharing Agreement as scoping is completed.

Definition of family scheme income

45. We estimate the one-off implementation cost to Inland Revenue to be around $0.500 million and no increase in ongoing cost over the forecast period 2025/26 to 2029/30. This would include updating forms and related content to help impacted customers understand the changes.

Combined administrative implications

46. Inland Revenue would be able to confirm how much can be covered through self-funding for both the above measures once the whole suite of initiatives covered in this report, their components and options, and the timing of implementation have been decided on by Ministers. In relation to the family scheme income proposal, the Ministry of Social Development can provide cost implications through the Budget 2026 process.

Indicative costings/financial implications

47. Overall, excluding the administrative implications noted above, the three proposals are expected to save $48.400 million over the forecast period. This would have a corresponding positive impact on the operating balance and the Budget 2026 operating allowance, as set out in the table below.

	$ million – increase/(decrease)					
Summary	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	Total
Residency requirements	-	-	(8.900)	(13.500)	(13.200)	(35.600)
Information sharing	-	-	(3.300)	(10.300)	(10.200)	(23.800)
Simplifying definitions	-	0.800	3.200	3.500	3.500	11.000
Total Operating	**-**	0.800	(9.000)	(20.300)	(19.900)	(48.400)

48. The fiscal impact of changing the Working for Families residence requirements with application from 1 April 2027 is set out in the following table. It is contingent on the information share with Customs being in place.

	$ million – increase/(decrease)					
Vote Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	Total
Non-departmental Benefits or Related Expenses						
Family Tax Credit	-	-	(4.500)	(4.400)	(4.300)	(13.200)
In-Work Tax Credit	-	-	(1.600)	(1.600)	(1.600)	(4.800)
Best Start Tax Credit	-	-	(0.500)	(0.500)	(0.500)	(1.500)
Subtotal	-	-	(6.600)	(6.500)	(6.400)	(19.500)
Non-departmental Other Expenses	-	-	(2.300)	(7.000)	(6.800)	(16.100)

Impairment of Debt and Debt Write-offs						
Total Operating	-	-	(8.900)	(13.500)	(13.200)	(35.600)

49. The fiscal impact of the introduction of the information sharing agreement with Customs from 1 April 2027 is as follows:

	$ million – increase/(decrease)					
Vote Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	Total
Non-departmental Benefits or Related Expenses						
Family Tax Credit	-	-	(2.800)	(8.600)	(8.500)	(19.900)
In-Work Tax Credit	-	-	(1.000)	(3.100)	(3.100)	(7.200)
Best Start Tax Credit	-	-	(0.300)	(1.000)	(1.000)	(2.300)
Subtotal	-	-	(4.100)	(12.700)	(12.600)	(29.400)
Non-departmental Other Expenses Impairment of Debt and Debt Write-offs	-	-	0.800	2.400	2.400	5.600
Total operating	-	-	(3.300)	(10.300)	(10.200)	(23.800)

50. The fiscal impact of changing the definition of family scheme income for Working for Families from 1 April 2027 is as follows:

	$ million – increase/(decrease)					
Vote Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & outyears	Total
Non-departmental Benefits or Related Expenses						
Family Tax Credit	-	0.600	2.400	2.600	2.600	8.200
In-Work Tax Credit	-	0.100	0.500	0.600	0.600	1.800
Best Start Tax Credit	-	0.100	0.300	0.300	0.300	1.000
Subtotal	-	0.800	3.200	3.500	3.500	11.000
Non-departmental Other Expenses Impairment of Debt and Debt Write-offs	-	-	-	-	-	-
Total Operating	-	0.800	3.200	3.500	3.500	11.000

Consultation

51. Inland Revenue have consulted with Customs on the relevant parts of this report.

52. Officials will provide further advice in our next report, before the end of 2025, regarding any further consultation on the proposals outlined in that report.

Next steps

53. If Ministers agree to proceed:

    53.1 Inland Revenue and Customs officials will continue to work on progressing towards an Approved Information Sharing Agreement for sharing border movements of Working for Families customers.

53.2 Officials will progress detailed policy design for simplifying the residence requirements and the definition of family scheme income for Budget 2026 consideration.

53.3 s 9(2)(f)(iv)

53.4

54. Policy advice on longer-term Minimum Family Tax Credit options will be provided in a separate report in November alongside the Budget 2026 advice.

Recommended action

We recommend that you:

1. **agree** that detailed policy design for simplifying the Working for Families residency requirements be progressed for Budget 2026 consideration

Agreed	**Agreed**	**Agreed**
Minister of Finance	Minister for Social Development and Employment Minister for Child Poverty Reduction	Minister of Revenue

2. **agree** that officials work on progressing an Approved Information Sharing Agreement enabling border movements of Working for Families customers to be shared between Inland Revenue and Customs

Agreed	**Agreed**	**Agreed**
Minister of Finance	Minister for Social Development and Employment Minister for Child Poverty Reduction	Minister of Revenue

3. **agree** that detailed policy design for simplifying the definition of family scheme income be progressed for Budget 2026 consideration

Agreed	**Agreed**	**Agreed**
Minister of Finance	Minister for Social Development and Employment Minister for Child Poverty Reduction	Minister of Revenue

4. **refer** this report to the Minister of Customs.

Referred/ Not referred	Referred/ Not referred	Referred/ Not referred
Minister of Finance	Minister for Social Development and Employment Minister for Child Poverty Reduction	Minister of Revenue

s 9(2)(a)

Shelley Robertson
Manager, Welfare and Oranga Tamariki
The Treasury

Sam Willis
Policy Manager, Welfare System and Income Support
Ministry of Social Development

s 9(2)(a)

Paul Young
Acting Policy Lead
Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Louise Upston
Minister for Social Development and Employment
Minister for Child Poverty Reduction
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

Briefing note

Inland Revenue
Te Tari Taake

Reference	BN2026/121
Date	9/04/2026
To	Revenue Advisor, Minister of Revenue – Angela Graham Private Secretary, Minister of Revenue – Melissa Zhen
From	Sam Aldridge
Subject	**BUDGET SENSITIVE: Fiscal implications in Working for Families report IR2026/090**

Purpose

1 This briefing note provides an explanation of the fiscal implications in the report *Working for Families: Design decisions for simplifying the definition of income and residence requirements* (IR2026/090), for Budget 2026.

Comment

2 In October 2025 we reported to Ministers seeking approval to progress simplification of the definition of family scheme income and the residence requirements. A third, connected, proposal relates to sharing information with Customs (*Working for Families – Changes to residency requirements, information sharing and definition of income* IR2025/379 refers). The three proposals would have a start date of 1 April 2027.

3 In the October 2025 report, the indicative non-departmental impacts over the forecast period were:

- simplifying the definition of family scheme income: $11 million cost
- changing the residence requirements: $35.6 million savings
- information sharing with Customs: $23.8 million savings

4 Over the forecast period, the indicative savings of all three proposals was $48.4 million. These non-departmental savings are currently included in the Budget 2026 welfare savings package.

5 A discussion document on the Approved Information Sharing Agreement with Customs will be considered by Cabinet on 20 April.

6 Today we provided a report (IR2026/090) to the Minister of Revenue seeking approval for detailed design of the other two Working for Families proposals (definition of income and residence requirements) for Budget 2026, and recommending that he refers the report to the Minister of Finance for her endorsement. The report updates the original indicative costings.

7 In relation to the definition of income, the report proposes to remove a number of income adjustments. This will significantly simplify the definition of income, reducing compliance and administration effort. In addition, the report seeks a decision on two options with different fiscal impacts:

Option A: Keep the "other payments" adjustment with a de minimis of $8,000

- $3 million cost over the forecast period

Option B: Remove the "other payments" adjustment

- $13.8 million cost over the forecast period (recommended).

8 Inland Revenue's preference is Option B (to remove the "other payments" adjustment) because of the additional simplification benefits it offers. However, we note that this option has a higher fiscal cost.

9 In relation to the residence requirements changes, the report updates the expected savings to $27.8 million over the forecast period. The revised costing reflects the 6-week grace period in the policy design, which is a pragmatic approach to preventing overpayments. Under this approach, someone who travels overseas for seven weeks, for example, would **not** be required to repay payments received during the first six weeks.

10 If Ministers prefer Option A, the total savings of all three proposals would be **$48.6 million** over the forecast period (i.e. $0.2 million more than is currently included in the welfare savings package).

11 If Ministers prefer Option B, the total savings of all three proposals would be **$37.8 million** over the forecast period (i.e. $10.6 million less than is currently included in the welfare savings package).

12 For your information, we are working with Treasury on how to reflect the savings from the residence requirements and information sharing proposals in the Budget. These are expected to be treated as tagged contingencies. This is because the final Cabinet decisions on the Customs Approved Information Sharing Agreement won't be made until after Budget 2026 (following the outcome of the Approved Information Sharing Agreement discussion document). The effectiveness of the residence requirements changes is related to the implementation of the Customs Approved Information Sharing Agreement, and therefore these changes are also expected to be treated as a tagged contingency for Budget.

13 Treasury and the Ministry of Social Development have been informed of this note.

Next steps

14 We suggest you refer this note to the offices of the Minister of Finance and the Minister for Social Development and Employment, along with the report (IR2026/090), for their information.

Sam Aldridge

Principal Policy Advisor

s 9(2)(a)

Tax policy report

Inland Revenue
Te Tari Taake

Working for Families: Design decisions to simplifying the definition of family scheme income and residence requirements

Date	9 April 2026	**Priority**	Medium
Security level	Budget Sensitive	**Report number**	IR2026/090

Action sought		**Deadline**
Minister of Revenue	**Agree** to proposed detailed design changes **Agree** to include these changes in Budget night legislation **Refer** the report to the Minister of Finance for her endorsement of the decisions **Refer** the report to the Minister for Social Development and Employment and Minister for Child Poverty Reduction for her information	16 April 2026

Purpose
This report seeks design decisions on simplifying Working for Families income and residence rules and asks you to note the associated fiscal impacts, ahead of final Cabinet decisions on the Budget package. It seeks approval for these changes to be introduced and enacted through Budget night legislation. These decisions are sought by 15 April 2026.

Contact for phone discussion, if required

Name	**Position**	**Phone number**	**First contact**
Sam Aldridge	Principal Policy Advisor	s 9(2)(a)	✓
Toby van Woerkom	Policy Advisor		☐

Working for Families: Design decisions to simplifying definition of family scheme income and residence requirements

Executive Summary

1 This report seeks your agreement to detailed design decisions for two Budget 2026 Working for Families proposals agreed to during the Budget 2026 Bilateral meeting on 31 March 2026. It notes the fiscal impacts of these proposals, which have been updated since indicative costings were provided to Ministers at the end of 2025.

2 The first proposal is to remove a range of low-risk adjustments from the definition of "family scheme income". This includes removing or amending the "other payments" adjustment. Officials also recommend an empowering provision to allow future income adjustments to be added or removed by Order in Council to respond to emerging risks.

3 The second proposal relates to residence requirements for Working for Families. Officials recommend replacing the current complex rules with a simpler test based on physical presence in New Zealand, supported by automated information sharing with New Zealand Customs. This would include a general six-week overseas travel exemption along with limited additional exemptions (for example, when in service of the New Zealand Government). The rule would retain the ordinarily resident requirement and current visa requirements to maintain the intended scope of eligibility. The automated information sharing solution is subject to the outcome of the proposed discussion document on the information sharing agreement, planned for release on 24 April 2026.

4 Officials recommend that legislation for both proposals be introduced and passed under urgency on Budget night and apply from 1 April 2027.

Background

5 In 2025, the Government released a discussion document proposing improvements to the Working for Families scheme, Empowering Families: Increasing certainty and preventing debt in the Working for Families scheme. That discussion document proposed shorter periods of assessment, simplifying the definition of family scheme income and the residence requirements for Working for Families, along with introducing automated information sharing between Customs and Inland Revenue.

6 In October 2025, you agreed that officials progress detailed policy design for two of these proposals for Budget 2026 consideration: simplifying the definition of family scheme income and simplifying residence requirements [IR2025/379, T2025/2673, REP/25/10/818 refers]. Officials have separately reported to you on introducing automated information sharing between Customs and Inland Revenue [IR2026/050, RPT 26/034 refers]. This package of proposals has been discussed alongside income support and social housing proposals for Budget 2026.

Proposal to simplify definition of family scheme income

7 Working for Families entitlements are based on family scheme income, which includes the income of the principal caregiver, their partner and dependent children. It is based on net income for tax purposes, with adjustments made to better reflect income available for day-to-day living expenses. Adjustments are intended to support the fairness and integrity of Working for Families and limit the artificial maximisation of entitlements. Adjustments were reviewed and added to in 2011 in response to integrity concerns. However, the number of adjustments has made family scheme income complex and confusing. All customers must check whether these income adjustments apply even though for most people family scheme income is the same as their net income for tax purposes.

8 Eligibility for Working for Families has narrowed over time due to the abatement threshold not increasing in line with inflation. Therefore, integrity risks arise across a narrower range of families and circumstances. Additionally, Inland Revenue also has an improved understanding of revenue risks across its products through better data and analytical approaches.

9 It is necessary to retain some adjustments for integrity and equity reasons, for example, for child support, and certain types of trustee income. However, the removal of low-risk adjustments from family scheme income would reduce complexity, improve compliance, payment accuracy and debt issues, and reduce the administrative burden.

10 The following table lists the proposed adjustments for removal. Based on our assessment of ease of income re-characterisation, the number of families declaring the adjustment type and the average value of each adjustment type, the removal of these adjustments would not materially increase integrity risk:

Table 1: Proposed adjustments for removal
• Depreciation recovered on the sale of a building used in business and/or rental activity
• Retirement savings scheme contributions
• Income from superannuation portfolio investment entities
• Pensions from a superannuation fund and certain life insurance annuities
• Distributions from superannuation schemes (if the current employer has made contributions)
• Distributions from retirement saving schemes (if the person is not eligible for New Zealand Superannuation at the time of the distribution)
• An Overseas pension that is exempt income
• Salary and wages under international agreements that are tax exempt income
• Trust distributions that are not beneficiary income and the recipient is not the settlor
• Main income equalisation account deposits
• Main income equalisation account refunds
• Employer-provided motor vehicles with salary sacrifice
• Vouchers and other short-term charge facilities, such as supermarket vouchers or Prezzy cards (more than $1,200; or 5% of salary or wages)

11 Employer-provided motor vehicles with salary sacrifice and vouchers and other short-term charge facilities relate to employment. While there may be some potential for a limited number of employees to take advantage of the Working for Families scheme, most employees do not have the opportunity to receive these forms of income and the numbers of adjustments declared currently per year is very low. Calculating the value of these adjustments can be complex, and, like with most adjustments, Inland Revenue is reliant on receiving the information from customers.

12 Integrity risks are also mitigated by an existing specific anti-avoidance rule for Working for Families that allows Inland Revenue to counteract arrangements when a person structures their affairs so that their income appears lower for Working for Families purposes

Remove or amend "other payments" income adjustment

13 Customers must adjust their family scheme income for "other payments" over $5,000 per year. "Other payments" are payments used by the family for day-to-day living expenses or that replace lost or diminished income from any source and paid directly or indirectly. It is subject to numerous legislative exclusions and additional technical guidance.

14 Many customers struggle to understand what counts as "other payments", often incorrectly declaring one-off capital payments, such as a grandparent paying for the installation of a heat pump. Inland Revenue reviews of the "other payments" adjustment show high error rates, and significant administrative effort, with almost half of adjustments having no impact on entitlements because income remains below the abatement threshold.

Option A

15 One option is to increase the de minimis from $5,000 to $8,000 to reflect inflation since the rules were last updated in 2011, which would reduce the need to use the "other payments" adjustment. However, complexity and uncertainty would remain because all customers would still be required to consider whether they receive "other payments" and calculate whether they are above or below the de minimis for the income year.

Option B

16 On balance, officials recommend removing the "other payments" adjustment. While removing all the proposed adjustments and "'other payments" has a higher fiscal cost than retaining the de minimis, this change would simplify the family scheme income definition and redirect effort to higher-risk areas.

Legislative flexibility to add, remove or alter income adjustments

17 Inland Revenue monitors integrity risks to Working for Families tax credits, alongside other products, on an ongoing basis. To enable emerging risks relating to income types to be addressed quickly in future, we recommend an empowering provision that enables Inland Revenue to add, remove or alter income adjustments through an Order in Council. Conversely, if future reviews indicate that existing adjustments present a low integrity risk, these adjustments could be removed if this offered simplification benefits.

Proposal to simplify residence requirements

18 Current residence requirements are both complex and difficult for customers to understand with different requirements for the principal caregiver and dependent child. The principal caregiver must be a New Zealand tax resident for the period they receive the tax credit, however, the test to determine tax residence is difficult for customers to understand. Tax residence is designed to be easy to gain and difficult to lose, meaning it is not always clear if or when tax residence is lost.

19 In October 2025 we reported to you on proposals to simplify these rules by aligning the requirements for principal caregiver and dependent child, so that both must meet all the requirements; allowing for short periods of physical absence; and providing limited exceptions when individuals would be treated as being present in New Zealand [IR2025/379, T2025/2673, REP/25/10/818 refers].

20 Inland Revenue has commenced work on an Approved Information Sharing Agreement with Customs. This information share, in combination with the simplification of the residence rules, would allow Inland Revenue to use information from Customs about when a person has left the country to stop payments promptly when families are no longer eligible. The proposed information-sharing agreement would cover the border movement information of the principal caregiver but not the dependent child because of potential privacy concerns. Inland Revenue would receive information on a Working for Families principal caregiver when they leave New Zealand and if/when they return.

21 A discussion document on the proposed Approved Information Sharing Agreement is due to be considered by Cabinet on 20 April 2026 [IR2026/050, RPT 26/034 refers].

22 We recommend simplifying the residence requirements to require both principal caregiver and dependent child to be physically present and ordinarily resident in New Zealand with a six-week overseas travel exemption.

23 This would remove the complexity of determining a person's eligibility and would allow Inland Revenue to use the information received from Customs to stop payments once someone has been overseas for more than six weeks. The effectiveness of the proposed changes is dependent on Inland Revenue having automated information sharing in place with Customs. If information sharing is delayed or incomplete, Inland Revenue's ability to detect absences and stop payments would be constrained.

24 The October 2025 report outlined the need for a limited range of additional exceptions when individuals would continue to be treated as though they were present in New Zealand. [IR2025/379, T2025/2673, REP/25/10/818 refers]. This would allow payments to continue when someone has been overseas for more than six weeks. These exceptions are proposed below.

Base test

25 The current sources of complexity in the residence rules are the use of tax residence and the "either/or" test for principal caregivers and dependent children, primarily when trying to determine when eligibility ends.

26 We therefore propose two substantive changes:

- removing tax residence, and
- requiring both principal caregiver and dependent child to be physically present and ordinarily resident in New Zealand.

27 The approach we propose would preserve most of the entry requirements to ensure Working for Families payments are only available to those living in New Zealand while reducing the compliance and administrative burden for applicants:

	Principal caregiver	**Dependent child**
Both principal caregiver **and** dependent child:		
Physical presence	Physically present for the days on which they receive Working for Families and lived in New Zealand for a continuous 12-month period at any time.	Physically present in New Zealand for the entitlement period.
Lives in New Zealand	Ordinarily resident in New Zealand.	Ordinarily resident in New Zealand.
Either principal caregiver **or** dependent child:		
Visa status	New Zealand citizen or holds a residence class visa (not a temporary entry class visa).	New Zealand citizen or holds a residence class visa (not a temporary entry class visa).

28 We propose to retain the ordinarily resident requirement, and for the principal caregiver, the 12-month presence rule. This ensures eligibility for the scheme is appropriately limited to those who live in New Zealand. This avoids the scenario of visitors being granted a residence class visa on arrival qualifying without living in New Zealand.

29 Moving to a test for both the principal caregiver and dependent child would ensure Inland Revenue makes effective use of border movement information from Customs.

The proposed Approved Information Sharing Agreement would not share information on dependent children, primarily due to potential privacy concerns.

30 We propose to retain the "either/or" test for the visa status requirement to minimise compliance burden. In general, citizenship is straightforward to verify for New Zealand-born children, but requiring proof of citizenship for principal caregivers in all cases could create financial and access barriers, with disproportionate impacts on Māori and Pasifika families.

Six-week exemption

31 We recommend that Working for Families payments should continue when families are overseas for up to six weeks at a time. If either the principal caregiver or dependent child is overseas for more than six weeks, they would not be eligible for payments beyond the six-week period until they return to New Zealand.

32 To minimise overpayment risk, we recommend that eligibility under the six-week test should not be retrospectively determined, provided the family remains ordinarily resident in New Zealand. Any payments made during that time would not be considered an overpayment. However, if someone knows they are moving overseas permanently and advises Inland Revenue, eligibility should stop from the moment they leave New Zealand.

33 We consider that six weeks strikes a balance between simplicity, the prevention of overpayments and the objective of Working for Families to support children in New Zealand. Six weeks would be long enough to ensure families who travel overseas once a year during the end-of-year school holidays are not unfairly penalised, relative to those who travel during the term holidays.

34 Customers would not need to apply for an exemption for absences under six weeks. Inland Revenue would use up-to-date information from Customs on border movements to stop payments once the six-week period has passed. Under the terms of the proposed information sharing agreement, Inland Revenue would contact customers four weeks after leaving New Zealand so they are aware their payment may be stopped.

35 With any day count test, people may change their travel plans to ensure they do not lose eligibility. Since Working for Families is targeted at low- to middle-income families, we consider any potential integrity risk to be low due to the cost of international travel. Given the underlying requirement that recipients need to be ordinarily resident in New Zealand, data received from Customs may show regular travel patterns that would allow Inland Revenue to better determine whether someone lives in New Zealand.

36 However, we do recommend a rule in line with the approach used for the Australian Family Tax Benefit to mitigate some risk of taking advantage of the scheme. If someone returns after an absence exceeding six weeks and then leaves again within six weeks we recommend their payments should stop on the date of their second departure, assuming no additional exemptions are available (see paragraphs 41 to 42).

Main benefit day count test

37 In response to feedback on the discussion document, officials considered aligning the Working for Families period with the 28 days used for main benefits. This is on the basis that around 20% of Working for Families customers are paid by the Ministry of Social Development (half of eligible beneficiary families). Given that the policy objectives of Working for Families and main benefits are different, we consider 28 days to be too short to provide flexibility to all Working for Families customers.

38 While there would be some misalignment under a six-week period for families paid by the Ministry of Social Development, this already exists under the current rules and can be mitigated through Inland Revenue's end-of-year square-up process. When the Ministry of Social Development suspends someone's main benefit payment, it also stops their Working for Families payments. Any missed payments can then be paid out following the end of the tax year.

Main benefit application process for travel

39 Officials also considered whether Working for Families should have a similar application process to the income support system where overseas travel often needs prior approval. For main benefit recipients, this is embedded within a case management approach where they may have additional requirements to meet work obligations.

40 We consider that this approach is less appropriate for Working for Families because it would significantly increase compliance costs for the 80% of customers paid by Inland Revenue and increase administrative costs for Inland Revenue. It would require contact for each overseas trip, increasing call and message volumes, with impacts on Inland Revenue's ability to administer the wider tax system.

Exemptions for longer absences

41 We recommend that payments should continue for longer than six weeks in the following situations:

Table 2: Proposed exemptions for longer absence
• Overseas in the service of the New Zealand Government (for example, New Zealand Defence Force)
• Natural disaster (either in New Zealand or internationally) preventing or delaying travel
• Death, serious illness, or serious injury of the person or a family member
• Overseas seeking medical treatment not available in New Zealand
• Custody or criminal proceeding involving the person (including as a witness)
• For the dependent child, absences related to primary or secondary schooling (for example, student exchange or boarding school)
• Other global or regional shocks or events that may prevent or delay travel, including war, political or social unrest, and industrial action, provided the travel delay is outside of their control. The exemption would not apply if the person started their travel during the event or is participating in the unrest or action.

42 We consider these categories would be flexible enough to respond to life's complexities and cover the most common reasons why a family may be overseas for more than six weeks at a time, but where continued eligibility would be appropriate. The burden of proof would be on the customer to show that an exemption applies. Customers could apply for an exemption upfront to allow them to continue to receive payments while overseas or at a later date after payments have stopped, with any missed payments paid out as part of the end-of-year square up process.

Operational implications

Family scheme income

43 Removing lower-risk income adjustments would simplify the way Working for Families is administered by largely aligning family scheme income with net income for tax purposes. This reduces the need for customers to assess and report adjustment types and lowers Inland Revenue's reliance on customer-provided information that is difficult to verify and has high error rates. System changes are limited and would mainly involve removing existing income adjustment rules and updating supporting guidance and staff training. The enabling provision to amend income adjustments by Order in Council

would allow future changes to be implemented without primary legislation and would be managed through existing governance and monitoring arrangements.

Residence requirements

44 Removing the existing tax residence requirements and requiring both the principal caregiver and dependent child to be physically present and ordinarily resident would change how eligibility is administered. This would allow Inland Revenue to use border movement information from Customs to identify when payments should stop after the six-week overseas travel period. This reduces the need for retrospective adjustments and manual review compared with the current rules.

45 Delivery of the new approach is dependent on the proposed Approved Information Sharing Agreement with Customs. Exemptions for longer overseas absences would require customer evidence and manual decision-making but these are expected to be low volume and handled within similar processes currently used for student loans and child support liable parents.

Financial implications

Family scheme income

Option A (removing proposed adjustments but keeping the "other payments" adjustment with a de minimis of $8,000 from 1 April 2027)

46 The table below sets out the negative impact on the operating balance ($3.000 million over the forecast period) by June year.

	$m - increase/(decrease)				
Vote Revenue Family scheme income proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-departmental benefits or related expenses – PLA	-	0.100	0.700	0.700	0.800
Family Tax Credit	-	0.000	0.100	0.100	0.200
In-Work Tax Credit	-	0.000	0.100	0.100	0.100
Best Start Tax Credit					
Total Operating	**-**	**0.100**	**0.900**	**0.900**	**1.100**

Option B (removing proposed adjustments and the "other payments" adjustment from 1 April 2027)

47 The table below sets out the negative impact on the operating balance ($13.800 million over the forecast period) by fiscal year.

	$m - increase/(decrease)				
Vote Revenue Family scheme income proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-departmental benefits or related expenses – PLA	-	0.800	3.000	3.200	3.400
Family Tax Credit	-	0.200	0.600	0.600	0.700
In-Work Tax Credit	-	0.100	0.400	0.400	0.400
Best Start Tax Credit					
Total Operating	**-**	**1.100**	**4.000**	**4.200**	**4.500**

Residence requirements

48 Changing the residence requirements for Working for Families as outlined in this report from 1 April 2027 would have a positive impact on the operating balance ($27.800 million over the forecast period). This is set out in the table below by fiscal year.

	$m - increase/(decrease)				
Vote Revenue Residence requirements proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-departmental benefits or related expenses – PLA					
Family Tax Credit	-	-	(2.700)	(2.600)	(2.600)
In-Work Tax Credit	-	-	(1.000)	(1.000)	(0.900)
Best Start Tax Credit	-	-	(0.300)	(0.300)	(0.300)
Non-departmental Other Expenses		-			
Impairment of Debt and Debt Write-offs	-		(2.300)	(7.000)	(6.800)
Total Operating	**-**	-	**(6.300)**	**(10.900)**	**(10.600)**

49 This proposal is subject to the outcome of the discussion document on the automated information-sharing agreement between Inland Revenue and Customs. It is therefore proposed that the positive fiscal impacts of this proposal be held in a negative tagged contingency and counted against the Budget 2026 operating allowance. Cabinet approval would be sought to enable joint Ministers (Minister of Finance and Minister of Revenue) to draw down funding from this contingency.

50 For completeness, we reported to Ministers in October 2025 with indicative fiscal costings for these proposals. At that stage, simplifying the definition of family scheme income had indicated an increase in non-departmental expenditure of $11 million over the forecast period. Initial costings for changes to residence requirements had indicated a decrease in expenditure of $35.6 million over the forecast period. These costings have been updated (as above) to reflect the design decisions proposed in this report. Subject to endorsement by the Minister of Finance, these updated costings will be included in Budget 2026.

Administrative impact

51 The departmental costs to implement and deliver the two detailed design proposals are set out below. These costs are included within separate advice that the Treasury are providing to the Minister of Finance on departmental funding for all Budget 2026 initiatives being led by Vote Revenue.

52 There is a relatively small one-off cost to implement the system and process changes for the family scheme income proposal.

	$m - increase/(decrease)				
Vote Revenue Family scheme income proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
System build	-	0.200	-	-	-
Total Operating	**-**	**0.200**	-	-	-

53 The cost to implement and deliver the residence requirement proposal is estimated at $0.700 million capital and $0.820 million operating over the forecast period.

	$m - increase/(decrease)				
Vote Revenue Residence requirements proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
System build	-	0.700	-	-	-
Total Capital	**-**	**0.700**	**-**	**-**	**-**
System build	-	0.400	-	-	-
Depreciation and capital charge	-	-	0.140	0.140	0.140
Total Operating	**-**	**0.400**	**0.140**	**0.140**	**0.140**

54 The cost to implement and deliver the automated information sharing between Inland Revenue and Customs is estimated at $0.600 million capital and $0.490 million operating for Inland Revenue and $1.051 million operating for Customs over the forecast period.

	$m - increase/(decrease)				
Vote Revenue and Vote Customs Information sharing proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
System build (Inland Revenue)	-	0.600	-	-	-
Total Capital	**-**	**0.600**	**-**	**-**	**-**
System build (Inland Revenue)	-	0.100	-	-	-
System build (NZ Customs)	-	0.520	-	-	-
Ongoing cost (NZ Customs)	-	-	0.177	0.177	0.177
Depreciation and capital charge (Inland Revenue)	-	-	0.130	0.130	0.130
Total Operating	**-**	**0.620**	**0.307**	**0.307**	**0.307**

Consultation

55 Most submitters on the "Empowering Families: Increasing certainty and preventing debt in the Working for Families scheme" discussion document did not comment specifically on the proposals to simplify "family scheme income" or the residence requirements. However, a recurring theme from the consultation was the overall complexity of the Working for Families scheme, and the corresponding impact on customers of debt, stress, and difficulty managing their entitlement.

56 Submitters who commented supported the proposal to simplify the definition of family scheme income. However, they cautioned that families with irregular or seasonal income should not be disadvantaged. We expect the proposals will not have negative impacts on these families.

57 Submitters also supported simplifying the residence requirements provided these still allowed families to travel overseas for a reasonable period. While the proposed six-week period was broadly viewed as an appropriate length of time, some stakeholders thought there needed to be exemptions and that the rules would be clearer to families if they were consistent for both Working for Families and the income support system. Officials maintain that Working for Families should provide a degree of flexibility for customers, with stakeholder feedback informing the proposed exemption list.

58 The Ministry of Social Development and Treasury have been consulted in the preparation of this report and are comfortable with the recommendations.

Next steps

59 To achieve an implementation date of 1 April 2027, the proposed Working for Families changes would need to be introduced on Budget night and passed under urgency. This allows for legislative settings to be in force by December 2026, which would not be possible if the changes were included in the next omnibus taxation Bill. This timing is required to allow Inland Revenue sufficient time to incorporate the new settings into notices of entitlement issued in February 2027, which inform customers of their Working for Families entitlements ahead of the start of the 2027–28 tax year.

60 We recommend you refer a copy of this report to the Minister of Finance for her endorsement of your decisions and the Minister for Social Development and Employment and Minister for Child Poverty Reduction for her information.

Recommendations

We recommend you:

Family scheme income

1 **Agree** to remove the adjustments set out in Table 1 from the definition of family scheme income.

Agree / Disagree

Minister of Revenue

and either

2 **Agree** to retain the "other payments" adjustments with a de minimis of $8,000, with a negative impact on the operating balance of $3.000 million over the forecast period **(Option A).**

	$m - increase/(decrease)				
Vote Revenue Family scheme income proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-departmental benefits or related expenses – PLA					
Family Tax Credit	-	0.100	0.700	0.700	0.800
In-Work Tax Credit	-	0.000	0.100	0.100	0.200
Best Start Tax Credit	-	0.000	0.100	0.100	0.100
Total Operating	**-**	**0.100**	**0.900**	**0.900**	**1.100**

Agree / Disagree

Minister of Revenue

or

3 **Agree** to remove the "other payments" adjustment from the definition of family scheme income, with a negative impact on the operating balance of $13.800 million over the forecast period (**Option B** – officials' preferred option).

	$m - increase/(decrease)				
Vote Revenue Family scheme income proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-departmental benefits or related expenses – PLA	-	0.800	3.000	3.200	3.400
Family Tax Credit	-	0.200	0.600	0.600	0.700
In-Work Tax Credit	-	0.100	0.400	0.400	0.400
Best Start Tax Credit					
Total Operating	**-**	**1.100**	**4.000**	**4.200**	**4.500**

Agree / Disagree

Minister of Revenue

4 **Note** the one-off departmental cost of $0.200 million to implement the family scheme income proposal, to be considered separately for funding by the Minister of Finance.

	$m - increase/(decrease)				
Vote Revenue Family scheme income proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
System build	-	0.200	-	-	-
Total Operating	**-**	**0.200**	-	-	-

5 **Agree** to introduce an empowering provision to add, remove or alter family scheme income adjustments through an Order in Council.

Agree / Disagree

Minister of Revenue

Residence requirements and automated information sharing

6 **Agree** to remove the tax residence requirement for either a principal caregiver or a dependent child, and instead to require both principal caregiver and dependent child to be physically present and ordinarily resident in New Zealand.

Agree / Disagree

Minister of Revenue

7 **Agree** that families who otherwise live in New Zealand should continue to be eligible for Working for Families for up to six weeks while they are overseas.

Agree / Disagree

Minister of Revenue

8 **Agree** that in the specified circumstances set out in Table 2 in the report, families should be exempt from the six-week rule and should continue to be eligible for Working for Families for longer periods while overseas.

Agree / Disagree

Minister of Revenue

9 **Agree** that the $27.800 million positive operating balance impact over the forecast period from the recommended changes to residence requirements be held as a negative tagged contingency, subject to confirmation by Budget Ministers and Cabinet.

	$m - increase/(decrease)				
Vote Revenue Residence requirements proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-departmental benefits or related expenses – PLA		-			
Family Tax Credit	-	-	(2.700)	(2.600)	(2.600)
In-Work Tax Credit	-	-	(1.000)	(1.000)	(0.900)
Best Start Tax Credit	-	-	(0.300)	(0.300)	(0.300)
Non-departmental Other Expenses		-			
Impairment of Debt and Debt Write-offs	-		(2.300)	(7.000)	(6.800)
Total Operating	**-**	-	**(6.300)**	**(10.900)**	**(10.600)**

Agree / Disagree

Minister of Revenue

10 **Note** the departmental cost of $0.700 million capital and $0.820 million operating to implement and deliver the residence requirement proposal, to be considered separately for funding by the Minister of Finance.

	$m - increase/(decrease)				
Vote Revenue Residence requirements proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
System build	-	0.700	-	-	-
Total Capital	**-**	**0.700**	**-**	**-**	**-**
System build	-	0.400	-	-	-
Depreciation and capital charge	-	-	0.140	0.140	0.140
Total Operating	**-**	**0.400**	**0.140**	**0.140**	**0.140**

11 **Note** the departmental cost of $0.600 million capital and $0.490 million operating for Inland Revenue and $1.051 million operating for Customs, over the forecast period, to implement and deliver the automated information sharing between Inland Revenue and Customs, to be considered separately for funding by the Minister of Finance.

	$m - increase/(decrease)				
Vote Revenue and Vote Customs Information sharing proposal	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
System build (Inland Revenue)	-	0.600	-	-	-
Total Capital	**-**	**0.600**	**-**	**-**	**-**
System build (Inland Revenue)	-	0.100	-	-	-
System build (NZ Customs)	-	0.520	-	-	-
Ongoing cost (NZ Customs)	-	-	0.177	0.177	0.177
Depreciation and capital charge (Inland Revenue)	-	-	0.130	0.130	0.130
Total Operating	**-**	**0.620**	**0.307**	**0.307**	**0.307**

Other recommendations

12 **Agree** that the recommend options in this report should have an application date of 1 April 2027, to be given effect through Budget night legislation.

Agree / Disagree

Minister of Revenue

13 **Refer** the report to the Minister of Finance for her endorsement.

Refer - yes / no

Minister of Revenue

14 **Refer** the report to the Minister for Social Development and Employment and Minister for Child Poverty Reduction for her information.

Refer - yes / no

Minister of Revenue

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Carolyn Elliott

Policy Director

Policy | Inland Revenue

Hon Simon Watts

Minister of Revenue

/ /2026

Briefing note

Inland Revenue
Te Tari Taake

Reference	BN2026/128
Date	15/04/2026
To	Revenue Advisor, Minister of Revenue – Angela Graham Private Secretary, Minister of Revenue – Melissa Zhen
From	Paul Young
Subject	**BUDGET SENSITIVE: Policy Decisions in Working for Families report IR2026/090**

Purpose

1 This briefing note further explains the policy decisions with fiscal implications in the report *Working for Families: Design decisions for simplifying the definition of income and residence requirements* (IR2026/090), for Budget 2026.

Comment

2 The report provided last week (IR2026/090) recommends two policy decisions that shift the fiscal outcome of the package from the previous costings in the October 2025 report (IR2025/379 refers). These are in the residence rule changes and in the treatment of 'other payments' in the family scheme income rules. The key objectives of these changes are simplification and the reduction of overpayments and debt.

Residence rule changes

3 The October 2025 report (IR2025/379) recommended that the simplified residence rules include a tolerance for short periods so that people who are ordinarily resident in New Zealand can go overseas on holiday or to visit family.

4 For that report, the proposed residence rule changes were costed on the basis that if a family is overseas for more than 6 weeks, the family would no longer be entitled to Working for Families from the date of their departure (i.e. day 1). This would apply even if the family was returning and continued to live in New Zealand.

5 In the report provided last week (IR2026/090), the recommended residence rule changes had two slightly different outcomes depending on whether families continue to live in New Zealand:

- **People leaving the country permanently would lose their Working for Families entitlement from day 1.** This means that if they did not tell Inland Revenue and payments did not stop until after 6 weeks, they would not be entitled to the payments made during those 6 weeks. That is, they would owe 6 weeks' worth of overpayments.
- **People only going overseas temporarily (for example, on holiday) would lose their Working for Families entitlement after the end of the 6 weeks.** If Inland Revenue stops their payments using Customs data because they have not returned within the 6 weeks, they remain entitled to those payments already received. That is, payments made during that period would not be considered

overpayments. When they return to New Zealand, payments can resume from that date.

6 This approach would reduce overpayments and debt, and would also reduce compliance and administration costs. It would also resolve equity concerns. For example, under the originally costed approach, if one person was on holiday for 41 days, they would retain their full Working for Families entitlement while a second person who was away for 43 days would lose their entitlement for the full 43 days. Under the recommended approach the second person would only lose their entitlement for one day.

7 The revised costing for the residence rule change that officials have recommended reduces the savings by $10.6 million over the forecast period.

8 While officials do not recommend it, the Minister could choose to apply the loss of entitlement back to day 1 for all people that are out of New Zealand for more than 6 weeks. This would return costings for this element closer to the original October 2025 forecast. However, it would mean that overpayments and debt would not be reduced, and compliance and administrative costs would increase. It also raises the equity concern noted above.

9 While we have not previously done a costing of a 28-day rule, the table in the appendix sets out the pros and cons of a 4-week period compared to the proposed 6-week period. A second table also sets out the pros and cons for the proposed rule allowing people returning to New Zealand to retain their entitlement for 6 weeks compared with losing their entitlement from day 1.

Interaction with the income support system

10 Under the status quo, about half of main benefit recipients receive their Working for Families payments from the Ministry of Social Development. Main benefit recipients are required to seek approval for all overseas travel.1 Holidays are not listed as an approved reason, and visiting family must be for an important event (e.g. they are seriously ill, funeral, wedding). For this group, if their main benefit is stopped, their Working for Families payments are stopped even if they remain eligible. Missed Working for Families payments will continue to be paid out as part of Inland Revenue's square up following the end of the tax year, however beneficiaries earning less than $42,700 will only be squared up if they request this.

11 Officials consider that full alignment with the main benefit system (that is, requiring all families to seek approval upfront for all travel and for travel to be for an approved reason) would not be administratively feasible for Inland Revenue. It would be a substantial shift in the underlying policy design of Working for Families as the scheme does not impose ongoing obligations on families.

12 As the Ministry of Social Development only pays Working for Families while someone receives a main benefit, misalignment with the income support system would continue regardless of what period is chosen.

Treatment of 'other payments' for family scheme income

13 The second policy decision relates to the treatment of 'other payments' in the family scheme income rules. 'Other payments' captures monetary payments from any other person or entity that are used for the family's day-to-day living expenses. In the report we have proposed two main options and have recommended option B (to remove the 'other payments' adjustment) because of the additional simplification benefits it offers. However, we note that this option has a higher fiscal cost.

[1] https://www.workandincome.govt.nz/on-a-benefit/overseas-travel/main-benefit/temporarily-overseas.html

Option A: Keep the 'other payments' adjustment with a de minimis of $8,000
- $3 million cost over the forecast period

Option B: Remove the 'other payments' adjustment
- $13.8 million cost over the forecast period (recommended).

14 Option A adjusts the existing $5,000 threshold for inflation but retains the 'other payment' category. This would offer some simplification for people that receive between $5,000 and $8,000 income but offers less simplification benefits than option B.

Fiscal package

15 The table below shows how different packages of options can achieve different policy and fiscal objectives over the forecast period depending on Ministers' preferences:

Initial costings (IR2025/379)	**Officials' recommendation in latest report (IR2026/090)**	**Option if Ministers want to maintain fiscal envelope (IR2026/090)**	**Not recommended alternative option 1**	**Not recommended alternative option 2**
	Residence change (grace period) *and* 'Other payments' removal (option B)	Residence change (grace period) *and* 'Other payments' increased cap (option A)	Residence change (day 1) *and* 'Other payments' removal (option B)	Residence change (day 1) *and* 'Other payments' increased cap (option A)
	Best meets policy objectives but lower fiscal savings	*Meets most policy objectives and maintains fiscal envelope*	*Less effective for similar fiscal outcome*	*Least effective but highest fiscal savings*
Total: $48.4m	**Total: $37.8m**	**Total: $48.6m**	**Total: $45.6m**	**Total: $56.4m**

16 The Treasury and the Ministry of Social Development have been informed of this note.

Next steps

17 We suggest that you refer this note to the offices of the Minister of Finance and the Minister for Social Development and Employment, along with the report (IR2026/090), for their information.

Paul Young

Acting Policy Lead

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Table 1: Choice of period		
	4 weeks	**6 weeks**
Pros	Aligns with period used for main benefits. Slightly higher fiscal savings.	Aligns with education system and end-of-year school holidays. Recognises that some families may prioritise travelling for longer periods at the end of year to visit family due to long distances and the fixed/high cost of flights (rather than during term holidays).
Cons	May prevent reasonable overseas travel consistent with maintaining employment in New Zealand. There would still be misalignment with the income support system. Even for a trip that is less than four weeks long, someone's main benefit payment and Working for Families may have stopped but they could still be entitled to receive Working for Families.	Some submitters on 2025 discussion document argued that 6 weeks was not long enough (officials did not consider a default period longer than 6 weeks to be a feasible option as it would create misalignment with the education system). Some misalignment with the income support system. Someone's benefit and Working for Families may have stopped, but they could still be entitled to Working for Families.
Table 2: If travel exceeds the defined period (e.g. 6 weeks)		
	All travellers lose entitlement from day of departure	**Only people leaving New Zealand permanently lose entitlement from day of departure**
Pros	Higher fiscal savings. However, this is only to the extent that overpayments can be recovered.	Fewer overpayments and less debt, less compliance and administrative cost.
Cons	Creates a steep cliff face, as a difference of one day could lead to 6 weeks' worth of payments needing to be repaid. This would systematically cause greater overpayments and debt because of the backdating/retroactive nature of the rule, higher compliance and administration costs, and equity issues.	Lower fiscal savings. Families who have left New Zealand permanently but have not informed Inland Revenue would still need to repay payments during the first 6 weeks before payments are stopped. It may be difficult to recover these outstanding debts.

Briefing note

Inland Revenue
Te Tari Taake

Reference	BN2026/148
Date	8/05/2026
To	Revenue Advisor, Minister of Finance – Carl Harris Revenue Advisor, Minister of Revenue – Angela Graham Private Secretary, Minister of Revenue – Melissa Zhen
From	Sam Aldridge
Subject	**Budget Bill - Family scheme income legislative flexibility**

Purpose

1 As part of the proposal to simplify the definition of family scheme income, Cabinet has agreed to legislative flexibility to amend income adjustments by Order in Council.

2 Following discussion with the Parliamentary Counsel Office, the approach in the Budget Bill has been refined so that it achieves the key policy objectives while meeting legal requirements.

3 This note provides you with background on the issue.

Comment

Removal of adjustments

4 Cabinet has agreed to remove several income adjustments from the definition of family scheme income and to increase the threshold for the 'other payments' adjustment. The policy rationale for removing and modifying the adjustments is to make the Working for Families scheme easier to understand and administer.

5 However, removing the adjustments comes at a potential integrity and fiscal risk. Overall, we consider that this risk is low, and the benefit from simplification outweighs the low risk. The adjustments that are proposed for removal have been identified as low to medium risk in terms of value and integrity of the system[1]. There is also an existing anti-avoidance rule within the Working for Families rules to supplement integrity.

6 We intend to continue to use and strengthen START analytics and data to monitor emerging risks. If our data subsequently shows that the integrity risk for a specific adjustment becomes materially more significant, we will recommend changing the law in the soonest available legislative vehicle to limit the integrity and fiscal consequences.

[1] The fiscal cost of removing and modifying the adjustments is estimated to be approximately $1 million per year.

Legislative approach to changing adjustments in future

7 Ideally, any changes would be made via primary legislation. The problem is the interaction between the usual timing of legislative vehicles and Inland Revenue's annual process for Working for Families. Inland Revenue pays most people their Working for Families throughout the year, and therefore needs to confirm their expected entitlement before 1 April.

8 In general, it is only administratively feasible to make changes to the Working for Families entitlement rules if the legislative vehicle is enacted by 1 December of the year preceding the tax year in which the change will apply[2]. After that time, changes to START for the next tax year are largely locked in.

9 If the issue is identified early enough and a change made in (for example) a Bill enacted in June 2028, the change could be applicable from April 2029. However, information from the previous tax year is not generally available until June of the following year, which makes it less likely that Inland Revenue would be able to identify the problems within this time period. If the change is made in a Bill that is enacted after December 2028, it would generally not be feasible from a systems perspective to apply the change until 1 April 2030.

Legislative flexibility

10 To address this, we recommended an empowering provision for family scheme income adjustments to be added, removed or modified by Order in Council. This was agreed in the Budget Cabinet paper considered on 7 May 2026.

11 Following discussions with PCO, this empowering provision has been drafted to be more specific and targeted to ensure that it meets legal requirements. It allows three adjustments to be brought back into force by Order in Council. These three adjustments (specific types of trust distributions, employer-provided motor vehicles and short-term charge facilities), while still relatively low risk, are ones that we consider should be monitored.

12 We consider that this approach meets the underlying policy intent to limit integrity and fiscal risk, while also meeting legal requirements. Under this approach, if Inland Revenue identified that a change to these adjustments was needed between July and October 2028, this could apply from 1 April 2029 – that is, one year earlier than would ordinarily be the case.

13 There are no fiscal costs associated with this revised approach.

14 We note that the revised approach only relates to the reinstitution of the three adjustments that merit monitoring and does not provide for the addition, removal or modification of other adjustments. We will report back to the Minister of Revenue on whether additional legislative flexibility would be useful in other situations, for potential consideration for a future tax Bill.

Consultation

15 The Treasury and the Ministry of Social Development have been informed of this issue.

[2] There are some limited exceptions to this that do not relate to income adjustments.

Next steps

16 This approach has been reflected in the draft LEG paper and the attached draft RIS. The attached draft RIS is currently being assessed by Inland Revenue's Quality Assurance Panel and will be included with the other finalised RISs next week.

17 We will report back to Ministers on whether any further legislative flexibility may be needed, for potential inclusion in a future tax Bill.

Sam Aldridge

Principal Policy Advisor

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Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **Timeframes for further FIF changes and migrant-related reforms – Phase One and Two**

Date:	8 April 2025	**Priority:**	Low
Security level:	Sensitive - Budget	**Report number:**	IR2025/161

Action sought

	Action sought	**Deadline**
Minister of Revenue	**Note** the contents of this report **Confirm** the inclusion of Phase Two of the FIF rule changes and other migrant-related reforms to the Tax and Social Policy Work Programme **Refer** a copy of this report to the Minister of Finance for their information	24 April 2025

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**	**Suggested first contact**
Sam Rowe	Policy Lead	s 9(2)(a)	☐
Lonnie Liu	Senior Policy Advisor		☒

8 April 2025

Minister of Revenue

Timeframes for further foreign investment fund changes and migrant-related reforms – Phase One and Two

Purpose

1. This report provides you with an overview of the timeframe officials are working towards to implement two tranches of tax changes ('Phase One' and 'Phase Two') which will reduce barriers for migrants and residents coming to and staying in New Zealand.

2. We also seek your confirmation for Phase Two to be included on the Government Tax and Social Policy Work Programme, given Cabinet has noted that the Ministers of Finance and Revenue would report back to Cabinet about further policy changes for inclusion in legislation in 2025/26 [*ECO-25-MIN-0020 and CAB-25-MIN-0061 refer*].

Background

3. On 10 February 2025, we reported to you on the outcome of public consultation on the effects of the foreign investment fund (FIF) tax rules on migration. We proposed changes to the regime to help attract and retain high value migrants in New Zealand [*IR2025/007 refers*].

4. The focus of the proposed changes was on the FIF rules as it was commonly raised to be the most serious barrier, including by the New Zealand Institute of Economic Research in April 2024 in their paper *The place where talent does not want to live*.

5. You agreed to the proposal to introduce narrowly-targeted changes as a minimum viable product but also directed officials to undertake further work on a programme of tax changes to enhance New Zealand's competitiveness in attracting and retaining talent. The Cabinet paper proposed a review of tax settings beyond just the FIF rules, reflecting submissions received during public consultation that noted the proposed changes were too narrow or would be more effective with other tax policy changes.

6. Officials have therefore begun planning the further programme of work. 'Phase One' refers to the current work to add a new method (the revenue account method) to the FIF regime to allow migrants to be taxed on a realisation basis for specified FIF interests, with a special carve-out for taxpayers who may face double taxation due to being subject to taxation on a citizenship basis by another jurisdiction (this will mostly be United States (US) citizens).

7. 'Phase Two' refers to the further work programme. This programme of work would be undertaken in three workstreams:

   7.1 Further changes to the FIF regime s 9(2)(f)(iv) ;

   7.2 Changes to the financial arrangements regime; and

   7.3 Tax changes to support the new digital nomads visa.

Timeframe – Phase One changes

8. Following Cabinet approval of the proposed changes [*CAB-25-MIN-0061 refers*], officials are working to include the changes in the Taxation (Annual Rates for 2025-26) Bill, currently scheduled for introduction in August.

9. The current focus of this workstream is to finalise a technical paper for targeted consultation on some outstanding administrative and technical issues – including an exit tax and details of the eligibility criteria.

10. We expect to begin targeted consultation late-April, with a view to report to you and the Minister of Finance in May after the Budget moratorium. Appendix One provides a visual representation of this timeframe.

Timeframes – Phase Two changes

Digital nomads visa changes

11. Tax changes to support the digital nomads visa will also be included in the Taxation (Annual Rates for 2025-26) Bill. Reporting on the required changes are likely to be included in the omnibus policy report and Cabinet paper for this Bill, which are provisionally planned to be sent to Ministers late-May to early-June.

12. Further detail on the approximate timeframe of these changes is outlined in Appendix One. This is subject to change in line with the Bill's wider timeframe.

Foreign investment fund rule changes s 9(2)(f)(iv)

13. This workstream includes expanding the scope of the revenue account method to include non-migrant New Zealand residents as well as the consideration of other proposals raised during public consultation, including raising the FIF de minimis threshold s 9(2)(f)(iv)

14. Any changes arising from the Phase Two review of the FIF rules will aim for enactment via the Taxation (Annual Rates for **2026-27**) Bill. The details of the policy design would require targeted stakeholder consultation and the final legislation would benefit from public consultation during select committee stage. For these reasons we do not recommend accelerating the proposed timeframe.

Financial arrangements rule changes

15. The workstream is in its early stages with the full scope of the change required still being determined - so more detailed timeframes are not yet available. The goal of the workstream is to remove some tax issues which the financial arrangements rules can pose for migrants in respect of their foreign currency loans (such as a foreign currency mortgage the migrant took out to purchase a house overseas). We recommend advancing the FIF and financial arrangements rules together as a pro-migration package if possible, and so it is likely that this workstream will follow a similar timeframe as the Phase Two FIF s 9(2)(f)(iv) , with the aim of introducing any changes via the Taxation (Annual Rates for 2026-27) Bill.

Government Tax and Social Policy Work Programme

16. While work on Phase Two has begun and will continue, the Phase Two workstreams have not been formally added to the published Government Tax and Social Policy Work Programme. We seek your confirmation to formally add the Phase Two workstreams to the Programme in an upcoming refresh. This could be useful to use the Programme to signal to interested and affected stakeholders that the Government has formally committed to the Phase Two workstream.

Next steps

17. Officials will continue to work on Phase One changes with the aim of including them in the upcoming Taxation (Annual Rates for 2025-26) Bill.

18. We will report back to you on the three workstreams that form Phase Two later in the year. As the three workstreams are advanced on different timeframes and deal with different parts of the Income Tax Act, each workstream will report to you independently.

Recommended action

We recommend that you:

1. **Note** that work on a narrowly-targeted foreign investment fund reform continues and officials aim to include the proposed changes in the upcoming Taxation (Annual Rates for 2025-26) Bill.

   Noted

2. **Note** that the changes to complement the digital nomads visa are being advanced with the aim for their inclusion in the upcoming Taxation (Annual Rates for 2025-26) Bill.

   Noted

3. **Confirm** the inclusion of 'Phase Two' changes on the Government Tax and Social Policy Work Programme.

Changes complementing the digital nomads visa	Yes/No
Further foreign investment fund rule changes s 9(2)(f) s 9(2)(f)(iv)	Yes/No
Financial arrangements rule changes	Yes/No

4. **Note** that officials will report to you later this year on the financial arrangements rule changes and Phase Two of the foreign investment fund reforms, s 9(2)(f)(iv)

   Noted

5. **Refer** this report to the Minister of Finance.

   Referred

s 9(2)(a)

Sam Rowe
Policy Lead
Policy

Hon Simon Watts
Minister of Revenue
/ /2025

Appendix one – Gantt chart for Phase One and Two

	2025 Q2			2025 Q3			2025 Q4			2026 Q1			2026 Q2			2026 Q3		
	April	May	June	July	August	September	October	November	December	January	February	March	April	May	June	July	August	September
Key dates	Budget moratorium (14 April - 22 May) Budget day (22 May)		Annual Rates 25-26 Bill Cabinet paper		Annual Rates Bill 25-26 introducti on			HYEFU				Annual Rates 25-26 Bill enacted	Budget moratorium Budget day		Annual Rates 26-27 Bill Cabinet paper		Annual Rates Bill 26-27 introducti on	
Phase One																		
Technical paper drafting	■																	
Targeted consultation on technical paper	■	■																
Report to Ministers on minor and technical details for approval		■	■															
Develop drafting instructions			■	■														
Progress through bill process for the Annual Rates 25-26 Bill				■	■	■	■	■	■	■	■	■						
Phase Two																		
Digital nomads visa																		
Targeted consultation on technical details	■	■	■															
Report to Ministers on minor and technical details for approval		■	■	■														
Progress throgh bill process for the Annual Rates 25-26 Bill				■	■	■	■	■	■	■	■	■						
FIF rules s 9(2)(f)(iv)																		
Targeted consultation on decisions sought in Report						■	■											
Report to Ministers							■	■										
Cabinet approval sought								■	■									
Technical paper drafting									■	■								
Targeted consultation on technical paper										■	■							
Report to Ministers on minor and technical details for approval											■	■						
Progress through bill process for Annual Rates 26-27 Bill												■	■	■	■	■	■	■

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **Reducing tax barriers to retaining and attracting highly skilled people: phase two**

Date:	21 August 2025	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2025/345

Action sought

	Action sought	**Deadline**
Minister of Revenue	**Agree** to recommendations **Refer** a copy of this report to the Minister of Finance for her information	29 August 2025

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**	**Suggested first contact**
Sam Rowe	Policy Lead, International	s 9(2)(a)	☒
Rory Tait	Senior Policy Advisor		☐

21 August 2025

Minister of Revenue

Reducing tax barriers to retaining and attracting highly skilled people: phase 2

Executive summary

Purpose

1. This report seeks your feedback on a package of policy options to simplify outbound investment tax rules for existing New Zealanders and new migrants. Pending your feedback, we will prepare the attached draft consultation paper for circulation with relevant stakeholders in September.

Context and background

2. The Government wants to ensure that the tax system does not incentivise highly skilled New Zealanders to leave, or disincentivise highly skilled migrants from moving here. This is because a highly skilled workforce can help lift living standards and support businesses to compete globally and grow. New Zealand's outbound investment tax rules can be a barrier to the retention and attraction of such talent. While important for the integrity of the tax system, their compliance cost and tax burden can be an undue impediment to retaining people in New Zealand.

3. Earlier this year, Cabinet agreed to a first phase of narrowly targeted reforms to the foreign investment fund (FIF) rules [CAB-25-MIN-0061 refers]. These seek to address tax barriers to attracting talent to New Zealand and will be included in the upcoming Taxation (Annual Rates for 2025-26) Bill.

4. While the previous reforms were developed as a 'minimum viable product', the Government is also interested in addressing tax barriers to retain highly skilled people who are already in New Zealand and further incentivising new migrants and overseas Kiwis to return. Cabinet is expecting a report back on further options before the end of the year [CAB-25-MIN-0061 refers]. To support this, a second phase of work has been added to the Tax and Social Policy Work Programme [IR2025/161 refers]. Accordingly, officials have begun preparing policy options for inclusion in this work programme.

5. You have already received advice on tax changes related to the digital nomads visa, with relevant legislation to be included in the upcoming tax bill. We will report on changes to the financial arrangements regime in due course.

Policy options

6. This report presents a package of policy options for targeted consultation which:

    - encourages existing New Zealanders to stay and grow their businesses here, and
    - builds on the earlier FIF reforms by further encouraging highly skilled migrants to move to New Zealand.

7. The package focuses on removing tax barriers to attracting and retaining skilled individuals while still maintaining the overall policy goals of the current rules. It considers changes to the FIF rules, s 9(2)(f)(iv) . These changes could also be combined with potential changes to the financial arrangement rules to remove further barriers to migration (which we will report to you on separately). The proposals in this package are outlined in more detail below:

   - **Expanding the scope of the revenue account method:** this method was introduced as part of the earlier reforms. It addresses liquidity and double taxation concerns for taxpayers who hold unlisted foreign shares. Currently it allows only eligible taxpayers (new migrants) to have their eligible unlisted shares taxed on a realisation basis rather than by attributing income to them. While earlier reforms focused on new migrants, for this package we now propose allowing all taxpayers to use the revenue account method for eligible unlisted foreign shares. This would reduce incentives for highly skilled people already in New Zealand to leave and improve horizontal equity between taxpayers in similar circumstances. Early fiscal estimates indicate this change could cost around $8 million per year.

   - **Expanding access to the attributable FIF income method:** taxpayers with an interest of 10% or more in a FIF can use the attributable FIF income method. Under this method, in many cases only dividends are taxed. However, there are cases where executives and founders can lose access to the attributable FIF income method as their ownership share is diluted below 10% during expansion. We recommend allowing access to the attributable FIF income method for taxpayers who previously held a 10% or greater interest in the FIF (with a lower limit of 5%) and who are still actively involved in the FIF (for example as a director or manager). This should remove an incentive for New Zealand entrepreneurs to emigrate.

   - s 9(2)(f)(iv)

   - **Raising the de minimis threshold:** the FIF rules do not apply if the total cost of attributing interests in all FIFs is below a $50,000 de minimis threshold. However, this threshold hasn't been updated since 2000. While adjusting the threshold may not materially help retain or attract highly skilled individuals, there is merit in doing so to reduce compliance costs for small taxpayers investing offshore. Increasing the de minimis threshold to $100,000 would balance these compliance cost benefits with the fiscal cost and effects on neutrality of the tax system. The fiscal cost is expected to be around $2.8 million per year.

8. s 9(2)(f)(iv)

s 9(2)(f)(iv)

9. We are also considering whether there are minor and technical amendments we could make to the FIF rules as part of this package. Should any arise, we will report to you on these in due course.

Officials' recommended approach

10. We recommend consulting on expanding the scope of the revenue account method and raising the de minimis threshold to $100,000, as outlined above. We attach a draft consultation paper covering these proposals for your review. We do not see a need to consult on expanding access to the attributable FIF income method (as it was consulted on earlier), however we recommend informing taxpayers that this policy is also being considered by the Government as part of the targeted consultation.

11. s 9(2)(f)(iv)

12.

Next steps

13. If you agree to consultation, we will incorporate any feedback you have into the draft consultation paper. We would then provide this to selected stakeholders and seek their feedback in September. We would provide you with a briefing note outlining our communications plan for this consultation.

14. s 9(2)(f)(iv)

15. Following this, we would proceed to detailed policy design and development (including finalising fiscal estimates) with a view to seeking policy approval from you and Cabinet before the end of this year.

Recommended action

We recommend that you:

1. **agree** to include expanding access to the revenue account method in the consultation paper;

   Agreed/Not agreed

2. **agree** to include adjusting the de minimis threshold in the consultation paper;

   Agreed/Not agreed

3. **agree** for Officials to circulate the attached consultation paper with relevant stakeholders, pending incorporation of your feedback and minor editorial changes;

   Agreed/Not agreed

4. s 9(2)(f)(iv)

5.

s 9(2)(a)

Sam Rowe
Policy Lead, International Policy

Hon Simon Watts
Minister of Revenue
/ /2025

Background

Problem definition

6. A highly skilled workforce can help lift living standards and support businesses to compete globally and grow. The Government wants New Zealand to be an inviting country for highly skilled people. This includes retaining the people who are already here as well as incentivising new migrants and overseas Kiwis to return. Our outbound investment tax rules, in particular the foreign investment fund (FIF) rules, are commonly cited as a significant barrier to this. This report proposes a package of reforms designed to reduce the tax barriers that may prevent people from remaining in New Zealand long-term or migrating here in the first place.

Previous reforms

7. In late 2024 we conducted a public consultation on the effects of the FIF tax rules on migration and subsequently proposed changes to the regime to mitigate these. You agreed to a package of narrowly targeted changes to the FIF rules to be implemented quickly [IR2025/007 refers]. These changes are designed as a minimum viable product for inclusion in the Taxation (Annual Rates for 2025-26) Bill, which is scheduled for introduction in August 2025 [CAB-25-MIN-0061 refers]. These changes will allow migrants to be taxed on a realisation basis for specified FIF interests, with a special carve-out for taxpayers who may face double taxation due to being subject to taxation on a citizenship basis by another jurisdiction.

Further work programme

8. Throughout the consultation on the previous reforms, a range of further tax issues relating to both migration and retaining existing New Zealanders were raised by stakeholders. To address these and build on the previous reforms, you proposed a further review of tax settings to encourage highly skilled individuals to both migrate to and remain in New Zealand. As agreed by Cabinet [CAB-25-MIN-0061 refers] this next phase of reform includes the three workstreams below:

    - Further changes to the FIF regime s 9(2)(f)(iv)

9. Changes to the financial arrangements regime; and

    - Tax changes to support the new digital nomads visa.

10. This report focuses on the first workstream. It explores options for removing identified tax barriers to retaining existing skilled individuals and attracting new ones. In particular, it considers the following potential measures:

    - expanding the scope of the revenue account method to include non-migrant New Zealand residents;
    - expanding access to the attributable FIF income method;
    - s 9(2)(f)(iv)
    - raising the FIF de minimis threshold.

11. Following your feedback, Officials will prepare targeted stakeholder consultation on the details of any policy design with a view to including changes in the Taxation (Annual Rates **2026-27**) Bill.

12. The Taxation (Annual Rates for 2025-26) Bill (the August Bill) will adjust the cash basis persons thresholds in the financial arrangements rules. This was a specific issue raised with us and will alleviate the concerns of many people, as they will only be required to return income on a cash rather than an accruals basis. However, it will not address concerns for higher wealth migrants and other individuals who will still be subject to the rules and potentially be subject to tax on unrealised gains on their foreign currency loans. Whether further work on the financial arrangements rules should be undertaken is currently being considered by you and the Minister of Finance as part of the work programme refresh.

13. We have already reported on the tax changes to support the digital nomads visa [IR2025/187 refers], and the legislation implementing these changes is included in the current tax bill.

Policy options to retain highly skilled people in New Zealand

14. The Government wants to minimise tax barriers that may encourage highly skilled people already in New Zealand to leave. The below options aim to support this by eliminating some pain points with the current FIF rules as identified in our previous consultation, and make New Zealand a more attractive place to settle permanently.

Expanding the scope of the revenue account method

15. The revenue account method (RAM) proposed as part of the previous changes would address liquidity and double taxation concerns arising from the current FIF rules for new and recent migrants. It enables eligible new migrants to pay tax on certain unlisted foreign shares on a realisation basis, rather than on a deemed dividend. For some new taxpayers that are particularly exposed to double taxation risks (primarily United States citizens and permanent residents), an 'extended revenue account method' is available to apply to all foreign share holdings.

The merits and risks of expanding access

16. There is merit in allowing all taxpayers to access the revenue account method for unlisted foreign shares. This would support the retention of ordinary New Zealanders as well as current and future migrants in respect of post-migration investments. It also removes the horizontal inequity of restricting the revenue account method to new migrants, by allowing all taxpayers to be taxed under the same method for the same kind of income.

17. However, there is a trade-off between expanding access to the revenue account method and the neutrality of the tax system. Relative to the status quo, there is a risk that the RAM creates a more favourable tax treatment for investment in eligible offshore assets relative to their domestic counterparts. However, this risk is mitigated by the illiquidity of unlisted foreign shares which restricts the ability of taxpayers to change their investment behaviour in response to the potential tax incentive. Based on estimates developed for the earlier package of reforms, we expect this could cost around $8 million per year. We will update this costing as the policy process progresses.

18. If the extended revenue account method (applying to all foreign shares) was made available to all taxpayers, this would be a significant reform to the FIF regime and carry a substantial fiscal cost. The extended revenue account method was designed as an additional concession to mitigate double taxation risks. Most taxpayers do not face the same double taxation risks as someone from a jurisdiction that taxes based on citizenship (e.g., the United States). Foreign liquid shares also do not face the same liquidity risks as illiquid shares for most taxpayers. As such it would not address a policy problem for the wider population (e.g., non-migrant New

Zealanders). Accordingly, we do not recommend broadening access to the extended revenue account method to all New Zealanders.

19. However, we recommend allowing earlier migrants who suffer double taxation on a citizenship or right to work basis to access the extended revenue account method for their liquid foreign shares. This would support the retention and permanent settlement of these earlier migrants in New Zealand.

Proposed approach

20. We recommend allowing all taxpayers to use the revenue account method for their eligible unlisted foreign shares. The extended revenue account method would remain targeted only at those subject to double taxation, though now available to eligible people already in New Zealand in addition to new migrants. We have included this approach in the attached draft consultation paper.

21. To provide certainty and reduce compliance costs for taxpayers we suggest retaining the consequential policy decisions from the previous reforms to the extent possible. However, we would p ropose allowing people to elect back into the revenue account method after electing out. This is because locking taxpayers into or out of the revenue account method would no longer be appropriate given the method would be applicable beyond only eligible shares held on migration. To counter misuse of the method to gain a tax advantage, we would develop some integrity measures (e.g., only allowing a taxpayer to elect in or out once every five years).

Expanding access to the attributable FIF income method

22. Currently, taxpayers with interests of 10% or more in a qualifying FIF[1] may choose to calculate their FIF income under the attributable FIF income method. Under this method, if the FIF passes an active business test, only dividends are taxed. Any gain from the disposal of the FIF interests is not taxed unless the interest is held on revenue account.

23. However, there are cases where executives and founders who have used the method fall below 10% shareholding in their company as their stake is diluted during expansion. In the 2024 consultation, we included a proposal to remove the 10% threshold required to access the attributable FIF income method, provided the shareholder played an active role in the company. While submitters did not think this proposal would be as effective as the revenue account method at achieving the overall policy object of attracting and retaining highly skilled migrants, submitters considered this proposal would resolve current issues with the attributable FIF income method and would be worth progressing.

A targeted amendment still has merit

24. A narrowly targeted amendment to allow existing users of the attributable FIF income method to still use the method even after their share has been diluted below 10% still has merit. This is because it would remove a barrier to remaining in New Zealand for entrepreneurs already living here, should their ownership share fall below 10%. This was raised as a concern by external stakeholders in our first round of consultation.

Proposed approach

[1] A qualifying FIF interest for the attributable FIF income method are those that pass the active business test - where at least 95% of its income is from business activities rather than passive income such as interest, royalties and rent. If it does not pass the test, shareholders are taxed on their share of the FIF's passive income.

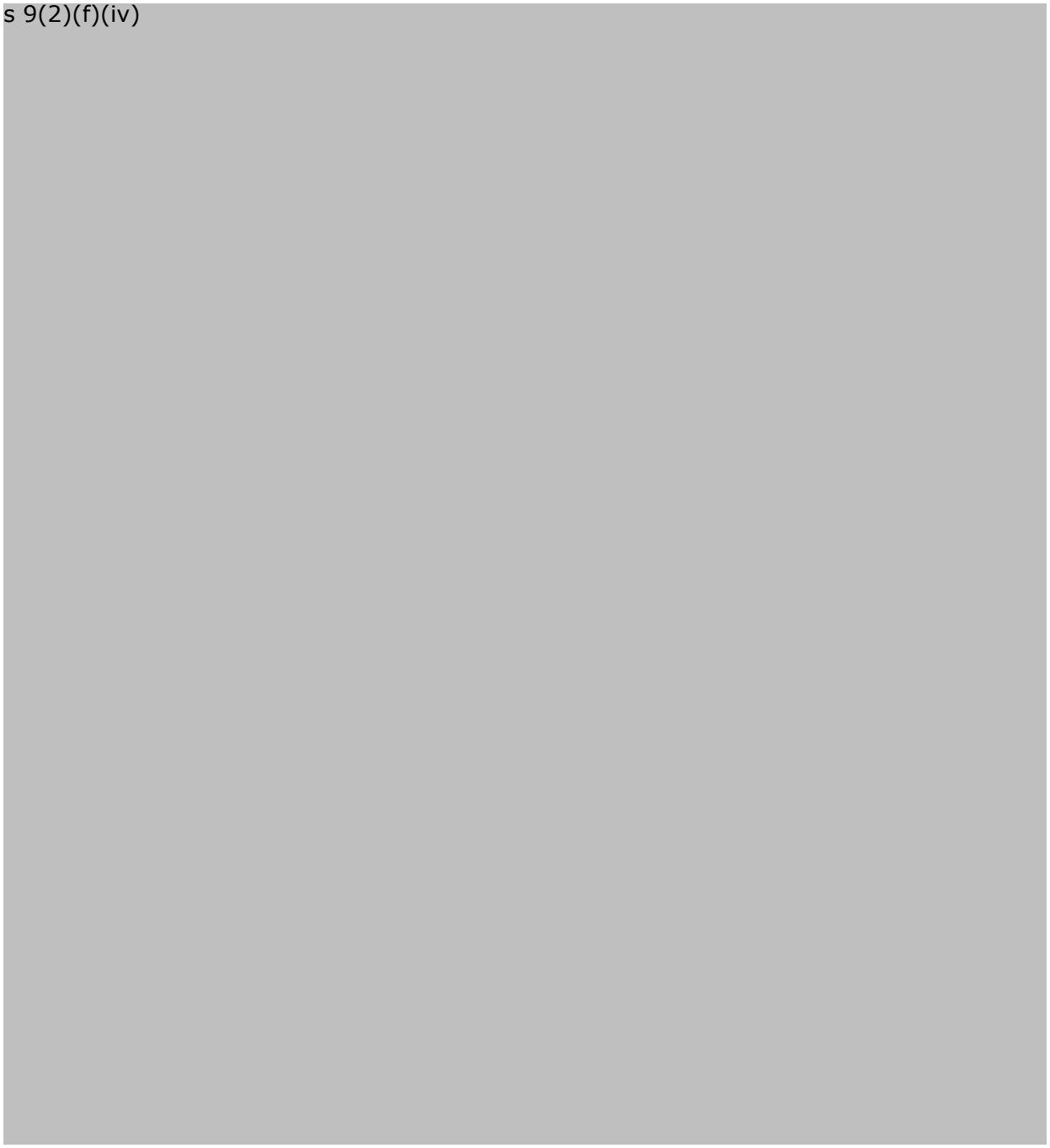
25. We recommend allowing access to the attributable FIF income method for taxpayers with an active role in the enterprise (such as employees or those with management roles) who previously held a 10% or greater interest in the FIF (and still hold at least 5%). The active role and 5% minimum tests are designed to ensure that this method remains limited to active investments.

26. Given this policy was more broadly consulted on last year, we do not see a need to include this proposal in the consultation paper. However, we should note it as a measure the Government is still considering as part of the package.

Policy options to attract migrants to New Zealand

27. While earlier reforms to the FIF rules sought to address barriers to attracting talent to New Zealand, there remains further work that could be done to ensure New Zealand is welcoming to highly skilled people. Two options for consultation are outlined below.

s 9(2)(f)(iv)



s 9(2)(f)(iv)

[redacted]

Raising the FIF de minimis threshold

35. A common piece of feedback from the previous consultation was that the de minimis threshold for the FIF regime should be amended.

36. The FIF rules do not apply if the total cost of attributing interests in all FIFs is below a $50,000 de minimis threshold. This is to reduce compliance costs for small taxpayers. However, as the threshold has not been adjusted since it was set in 2000, the real term value has been eroded over time. $50,000 in year 2000 would be worth around $95,000 in 2025. This means that more investors now have to apply the FIF rules on their offshore investments.

The merits and risks of raising the de minimis threshold

37. There is merit in lifting the de minimis threshold, to preserve the size of its original compliance cost benefits, for example by adjusting it for inflation. We note that raising the de minimis threshold would not support the Government's objectives of removing barriers to attracting and retaining high value migrants, as high value migrants are likely to have sufficient quantum of investments to remain in scope of the FIF rules. However, it would reduce compliance costs for ordinary New Zealanders.

38. Raising the de minimis threshold carries material fiscal implications. It also affects the neutrality of the tax system by increasing the amount that can be invested offshore before the FIF rules apply. Relative to the status quo this could improve the efficiency of investment decisions by increasing the amount that can be invested offshore without FIF taxation. However, it could also marginally decrease the proportion of New Zealanders' savings invested in New Zealand shares. Any decrease in domestic investment by New Zealanders may be offset by increased investment from non-resident investors, which could mitigate the impact on the pool of domestic capital.

Proposed approach

39. We recommend against increasing the de minimis threshold if the primary objective is to attract and retain high value migrants. However, it would be worth increasing the threshold if your goal was to instead reduce compliance costs for small taxpayers investing offshore. In that case, we would recommend increasing it to $100,000 to balance the benefits with the fiscal cost (approximately $2.8 million per year based on earlier work) and distortionary effects. We expect this would be well received by taxpayers. Pending your feedback on whether you wish to consult on adjusting the threshold, we have included this approach in the attached draft consultation paper.

Other issues

40. As part of the eventual package of reforms, we could consider other smaller remedial amendments. Should any arise, we will report to you on these in due course. Beyond this, we could provide advice on further amendments to simplify the FIF rules in the future.

Consultation

41. The Treasury was informed about this report.

Next steps

42. Pending your approval and any feedback on the above policy options and the attached draft consultation paper, we will prepare the consultation paper for engagement with selected stakeholders in September. We will provide you with a briefing note outlining our communications plan for this consultation.

43. Previous public statements and Cabinet decisions have indicated more detail on further reforms would be announced before the end of 2025. As such, we have prepared the below possible timelines on consultation, reporting, and decision-making to allow for end-of-year announcements.

Time	Action
End August to Mid September	3-week targeted consultation on FIF amendments commences, s 9(2)(f)(iv)
s 9(2)(f)(iv)	
Early November	Report to Ministers on submissions feedback and draft Cabinet paper for policy approval
Wednesday 3 December	Intended Cabinet Committee (ECO) date
Monday 8 December	Cabinet date

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **Reducing tax barriers to retaining and attracting people with skills and capital: policy decisions**

Date:	19 November 2025	**Priority:**	Medium
Security level:	Sensitive - Budget	**Report number:**	IR2025/405

Action sought

	Action sought	**Deadline**
Minister of Finance	**Agree** to recommendations	5 December 2025
Minister of Revenue	**Agree** to recommendations	5 December 2025

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**	**Suggested first contact**
Sam Rowe	Policy Lead, International	s 9(2)(a)	☒
Rory Tait	Senior Policy Advisor, International		☐

19 November 2025

Minister of Finance
Minister of Revenue

Reducing tax barriers to retaining and attracting people with skills and capital: policy decisions

Executive summary

1. The Government considers that a highly skilled and capital-intensive workforce can help lift living standards and support New Zealand businesses to compete globally and grow. It wants New Zealand to be an inviting country for highly skilled people, which includes retaining the talent that is already here as well as incentivising new migrants and overseas Kiwis to return. Our outbound investment tax rules, particularly foreign investment fund (FIF) rules, are commonly cited as a significant barrier to this.

2. This paper seeks policy decisions on Phase 2 of the work to reduce tax barriers to better retain and attract skills and capital. Cabinet agreed to Phase 1 earlier this year, with narrowly targeted reforms to the FIF rules

3. We last reported to you on Phase 2 in August 2025 [*IR2025/345 refers*]. The August report sought your feedback on a set of policy options to simplify the FIF rules for existing New Zealanders and new migrants, and your approval for us to undertake consultation with key stakeholders.

4. The final policy recommendations in this paper incorporate the feedback we received from targeted consultation. s 9(2)(f)(iv)

Proposed package of reforms

5. We recommend you progress a policy package through Budget 2026 that includes:

   a. Expanding the scope of the revenue account method (RAM) for all taxpayers with unlisted foreign shares to address liquidity concerns and double taxation risks for any foreign shares held by migrants that are subject to double taxation.

   b. Raising the FIF *de minimis* threshold to adjust for inflation since the introduction of the threshold and to reduce compliance costs for smaller taxpayers.

   c. Expanding access to the attributable FIF income method to reduce the risks of founders emigrating if they lose access to this method during business growth.

   d. Ensuring the 10-year FIF exemptions continue to apply for corporate migration, mitigating emigration risks by aligning legislation with the policy intent and commercial practice.

6. The set of changes proposed in this report will help ensure that New Zealand's tax system supports and attracts a highly skilled and capital-intensive workforce, which in turn supports the Government's broader growth objectives. We appreciate that you may wish to stagger some of these measures in light of fiscal constraints, and we provide further advice on prioritisation as part of this report.

7. You are due to report back to Cabinet on policy options. As further decisions on this project (including funding) will be part of the Budget 2026 process, we recommend deferring your report back to Cabinet until then.

Background

Overview of the problem

8. The Government wants to ensure that the tax system does not incentivise highly skilled New Zealanders to leave, or disincentivise highly skilled migrants from moving here. This is because a highly skilled workforce can help lift living standards and support businesses to compete globally and grow.

9. Our outbound investment tax rules, in particular the foreign investment fund (FIF) rules, are commonly cited as a significant barrier to the attraction and retention of talent and capital. As such, we seek your decisions on a package of reforms designed to reduce the tax barriers that may prevent people from remaining in New Zealand long-term or migrating here in the first place. Taken together, these tax policy changes will make New Zealand a relatively more favourable destination for skills and capital, in turn supporting the Government's growth agenda.

Background and proposed package of reforms

10. Earlier this year, Cabinet agreed to a first phase of work to reduce New Zealand's tax barriers to retaining and attracting people with skills and capital. This included narrowly targeted reforms to the FIF rules, specifically in relation to the adoption of the revenue account method (RAM) for FIF interests to be taxed on a realisation basis [*ECO-25-MIN-0020/CAB-25-MIN-0061 refers*]. These changes only apply to recent migrants and are included in the Taxation (Annual Rates for 2025-26, Compliance Simplification, and Remedial Measures) Bill to address the imminent risk of emigration of new migrants who arrived at the beginning of COVID-19.

11. On 21 August 2025 we reported to you on Phase 2 of this FIF workstream [*IR2025/345 refers*]. The August report sought your feedback on a set of policy options to simplify the FIF rules for existing New Zealanders and new migrants, and your approval for us to undertake consultation with key stakeholders.

12. s 9(2)(f)(iv)

13. In relation to Phase 2 reforms, targeted consultation with stakeholders has now been completed. This report sets out the outcomes of this consultation, and seeks your policy decisions in relation to:

    a. Expanding the scope of the revenue account method (RAM);

    b. Raising the current $50,000 FIF *de minimis* threshold;

    c. Expanding access to the attributable FIF income method; and

    d. Ensuring the 10-year FIF exemptions continue to apply for corporate migration (this is a new remedial to address an issue which emerged during consultation).

14. Stakeholder submissions have been incorporated into our analysis below. If you would like a more detailed summary of submissions, we can provide this.

15. We note that you are interested in a package of reforms with a fiscal cost of around $10 million per year. We have taken this into consideration in our advice below.

Expanding the scope of the revenue account method

16. The revenue account method was introduced as part of the first phase of reforms, included in the Taxation (Annual Rates for 2025-26, Compliance Simplification, and Remedial Measures) Bill currently before the House.

17. The revenue account method addresses liquidity and double taxation concerns for taxpayers who hold unlisted foreign shares. This is because the current FIF rules charge tax on deemed income, which can be challenging to fund if a taxpayer holds unlisted shares that cannot easily be sold and which may not pay dividends. Some jurisdictions also do not recognise the current FIF rules for tax credit purposes[1], resulting in double taxation. The revenue account method resolves this by allowing eligible taxpayers to have their eligible unlisted shares taxed on a realisation basis rather than by attributing income to them.

18. The measure in the current bill is, however, restricted to new migrants only. The consultation paper proposed extending the revenue account method so that all taxpayers would be able to use this method for eligible unlisted foreign shares. This would reduce incentives for highly skilled people already in New Zealand to leave and it would improve horizontal equity between taxpayers in similar circumstances. The consultation paper proposal would also allow all migrants who are subject to double tax due to citizenship or right to work in another country (primarily migrants from the United States) to use the revenue account method for their listed shares as well, regardless of the date they migrated (the measure in the current Bill does not apply to migrants who became fully tax resident before 1 April 2024).

Key themes from consultation

19. Across stakeholders there was broad support for expanding access to the revenue account method, with a mix of views as to whether it would improve retention or whether further work would be required to achieve that outcome. There was consistent enthusiasm for the revenue account method to apply to all foreign shares, both listed and unlisted.

20. There was also continued debate over the discount rate, with some stakeholders encouraging us to increase this from the currently proposed 30% to 50%. At the same time, stakeholders were supportive of retaining as many settings from Phase 1 as possible in order to provide certainty for taxpayers. Some submitters also supported guardrails on switching between methods from year to year, and suggested that any consistency rule align with other similar measures.

Broader reform and expanding the revenue account method to all foreign shares

21. We received several submissions calling for a wider review of the FIF regime in its entirety so it is better fit for purpose, though without specifying any other issues the FIF rules pose beyond liquidity and double taxation. We consider this to be outside the scope of this workstream, which is focused on removing "rough edges" that deter people with skills and capital from settling in New Zealand permanently.

22. Many stakeholders also suggested that we further expand the revenue account method to all foreign shares held by all taxpayers, on the basis that this would improve the neutrality of the tax system and reduce compliance costs by not distinguishing between listed and unlisted investments.

[1] This is because other jurisdictions typically tax on a realisation basis, so may not recognise FIF tax on deemed income as a creditable tax.

23. The current proposal would already allow the revenue account method to be applied to all foreign shares (listed and unlisted) held by migrants subject to double taxation. We consider a wider expansion of the revenue account method to be a more fundamental change to the FIF regime, and this would carry a large fiscal cost (approximately $115 million per year or $443 million over the forecast period). This would require further review and analysis, as wider use of this method may remove the need for other FIF calculation methods (such as the fair dividend rate method).

24. Such a change does not address the policy problem of liquidity and double taxation arising from the current FIF rules. These concerns do not arise for listed investments where the taxpayer is able to sell some shares to meet their tax obligations and is not subject to double taxation. More broadly, we also recommend retaining the existing fair dividend rate method (and other supplemental FIF calculation methods) as an effective taxation approach for foreign shares where liquidity and double-tax are not concerns. This is because they remove the tax-driven incentive to invest offshore and provide a stable revenue stream for the government.

Officials' recommendation

25. We continue to recommend expanding the revenue account method to be accessible to all taxpayers. We do not support changing the assets that are currently covered by the revenue account method (eligible unlisted foreign shares only) and extended revenue account method (all foreign shares for certain taxpayers facing double taxation).

26. Our recommended approach is estimated to cost around $9.2 million per year, or $38.5 million over the forecast period, when accounting for some offsetting revenue from tax on realised gains under the revenue account method.

Raising the FIF *de minimis* threshold

27. The FIF rules do not apply if the total cost of attributing interests in all FIFs is below a $50,000 *de minimis* threshold. This is to reduce compliance costs for small taxpayers. However, as the threshold has not been adjusted since it was set in 2000, the real term value has been eroded over time. $50,000 in the year 2000 would be worth around $95,000 in 2025. This means that more investors now have to apply the FIF rules on their offshore investments.

28. As noted in earlier reporting, raising the *de minimis* threshold won't affect the attraction and retention of high value migrants as they are likely to have assets well above the threshold. Despite this, there is merit in raising the threshold to address its erosion by inflation and reduce compliance costs for smaller investors. The consultation paper did not propose increasing it to a particular level, instead asking submitters for their view generally on an increase.

Themes from consultation

29. There was broad support from stakeholders on increasing the *de minimis* to restore the real term value of the threshold. However, submitters agreed that it would not materially affect migration decisions, with some adding that the money could be better spent on other measures to support retention. Among those that did support an increase, a subgroup suggested the new *de minimis* threshold be set above $100,000 to guard against future inflation.

Officials recommendation

30. Absent the fiscal cost, we would recommend an increase to $100,000 which would reduce compliance costs by fully addressing the impacts of inflation on the threshold since 2000. Relative to the status quo it would also improve the efficiency of investment decisions by increasing the amount that can be invested offshore

without FIF taxation. Any decrease in domestic investment by New Zealanders as a result of increased offshore investment may be offset by investment from non-residents, which could mitigate the impact on the pool of domestic capital.

31. However, any uplift to the *de minimis* threshold will need to be considered against the material fiscal costs and other parts of this package. Increasing the *de minimis* threshold to $100,000 comes at a cost of $34.4 million across the forecast period (or $8.1 million per year). An alternative option is to make a smaller increase in the threshold to $80,000, which lowers the fiscal cost to $30.2 million over the forecast period (or $7.1 million per year). While this would not fully address the impacts of inflation, it would still have compliance cost benefits to smaller taxpayers.

Expanding access to the attributable FIF income method

32. Some taxpayers with an interest of 10% or more in a FIF can use the attributable FIF income method. These taxpayers typically have a more active role in their investment, as such it makes sense for them to be taxed on this holding similarly to how controlled foreign companies are taxed (as these are also active investments). This means that in many cases only dividends are taxed.

33. However, there are cases where founders who previously used this method can lose access to it as their ownership share is diluted below 10% during business expansion. This can mean an individual goes from paying nil tax (as their business may not be paying dividends yet) to paying a deemed dividend under the fair dividend return method, with no means to liquidate their holdings to pay the tax liability. The revenue account method only partially addresses the concerns of this group as they would still be taxed on any capital gains that have accrued when they dispose of their interest under the revenue account method. Stakeholders submitted that without this amendment the high-profile entrepreneurs that the government would most like to retain, would be incentivised to leave New Zealand once their stake in their businesses drop below 10%.

34. In the consultation paper we proposed an amendment that would allow taxpayers who previously used the attributable FIF income method to continue doing so if their ownership share falls below 10%, provided it remains above 5% and they continue to hold an active role in the company. This would address the tax incentive for such taxpayers to emigrate as their businesses expand overseas.

Themes from consultation

35. Stakeholders were broadly supportive of expanding access to this method, with some modifications to the exact parameters of the proposal. While expanding access to this method would affect only a small number of taxpayers (in particular New Zealand startup founders who wish to remain here), it would make a material difference to them and address some more niche circumstances that are not addressed by the revenue account method.

36. Most stakeholders considered that the proposed 5% floor was too high, particularly where a business had been acquired by an offshore firm, meaning the taxpayer's shareholding is a small sliver of a now much larger business. Some submitters suggested to drop the 5% floor altogether and instead rely on an active role test.

37. Some other submitters said they would prefer that the 10% interest test be dropped to 5% in all cases, rather than creating a second shareholding floor as per the original proposal. This would allow more taxpayers to use the method at any stage of business growth.

Officials' recommendation

38. Following discussions on how the proposed 5% floor may still be too high to prevent the emigration of entrepreneurs whose businesses have been acquired offshore, we propose dropping this element of the proposal. Instead, we recommend requiring taxpayers who wish to continue using the attributable FIF method after their shareholding falls below 10% to hold an active role in the company (such as being a director, executive, or employee). This active role test is an integrity measure to ensure this method is only used in the intended circumstances.

39. Progressing this expansion to the attributable FIF income method is expected to cost around $0.7 million per year (or $1.5 million over the forecast period). This estimate accounts for some of these taxpayers moving abroad in the absence of this amendment, but also reflects that for those who would stay anyway, their tax liability could reduce to nil.

Ensuring the 10-year FIF exemptions continue to apply for corporate migration

40. This issue was recently raised with us in a discussion with stakeholders, so we have not reported on it to you before and it was not included in the FIF Phase 2 consultation. We have included this remedial measure in the proposed package as we believe it fits with your policy objectives by addressing the retention of New Zealand entrepreneurs and venture capitalists whose businesses or investments migrate to the United States.

Context

41. A New Zealand business could migrate offshore for a number of reasons, such as to gain access to additional equity financing. When this happens, the New Zealand business could become a FIF, and the New Zealand business owner or venture capitalist could start deriving FIF income unless they meet one of the existing exemptions. This was considered undesirable because this could result in a large tax liability arising when there is no underlying income stream, as these investments tended to be in its growth phase and were making losses.

42. Currently, there is a 10-year exemption available to New Zealand shareholders, in particular owners and venture capital funds, when a business migrates offshore. This exemption requires that the shareholder acquired the shares before the company migrated from New Zealand and before the shares were listed on a recognised exchange.[2] It is intended that these investors will be able to continue to invest in the company after it has listed without losing the exemption.

43. However, New Zealand shareholders are currently falling out of this exemption when the business lists on a US stock exchange due to a recent rise in popularity in listing using special purpose acquisition companies (commonly known as SPACs).

44. Special purpose acquisition companies are formed specifically for the purpose of raising capital through an initial public offering which it subsequently uses to acquire or merge with another company. For a New Zealand business wanting to list on a US stock exchange, a special purpose acquisition company is formed and listed on that US stock exchange first. After the capital has been raised, the New Zealand business is merged with the special purpose acquisition company. The shares in the New Zealand business are cancelled in exchange for shares in the newly listed special purpose acquisition company. The 10-year exemption would then no longer apply to the New Zealand business as its shares are cancelled. The exemption would also not apply to the newly listed special purpose acquisition company either

[2] There are several other requirements, such as the business must continue to have a presence in New Zealand.

because the New Zealand shareholders would not have acquired shares in the special purpose acquisition company before it listed.

Analysis

45. The original policy intent of the provisions was to provide a 10-year exemption from the FIF rules for shareholders in New Zealand businesses which migrated and listed overseas – the manner of their listing was not a relevant consideration. Therefore it is within the original policy intent for overseas listings via special purpose companies to be eligible for the exclusion (provided the other requirements are met). The absence of the exemption could incentivise New Zealand entrepreneurs to emigrate when they list their business on a US stock exchange. It could also have a chilling effect on New Zealand venture capital funds investing in industries where businesses are likely to move to the US, such as the tech sector.

46. Further if a New Zealand business lists directly on a foreign exchange, the New Zealand shareholders will still be eligible for the 10-year exemption provided all other requirements are also met. This creates a horizontal equity issue as shareholders are treated differently depending on the method of listing used, which New Zealand shareholders generally do not have control over.

Officials' recommendation

47. We recommend that the wording of the requirement be amended to align with its original intent that, regardless of the method used by a New Zealand business to list on a foreign exchange, the New Zealand shareholders are eligible for a 10-year FIF exemption (provided all the other requirements are also met). This is estimated to have a small fiscal cost of $100,000 per year (or $0.425 million over forecast).

s 9(2)(f)(iv)

Other issues raised by submitters

Mirroring tax concessions on retirement savings accounts

50. Several stakeholders have raised their dissatisfaction that foreign retirement savings accounts with overseas tax concessions (such as 401k accounts in the United States) do not have those tax concessions mirrored in New Zealand. New Zealand does have specific tax rules for transfers and withdrawals from foreign superannuation schemes. These rules seek to recognise that New Zealand should only have taxing rights over the portion of the scheme accrued during the taxpayer's residence here. However, we should tax that portion, as otherwise migrants would have an incentive to retain their funds offshore where they would not be subject to New Zealand tax. This would put them in a better position than other New Zealanders saving for retirement. It would also deprive the government of tax which

could fund the public services such migrants are likely to consume in retirement here. Accordingly, it would be directly contrary to the policy rationale of our current settings for New Zealand to provide tax concessions for these accounts, especially if the concessions were only for any one jurisdiction. Further, this issue is unrelated to the FIF rules, as such accounts are generally not subject to that regime.[3] As such, we do not propose any changes to our tax settings.

Conclusion

51. It is clear that the current FIF rules are widely viewed as significant barriers for talent and capital in New Zealand. Taken together, this package of reforms can be expected to reduce the tax barriers that prevent people from remaining in New Zealand long-term or from migrating here in the first place.

52. We recommend you consider these changes as a package of initiatives, funded and communicated together. This will maximise the impact of the policy changes, demonstrating that the Government is committed to ensuring New Zealand remains an attractive place for skills and capital.

Financial and Budget implications

53. The total fiscal cost of the Phase 2 package will be determined by your decisions on the options set out above. The table below sets out the possible costs, which will be revised following final policy decisions as part of the Budget 2026 process.

$m – increase/(decrease)					
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & outyears**
1A: Expanding the scope of the revenue account method – allowing everyone to use the revenue account method for unlisted shares (officials' recommended option)					
Tax Revenue:					
Other Persons tax (turning off FIF)	(4.900)	(19.800)	(18.800)	(19.000)	(19.600)
Other Persons tax (replacement tax treatment)	2.600	10.500	10.000	10.100	10.400
Net impact	(2.300)	(9.300)	(8.800)	(8.900)	(9.200)
1B: Expanding the scope of the revenue account method – allowing everyone to use the revenue account method for all foreign shares					
Tax Revenue:					
Other Persons tax (turning off FIF)	(51.000)	(207.000)	(198.00)	(244.000)	(245.000)
Other Persons tax (replacement tax treatment)	27.000	110.000	105.000	130.000	130.000
Net impact	(24.000)	(97.000)	(93.000)	(114.000)	(115.000)
2A: Fiscal impact of FIF threshold moving to $100k (officials' recommended option)					
Tax Revenue:					

[3] Some taxpayers whose superannuation scheme was taxed under the FIF rules before 2014 may choose to continue to be taxed under the FIF rules on such accounts.

Other Persons Tax	(2.000)	(8.100)	(8.100)	(8.100)	(8.100)
2B: Fiscal impact of FIF threshold moving to $80k					
Tax Revenue:					
Other Persons Tax	(1.800)	(7.100)	(7.100)	(7.100)	(7.100)
3: Expanding access to the attributable FIF income method					
Tax Revenue:					
Other Persons tax	-	(0.200)	(0.100)	(0.500)	(0.700)
4: Ensuring the 10-year FIF exemptions continue to apply for corporate migration					
Tax Revenue:					
Other Persons Tax	(0.025)	(0.100)	(0.100)	(0.100)	(0.100)
Total possible change in Revenue (range)	(4.125) - (26.025)	(16.700) – (105.400)	(16.100) – (101.300)	(16.600) – (122.700)	(17.100) – (123.900)
Officials' Recommended Package	(4.325)	(17.700)	(17.100)	(17.600)	(18.100)

54. Several of these costings have been revised upwards relative to initial indications in our previous advice [*IR2025/345 refers*]. This is because we now have data from the latest tax returns and there has been a substantial increase in both the number of taxpayers filing FIF income and their FIF tax liabilities. As a result, total government revenue will increase as a result of higher FIF income, but concessions from the rules will incur a proportionately greater fiscal cost and prioritisation may be required to fit within fiscal envelopes.

55. We also note that, while the estimated revenue loss for expanding the scope of the revenue account method is somewhat uncertain, the revenue gain is highly uncertain because it is reliant on the payment of dividends or the sale of shares. It is challenging to estimate what revenue will be recouped as the taxpayer has control over when they realise their assets. This means more volatility and significantly more uncertainty on the offsetting revenue gain side of the proposed changes.

Package options

56. While we support all of the above measures in principle, we understand they may need to be prioritised considering fiscal constraints. You have previously indicated interest in a package of policy changes that fits within an envelope of around $10 million per annum. This is challenging with the revised costings, particularly if you wish to progress lifting the de minimis threshold. A package that includes the below measures is estimated to cost around $18.1 million per year:

    a. expand the scope of the revenue account method to unlisted shares for all taxpayers and to both listed and unlisted shares for those subject to double tax,

    b. lift the *de minimis* threshold to $100,000,

    c. expand access to the attributable FIF income method, and

    d. ensure the 10-year FIF exemptions continue to apply for corporate migration.

57. Amending the *de minimis* threshold is in our view a lower priority change that has a weaker alignment with this package's objectives of retaining and attracting talent, despite its other merits. Therefore, it could be deferred at this time to deliver a package that fits within a $10 million per annum envelope. Progressing the

expansion of the revenue account method, expanded access to the attributable FIF income method and the 10-year FIF exemptions remedial is estimated to cost around $10 million per year. If further savings are required, you could defer expanding access to the attributable FIF income method, as some, but not all, of the challenges this seeks to address are resolved by the revenue account method.

58. We seek your guidance on which measures to include in a package to progress further through the Budget process. Once a package is selected, costings will need to be further revised to account for the interactions between the measures and prevent any double-counting of costs.

Administrative implications

59. We propose that these measures be included in the Taxation (Annual Rates 2026-27) Bill, to be passed before 31 March 2027. The proposals could apply retrospectively from 1 April 2026. This retrospective application is consistent with the approach taken with the FIF Phase 1 reforms and should have a minimal compliance impact because the relevant tax returns for the 1 April 2026 tax year are due after 31 March 2027.

60. Implementing these changes via Budget 2026 legislation is not desirable, as this would not allow any consultation on the proposed legislation.

61. From a delivery perspective, the changes proposed in this paper are relatively straightforward. We estimate the implementation and ongoing administrative cost to be small enough for Inland Revenue to absorb in their baselines over the forecast period.

Consultation

62. The Treasury has been informed about this report.

Next steps

63. Cabinet has noted your intention to report back on further policy options for inclusion in legislation [*ECO-25-MIN-0020/CAB-25-MIN-0061 refers*]. As progressing this work further requires funding to be sought via Budget, we propose not reporting to Cabinet at this time as initially envisaged. Instead, final decisions can be made through the Budget process.

64. We understand you also wish to consider how and when to announce your chosen package of changes. Confirming this package will proceed would require Cabinet's agreement to the policy and funding. As these changes need to be confirmed through the Budget 2026 process, the announcement would normally not happen until after Cabinet's agreement to Budget 2026, either on Budget Day or as a pre-Budget announcement with the approval of the Prime Minister's Office and Minister of Finance.

65. Any confirmation of a package of changes prior to Cabinet's agreement to Budget 2026 would require a standalone Cabinet paper and Budget pre-commitment. The Minister of Finance's endorsement of any Budget pre-commitment is necessary, and officials generally recommend against pre-commitments except for where there is a clear rationale for out-of-cycle funding.

66. However, it would still be possible to announce your interest in adopting the measures prior to Cabinet confirmation that they will definitely proceed.

67. Officials are available to discuss the contents of this report if desired.

Recommended action

We recommend that you:

1. **Indicate** below your preferred policy options for inclusion in a package of measures to reduce tax barriers to retaining and attracting people with skills and capital:

   a. allowing all taxpayers to apply the revenue account method on eligible interests (all foreign shares for migrants subject to double taxation and unlisted foreign shares only for other taxpayers);

      Agreed / Not agreed Agreed / Not agreed

   b. lifting the foreign investment fund *de minimis* to $80,000 or $100,000;

      $80,000 / $100,000 / Not agreed $80,000 / $100,000 / Not agreed

   c. allowing taxpayers who have previously used the attributed foreign income method and continue to have access to the relevant information, but have subsequently fallen below the 10% ownership requirement, to continue to use the attributed foreign income method if they have an active role in the company; and

      Agreed / Not agreed Agreed / Not agreed

   d. amending the eligibility for the existing 10-year foreign investment fund exemptions to ensure they continue to apply when New Zealand businesses emigrate and list overseas, regardless of the method of the listing;

      Agreed / Not agreed Agreed / Not agreed

2. **Agree** to report back to Cabinet on your chosen policy options as part of the Budget 2026 process:

   Agreed / Not agreed Agreed / Not agreed

s 9(2)(a)

Sam Rowe
Policy Lead, International Policy

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

Reference	BN2026/067
Date	26/02/2026
To	Revenue Advisor, Minister of Revenue – Angela Graham Private Secretary, Minister of Revenue – Melissa Zhen
From	Lonnie Liu
Subject	**Going for Growth Ministers' meeting 11 March**

Context

1 The foreign investment fund (FIF) reforms have been added to the agenda of the next Going for Growth Ministers' meeting on global trade and investment. The meeting is currently scheduled to be held on Wednesday, 11 March.

2 Inland Revenue has been asked to provide an update on the FIF workstreams to support the discussion at the meeting.

3 Attached to this note are:

- Your speaking notes for the meeting (see Appendix One)
- An update on Phase One and Phase Two of the FIF reforms (see Appendix Two)

4 Please note that the options being considered for Phase Two are Budget Sensitive. The paper that will be circulated for the meeting (Appendix Two) therefore does not include any of the options that are not already public. However, the details of these options have been included in your speaking notes to support any discussion you may have at the meeting.

Lonnie Liu

Senior Policy Advisor

s 9(2)(a)

Appendix Two: Proposed update on the foreign investment fund workstreams

Update on first phase of reforms

1 The first phase of reforms to the FIF rules are in the Taxation (Annual Rates 2025-26, Compliance Simplification, and Remedial Matters) Bill, currently before the Finance and Expenditure Committee. The Committee is due to report the Bill back to the House in March. The Bill needs to be passed before 31 March 2026.

2 The Bill proposes to introduce the revenue account method (RAM) for new migrants. The RAM is a new way of calculating FIF income for certain qualifying foreign equity investments. The new method is more aligned with international norms because it allows income to be taxed as it is received. In contrast, the existing calculation methods tax "paper gains" which can lead to difficulties funding the tax liability and mostly do not reflect the economic reality of the investment. Further, it is ambiguous whether the taxing foreign equity investments under the current settings would give rise to a foreign tax credit in the other jurisdiction to offset foreign capital gains taxes (i.e., in the US). Thus, the RAM also mitigates the double taxation risk for migrants who also pay taxes in another jurisdiction.

Issues with the FIF rules

3 Stakeholders have raised two issues with the RAM proposal in their discussions with MBIE and Ministers:

- The discount is not high enough.
- An "exit tax" should not be introduced alongside the RAM proposal.

4 Officials note that the two issues have been raised in various forums throughout the development of the RAM proposal, including submissions to the Finance and Expenditure Committee (IR2024/299, BN2025/051, IR2025/072, IR2025/233, and Departmental Report refer).

5 The proposal has been designed based on feedback from robust stakeholder engagement, and Cabinet has agreed to the current proposal, having balanced a range of competing feedback. The issues have also been considered at the Finance and Expenditure Committee as part of submissions on the current omnibus tax Bill. The Committee is due to report the Bill back to the House later this month.

Discount rate

6 Under the existing FIF rules, taxpayers are deemed to have earned income up to 5% of the opening market value of their portfolio of foreign shares each year. This is regardless of whether any dividends have been received or whether any gain is crystalised from the disposal of any foreign shares. This income is then taxed at the person's marginal tax rate, which can be up to 39% depending on their annual income from all other sources.

7 The RAM proposal taxes qualifying foreign shares on a realisation basis. For most migrants, the RAM would only apply to unlisted foreign shares that were acquired before they migrate to New Zealand. For US migrants, the RAM would apply to all foreign shares because they remain subject to a capital gains tax in the US even after moving to New Zealand. This resolves the double taxation issue that is unique to US migrants.

8 Rather than deeming income up to 5% of the value of the portfolio, the RAM proposal taxes dividends received and the gain or loss from the disposal of any disposal of foreign shares. The proposal discounts any gains and losses from the disposal of foreign shares by 30%, and the income is taxed at the person's marginal tax rate.

9 Officials have continued to recommend maintaining this 30% discount rate because the resulting effective tax rate (70% of gains x 39% top marginal tax rate) is 27.3%. This approximates the tax rate that would apply if these investments were held in a company (28%) or a portfolio investment entity (28%). This alignment is important as there would otherwise be a tax-driven incentive to invest in certain ways, which would be distortionary.

10 For context, the effective tax rate on capital gains across the OECD's 38 members range from 0% to 42%. At 27.3%, New Zealand would rank ahead of 14 other countries including Korea (27.5%), Spain (30%), Sweden (30%), Ireland (33%), and France (34%).

11 Officials are doubtful of the trade-off of increasing the discount rate to 50% (which would result in a 19.5% effective tax rate). The FIF rules have only ever been raised as a barrier to migration to and permanent settlement in New Zealand due to the hard-to-fund nature of the tax liability and the double taxation issue unique to US migrants. The current RAM proposal addresses those issues.

12 Migration decisions are complex and are generally influenced by many factors, such as economic conditions, political stability, and family links. While there is some general evidence that tax can affect migration decisions for higher-skilled and wealthier individuals, international evaluation on the impact of migrant tax incentives on either migration or economic growth has been inconclusive.

13 To the extent an individual is not very tax sensitive, officials are unconvinced a higher discount rate would attract and retain enough additional migrants (who otherwise would not have migrated or stayed) to justify the cost of tax competition. To the extent an individual is very tax sensitive, it can be argued that a 50% discount rate would be insufficient when compared to the 16.7% tax rate in Canada, or the 0% tax rate available in Singapore.

14 Further, while stakeholders often argue that New Zealand needs to be comparable to the US top capital gains tax rate (20%), officials note that headline tax rates rarely tell the full story. In the US, a 3.8% net investment income tax applies on top of the federal capital gains tax, and state taxes can range from 0% to 14.4%. Once those additional taxes have been included, the top tax rate for a US taxpayer can range from 23.8% to 38.2%. In light of this, officials consider the proposed 27.3% effective tax rate is reasonably comparable.

Exit tax

15 An "exit tax" is a common integrity measure that is seen in most foreign tax regimes where gains and losses of assets are taxed on a realisation basis. Despite the nomenclature, it is not an additional tax – it is merely a deemed disposal rule to prevent people from avoiding paying taxes by simply leaving the country and taking the asset out of that country's tax base.

16 Not having an exit tax would reduce the integrity of the proposal and would incentivise migrants to leave New Zealand before selling their appreciated foreign shares. This is contrary to the policy intent of the reform to attract and retain them. Officials note that the concept of an "exit tax" is not new in New Zealand as the current rules already deem a disposal of foreign shares under the FIF rules when a person leaves New Zealand, and we have similar rules in our financial arrangement and corporate migration regimes.

17 Based on our engagement with stakeholders, officials understand that the main concerns stakeholders have regarding the proposal are that it would be a deterrent to individuals' migration decision, especially when compared to other countries like Australia, and that taxes paid in New Zealand would not give rise to a foreign tax credit in the US.

18 Australia has an exit tax where a migrant is deemed to have sold for market value any taxable assets they hold with some exemptions. They have the option to defer the tax liability until death or realisation. Most of Europe also adopts exit taxes, though the form varies between jurisdictions. For example, Germany deems a disposal but allows for the tax liability to be paid over seven annual instalments. France also deems a disposal but allows the deferral of the tax payment until actual realisation if the person moves to a qualifying country. The US also has an exit tax that is targeted towards high-net-worth migrants and triggers when the person renounces their citizenship.

19 The current proposal deems a disposal of foreign shares when a person leaves New Zealand, but the income is suspended until the share is sold. If the share is not sold within three years of leaving New Zealand, the deemed disposal is reversed and there is no tax to pay. The proposal was designed to focus on abuse cases and is comparatively more friendly than Australia's exit tax.

20 Given the ubiquity of exit taxes around the world, it is difficult to understand why stakeholders think the New Zealand proposal would be a deterrent for foreign migrants. Further, officials have not heard of other jurisdictions having foreign tax credit issues with their exit tax.

Further work on providing clarification

21 Officials have been engaging with stakeholders and have heard their concerns that the RAM proposal may not give rise to a foreign tax credit in the US. Work is underway to engage with the US Treasury under the mutual agreement procedure to clarify whether they see any issues with the proposal that might prevent a foreign tax credit claim in the US. However, the speed at which this work progresses will depend on the resourcing and prioritisation of the US Treasury.

22 As discussed above, given the ubiquity of the exit taxes around the world, officials see no reason why the introduction of the exit tax should be deferred until the conclusion of our engagement with the US Treasury.

Update on a possible second phase of reforms

23 Inland Revenue is working on further reforms to the FIF rules. A package of changes will be put together for Budget Ministers and Cabinet to consider as part of Budget 2026. If approved, these further changes would be introduced in August or September this year as part of the next annual rates tax Bill, to be passed before the end of March 2027.

24 Although the objective to remove tax barriers to migrants coming to New Zealand remains, a key focus of this second phase of FIF reforms is on the retention of homegrown talent. One area of reform that we are considering is the expansion of RAM, including the discounted rate and the exit tax, so it would be available to all New Zealand tax residents.

25 This second phase of work is progressing under Budget secrecy, however work on the expansion of RAM has already been communicated to the public as part of the communication strategy during the first phase of reforms.

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **Financial arrangements rules – options to support new migrants**

Date:	11 November 2025	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2025/431

Action sought

	Action sought	**Deadline**
Minister of Revenue	**Agree** to recommendations **Refer** to the Minister of Finance	25 November 2025

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**	**Suggested first contact**
Fiona Wellgreen	Principal Policy Advisor, Policy Inland Revenue	s 9(2)(a)	☐
Dan Doughty	Senior Policy Advisor, Policy Inland Revenue		☒

Financial arrangements rules – options to support new migrants

Purpose

1. This report provides an overview of how the financial arrangements (FA) rules may be creating barriers that prevent some highly skilled individuals from immigrating to New Zealand, and discusses options to reduce these barriers.

2. We seek your approval to progress policy options targeting specific issues identified by officials, including those proactively raised with us by stakeholders. Alternatively, we seek your decision to expand the scope of this project to allow for a more fundamental review of the FA rules.

Executive summary

3. In March of this year, Cabinet commissioned advice on how to lower tax barriers to attract highly skilled migrants. The FA rules have been identified by stakeholders as imposing disproportionately high costs on migrants. As a result, you included targeted changes to the FA rules on the refreshed Tax and Social Policy Work Programme – announced on 29 October.

4. Work to-date (including limited conversations with stakeholders) has identified that the FA rules are highly complex when applied to arrangements (such as, loans, bonds) denominated in foreign currencies. Migrants are more likely to be party to these types of arrangements. The rules can also result in unrealised gains on these arrangements being subject to tax.

5. Our initial view is that low-cost, bespoke policy solutions could be implemented to mitigate the issues caused by foreign currency arrangements. However, given the complexity of the FA rules, we need to consult more widely with stakeholders to:

    - confirm that the proposed solutions would not result in unforeseen issues when applied in practice, and
    - ensure that any other areas of the FA rules that are imposing disproportionately high costs on migrants are identified and included in this review.

6. We recommend that you approve Inland Revenue undertaking targeted consultation on the proposed policy options in this report. Following consultation, Officials will report back to you in early 2026 with updated policy proposals. This report only covers the issues we have identified to date so we expect that consultation will raise further low-cost, bespoke solutions, which we will also include in further reporting.

7. We note that stakeholders have also raised broader concerns with the application of the FA rules (not limited to the effect on new migrants). It is likely that stakeholders will advocate for a more fundamental review of the FA rules as part of our consultation to resolve these broader concerns.

8. A broader review of the FA rules is not within the current scope of this project. Given the likely fiscal costs and resourcing requirements we would not recommend expanding the scope of this project to accommodate such a review. Instead, we recommend a focus on targeted changes that will have a tangible benefit for taxpayers and can be progressed quickly.

Problem definition and project scope

9. The Government is seeking to incentivise more highly skilled individuals to migrate to New Zealand to support its economic strategy. To achieve that objective, Cabinet has commissioned advice on options to address tax barriers to attracting and retaining these migrants (CAB-25-MIN-0061 refers).

10. The FA rules impose disproportionately high costs on migrants (relative to non-migrants). This unequal treatment may be disincentivising some migrants with FAs from moving to New Zealand. The scope of this policy project is therefore to identify which aspects of the FA rules are causing these disproportionate costs, and to provide policy options that equalise the outcomes for migrants with the outcomes for non-migrants.

11. The FA rules are also an inherently complex area of law that impose high costs on anyone who must comply with them. The rules will likely still disincentivise some migrants even if their treatment is made the same as non-migrants. Addressing the concerns of these migrants (and of stakeholders more generally) would require a fundamental review of current settings, which is not within the proposed scope of the project. We discuss expanding the scope of the project below.

Overview of FA rules

12. The FA rules apply to any arrangement when a person provides another person with money with the expectation of repayment (with or without interest) at some point in the future. The purpose of the rules is to prevent taxpayers using these arrangements to shift taxable income into future years, while bringing forward deductions, that is, functionally deferring tax payments.

13. To achieve that purpose, the FA rules require parties to an FA to recognise income and expenses over the duration of the arrangement:

    - **During an FA** – parties are required to use spreading rules to apportion income and expenses over the duration of the arrangement. Importantly, these rules account for income on an accrual basis and not on cashflow (like most New Zealand tax rules).

    - **At the end of an FA** – parties are required to complete a base price adjustment when the FA ends (that is, when the arrangement is repaid in full, has matured, or is otherwise disposed of). A base price adjustment is functionally a "wash up" calculation, where any income and expenses not accounted for under the spreading rules is brought to account.

14. The legislative definition of an FA is very broad, and intentionally captures many common arrangements such as bank accounts, mortgages, and investments in bonds. A narrow subset of arrangements is then carved out from the FA rules altogether (arrangements that do not need to use the spreading rules or complete a base price adjustment), referred to as excepted financial arrangements. Common examples include shares and superannuation schemes.

15. Despite most taxpayers being party to one or more arrangements that are captured by the FA rules, very few natural persons ever interact with the rules for two main reasons:

    - To reduce compliance costs, the cash basis person rules allow any eligible taxpayers to account for FA income and expenses on a realisation basis (they can ignore the spreading rules). A person will be a cash basis person if the value or income of their FAs is below certain thresholds during the year (discussed below). Most individuals will not breach these thresholds.

- Despite technically being required to complete a base price adjustment calculation (even as a cash basis person), many arrangements will not have income or expenses to "wash up".

16. As a result, only high-wealth individuals with sophisticated investments will generally be required to apply all aspects of the FA rules. This is intentional because, generally, it is only more complex FAs that carry the material integrity risks that justify the costs imposed by the rules. The key concerns with the application of the rules are:

    - ***High compliance costs*** – the FA rules are highly complex and contained in both primary and secondary legislation. Most taxpayers are largely unaware of these rules and the complexity involved in applying them. Taxpayers who must deal with these rules will generally require specialist advice to remain compliant.

    - ***Tax on unrealised income –*** the FA rules operate on an accruals basis, so many taxpayers will incur tax on unrealised income. This can cause liquidity issues when realised income is significantly different from accrued income.

Core issue – interaction between FA rules and foreign currencies

17. Fundamentally, FAs are intangible financial assets and liabilities, which therefore have a value. The various components of the FA rules operate by assessing the value of the FAs each year and treating changes in value as either income or expenditure. Importantly, the rules assess those values in New Zealand dollars.

18. When a taxpayer is party to an FA denominated in a foreign currency, the FA rules become materially more complex, attracting both high compliance costs and taxing unrealised income. Because migrants are more likely to have FAs denominated in foreign currencies, they are disproportionately more exposed to these issues.

19. The rules will always need to account for exchange rate movements to some degree. However, officials have identified three main areas where it is being overemphasised, resulting in higher than intended compliance and tax costs.

Interaction between foreign currencies and cash basis person rules

20. As discussed above, a cash basis person is not required to use the spreading rules. A taxpayer is considered a cash basis person if they are below either of the following thresholds (in New Zealand dollars):[1]

    - the person does not have FAs with a total value of more than $2 million on any day in the income year (the "absolute value threshold"), or

    - the person does not have accrued income of more than $200,000 across all their FAs for the income year (the "accrued value threshold"), and

    - if below either of the first two thresholds, the person must also not have a difference in their accrued and realised income of more than $100,000 (called "the deferral threshold").

21. Under the current law, a taxpayer is required to revalue their FAs daily to determine whether they meet these thresholds, and therefore whether they are required to use the spreading rules for the income year (and incur the high associated costs).

22. These revaluations cause issues for migrants because they must account for the effect of exchange rate movements. This can cause some migrants to breach the

[1] The thresholds reported here are the updated thresholds proposed in the Taxation (Annual Rates for 2025−26, Compliance Simplification, and Remedial Measures) Bill. The thresholds contained in current legislation are generally half the thresholds reported here.

relatively low deferral threshold, which requires that they then use the spreading rules (and incur the associated costs).

Issues with spreading rules and foreign transaction accounts

23. When a taxpayer has an FA denominated in a foreign currency they must use special spreading rules. For many FAs, any foreign exchange gains or losses can be deferred until a base price adjustment calculation is completed. However, if the FA has an unpredictable cashflow, these gains and losses must instead be recognised annually.

24. This is a particular issue for migrants with foreign private transaction accounts because their private transactions force them to pay tax on unrealised foreign exchange gains annually, but do not always allow for the taxpayer to recognise any foreign exchange losses.

25. Stakeholders have raised concerns with this inconsistent treatment causing different treatment year-to-year on the same foreign FAs, without the ability to offset previous non-deductible unrealised losses against their current taxable unrealised gains.

FA rules and investor visa requirements

26. Migrants who apply for certain visas (such as the Active Investor Plus visa) are required to make investments into New Zealand to meet visa eligibility requirements. Many of these investments (particularly bonds) will be FAs, and once these investors become New Zealand tax residents they will need to apply the FA rules.

27. Unlike their foreign FAs (which are excluded under the transitional residency rules), these FAs will have a New Zealand source and so are subject to the FA rules from the date of their arrival into the country. Importantly, the FA rules will require that these investors revalue the FAs they acquired for visa-eligibility purposes at the date they became subject to the rules.

28. This causes an issue when changes in exchange rates can result in taxable unrealised gains from the date the investor arrives in New Zealand. Stakeholders report that this interaction is undermining the attractiveness of the Active Investor Plus and other visa categories.

Foreign tax credits for United States migrants

29. Separate from the foreign exchange related issues, officials have also heard anecdotal evidence that some US migrants are being denied foreign tax credits by US tax authorities on their FA income. This is an issue that arises under foreign rules, so we do not have the necessary expertise to comment on this problem at this stage. We intend to undertake further consultation and will provide recommendations at the next stage of this project.

Immediately actionable policy options

30. Separate from this report, officials will shortly seek your agreement on recommendations to the Finance and Expenditure Committee on amendments to the Taxation (Annual Rates for 2025−26, Compliance Simplification, and Remedial Measures) Bill. As part of that report, we intend to recommend two changes to the cash basis person threshold proposals contained in that Bill:

- ***Remove the deferral threshold altogether:*** The Bill currently proposes to lift the deferral threshold from $40,000 to $100,000. Policy work subsequent to the introduction of the Bill has convinced officials that the deferred income captured by the threshold is already brought to tax by the base price adjustment rules,

and so its removal is warranted given low integrity risks and the issues it causes with many modern FAs.

- ***Have the absolute value threshold ignore foreign exchange movements:*** Officials will recommend that the absolute value threshold ignores foreign exchange movements year-to-year. This would prevent exchange movements from causing alternating treatment of the same FA between income years based solely on those movements.

31. Together, we expect these changes will prevent most migrants from losing cash basis person status solely because they hold foreign currency denominated FAs. This will materially reduce both their compliance costs and tax payable on unrealised gains. These changes would also address some of the specific concerns raised with you on the FA rules at the public launch of the Tax and Social Policy Work Programme on 29 October 2025.

32. If progressed, these changes would be effective from 1 April 2026 and could be announced early 2026 when the Taxation (Annual Rates for 2025−26, Compliance Simplification, and Remedial Measures) Bill is reported back to the Committee of the Whole House. These proposals can be progressed without further consultation, and independently of your decision on the options below.

Further policy options to address remaining issues

33. Officials have developed several policy options that would mitigate the specific issues identified above. We intend to consult on these issues with stakeholders if this project is progressed. We also expect that consultation will identify further low-cost, bespoke policy options.

Except private foreign currency transaction accounts from FA rules

34. The excepted FA rules currently except loans in foreign currencies that have a private or domestic purpose (that is, mortgages for overseas homes, personal cars, etc). We propose that the same treatment be extended to foreign private transaction accounts. This will prevent the inconsistent treatment of foreign exchange gains and losses discussed above.

Loosen requirements for foreign currency private loans to qualify as excepted FAs

35. The current rules that except private loans in foreign currencies also require that the borrower be considered a cash basis person for the loan to qualify. We recommend removing this requirement because we do not believe that private loans pose a material integrity risk, and the current settings are exposing taxpayers to tax on unrealised gains on their mortgage debt (when gains in the foreign currency mean the New Zealand dollar value of the debt has decreased).

Ignore foreign exchange movements for certain foreign on-call credit accounts

36. The FA rules also except variable principal debt instruments (on-call credit accounts) if the credit limit does not exceed $100,000 in the income year. However, that limit is calculated in New Zealand dollar, which means it is also exposed to issues with changes in foreign exchange rates.

37. We recommend that this threshold also ignore foreign exchange movements to prevent taxation of unrealised foreign exchange gains on these debt instruments (when foreign exchange movements decrease the New Zealand dollar value of the balance of a foreign on-call credit account).

Fiscal costs associated with policy proposals

38. We have not costed these proposals at this stage because we cannot confirm whether further changes may be required post-consultation. However, our initial view is that these options would all have an unquantifiable impact that could be either a net gain or loss to the Crown. In situations such as this, Inland Revenue will generally forecast a nil fiscal impact.

Broader issue in meeting Ministers' stated objectives

39. The policy options outlined above will limit instances when the compliance and tax costs resulting from the FA rules are disproportionately imposed on migrants. However, particularly high-wealth migrants will still be exposed to the FA rules (and their associated costs) in the same way that high-wealth non-migrants are.

40. To the extent that those individuals are disincentivised by the costs of the FA rules generally, these policy options may not fully meet Ministers' objectives for attracting highly skilled migrants. Meeting that broader objective would require a more fundamental review of the FA rules.

Fundamental review of FA rules

41. The FA rules were designed over 30 years ago, and it is unclear if the integrity risks that motivated design decisions then are still as prevalent today given changes in commercial practice and the wider legislative landscape since then. Fundamentally reviewing the FA rules could potentially lower costs for all taxpayers with FAs,[2] while preserving the integrity of the tax system.

42. For example, we understand that the Australian equivalent of the FA rules generally exempts natural persons from the application of the rules, with different mechanisms for ensuring the integrity of the Australian tax system. New Zealand could consider a similar regime, but we expect doing so would require extensive policy work.

43. We do not believe that this work could be completed within this Parliamentary term, and that beginning this work would require reprioritising policy resources away from other projects in the meantime. Given the uncertain fiscal costs involved, and your broader legislative priorities, we would not recommend commissioning this work at this time.

Consultation

44. The Treasury was consulted on the contents of this report and agrees with Inland Revenue's recommendations.

Next steps

45. Officials can meet with you to discuss the contents of this report.

46. We recommend that you agree to officials conducting targeted consultation on the specific policy options recommended above during November and December 2025. We expect that we would complete this consultation in late 2025 or early 2026. Following consultation, we would report to you with final policy recommendations in February or March 2026.

[2] For example, we are aware of broader concerns with applying the FA rules to modern financial assets.

Recommendations

We recommend that you:

1. **Note** that officials will separately report to you on changes to the cash basis person thresholds as part of the Taxation (Annual Rates for 2025−26, Compliance Simplification, and Remedial Measures) Bill, and that officials support those changes as an immediate policy response to the issues noted in this report.

   Noted

2. **Agree** to allow officials to conduct targeted consultation on the specific policy options discussed in this report. Following consultation, we will report back to you in early 2026 with final policy recommendations.

   Agreed/Not agreed

3. **Agree** that the scope of this project on financial arrangements is limited to the specific policy options in this report, and not to a general review of the financial arrangements rules.

   Agreed/Not agreed

4. **Refer** a copy of this report to the Minister of Finance for her information.

   Referred

s 9(2)(a)

Fiona Wellgreen
Principal Policy Advisor
Policy

Hon Simon Watts
Minister of Revenue
/ /2025

Tax policy report

Inland Revenue
Te Tari Taake

Financial arrangements rules – decisions on migrant-specific proposals following consultation

Date	31 March 2026	**Priority**	Medium
Security level	Budget Sensitive	**Report number**	IR2026/053

Action sought		**Deadline**
Minister of Finance	**Agree** to recommendations	21 April 2026
Minister of Revenue	**Agree** to recommendations	21 April 2026

Purpose

This report relates to the Tax and Social Policy Work Programme workstream: *Review the impact of the financial arrangements rules on new migrants*. The report:

- provides an update on stakeholder feedback from our recent consultation, and
- seeks Ministers' decisions on which policy proposals to progress.

Contact for phone discussion, if required

Name	**Position**	**Phone number**	**First contact**
Fiona Wellgreen	Principal Policy Advisor, Inland Revenue	s 9(2)(a)	☐
Dan Doughty	Senior Policy Advisor, Inland Revenue		✓

Financial arrangements rules – decisions on migrant-specific proposals following consultation

Executive summary

1 The Government seeks to lift economic productivity and living standards by ensuring New Zealand businesses can attract and retain highly skilled talent, including offshore talent. Stakeholders report that the financial arrangement rules act as a barrier to accessing this talent. This is because the rules capture volatile (and unrealised) exchange rate movements when applied to foreign currency arrangements, resulting in high compliance costs and cashflow uncertainty.

2 We previously reported to you (IR2025/431 refers) on **four** targeted policy proposals (relating to common private arrangements and certain investor visas) and sought permission to consult with stakeholders. Stakeholders supported the proposals, but encouraged us to consider a more comprehensive solution to issues with foreign currency arrangements that were affecting all taxpayers.

3 Following this feedback, we now recommend progressing an expanded package of **six** proposals. This package includes updated versions of the targeted proposals we previously reported on, but also includes two more comprehensive reforms:

- an elected functional currency rule that would allow individuals to calculate income from foreign-currency financial arrangements in a foreign currency, and
- extend cash-basis treatment to United States (US) migrants to limit double taxation issues caused by unique interactions between US and New Zealand tax rules.

4 We recommend progressing the full package in the 2026–27 annual rates taxation Bill, noting it could be announced at Budget 2026. The total estimated fiscal cost is low at $2.06 million over forecast, which could be managed within the Tax Policy Scorecard.

5 Despite the modest fiscal impact, the proposals are expected to have a meaningful impact for migrants and other taxpayers because the changes would materially reduce both compliance costs and cashflow uncertainty.

Background

6 As part of the Government's focus on attracting and retaining highly skilled migrants, a review of the impact of the financial arrangements rules on migrants was included on the current Tax and Social Policy Work Programme. Stakeholders identified these rules for review as part of work on the related project on the foreign investment fund rules.

7 In November 2025, we reported to the Minister of Revenue on situations when the financial arrangements rules may be imposing disproportionately high costs on migrants and potential solutions (IR2025/431 refers).

8 Between December 2025 and February 2026, we undertook targeted consultation with a small group of tax practitioners with relevant experience in the financial arrangements rules. We sought views on the problem as we understood it, and the four targeted policy changes we were considering. This report follows that consultation and updates you on our recommendations post stakeholder feedback.

Relationship to foreign investment fund rules project

9 In November 2025, you received advice on another barrier to highly skilled migrants, the foreign investment fund rules (IR2025/405 refers). You recently agreed to consider a package of changes to those rules as part of Budget 2026. While both projects target migrants, these packages do not overlap and could be introduced independently of one another. However, you may wish to consider both together as part of a larger offshore talent attraction-and-retention package for Budget 2026.

Refresher on financial arrangements rules

10 The financial arrangements rules apply to any arrangement when persons exchange money with the expectation of repayment (with or without interest) in the future. The rules account for income on an accrual basis. This is different from most New Zealand tax rules, which operate on a cash basis. This is to prevent taxpayers using these arrangements to shift taxable income into future years, while bringing forward deductions (artificially deferring tax payments).

11 The legislative definition of a financial arrangement is very broad, and intentionally captures many common arrangements such as bank accounts, mortgages, and bonds. A narrow subset of arrangements (excepted financial arrangements) are then carved out from the rules altogether; either because other rules cover those arrangements (such as in the case of shares) or when the arrangement carries a low integrity risk.

12 When the financial arrangements rules apply, a party to a financial arrangement is required to comply with two main components of the rules:

- **During the financial arrangement** – parties to a financial arrangement are required to use a spreading method to apportion income and expenses over the duration of the arrangement. Because the spreading rules are highly complex, many individual taxpayers are treated as "cash basis persons" and excluded from the requirement to apply a spreading method (and can instead recognise income and expenses on a cash basis).
- **At the end of the financial arrangement** – parties are required to complete a base price adjustment when the financial arrangement is repaid in full, has matured, or is otherwise disposed of. This is essentially a wash-up calculation of any income and expenses not previously accounted for by the spreading rules.

Problem definition following consultation

13 In our previous report we stated the main barrier to attracting and retaining migrants was that the financial arrangements rules taxed unrealised gains on foreign currency arrangements. We understood that this frustrated migrants who were not subject to this treatment in their home jurisdiction. We therefore recommended options that would stop the taxation of unrealised gains for common arrangements (for example, bank accounts, mortgages, credit cards, and investments made for visa eligibility).

14 However, during consultation, stakeholders emphasised that the real problem was that the rules capture both unrealised gains **and** losses on foreign currency arrangements. They reported relatively modest movements in exchange rates can result in significant but unpredictable tax outcomes, with large tax payments due one year and then large deductible expenses available the next.

15 Practically, this means taxpayers (both migrants and non-migrants) have low certainty over cashflow from their foreign investments and must incur relatively large costs to manage that uncertainty. Meanwhile, the Crown collects minimal revenue because (in aggregate) taxpayers are incurring a roughly equal amount of taxable gains and deductible losses each year.

16 Therefore, while stakeholders agreed that our original proposals would resolve issues for common arrangements, they noted issues would remain for all other foreign currency arrangements (particularly for US migrants). Various stakeholders recommended we consider more comprehensive solutions that would address issues for all foreign currency arrangements.

17 Following this feedback, we investigated more comprehensive solutions and developed two new proposals (discussed below). We believe these new proposals would meaningfully address the concerns raised by stakeholders, and better support your objectives. For completeness, we still recommend our original proposals progress alongside these new proposals (for the reasons discussed below).

New proposals recommended following consultation

18 The proposals discussed below were developed following consultation and have not been discussed with stakeholders yet. If you agree to progress these proposals, we recommend you permit us to re-engage with stakeholders on the updated package of proposals. The main point of further consultation would be to test the detailed design of these new rules, and to troubleshoot any issues before potential introduction in the 2026–27 annual rates taxation Bill.

Proposal 1: Elected functional currency rule

19 Under the status quo, taxpayers must convert the value of their foreign currency arrangements to New Zealand dollars when applying the spreading rules. Because exchange rates shift year-to-year, the spreading rules revalue these arrangements and capture the resulting unrealised gain or loss. This then leads to uncertainty because taxpayers cannot predict exchange rate movements in advance.

20 We propose introducing an elected functional currency rule to resolve this issue. This would permit natural person taxpayers to elect to use a single foreign currency when applying the spreading rules to foreign currency arrangements. This would ensure only net income or expenditure is converted to New Zealand dollars (not the value of the arrangement). This would then prevent the rules from capturing unrealised gains and losses resulting from exchange rate movements each year.

21 An elected functional currency rule would be taxpayer friendly, resulting in taxpayers having more predictable annual tax consequences on their foreign currency financial arrangements. This would materially reduce compliance costs for all natural person taxpayers with foreign currency financial arrangements, with a particular benefit for migrants who generally have more of these arrangements.

22 We recommend you progress an elected functional currency rule for introduction in the 2026–27 annual rates taxation Bill.

Stakeholders' views

23 Various stakeholders (including CA ANZ, Deloitte, and PwC) expressed that an elected functional currency rule would be the single most effective change you could make to the financial arrangements rules for migrants generally (and highly skilled migrants specifically). They emphasised this would largely resolve frustrations with the uncertainty caused by the rules at status quo.

Risks associated with proposal

24 s 9(2)(g)(i)

Proposal 2: Cash basis person extension for US migrants

25 Uniquely, US citizens are subject to tax by virtue of their citizenship regardless of where they reside. This means these taxpayers are reliant on New Zealand's Double Tax Agreement with the US for relief from taxation in both jurisdictions. However, that agreement only extends relief when both jurisdictions recognise the same basis of taxation, and the US does not always recognise the accruals basis of the financial arrangements rules.

26 We propose extending the cash basis person treatment to any individuals taxed on a citizenship basis (US migrants). This would allow those taxpayers to pay tax on foreign-source financial arrangement income when it is realised (not when it is accrued). We note this proposal would only relieve US migrants from the requirement to apply a spreading method, and not from the requirement to calculate and pay any tax owing at the end of the financial arrangement.

27 This proposal would be taxpayer friendly, but only for US migrants. These taxpayers would be relieved from the broader costs imposed by the financial arrangements rules not otherwise discussed in this report (generally high levels of complexity and compliance costs).

28 We recommend you progress the cash basis person extension for US migrants for introduction in the 2026–27 annual rates taxation Bill.

Stakeholders' views

29 Stakeholders have repeatedly raised the accrual basis of the financial arrangements rules as a major barrier to US migrants, given the double tax implications it carries for these individuals. While we have not tested this specific proposal with stakeholders, we believe it resolves their core concerns and would likely be supported.

Risks associated with proposal

30 This proposal largely replicates the foreign investment fund "revenue account method" rules recently introduced for US migrants. While stakeholders were supportive of those rules, they also led to calls for broader rules that apply to all taxpayers. It is likely that stakeholders will react the same way to this proposal and may seek either broader exemptions for other migrants, or a broader review of the financial arrangements rules. We discuss our views on a broader review later in this report.

31 s 9(2)(g)(i)

Updated proposals from previous report

32 As noted above, we still recommend you progress the targeted policy options discussed in our previous report for introduction in the 2026–27 annual rates taxation Bill:

- **Proposal 3: Except private foreign currency transaction accounts from the financial arrangements rules.** Under the current law, loans in foreign currencies that have a private or domestic purpose are an excepted financial arrangement. We recommend the same treatment be extended to foreign private transaction accounts (such as personal bank accounts).
- **Proposal 4: Loosen requirements for foreign currency private loans to qualify as excepted financial arrangements.** Under the current law, private loans in foreign currencies only qualify as an excepted financial arrangement if the borrower is a cash basis person. We recommend removing this requirement to exclude all foreign private loans from the financial arrangements rules.
- **Proposal 5: Ignore foreign exchange movements for certain foreign on-call credit accounts.** A variable principal debt instrument (on-call credit accounts like a credit card) are excepted financial arrangements if the credit limit does not exceed NZ$100,000 each year. We recommend this rule be amended to allow taxpayers to ignore any exchange rate movements when calculating this amount.
- **Proposal 6: Introduce special rules for financial arrangements acquired for the purpose of meeting visa requirements.** Migrants who acquire a New Zealand-sourced financial arrangement to qualify for certain visas (such as the Active Investor Plus visa) must revalue those arrangements on the date they arrive in New Zealand. We propose specific rules to prevent this, improving the attractiveness of these visas. We recommend this proposal should be backdated to the introduction of the Active Investor Plus visa (1 April 2025).

33 We note stakeholders were supportive of all these proposals, even if more holistic options were progressed. Stakeholders noted that these were common pain points for migrants, particularly less wealthy migrants who did not know they had to comply with the financial arrangements rules for these relatively common offshore arrangements.

Financial implications

Tax revenue impact

34 The total tax revenue impact of the proposed package is $2.060 million over the forecast period. This is made up of the following:

- **Proposal 1:** Our costing process assumes equal "up and down" future exchange rate movements that would lead to gains and losses, meaning this proposal carries a nil impact because it would eliminate both unrealised gains and losses.
- **Proposal 2:** We estimate the fiscal cost of this proposal at $1.260 million over the forecast period. The relatively low fiscal cost is due to US migrants holding a relatively small proportion of foreign arrangements, and the fact that the proposal only defers taxation (with some deferred income realised each year over forecast).
- **Proposals 3 to 5:** We estimate the fiscal cost of these three proposals collectively as $0.800 million over the forecast period.
- **Proposal 6:** This proposal would not carry a fiscal impact because we estimate these rules would eliminate an equal number of pre-arrival gains and losses.

35 This is summarised in the following table:

	$m - increase/(decrease)					
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total**
Crown Revenue and Receipts:						
Tax Revenue – Other Persons						
Cash basis person extension for US migrants (proposal 6)	-	(0.500)	(0.380)	(0.250)	(0.130)	(1.260)
Proposals 1 to 3	-	(0.200)	(0.200)	(0.200)	(0.200)	(0.800)
Total Operating	**-**	**0.700**	**0.580**	**0.450**	**0.330**	**2.060**

36 We note the fiscal cost of the proposed package is relatively low and could be managed against the Tax Policy Scorecard, subject to decisions on other proposed Tax and Social Policy Work Programme initiatives.

Administrative impact

37 Based on the proposed policy and design decisions for the package we estimate the one-off implementation cost to be $0.100 million. This cost is based on content updates and no system changes. Inland Revenue would manage this cost as part of its annual content updates process.

Views on broader review of financial arrangements rules

38 Regardless of the decisions you make on the proposals in this report, we expect stakeholders will call for a broader review of the financial arrangements rules. These rules have not been comprehensively reviewed since they were introduced over 30 years ago, and we are aware of a range of issues beyond those relevant to this report. Stakeholders regularly raise these concerns with officials, and we expect some of the proposals contained in this report will intensify calls for a broader review.

39 We believe there may be merit in a broader review of the rules, and that this may support your broader economic objectives. However, the financial arrangements rules are highly complex, and a broad review would require significant resource investment. Delivering on that review would require reprioritisation of current Policy resources, which would require trade-offs with your broader work programme. As a result, we would not recommend a review at this time.

Consultation

40 In December 2026, we invited 16 stakeholders with relevant expertise in, and/or clients affected by, the specific financial arrangements proposals discussed in this report. We also invited stakeholders to share our proposals with their clients and professional network, and noted we would accept submissions from these third-party stakeholders.

41 Consultation closed in February 2026, and we received submissions from seven of the stakeholders we reached out to (PwC, Deloitte, EY, KPMG, CA ANZ, Patterson Legal, Buddle Findlay). Those stakeholders provided unanimously positive and constructive feedback, which has contributed to the design of the proposals provided in this report.

Treasury comment

42 The Treasury supports the recommendations outlined in this report. However, it acknowledges certain proposals may present integrity risks. To address these concerns, the Treasury recommends Inland Revenue actively monitor the implementation and outcomes of the proposals and promptly report back to Ministers should any issues or unintended consequences arise.

Next steps

43 If you choose to progress the proposals, we recommend they be included in the 2026–27 annual rates taxation Bill (scheduled for September 2026). This would allow us time to consult on the design of the proposals with stakeholders and prepare legislative drafting. Further consultation will be conducted with the previous targeted group of stakeholders on an informal but closed basis. We note that introducing the proposals as part of the 2026–27 annual rates taxation Bill would not prevent you announcing them as part of Budget 2026.

Recommendations

We recommend you:

1. Agree to progress the following proposals in the 2026–27 annual rates taxation Bill.

Proposal	Minister of Finance	Minister of Revenue
Except private foreign currency transaction accounts	Yes / No	Yes / No
Loosen requirements for foreign currency private loans to qualify as excepted financial arrangements	Yes / No	Yes / No
Ignore foreign exchange movements for foreign credit accounts	Yes / No	Yes / No
Introduce special rules for financial arrangements acquired for purpose of meeting visa requirements	Yes / No	Yes / No
Elected functional currency rule	Yes / No	Yes / No
Cash basis person extension for US migrants	Yes / No	Yes / No

Agree / Disagree — Agree / Disagree

Minister of Finance — *Minister of Revenue*

2. Note the following fiscal changes if you decide to progress all of the decisions in recommendation 1 above, with a corresponding total impact on the operating balance and net core Crown debt.

	$m - increase/(decrease)				
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Crown Revenue and Receipts:					
Tax Revenue – Other Persons	-	(0.700)	(0.580)	(0.450)	(0.330)
Total Operating	**-**	**0.700**	**0.580**	**0.450**	**0.330**

3. Note that if you decide to only progress some of the decisions in recommendation 1 above officials will report back with an updated fiscal impact.

4. Either:

a. **Agree** to manage the tax revenue decrease (fiscal cost) of recommendation 1 against the Tax Policy Scorecard.

Agree / Disagree — Agree / Disagree

Minister of Finance — *Minister of Revenue*

or

b. **Agree** to manage the tax revenue decrease (fiscal cost) of recommendation 1 through the 2026 Budget operating allowance.

Agree / Disagree — Agree / Disagree

Minister of Finance — *Minister of Revenue*

5. Agree to Inland Revenue conducting additional consultation on the detailed design of the proposals you have agreed to progress.

Agree / Disagree

Minister of Revenue

s 9(2)(a)

Fiona Wellgreen
Principal Policy Advisor
Policy | Inland Revenue

Hon Nicola Willis
Minister of Finance
/ /2026

Hon Simon Watts
Minister of Revenue
/ /2026

Tax policy report

Inland Revenue
Te Tari Taake

Targeted consultation outcomes on proposals to modernise and simplify non-resident contractors' tax

Date	9 March 2026	**Priority**	Medium
Security level	Budget sensitive	**Report number**	IR2026/026

Action sought		**Deadline**
Minister of Finance	**Agree** to recommendations	20 March 2026
Minister of Revenue	**Agree** to recommendations	20 March 2026

Purpose

This report:

1 informs Ministers of the outcome of targeted consultation on potential changes to non-resident contractors' tax; and

2 seeks confirmation from Ministers of their preferred package of changes to non-resident contractors' tax for inclusion in Budget 2026, subject to confirmation by Budget Ministers and Cabinet.

Contact for phone discussion, if required

Name	**Position**	**Phone number**	**First contact**
Pamela Law	Principal Policy Advisor	s 9(2)(a)	✓
Portia De Forest	Policy Advisor		☐

Targeted consultation outcomes on proposals to modernise and simplify non-resident contractors' tax

Executive summary

1 This report informs Ministers of stakeholders' views on proposed measures to modernise and simplify non-resident contractors' tax (NRCT).

2 The report also seeks Ministers' agreement to a preferred change/package of changes, subject to confirmation by Budget Ministers and Cabinet. This workstream is incorporated within the submitted Budget 2026 Tax and Social Policy Work Programme placeholder initiative.

3 Overall, the proposals to change four tax settings were supported by submitters, although one submitter advocated for fundamental changes to the NRCT regime.

4 Officials recommend that changes are made to all four settings consulted on, estimated at a cost of $3 million per year. Officials' recommended changes are to:

- Increase the de minimis monetary threshold from $15k to $60k (decreasing compliance costs).
- Implement a "single-payer view" of the monetary and de minimis thresholds, supported by clarifying the information retention requirement (increasing certainty of tax treatment). However, if Minister prefer to undertake more fundamental changes to NRCT, information requirements could be deferred.
- Exclude certain "low risk" non-resident contractors from the ambit of the rules, subject to conditions (decreasing compliance costs).
- Introduce a bespoke NRCT code (improving administration and compliance).

Background

5 Last year, we provided you with initial advice on specific issues arising from the obligation to withhold NRCT and potential options to reduce compliance costs (IR2025/402 refers). The options included consulting on a fundamental review of NRCT, or a limited, targeted consultation on some specific issues. The latter option was selected and formal consultation on the four targeted proposals occurred during November and December 2025.

6 This report also provides you with the costing of officials' preferred package. Should Ministers decide on an alternative package, we have included updated indications of the likely fiscal cost of the different changes. The indications are based on 2025 tax year data and assume no other changes.

7 Separate but relevant to this workstream, we also provided you advice last month on NRCT in the context of aircraft asset leasing (IR2026/001).

Stakeholders' views of the four NRCT measures

8 We received submissions from the Corporate Taxpayers' Group (CTG), Deloitte, the New Zealand Law Society (NZLS), and PwC. They were broadly supportive of the proposed measures but had varying degrees of opposition to the proposed additional reporting requirements associated with implementing a single payer view. The views on each option are covered in the relevant sections below.

9 Submitters also offered suggestions for other changes that would improve the system (see *Additional measures put forward by submitters* below). Notably, the CTG advocated for a wholesale change of approach to the NRCT system.

Increasing the monetary threshold

10 The underlying purpose of the threshold is to balance the tax integrity risk against the compliance and administration costs of withholding.

11 Stakeholders supported increasing the monetary threshold. All supported an increase to $60k, although Deloitte preferred $100k. CTG, NZLS and Deloitte also stated that the threshold should be future-proofed – either through a substantial one-off increase or through regular adjustments. Stakeholders considered that increasing the threshold will reduce the compliance costs and burden of NRCT, especially for the parties of relatively low value contracts, while safeguarding the tax base.

12 Inland Revenue prefers increasing the threshold to $60k. This choice offers a good balance between protection of the tax base and compliance costs. It will reduce compliance costs for payers who fall below the new threshold and who no longer need to withhold NRCT, and future-proof the threshold against inflation growth for some time.

13 Increasing the threshold to $100k would also reduce compliance costs and have a greater future-proofing quality, but would have a greater impact on tax base integrity than a smaller change and would incur a greater fiscal cost.

14 An increase to $30k represents an inflation adjustment. However, that threshold could become outdated within a few years and is not favoured by stakeholders or Inland Revenue.

15 The indicative cost (reduction to revenue) of each option will depend on how much the threshold is increased and whether the single-payer view (below) is also implemented as shown.

Table 1: Indicative fiscal cost of increasing the $15k threshold

Option	**Average annual cost (reduction to revenue)**
Increase to $30k	
Single-payer view implemented	$1.0m
Without single-payer view	$0.9m
Increase to $60k	
Single-payer view implemented	$2.8m
Without single-payer view	$2.6m
Increase to $100k	
Single-payer view implemented	$4.9m
Without single-payer view	$4.6m

Implementing a "single-payer" view

16 Under the single-payer view, when considering whether the monetary or day count threshold exemptions from withholding NRCT are available, a payer would only need to consider their own contractual activities with the contractor in a 12-month period. They would no longer need to consider the contractor's contractual activities with other payers when determining if they need to withhold NRCT.

17 Alongside implementing the single-payer view, officials also consulted on an additional reporting requirement to mitigate the integrity risk posed by implementing this approach. A reporting requirement would allow Inland Revenue visibility of contractors

who enter into multiple short-term or low-value contracts where currently NRCT should be withheld.

18 Stakeholders broadly support implementing a single-payer view as a way to reduce compliance costs, as this change would streamline the process and provide greater certainty to the payer. This is provided it is applied to both the monetary threshold and the 92-day threshold.

19 Stakeholders thought that the proposed additional reporting requirements would result in increased compliance costs for payers. CTG opposes additional reporting requirements on the basis that this is not an appropriate solution to reduce compliance costs and proposes a broader overhaul of the rules as described in paragraphs 35 to 37 below.

20 Deloitte, CTG and PwC believe that minimal information should be required and limited to what is "readily available" to the New Zealand taxpayer. "Readily available" is taken to mean information that can be easily or automatically collated and does not have to be manually compiled from multiple systems. NZLS, Deloitte and CTG all suggested that the non-resident contractors' name and tax identification or IRD number should be in scope of a requirement. Submitters also suggested other potential data points.

21 At present, there are no natural reporting lines within the PAYE system for this additional information to be reported or fully automated for enforcement purposes. As suggested in the January 2026 advice on NRCT and aircraft asset leasing (IR2026/001 refers), reporting could be incorporated into an existing regime (such as the approved issuer levy regime) or a similar solution with a low administrative cost. Nevertheless, sorting the reported information would be largely manual and could involve high administrative costs (given the uncertainty of the population size), particularly relative to the amount of tax at stake.

22 As an alternative, officials propose an information retention requirement, whereby payers would be required to keep sufficient records of their contractual activity with the non-resident contractor and provide proof of these records if required by Inland Revenue. The records would not need to be kept in a particular form or in a single place, so long as the required information could be collated. This would allow Inland Revenue to request the information for compliance and enforcement purposes. It also reflects the reality that NRCT information collected under that system would only be used by Inland Revenue when it wished to audit a particular taxpayer.

23 While New Zealand has a general documentation requirement under its tax laws, we believe it would be beneficial to have specific rules for transactions with non-residents, particularly given the variety of contractual practices and processes. This would provide New Zealand payers with clarity on what they are required to document, and to ensure this information is sufficient for Inland Revenue to carry out audits.

24 Should Ministers wish to progress specific changes in the NRCT regime, we broadly agree the information suggested by stakeholders should be sufficient for documentation purposes. We will confirm the details and approach in a future report.

25 However, if you wished to pursue fundamental change to the regime in the next two to five years (as sought by CTG), we suggest that the specific information retention requirement (outlined above) should not be required, as it would only incur administration and compliance costs for a system that would relatively shortly be superseded.

Excluding low-risk entities from the NRCT regime

26 Stakeholders supported excluding branches, limited partnerships and representative offices from NRCT as a measure to reduce compliance costs. These entities have an enduring presence in New Zealand, so do not present a material flight risk. They are already likely to be meeting their tax obligations. PwC flagged that this option would also better align the rules with existing compliance behaviours.

27 CTG and Deloitte recommended using broader measures as a basis for exclusion, such as excluding entities that have IRD numbers, are registered for GST, and/or are

registered with the Companies Office. Moving to these measures would broaden the scope of the exclusion, which would further reduce compliance costs.

28 In our view, the measures put forward by stakeholders do not of themselves indicate good compliance or low flight risk. We favour exempting certain specified types of taxpayers only – namely branches, limited partnerships and representative offices. As noted above these typically have an enduring connection with New Zealand and do not present a material flight risk.

29 In addition, we think that it would be sensible to also require an indicator of the branch's, limited partnership's or representative office's likely compliance with their New Zealand tax obligations. We presently favour requiring both that the non-resident contractor has an IRD number and is registered with the Companies Office.

30 Although many non-resident contractors may not have an IRD number, the non-residents we recommend excluding are those with a good compliance history in New Zealand. Such contractors will have an IRD number. The Companies Office Registers are publicly available and easy for payers to check. Overseas companies are already required to register with the Companies Office within 10 working days of commencing business in New Zealand. We think the combination of these factors would mean that Inland Revenue would be able to have confidence that the contractor intends to comply with their obligations and that there is a New Zealand address for service if required. We will confirm policy and system design in a future report.

31 It is arguable that this change will not affect revenue as the target group of taxpayers are those with a low risk of non-compliance in the absence of a withholding tax. Consequently, we estimate only a notional revenue loss of $200k per annum by excluding specified low-risk entities.

Improving NRCT administration

32 The submitters support improving NRCT administration by introducing a bespoke NRCT code. They note that this would reduce compliance costs for some payers (dependent on how they are currently paying NRCT through the PAYE system), and would increase the transparency and visibility of NRCT payments.

33 We agree with this change and note it would be purely administrative and would not have a fiscal cost.

Additional measures put forward by submitters

34 In addition to their responses to the identified issues, submitters also put forward additional measures for consideration. A number of them were operational, including fast-tracking exemptions in response to emergencies, extending or automating exemptions, reestablishing the non-resident contractor centre at Inland Revenue, and providing more operational guidance. These are out of scope of the present reform but will be raised internally for consideration.

Fundamental reform

35 CTG and Deloitte thought that it was worthwhile undertaking a wider review of NRCT as to whether it is fit for purpose and, if so, whether a more streamlined and effective system can better achieve the regime's objectives without imposing significant compliance costs on taxpayers.

36 They suggest that it would be preferable for non-resident contractors and Inland Revenue to interact directly, without involving the payer as an intermediary. This new system would work by setting up a "NRCT portal" through which non-resident contractors could self-certify and provide information straight to Inland Revenue. This process could be similar to the Australian model.

37 Although out of scope of the present reform, we think it could be worthwhile exploring this idea and alternative options in the medium term. One additional option would be a system similar to the approved issuer levy regime, as outlined in the aircraft asset leasing workstream report (IR2026/001 refers).

Technical changes to NRCT

38 Submitters also suggested minor or technical changes to the rules. Each of these ideas could be further considered for future targeted changes that would simplify NRCT settings without necessarily overhauling the system. These changes include:

- Changing the 92-day threshold to 183 days;
- Extending the existing 60-day grace period to 92 days,
- Reducing the NRCT withholding rate to recognise commercial return rates;
- Implementing an exemption for short-term visits; and
- Removing recourse to the New Zealand payer for failure to withhold if the non-resident contractor later fails to comply with their obligations.

39 As these changes are out of scope of the targeted consultation, we have not costed them for this report. Some are more likely to have an impact on the overall NRCT settings than others. We can provide further advice and costings if Ministers are interested in incremental improvements to the rules.

Officials' preferred package

40 NRCT's function is to protect the New Zealand tax base by mitigating flight risk – contractors who leave the country without paying the tax ultimately due. It is not intended to raise revenue in and of itself.

41 Officials recommend implementing the following package of changes to modernise and simplify NRCT through the 2026-27 omnibus tax Bill, which will be introduced later this year:

- Increasing the $15k threshold to $60k;
- Implementing the single-payer view of the monetary and day count thresholds, together with a requirement that payers keep relevant documentation (which can be provided to Inland Revenue on request) for integrity purposes;
- Excluding branches, limited partnerships and representative offices from NRCT provided they also meet certain additional indicators of good compliance, for example where they have an IRD number and are registered with the Companies Office; and
- Creating a bespoke NRCT code.

42 If Ministers prefer fundamental reform to overall NRCT settings in the medium term, you may prefer to defer specific information retention requirements pending that reform.

Financials for officials' preferred package

43 Inland Revenue is seeking funding for the departmental and non-department financial impacts of the officials' preferred package as part of Budget 2026.

44 The non-departmental fiscal cost of the officials' preferred package based on a 1 April 2027 effective date is estimated at $3 million per year, equating to a $9.750 million reduction in tax revenue over the forecast period.

	$m - increase/(decrease)					
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total**
Crown Revenue and Receipts:						
Tax revenue – Source Deductions (PAYE)	-	(0.750)	(3.000)	(3.000)	(3.000)	(9.750)
Total Operating		**0.750**	**3.000**	**3.000**	**3.000**	**9.750**

45 The one-off departmental costs to implement the system and process changes for the package are estimated at $0.330 million capital and $0.370 million operating. The ongoing cost to administer this package is estimated at $0.200 million each year. This mainly supports the manual effort reviewing contracts for compliance activities in relation to the proposal 'Implementing the single-payer view'.

	$m - increase/(decrease)					
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total**
Capital						
System build	-	0.330	-	-	-	0.330
Total capital	-	**0.330**	-	-	-	**0.330**
One-off operating	-	0.370	-	-	-	0.370
Ongoing operating	-	-	0.200	0.200	0.200	0.600
Total Operating	**-**	**0.370**	**0.200**	**0.200**	**0.200**	**0.970**

46 The primary benefit of this initiative is a reduction in compliance costs for both New Zealand payers and non-resident contractors.

Consultation

47 We have informed the Treasury of this report.

Next steps

48 We recommend that the proposed changes are made in the 2026-27 omnibus tax Bill, to be introduced in August or September this year. We will include advice on any detailed design or implementation decisions as part of the Bill process.

49 Modernising and/or simplifying NRCT is currently included within the Budget 2026 Tax and Social Policy Work Programme placeholder initiative but will ultimately be subject to confirmation by Budget Ministers and Cabinet.

Recommendations

We recommend that you:

1 **Agree** to increase the non-resident contractors' tax monetary exemption threshold (currently $15k) to:

a $30k

Agree / Disagree — Agree / Disagree

Minister of Finance — *Minister of Revenue*

or

b $60k (*officials' recommendation*)

Agree / Disagree — Agree / Disagree

Minister of Finance — *Minister of Revenue*

or

c $100k

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

2 **Agree** that the single-payer view should apply to the NRCT monetary and day count thresholds.

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

3 **Agree** that New Zealand payers of NRCT should be subject to a specific information retention requirement.

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

4 **Note** that a specific information requirement could be deferred if you prefer to explore further changes to the NRCT in the medium term.

5 **Agree** to exclude branches, New Zealand limited partnerships and representative offices from NRCT, subject to conditions.

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

6 **Note** we will provide further advice on the conditions for excluding the entities referred to in recommendation 5 as part of detailed design.

7 **Agree** that Inland Revenue will create a bespoke NRCT tax code within the PAYE system, noting this will be an administrative change.

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

8 **Agree** to implement the changes in the next omnibus tax Bill, noting that we will seek more detailed design or implementation decisions through the omnibus Bill process if necessary.

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

9 **Agree** for the changes to take effect from 1 April 2027.

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

10 **Note** the non-departmental fiscal cost of recommendations 1b, 2, 3, 5 and 7 above, is estimated at $3 million per year, equating to a $9.750 million reduction in tax revenue over the forecast period.

	$m - increase/(decrease)					
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total**
Crown Revenue and Receipts:						
Tax revenue – Source Deductions (PAYE)	-	(0.750)	(3.000)	(3.000)	(3.000)	(9.750)
Total Operating		**0.750**	**3.000**	**3.000**	**3.000**	**9.750**

11 **Note** the departmental costs to implement and administer this initiative are estimated at $0.330 million capital and $0.970 million operating over the forecast period.

	$m - increase/(decrease)					
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**	**Total**
Capital						
System build	-	0.330	-	-	-	0.330
Total capital	-	**0.330**	-	-	-	**0.330**
One-off operating	-	0.370	-	-	-	0.370
Ongoing operating	-	-	0.200	0.200	0.200	0.600
Total Operating	**-**	**0.370**	**0.200**	**0.200**	**0.200**	**0.970**

12 **Note** that, subject to your agreement and Budget Ministers' decisions, final fiscal and administrative costs will be included in the Budget 2026 Cabinet paper.

s 9(2)(a)

Pamela Law

Principal Policy Advisor

Policy | Inland Revenue

9 March 2026

Hon Nicola Willis

Minister of Finance

/ /2026

Hon Simon Watts

Minister of Revenue

/ /2026

Briefing note

Inland Revenue
Te Tari Taake

Reference	BN2026/122
Date	15/04/2026
To	Revenue Advisor, Minister of Revenue – Angela Graham Private Secretary, Minister of Revenue – Melissa Zhen
From	Portia De Forest
Subject	**Information on non-resident contractors' tax for the joint Ministers meeting on 20 April**

Background

1 The Minister has requested information on the non-resident contractors' tax (NRCT) threshold changes to support him in his joint Ministers meeting with the Minister of Finance on Monday 20 April.

2 Specifically, he indicated that he would like to increase the monetary exemption threshold (below which withholding tax does not need to be withheld in relation to NRCT) to $75,000. He has previously agreed to a monetary threshold of $60,000. The current threshold is $15,000.

3 Other NRCT modernisation and simplification changes that he previously agreed to [IR2026/026 refers] include:

- implementing a single-payer view, so a payer of NRCT needs to consider only their own contractual activity with the non-resident contractor when determining if either the monetary or 92-day thresholds exemptions are available, and
- excluding low-risk entities such as branches, limited partnerships and representative offices from the NRCT regime.

4 Alongside these changes, Inland Revenue will also create a bespoke NRCT tax code.

5 The Minister did not agree to implement a documentation requirement in connection with the single-payer view.

6 This note also provides an update in relation to the Budget proposal to exempt aircraft asset leases from NRCT.

Increasing the monetary exemption threshold to $75,000

7 The fiscal impact of increasing the monetary exemption threshold to **$75,000**, alongside the implementation of a single-payer view and the exclusion of low-risk entities (as already agreed) is shown below. The forecast period cost of the package, including the $75,000 monetary exemption threshold, is $13 million. The NRCT lost by increasing the threshold to $75,000 would be around $4 million per year (8% of the total amount of NRCT collected in 2025 of $49 million).[1]

[1] We reported last year that the total amount of NRCT collected in 2025 was $47 million (IR2025/402 refers). This figure has since been updated to $49 million.

8 Based on 2024 data, we estimate that around 3,224 taxpayers are within scope of the NRCT regime. Assuming no other exemption applies, around 1,129 of these taxpayers sit above the current $15,000 threshold and are required to withhold NRCT (NRCT payers).

9 Increasing the threshold to $75,000 would newly exempt around 684 current NRCT payers (61% of NRCT payers). This includes an additional 95 taxpayers (8% of NRCT payers) who would not be exempt under a $60,000 threshold as their contracts exceed $60,000.

	$m - increase/(decrease)				
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Crown Revenue and Receipts:					
Tax revenue - PAYE		(1.000)	(4.000)	(4.000)	(4.000)
Total Operating	**-**	**1.000**	**4.000**	**4.000**	**4.000**

10 The fiscal impact of increasing the monetary exemption threshold to **$60,000**, alongside the implementation of a single-payer view and the exclusion of low-risk entities (as already agreed) is shown below. The forecast period cost of this package, including the $60,000 monetary exemption threshold, is $9.750 million – $3.250 million less than with a $75,000 threshold over the forecast period. The NRCT lost by increasing the threshold to $60,000 would be $3 million per year (6% of the total amount of NRCT collect in 2025).

11 Based on 2024 data, around 589 taxpayers would be newly exempted under a $60,000 threshold (52% of NRCT payers).

	$m - increase/(decrease)				
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Crown Revenue and Receipts:					
Tax revenue - PAYE		(0.750)	(3.000)	(3.000)	(3.000)
Total Operating	**-**	**0.750**	**3.000**	**3.000**	**3.000**

12 Accordingly increasing the monetary exemption threshold to $75,000 compared with $60,000 would forgo approximately $1 million of NRCT per year (2% of total NRCT collected) but would exclude an additional 8% of NRCT payers.

Administration costs

13 We had previously advised that administration costs for the changes will total $1.3 million over the forecast period. This included the cost of implementing a documentation requirement, which you have agreed to not progress. With this revision, administration costs total $1 million over the forecast period.

14 The reduced administration costs slightly offset the increased fiscal cost of increasing the monetary threshold to $75,000. Over time, the fiscal impacts of several Revenue initiatives being considered for Budget 2026 have fluctuated in their costs/savings. For example, the overall cost for the foreign investment fund tax rules reforms has fallen by $2.3 million over the forecast period, and the charities/not-for-profits workstreams are generally raising more revenue than initially was the case. The higher fiscal cost of the $75,000 threshold would not have a significant impact on the overall Revenue package for Budget 2026, which would still be a net saving.

15 The revised administration costs reflects upfront transition support for New Zealand payers and non-resident contractors moving to the bespoke NRCT code, and accounts for some initial contact such as customer queries. Increasing the monetary exemption threshold from $60,000 to $75,000 does not materially impact administration costs, as it does not introduce additional system changes or compliance processes and only marginally reduces the number of affected taxpayers (by 95 taxpayers).

NRCT and aircraft leasing

16 The Ministers of Finance and Revenue have agreed to introduce a permanent, "by application" exemption from NRCT for the leasing of aircraft (excluding aircraft charters) and parts at a total cost of $17.850 million across the forecast period.

17 As we have worked through the design of the policy in legislation, it has become clear that providing this exemption "by application" is impractical. The purpose of the application process was solely to allow Inland Revenue to collect information on the exempt taxpayers, which, given the small number of taxpayers affected, is not necessary.

18 Instead, we propose that the exemption from NRCT for the leasing of aircraft is provided automatically by the enabling legislation. This does not change the fiscal implications of the proposal, as it was assumed that all eligible taxpayers would apply for the relevant exemption.

Next steps

19 As discussed at the most recent joint Ministers meeting, the Minister of Finance has delegated decisions on minor tax initiatives included in Budget 2026 to the Minister of Revenue.

20 Unless the Minister of Revenue indicates otherwise, we will progress on the basis that the package of NRCT changes for Budget 2026 includes a **$75,000** monetary exemption threshold, rather than a $60,000 threshold as previously agreed.

21 We will also progress on the basis that the NRCT exemption for aircraft leasing is an automatic exemption, rather than one that is provided by application.

22 We recommend that the Minister of Revenue inform the Minister of Finance of this change at the upcoming joint Ministers meeting, on 20 April.

Portia De Forest

Policy Advisor, International

s 9(2)(a)

MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

Inland Revenue
Te Tari Taake

BRIEFING

Options for enhancing the Research and Development Tax Incentive

Date:	6 November 2025	**Priority:**	High
Security classification:	Sensitive	**Tracking number:**	BRIEFING-REQ-0019154 IR2025/376

Action sought		
	Action sought	**Deadline**
Hon Dr Shane Reti **Minister of Science, Innovation and Technology**	**Indicate** through the body of this report which options you would like officials to further shape into a fully costed package to progress through Budget 2026. **Agree** the Minister of Science, Innovation and Technology will refer this briefing to the Minister of Finance.	17 November 2025
Hon Simon Watts **Minister of Revenue**		17 November 2025

Contact for telephone discussion (if required)			
Name	**Position**	**Telephone**	**1st contact**
Gina Williamson	Manager, Innovation Policy, MBIE	s 9(2)(a)	✓
Claire McLellan	Acting Policy Lead, Policy, IR		✓
Sarah Cordiner	Senior Policy Advisor, Innovation Policy, MBIE		
Callum Aldiss	Senior Policy Advisor, Policy, IR	s 9(2)(a)	

The following departments/agencies have been consulted
The Treasury, Callaghan Innovation

Minister's office to complete:

- ☐ Approved
- ☐ Noted
- ☐ Seen
- ☐ See Minister's Notes
- ☐ Declined
- ☐ Needs change
- ☐ Overtaken by Events
- ☐ Withdrawn

Comments

MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

Inland Revenue
Te Tari Taake

BRIEFING

Options for enhancing the Research and Development Tax Incentive

Date:	6 November 2025	**Priority:**	High
Security classification:	Sensitive	**Tracking number:**	BRIEFING-REQ-0019154 IR2025/376

Purpose

To provide Ministers with options for progressing enhancements to the Research and Development Tax Incentive (RDTI) to address feedback from its recent evaluation and stakeholder consultation. These options will inform Going for Growth: Innovation, Technology and Science Ministers' discussions on a package of options to progress through Budget 2026.

Executive summary

The five-year evaluation found the RDTI is working as intended but there is room for improvement

Earlier this year, Motu Research Trust delivered the first five-year evaluation of the RDTI. The evaluation found that the scheme overall is functioning as intended and its broad economic impacts compare well with international benchmarks. The evaluation also noted areas for potential improvement, such as reducing compliance costs — particularly for low research and development (R&D) expenditure firms, operational improvements to claims processing, and changes to the treatment of software development.

Ministers commissioned the development of options to address enhance the scheme

Going for Growth: Innovation, Technology and Science (ITS) Ministers subsequently commissioned officials to explore fiscally positive or neutral options to enhance the RDTI, that also:

- enhance the RDTI's "bang for buck",
- ensure the RDTI continues to support genuine R&D, and
- reduce the compliance burden for businesses and improve access for small businesses.

Recent stakeholder feedback — through Ministerial meetings with businesses and consultation by officials — aligned with Ministerial objectives and the evaluation findings. Consultation also raised additional areas that could be improved, such as: managing cashflow and greater clarity around eligibility. Stakeholders also expressed a desire for greater transparency of the scheme (for example, what stage of the process their claim is at, publication of previous determinations on common issues, clearer guidance), stable policy settings and an internationally competitive rate/scheme.

From Ministerial objectives, evaluation findings and stakeholder feedback, we identified two central issues to address:

- Ensuring the RDTI incentivises additional R&D that delivers innovation and productivity spillovers, and that payments apply only to activities consistent with the policy intent of the scheme.
- Ensuring that compliance with the scheme is not overly burdensome, especially for small businesses.

We have identified five settings where policy changes should be considered

To address these issues and meet Ministers' objectives we recommend considering changes to the five policy settings presented in **Table 1** below. This also outlines some potential policy packages and their indicative fiscal impacts.

At this stage of the Budget 2026 process, Inland Revenue can self-fund the departmental administration impacts of the potential policy changes, including the additional $2.1 million capital, from the previous commitment to self-fund $6.5 million for implementing in-year payments. The ability of agencies' to self-fund departmental impacts is subject to final policy decisions and the cumulative impact of other current and proposed initiatives. Officials will report back to Ministers in December 2025, with refined fiscal estimates for the preferred package of options, indicated in this report, to progress through Budget 2026.

Table 1 Potential option packages with indicative costings

RDTI setting	**Potential packages**			
	Fiscally neutral		**Fiscally positive**	
	Option	*Approx savings pa*	*Option*	*Approx savings pa*
In-year Payments	Implement through the tax system	($2.1 million) *	Do not implement	--
Internal software development	Reduce cap from $25m to $3m	$16.5 million	Make ineligible	$31.5 million
Overseas expenditure	Retain 10% cap	--	Make ineligible	$12.0 million
Mining exclusions	Relax exclusions	($0.4 million)	Maintain exclusions	--
Commissioner of Inland Revenue discretion for late filing	Allow discretion	($2.5 million)	Do not allow discretion	--
Total savings		**$11.4 million**		**$43.5 million**

*There is an additional one-off capital cost of $2.1 million in the first year

We recommend retaining the current settings for the credit rate (15 per cent flat rate), expenditure thresholds ($50,000 minimum, $120 million maximum) and refundability.

We consider operational enhancements to the RDTI filing processes and the Approved Research Provider (ARP) programme will also support Ministers' objectives, particularly in relation to reducing the compliance burden and improving access for small businesses.

Policy changes to achieve fiscal savings will require trade-offs against impacts to business expenditure on R&D, the wider economy, business certainty, tax system integrity, compliance burden for businesses and administrative feasibility.

s 9(2)(f)(iv)

s 9(2)(f)(iv)

Recommended action

The Ministry of Business, Innovation and Employment (MBIE) and Inland Revenue (IR) recommend that the Minister of Science, Innovation and Technology and the Minister of Revenue:

Minister of Science, Innovation and Technology	*Minister of Revenue*

A. **Note** that the RDTI is designed to incentivise increased business expenditure on R&D while maintaining integrity of the scheme and the tax system and managing compliance costs, and is informed by overseas practice and experience.

Noted	*Noted*

B. **Note** there are trade-offs to balance across the objectives of increasing impact, maintaining focus on genuine R&D, reducing compliance cost, and achieving fiscal neutrality. The relative priority of these may vary across portfolios.

Noted	*Noted*

C. **Note** the ability of agencies to self-fund departmental impacts is subject to final policy decisions and the cumulative impact of other current and proposed initiatives.

Noted	*Noted*

D. **Indicate** through the body of this report which options you would like officials to further shape into a fully costed package to progress through Budget 2026.

Indicated/Not indicated	*Indicated/Not indicated*

E. **Agree** the Minister of Science, Innovation and Technology will refer this briefing to the Minister of Finance.

Agree/Disagree	*Agree/Disagree*

Gina Williamson
Manager, Innovation Policy
Labour, Science and Enterprise, MBIE

..... / ..... / .....

Claire McLellan
Acting Policy Lead
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..... / ..... / .....

Hon Dr Shane Reti
Minister of Science, Innovation and Technology

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Hon Simon Watts
Minister of Revenue

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Background

1. The RDTI is the Government's primary investment to incentivise business to invest in research and development (R&D). Introduced in 2019, the RDTI provides a 15 per cent tax credit on eligible business R&D expenditure.

2. The RDTI's design is informed by the need to balance between maintaining integrity (i.e. not funding ineligible activities) and reasonable compliance costs. The level of scrutiny a claim undergoes needs to be proportionate to the risk of fraud or deliberate non-compliance to ensure the cost of compliance or administration of the scheme does not outweigh the benefit.

The five-year evaluation found the RDTI scheme is working well but there are some areas that could be improved

3. The evaluation found that the scheme overall is functioning as intended and its broad economic impacts compare well with international benchmarks. Specifically, the RDTI delivers an estimated return of $1.40 in additional R&D for every $1 of Government investment (comparable to the OECD average of $1.37) with broader economic returns estimated between 2.1 and 6.3 times the initial investment. However, the evaluation also highlighted mixed stakeholder views on the appropriateness of the compliance costs — particularly for low R&D expenditure firms. Ministers have previously been briefed in greater detail on the findings of the evaluation (BRIEFING-REQ-0011218, IR2025/147 and BRIEFING-REQ-0018779 refer).

Ministers have requested advice on enhancing the RDTI to address feedback from the evaluation and stakeholders

4. At the Going for Growth Innovation, Technology and Science (ITS) Ministers' meeting on 28 July 2025, Ministers commissioned MBIE and IR to explore options to enhance the RDTI to address feedback from the evaluation.

5. ITS Ministers advised that enhancements should be fiscally positive or neutral, and that their objectives are to:

   - enhance the RDTI's "bang for buck";
   - ensure the RDTI continues to support genuine R&D; and
   - reduce the compliance burden for businesses and improve access for small business.

6. This briefing provides Ministers with details on the current RDTI settings most relevant to Ministers' objectives and provides policy options (both settings to maintain and to consider changing) in response to Ministerial commissioning. It also provides an overview of operational enhancements that are being or could be progressed to support Ministers' objectives.

7. More work needs to be done to get accurate fiscal costings on potential policy packages. Based on Ministers directions in response to this advice, officials will report back to Ministers in December 2025, with refined fiscal estimates for the preferred package of options to progress through Budget 2026.

Current RDTI settings

The RDTI incentivises business investment in R&D, benefitting the wider economy

8. Business investment in R&D delivers benefits beyond the investing firm, including increased productivity, job creation, knowledge transfer between firms (via workforce mobility, both domestically and internationally), and demand for complementary goods. These wider economic benefits known as spillovers, are not fully captured by individual firms and therefore are not factored into their investment decisions. As a result, businesses tend to underinvest in R&D relative to what is optimal for the country as a whole.

9. The RDTI helps address this gap by reducing the cost of R&D, incentivising greater business investment. This is particularly important given New Zealand's relatively low business R&D expenditure. In 2024, Business R&D investment was 0.97 per cent of GDP — up from 0.79 per cent of GDP in 2019 but still below the OECD average of 1.99 per cent[1]. Over the first five years of the RDTI scheme (2019 to 2024), a total of $1.1 billion has been claimed in RDTI credits by 1,752 firms. The average annual credit claimed per firm is $262,000.

10. A tax credit was selected because of the wide reach of the tax system. A flat 15 per cent rate was chosen to provide a similar level of support to the grants the RDTI replaced, and to ensure the incentive would be accessible, inclusive and not distort business structuring or spending decisions.

The RDTI is intended to target R&D that will maximise wider economic benefits (spillover benefits)

11. The RDTI's definition of eligible R&D is based on the internationally recognised standard, the Frascati Manual. This definition is highly targeted towards scientific and technical uncertainty and is supported by specific expenditure and activity exclusions — such as exclusions for social sciences or market research.

12. The RDTI also caps overseas R&D expenditure at 10 per cent of total expenditure, to ensure the scheme is focused on developing domestic R&D capability, while acknowledging the commercial reality of trading and operating across borders. Firms must be a tax resident and have a fixed establishment in New Zealand. Eligibility does not require that businesses or resulting intellectual property be New Zealand owned.

The RDTI's design balances maintaining integrity and managing compliance costs

13. Robust integrity measures help minimise fraud risk but create compliance requirements and therefore costs for applicants. Conversely, less vetting of a claim reduces the compliance cost of applying but contributes to a greater risk of incorrect claims and payments.

14. A commonly held concern with R&D tax incentives is that businesses will abuse the scheme — for example, by recharacterising business-as-usual expenditure as eligible R&D expenditure. The evaluation found no evidence that firms were engaging in this behaviour and, to date, IR has not seen significant evidence of businesses attempting to classify non-R&D expenditure as R&D.

The RDTI's integrity mechanisms were informed by overseas experience

15. When the RDTI was designed, officials consulted with administrators of R&D tax incentives in the United Kingdom (UK), Australia, and Norway. These countries had expanded access to their schemes to encourage greater business investment in R&D. However, more liberal settings led to increased fraud, particularly among small and medium enterprises (SMEs).

16. In the UK, for example, His Majesty's Revenue and Customs (HMRC) reported that in the 2021–22 tax year, £1.2 billion – 25.8 per cent of total expenditure – was fraudulently claimed under the SME tax credit scheme.[2] In contrast, fraudulent claims under the large enterprise scheme totalled £134 million (4.6 per cent of total expenditure). That same year, 30 per cent of SME claims were fully non-compliant, rising to approximately 50 per cent when partially non-compliant claims were included.

17. These outcomes are linked to reduced scrutiny. HMRC initially reviewed 100 per cent of SME claims, but by 2018, only 1 per cent were checked due partly to rapid growth in claim volumes and resource constraints. More generally, international experience shows that aggressive marketing by boutique tax advisories can drive up the volume of SME applications, increasing both fiscal and integrity risks. New Zealand's settings, in particular

[1] Stats NZ 2024 R&D Survey
[2] Approach to Research and Development tax reliefs 2023 to 2024 - GOV.UK

the two-stage approval and claim process, were specifically designed to prevent similar outcomes.

Complementary business R&D initiatives

There are two other key government interventions to support business R&D activity alongside the RDTI

18. **The New to R&D (N2RD) grant** supports businesses without established R&D capabilities[3] and provide an "on-ramp" to the RDTI. It was introduced in 2022, to improve access to the RDTI for small expenditure firms. The grant offers 40 per cent co-funding up to a maximum total combined cost of $1 million ($400,000) for two years. This covers costs associated with the first project and funding to build R&D skills and capabilities within the business, including support for applying for the RDTI in future.

19. **The RDLTC** was introduced in 2016 and supports early-stage R&D-intensive firms. It allows eligible businesses to cash out a 28 per cent credit on tax losses up to $2 million annually — providing a maximum credit of $560,000. This helps overcome tax system barriers that disadvantage start-ups unable to offset losses against future profits. Cashed-out losses are cancelled, meaning firms move into profit sooner and eventually pay the same amount of tax as they would have without the credit. If a firm never becomes profitable, its credit is not repaid.

20. Most countries offering an R&D tax incentive also include a provision for firms in a loss-making position[4]. If a firm claims both the RDTI and the RDLTC, their total tax benefit (43 cents in the dollar) is comparable to that of Australia which offers a 43.5 per cent tax credit for SMEs. In the 2023-24 tax year, the RDLTC paid out $119 million — approximately half of the value of credits paid out by the RDTI.

Consultation insights and problem definition

Stakeholder consultation shows strong business support for the RDTI and similar areas for improvement

21. Officials have undertaken consultation to complement the evaluation insights to inform development of policy options.[5] This consultation revealed strong support for the RDTI but highlighted key areas for improvement, specifically around reducing the compliance burden, improving SME access, improving ability for businesses to manage cashflow around their RDTI claim, shorter and more consistent processing times and clarity around eligibility. Stakeholders expressed a desire for greater transparency of the scheme (for example, what stage of the process their claim is at, publication of previous determinations, clearer guidance), stable policy settings and an internationally competitive rate/scheme.

Problem definition

22. From Ministerial objectives, evaluation findings and stakeholder feedback, we identified two issues to address:

    a. Ensuring the RDTI incentivises additional R&D that delivers innovation and productivity spillovers, and that payments apply only to activities consistent with the policy intent of the scheme.

[3] In the three years prior to submission, eligible businesses must not have spent more than $150,000 or received more than $5,000 in Government support (including the RDTI or RDLTC).
[4] At least 18 OECD countries, including Australia and Ireland.
[5] Stakeholder consultation was undertaken by IR and MBIE during September and October 2025. Feedback was provided by in-person meetings or via email correspondence.

b. Ensuring that compliance with the scheme is not overly burdensome, especially for small businesses.

23. We have reviewed the current RDTI settings that could address or exacerbate the above concerns. An overview of "pain points" identified in the scheme can be found in **Annex One**. We have considered changes to both policy and operational settings to address these. In developing options, we assessed them against their ability their impact on:

    a. business expenditure on R&D,

    b. the wider economy,

    c. business certainty,

    d. integrity,

    e. compliance burden,

    f. fiscal costs/savings, and

    g. administrative feasibility.

Opportunities to change policy settings to enhance the RDTI

24. The following sections present the options we view could be adjusted to enhance the RDTI and meet Ministers' objectives. All options considered are summarised in **Annex Two.** This section covers new opportunities, while the following section covers options for which Ministers have previously received advice and deferred decisions until after receipt of the evaluation.

Non-administrative internal software development

25. Software that is used for the internal administration of the business, such as HR and payroll, is excluded from the RDTI, because it is unlikely to produce wider economic benefits. Non-administrative internal software is eligible but is capped at $25 million of expenditure, recognising that there are some spill-over benefits from the development of non-standard internal software. Both the expenditure cap and exclusion of administrative software mitigate the risk of firms misclassifying routine software development as eligible R&D.

Determining legitimate activity is difficult and causes administrative burden for agencies and compliance costs for businesses

26. Due to similarities between administrative and non-administrative internal software activities, determining legitimate eligibility of expenditure in this area can be difficult. This causes administrative burdens for assessors and a compliance cost to companies (e.g. through responding to requests for information). The average number of working days to conclude a case involving internal software development is 304 days (including assessors and applicants time). Despite representing just 15 per cent of claims and 11 per cent of total R&D expenditure, these claims consume a disproportionately large amount of assessors' time at the claims stage. This is due to the complexity of claims requiring requests for information from the firms. This problem is observed in other jurisdictions too.

27. Stakeholders generally supported retaining eligibility of non-administrative internal software, saying it provides integral support to improve productivity in heavily digitised sectors (for example, game and digital development sectors, service companies) where internal software has a critical link to products they deliver. We have considered two options to change the rules for non-administrative internal software that could improve RDTI scheme integrity and deliver savings.

Making non-administrative internal software ineligible for the RDTI will reduce fiscal costs and could improve "bang for buck" but may reduce wider economic benefits

28. There is limited evidence regarding the economic impacts (spillovers and additionality) of non-administrative internal software R&D. However, at inception of the RDTI, on the basis of international literature, these were assumed to be lower than for other types of R&D. Excluding all internal software development expenditure from the RDTI therefore could increase the impact per dollar spent on the RDTI, in line with Ministers' objective to increase the scheme's 'bang for buck'. This option would reduce administrative and compliance costs (due to the expenditure being ruled ineligible). It would provide a fiscal saving of around $30 million per annum in fewer RDTI credits paid out.

29. If internal software were made ineligible, other forms of support would still exist for smaller software development firms, such as the RDLTC (discussed below). However, MBIE is concerned that excluding non-administrative internal software this expenditure from the RDTI could adversely impact the level of R&D expenditure and the overall spillover benefits of the scheme and may not align with wider Going for Growth objectives, including a push for greater digitisation.[6]

Reducing the eligible expenditure cap continues to support this type of R&D but will not generate as large a fiscal saving

30. An alternative option is to reduce the eligible expenditure cap from $25 million to $3 million. This would generate fiscal savings while continuing to recognise non-administrative internal software as eligible R&D, particularly for SMEs. We note this cap was originally $3 million but was raised prior to introduction in response to stakeholder feedback.

31. A $3 million cap would have resulted in approximately $16.5 million fewer RDTI credits paid out in 2024. However, a lower cap will mostly affect large firms and those in the digital technologies sectors.

Minister of Science, Innovation and Technology	*Minister of Revenue*
1. **Note** that reducing the cap or excluding expenditure on non-administrative internal software development will reduce fiscal, administrative and compliance costs, and could increase the bang for the buck of the RDTI but may have negative impacts on some sectors (particularly the digital sector) and wider economic benefits provided by the scheme.	
Noted	*Noted*
EITHER	
2. **Agree** to cap eligible internal software at $3 million of eligible expenditure.	
Agree/Disagree	*Agree/Disagree*
OR	
3. **Agree** to exclude all internal software development expenditure from the RDTI.	
Agree/Disagree	*Agree/Disagree*

[6] The Government's AI Strategy explicitly refers to the RDTI as a way that businesses can leverage the NZ Science, Innovation and Technology System to accelerate adoption of AI.

Overseas expenditure

Overseas expenditure enables New Zealand companies to access expertise and capabilities not available domestically

32. The RDTI aims to incentivise R&D activities performed in New Zealand. Recognising that activities or expertise in certain fields may only be available overseas, the current settings allow 10 percent of a firm's total claim to be for expenditure on activities conducted overseas — provided this supports a main R&D activity in New Zealand. This balances the policy intent of the RDTI with the commercial reality of businesses operating across borders, supporting the international connectedness of New Zealand's innovation system.

33. During consultation, stakeholders — particularly those in the pharmaceutical and health tech sectors — advised that some R&D capabilities are only available or feasible offshore and some overseas activities are requirements for market access. They expressed a desire for an increased overseas expenditure cap balanced by requiring intellectual property remains in New Zealand or domestic ownership provisions to ensure benefit to New Zealand.

Excluding overseas expenditure could deliver fiscal savings but would increase R&D costs for businesses and could negatively impact the wider economy

34. The overseas expenditure allowance could be viewed to not directly support domestic R&D or generate spillovers in New Zealand. Removing its eligibility would better target R&D that delivers local benefits and result in fiscal savings. Had it been excluded, $12 million in RDTI credits would not have been paid out in the 2023–24 income year. Beyond the savings, excluding overseas expenditure would also strengthen the integrity of the RDTI by ensuring it only funds R&D conducted in New Zealand. This change would disproportionately affect larger firms, which typically incur a higher share of overseas R&D costs compared to smaller spenders.

35. While spillovers directly attributable to overseas expenditure may be lower than for domestic expenditure on R&D, it enables businesses to access to expertise and capabilities not available domestically and retaining their broader R&D activity in New Zealand. Without such an allowance, given New Zealand's size and distance from international markets, MBIE judges there is a risk that some businesses could relocate a significant portion of their R&D programmes elsewhere, reducing overall economic benefit to New Zealand.

Minister of Science, Innovation and Technology	*Minister of Revenue*
4. **Note** that RDTI support for overseas expenditure helps businesses to access expertise and capabilities not available in New Zealand but can be difficult to verify and is less likely to directly generate spillover benefits within New Zealand than domestic R&D expenditure.	
Noted	*Noted*
EITHER	
5. **Agree** to retain the 10% cap on overseas expenditure.	
Agree/Disagree	*Agree/Disagree*
OR	
6. **Agree** to exclude all overseas expenditure from the RDTI.	
Agree/Disagree	*Agree/Disagree*

Options previously advised on

36. Ministers have previously received advice on including a provision for in-year payments through the tax system, revising the mining exclusions in the RDTI and a discretionary power for the Commissioner of Inland Revenue to accept and amend late RDTI filings (IR2024/209 refers). Decisions were held off until the results of the final five-year evaluation were available. These settings were raised by stakeholders in recent consultation as areas of the RDTI that could be improved.

In-year payments

In-year payments will support start-ups and SMEs by providing regular payments, improving cashflow

37. Businesses currently experience a delay between incurring R&D expenditure and receiving the associated tax credit. This delay can create cash flow challenges for businesses, particularly loss-making businesses and pre-revenue start-ups.

38. Stakeholders, particularly smaller businesses or their representatives, raised this delay as a barrier to involvement with the RDTI and expressed that in-year payments would help mitigate the variable processing times of claims by providing regularity of payments. This could support Ministers' objective of improving access to the RDTI for small businesses.

However, in-year payments introduce risks to the tax system and could require additional funding

39. In-year payments introduce integrity risk and the risk of debt, because entitlements are based on estimated expenditure and only confirmed retrospectively when a claimant's return is processed. Measures such as capping payments at 80 per cent of estimated expenditure and/or applying the RDTI's refundability cap could mitigate these risks. These mitigations may disadvantage some small businesses that do not pay much labour-related tax.

40. While the initiative has no non-departmental fiscal implications, IR has previously costed implementation at $6.5 million over the forecast period and notes that the complexity and large resource demands of delivering this initiative would necessitate careful consideration of IR's ability to deliver other initiatives. If this option is to be progressed, IR would need to take into account the cumulative impacts of all Budget initiatives that impact Vote Revenue.

41. Due to these considerations, IR recommends against the in-year payments proposal in favour of implementing the Government's already stated tax system priorities. However, if you decide to proceed with in-year payments, IR will update the costings based on the preferred policy options and will advise if any of these options exceed its ability to self-fund, without directly impacting core service delivery, tax revenue, or tax debt.

42. The previous Government agreed to implement in-year payments of the RDTI through the tax system. However, due to the long lead-in time, a loan scheme was introduced in March 2023 as a temporary measure to provide in-year payments. This scheme was closed in January 2024 on the basis that it was costly to administer with significant operational risks, had low uptake (only 203 loans were issued compared to a forecast of 3,650 loans over three years) and was overall not delivering value for money.

Operational fixes could meet stakeholder needs without the risks of in-year payments

43. While in-year payments could provide some cashflow relief, they would not address the variable processing times of supplementary returns that were more widely emphasised by stakeholders. The operational improvements to supplementary return processing, discussed in the section below, are a better solution for this aspect. Reducing the lag in RDTI credits being paid out would improve business certainty, without introducing an additional integrity risk to the RDTI scheme. However, this would not help those businesses for whom cashflow constraints are an issue.

Minister of Science, Innovation and Technology	*Minister of Revenue*
7. **Note** that while in-year payments may provide cashflow support for some businesses, delivering in-year payments for the RDTI through the tax system will require prioritisation against delivering other Government's priorities.	
Noted	*Noted*
8. **Agree** to progress delivering in-year payments of the RDTI through the tax system.	
Agree/Disagree	*Agree/Disagree*
9. **Note** if agreed, officials will provide further advice on fiscal and operational implications	
Noted	*Noted*

Mining

44. Mining businesses[7] are currently only able to claim RDTI credits for labour expenditure and expenditure on R&D prototypes. This puts these businesses at a disadvantage compared with other businesses enrolled in the RDTI. Mining businesses cannot claim for expenses such as materials, repairs and maintenance, and overheads, while businesses in other industries can in relation to R&D expenditure.

45. Easing the mining exclusions brings eligibility criteria for the sector in-line with the sector-agnostic design of the RDTI scheme. This constitutes a broadening of the RDTI's targeting, providing the incentive to a wider range of activities. However, it would lead to more RDTI credits being paid out. This change has previously been costed at $1.4 million over the forecast period.

46. You may wish to retain the status quo settings, because revising the mining exclusions does not address your stated objectives or most of the stakeholder feedback. Revising the mining exclusions only increases the incentive for a narrow segment of R&D performing businesses.

Minister of Science, Innovation and Technology	*Minister of Revenue*
10. **Agree** to align the eligibility of mining-related R&D expenditures with other industries.	
Agree/Disagree	*Agree/Disagree*

[7] minerals, petroleum, natural gas or geothermal energy.

Commissioner of Inland Revenue discretion

47. Under current law, RDTI applications and returns cannot be accepted or amended once the filing deadline has passed. This could result in a business being denied its RDTI credit for the relevant income year even due to relatively minor errors such as editorial errors or missing filing deadlines due to illness.

48. In the most recent round of consultation, the stakeholder who had previously raised this issue again suggested this change. They noted that RDTI filing must currently be prepared with excessive care which raises compliance costs and that a company that is denied a credit due to an incorrect filing may be disincentivised from taking up the RDTI in future.

49. A Commissioner of Inland Revenue discretion could meet your objective of reducing compliance costs. Although, we note this would benefit only a small number of firms. This proposal has previously been costed at $10 million over the forecast period. This fiscal cost relates to the additional RDTI credits that would be paid because of this change. You may wish to weigh this against other options to achieve an overall fiscally neutral or positive suite of enhancements.

Minister of Science, Innovation and Technology	*Minister of Revenue*
11. **Agree** to progress with granting a discretion to the Commissioner of Inland Revenue to accept and amend late RDTI filings.	
Agree/Disagree	*Agree/Disagree*

Recommendations to maintain key policy settings

We recommend maintaining current settings relating to the credit rate, expenditure thresholds and refundability

50. The positive evaluation findings and strong stakeholder support show that the RDTI is functioning effectively. In recent consultation, stakeholders emphasised that stable policy settings are critical for ensuring business certainty and confidence in continuing to invest in R&D.

51. Therefore, we recommend you retain the status quo settings for the credit rate, expenditure thresholds and refundability. Policy changes to these features would be substantial and are unlikely to deliver satisfactorily on your objectives, while also having potential unintended consequences on firm behaviour and/or negative impacts on the wider economy.

52. We provide a summary of our reasoning for the status quo settings below. We have provided a fuller analysis for the credit rate, given its ability to incentivise business R&D investment and for adjustments to deliver fiscal savings. **Annex Three** contains a summary of all options considered.

Credit rate

53. The RDTI currently provides a 15 per cent flat rate to all eligible businesses. While the headline rate is lower than the average, New Zealand's current implied subsidy rate (18%) is around the OECD median — comparable to Australia. As such, officials consider that the

current rate is appropriate in the international context. However, in recent consultation stakeholders expressed that the current rate is too low to remain internationally competitive[8].

54. Given the Ministers' objectives, maintaining the status quo is recommended. This option is fiscally neutral and maintains business confidence as well as benefits to the wider economy and additional business R&D activity identified in the evaluation.

Lowering the rate would reduce the fiscal cost of the scheme but could undermine broader economic objectives

55. Lowering the rate could reduce the fiscal cost of the scheme. For example, dropping the rate to 12.5 per cent would result in around $48 million fewer RDTI credits paid out per year. However, based on the evaluation findings of the RDTI generating additional R&D expenditure, it would likely reduce business R&D expenditure and the corresponding spillover benefits, undermining broader economic objectives. A reduced flat rate would also disproportionately affect small businesses, because compliance costs would remain high relative to the incentive.

Tiered rates could meet your objectives but will increase scheme complexity

56. International literature tends to support RDTI regimes that are broad-based with a single flat rate. However, if raising the overall rate was not an option, stakeholders expressed interest in the possibility of higher rates for SMEs or firms with higher R&D intensity. There are several ways you could target the credit depending on your objectives. More targeting generally increases complexity of the scheme and can introduce unintended consequences, such as firms structuring themselves or timing research projects to meet target criteria. Increased complexity can also increase the compliance burden and the cost to Government of administering the scheme.

Targeting SMEs

57. Smaller and/or younger firms may require more support to undertake R&D compared to larger firms for a variety of reasons — for example, being less capable of effectively capturing R&D outcomes (such as being unable to file for patents due to financial constraints). We consider such supports are more effectively delivered via targeted interventions such as grants, additional to the tax incentive. However, some countries target the credit towards small businesses by offering them a greater incentive. A higher rate for small businesses increases the average subsidy they receive recognising they have proportionately higher compliance costs. Small businesses are often defined according to a turnover threshold. A significant limitation of this approach is that it can introduce a disincentive for small businesses to grow because their total subsidy can decrease when they cross over the small business threshold.

58. This effect can be mitigated by providing a higher subsidy rate up to a certain level of R&D expenditure and a lower rate for expenditure above that level of expenditure. This eliminates the "cliff-edge" effect because a firm's total subsidy still increases with every dollar of additional expenditure.

59. However, this approach generally delivers poor value for money, because it provides a higher subsidy for a baseline level of R&D expenditure and a lower subsidy for additional (or marginal) R&D expenditure.[9] This is supported by the evaluation, which modelled a 20 per cent tax credit rate on the first $300,000 of eligible expenditure and a 15 per cent rate thereafter. This modelling indicated that the additional R&D activity generated would be outweighed by the additional cost to Government (net negative $6.2 million). Despite this,

[8] Of the 38 OECD countries, 33 offer some form of tax incentive. In 2024, profitable SMEs can expect to receive an average 19% tax subsidy on R&D expenditures, compared to 16% for large profitable firms.
[9] Identifying Technology Spillovers and Product Market Rivalry. Bloom *et al.* (2013)

and to give a sense of potential savings, reducing the rate to 12.5 per cent for each dollar of expenditure above $300,000 would result in $40 million fewer RDTI credits paid per year.

Targeting higher R&D intensity

60. Some countries have designed their RDTI schemes to reward firms with higher R&D intensity. Australia applies an intensity test for firms with a turnover above AU $20 million. Their scheme provides a lower credit rate to the first 2 per cent of a firm's total expenditure that is spent on R&D. For example, if a firm has $100 million of total expenditure and $5 million of R&D expenditure, the first $2 million of R&D expenditure would get half the standard credit rate and the next $3 million would get the standard credit rate.

61. The intensity threshold is based on two assumptions. First, that spillovers are more likely to come from firms with higher R&D intensity. Second, that large innovative firms can be expected to perform a base level of R&D, so subsidising the first 2 per cent is less likely to incentivise additional R&D activity. Adopting similar settings in New Zealand would add significant complexity to the scheme. It could also disincentivise firms from growing the non-R&D part of their operations to keep a high R&D intensity ratio.

Targeting certain kinds of R&D

62. A third way to target the credit, suggested in consultation, is to provide higher rates to certain kinds of R&D (for example, R&D in sectors or technologies that align with Government priorities). We do not consider the RDTI an appropriate tool for targeting specific types of R&D. If more targeted support is desirable, grant schemes with higher accountability would be more appropriate.

Minister of Science, Innovation and Technology	*Minister of Revenue*

12. **Agree** to retain the single flat credit rate for the RDTI at 15 per cent.

Agree/Disagree	*Agree/Disagree*

OR

13. **Indicate** which option you direct officials to provide you with further advice on**:**

    a. A tiered RDTI credit rate, including options to offer a premium rate to SMEs or high R&D intensity firms

    b. Reducing the RDTI credit rate

Minimum and maximum expenditure thresholds

63. Lower and upper limits apply to eligible expenditure of $50,000 and $120 million respectively, although mechanisms are in place to allow exceptions at both ends. These thresholds balance access and integrity. The minimum threshold aims to prevent the scheme being overwhelmed by low expenditure claims unlikely to generate spillovers, while the maximum acts as a safeguard against excessive claims that may not deliver sufficient benefit to the broader economy.

64. We recommend maintaining the status quo threshold settings. While the minimum threshold does not reflect the true cost of participating in the RDTI (effective minimum spend is likely more than $50,000) and the maximum has only been exceeded once, there is little benefit to be gained from any adjustment. Raising the minimum threshold works against your objective

of improving access to the RDTI for smaller businesses. Lowering the maximum threshold would provide limited fiscal savings due to the small number of firms in higher expenditure bands. It also reduces businesses' incentive to invest more in R&D by increasing the compliance burden for larger firms, creating a perception of instability and uncertain commitment to supporting R&D. Retaining the status quo maintains the stability and predictability of settings for businesses.

65. Targeted support, such as grants, and/or the operational enhancements identified and described later in this briefing are better options for providing support to low expenditure firms.

Minister of Science, Innovation and Technology	*Minister of Revenue*

14. **Agree** to retain the current minimum and maximum expenditure thresholds at $50,000 and $120 million.

Agreed/Not agreed	*Agreed/Not agreed*

OR

15. **Indicate** which option you direct officials to provide further advice on**:**
    a. Raising the minimum threshold
    b. Reducing the maximum threshold

Refundability

66. Refundability is a key setting to ensure businesses in loss do not need to wait until they are profitable to benefit from the RDTI, ultimately supporting take-up. Currently refundability is capped based on labour-related taxes (such as PAYE). This means that firms in loss can only receive a tax credit up to the amount of labour-related taxes they pass on. The tax credit that exceeds this amount must be carried forward. This policy setting mitigates fiscal and integrity risks by ensuring a company is real and cannot claim more than it contributes to the tax system. This design is administratively simple and incurs no additional compliance cost for businesses, because this is information already held by IR.

67. When this setting was implemented, there was concern that businesses who rely on contractors would be disadvantaged because contractor expenses are not included in the cap[10]. These businesses are typically smaller firms, who are more likely to use contractors for R&D, or R&D intensive start-ups who have high R&D expenses relative to staff costs. However, administrative data shows the current settings support most businesses: in the 2023-24 income year, over 80 per cent of RDTI credits were refunded across all expenditure bands up to $5 million; for SMEs, 91 per cent of RDTI credits were refunded.

[10] This is mitigated by employer superannuation contribution tax (ESCT) and fringe benefit tax (FBT) being included in the cap, the ability of businesses to enter an agreement with a contractor to deduct withholding taxes and that all ARP expenditure is fully refundable.

68. We do not recommend changes to the current refundability settings. The status quo works for most businesses and the alternatives present considerable trade-offs for limited improvement. A tangible economic presence test would give all businesses a path to refundability but increase administrative and compliance cost; and a cap based on R&D refundability would increase complexity significantly, narrow refundability and create a perverse incentive for firms to artificially inflate R&D intensity (for instance, by restricting growth).

Minister of Science, Innovation and Technology	*Minister of Revenue*

16. **Agree** to retain the current refundability requirements.

Agreed/Not agreed	*Agreed/Not agreed*

OR

17. **Indicate** which option you direct officials to provide further advice on:
    a. A refundability cap based on R&D intensity
    b. A tangible economic presence test.

Operational enhancements

69. Operational enhancements would also contribute meaningfully to achieving Ministers' objectives. Improvements to the General Approval application process, the claims process and the ARP programme can continue to reduce compliance costs. Reduced compliance costs will especially benefit SMEs, because these are disproportionately high under current settings.

70. IR and Callaghan Innovation (now MBIE) have already been working through operational changes to reduce the compliance burden. Current and additional operational enhancements could be progressed to further reduce the compliance burden include:

a. The General Approval application process

i. Allowing multiple small projects to be consolidated into a single application, reducing the compliance burden for firms applying through the General Approvals pathway.

ii. Reorienting a portion of free Government advisory services to provide early intervention targeted at SMEs, reducing the compliance burden and supporting SME access.

iii. Developing an AI prompt resources to guide businesses through applications, reducing the compliance burden for all businesses.

b. **The claims process**

i. Removing the requirement for a breakdown of expenditure by core and supporting activities, reducing the compliance burden for businesses.

ii. Extending free Government advisory services to provide post-application support, reducing the compliance burden and supporting SME access.

iii. Improving quality assurance processes and guidance for Requests for Information, reducing the compliance burden and promoting transparency and integrity.

c. **The Approved Research Provider (ARP) programme**

i. Upskilling ARPs to support businesses through applications, reducing the compliance burden for businesses.

ii. Promoting greater awareness of the ARP programme, improving SME access to the RDTI.

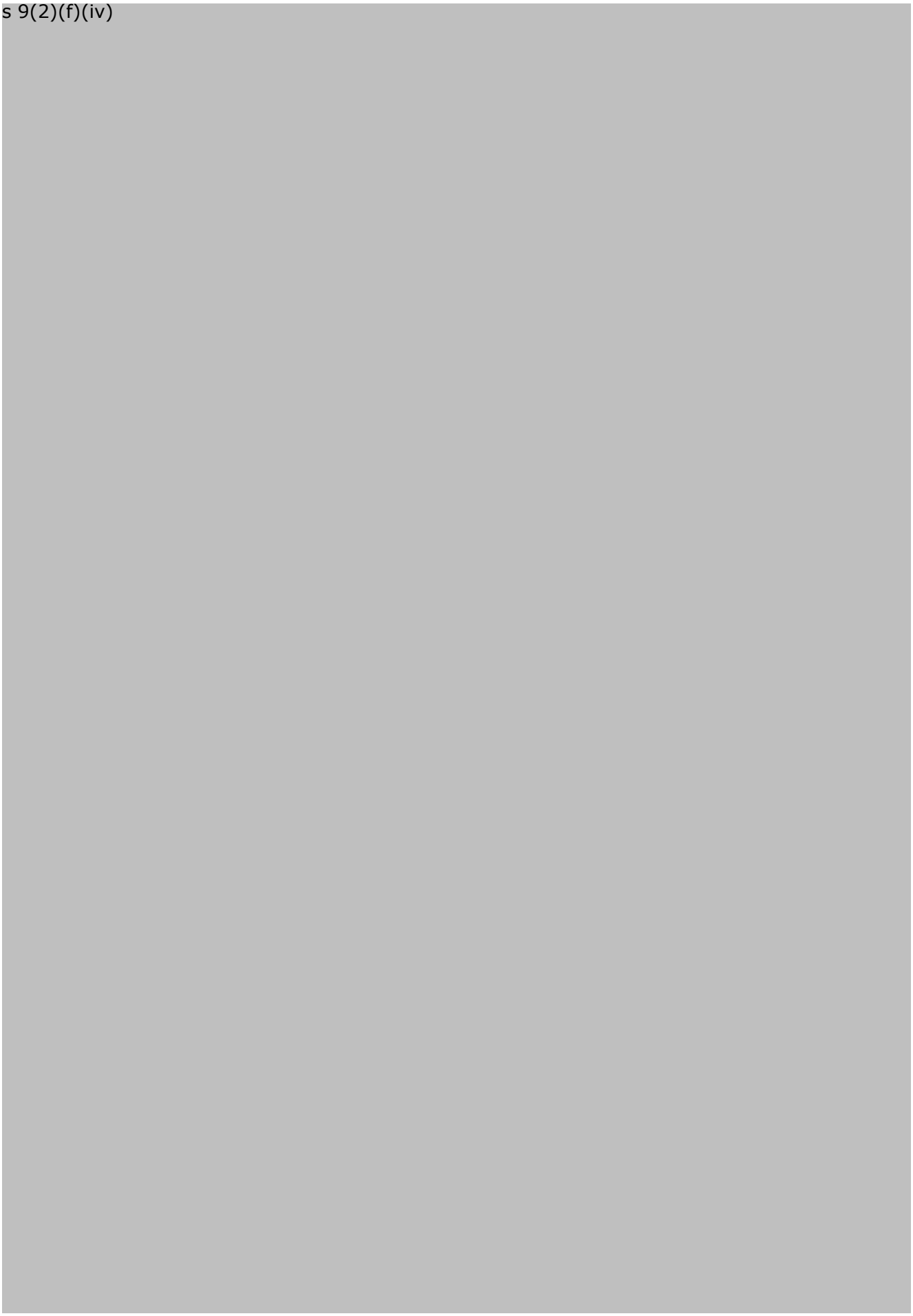
iii. Reviewing the eligibility criteria and status of current ARPs, ensuring ARPs can deliver eligible R&D activities.

71. These improvements would leverage existing business support services and established operational processes, ensuring efficient and cost-effective implementation, with minimal need for additional departmental appropriations. Details of these operational enhancements can be found in **Annex Four**.

Minister of Science, Innovation and Technology	*Minister of Revenue*
18. **Note** officials will continue consider and deliver operational improvements to the RDTI, focussing on the General Approval application process, the claims process and the Approved Research Provider programme.	
Noted	*Noted*

s 9(2)(f)(iv)

[redacted]


s 9(2)(f)(iv)

s 9(2)(f)(iv)



Next steps

85. For options where you agree to receive further advice, we will refine costings and report back to you in December 2025 with a refined package of options to progress through the Budget 2026 process.

Annexes

Annex One: Pain points identified in the scheme – customer journey

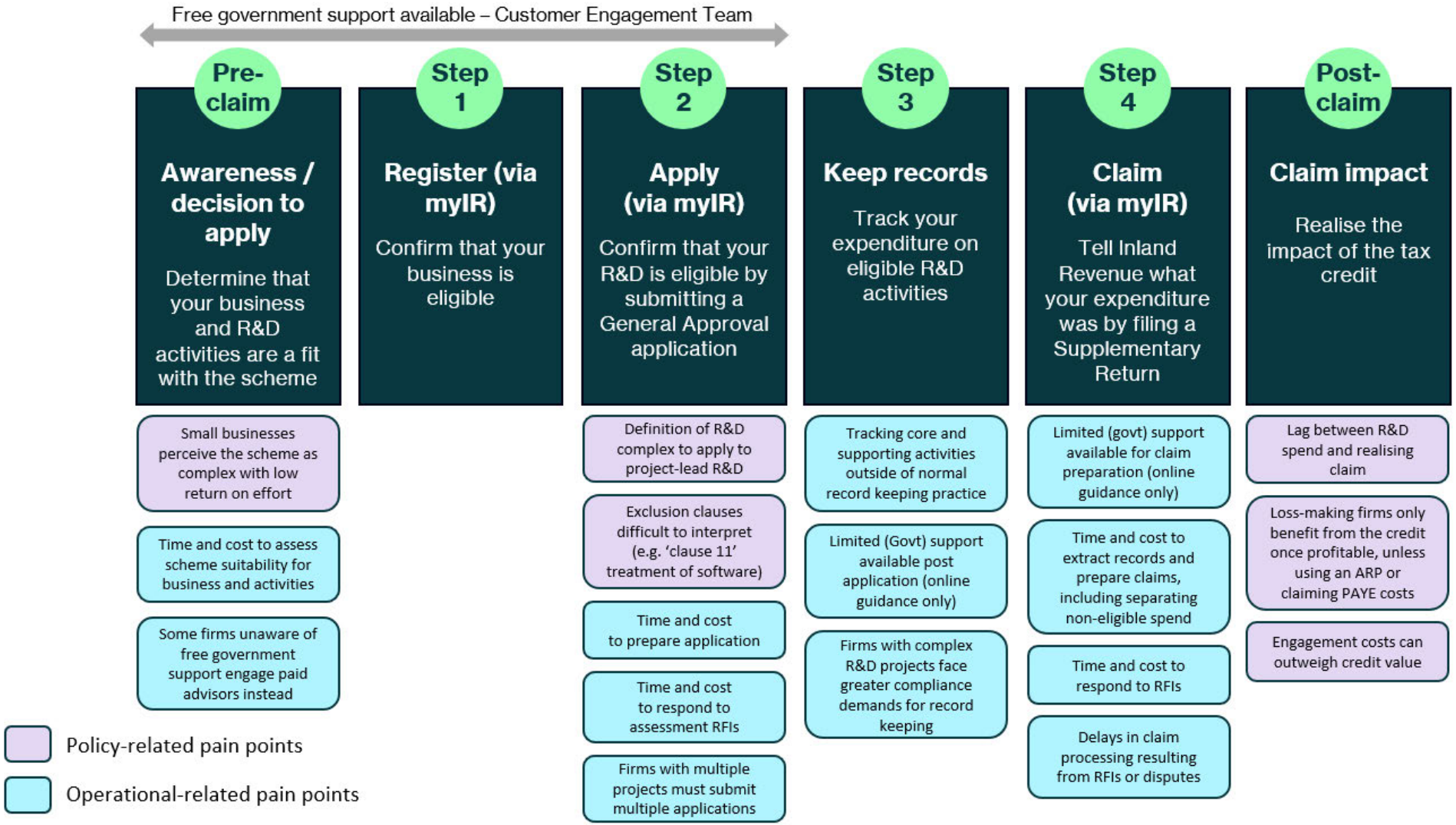
Annex Two: Opportunities to enhance policy settings

Annex Three: Options considered for key policy settings

Annex Four: Operational enhancements

Annex Five: Interactions of the N2RD grant, R&D Loss Tax Credit and the RDTI

Annex One: Pain points identified in the scheme – customer journey



**A number of pain points that present as operational-related may have their root cause in the policy settings*

Annex Two: Opportunities to enhance policy settings

RDTI setting	Option 1	Option 2	Option 3
Non-administrative internal software development	***Status quo*** Internal administration software development is excluded. Non-administrative internal software development is eligible but capped at $25 million, while external software development remains fully eligible with no cap. Note: 'Non-administrative internal software development' refers to software developed for both internal and external purposes. For example, a smart inventory system that speeds up customer deliveries while also improving internal operations qualifies as 'non-administrative internal software development' due to its dual internal and external purpose.	***Reduce the eligible expenditure cap from $25 million to $3 million:*** A $3 million cap balances support for SMEs, fiscal savings, and reduced administration costs and delays. It discourages low-quality claims, aligns with international practice, and supports genuine R&D. While a cap reduction may disadvantage larger firms, the data shows that under a $3 million cap most businesses remain unaffected.	***Exclude all internal software from eligibility:*** Excluding internal software claims reduces integrity risks, administration and compliance costs, and saves around $30 million annually. While it may lower long-term R&D investment, other support like the RDLTC remains available for smaller software-focused firms.
Overseas expenditure	***Retain overseas expenditure settings [status quo]:*** This approach strikes a balance between the RDTI's policy intent — to encourage R&D activity within New Zealand — and the commercial realities of operating across borders. It supports New Zealand's international innovation connections while aligning with Ministers' goal of maintaining fiscal neutrality.	***Exclude overseas expenditure from the RDTI:*** This option delivers some fiscal, compliance, and administrative savings. However, it reduces support for affected firms — likely large R&D spenders — and may have wider economic impacts, as it may see some businesses relocate significant portions of their R&D programmes overseas. If SMEs are affected, it could undermine efforts to improve RDTI access for small businesses.	

Annex Three: Options considered for key policy settings

RDTI setting	Option 1 [preferred]	Option 2	Option 3
Credit rate	***Status quo*** A flat 15% tax credit on eligible R&D expenditure. This is the preferred option given Ministers' objectives. It is fiscally neutral, supports business confidence, and delivers broader economic benefits. Officials are continuing to improve forecast accuracy for the appropriation.	***Decrease the flat rate*** Decreasing the RDTI rate could help achieve your fiscal objectives. However, this option would decrease the benefit of the scheme for SMEs, thereby reducing take-up. Further, decreasing the rate of the RDTI would negatively impact on New Zealand's productivity in two ways: 1. Less R&D activity in New Zealand reduces spillover benefits. 2. Policy instability, like rate changes, weakens long-term business confidence and investment. The Motu evaluation found the RDTI is effective in stimulating business R&D. Reducing the RDTI rate could lead to lower innovation and investment, undermining the Government's economic objectives. Further modelling is needed to understand the impact on additional R&D generated. Any fiscal savings from a lower rate are likely to be offset by reduced benefits to the wider economy.	***Tiered rate*** A tiered RDTI rate could improve access for small businesses by increasing RDTI credits relative to compliance costs. The evaluation considered a 20% rate on the first $300,000 of eligible spend. While this could boost support for small firms, most benefits would go to larger firms, with little impact on marginal R&D investment. Alternative structures could include: 1. Higher rate for SMEs, lower rate for large firms. Could better reflect access costs and target support where impact is greatest. However, may incentivise gaming and increase administrative complexity due to firm size verification, creating integrity risks. 2. Additional incentive to firms above an R&D intensity threshold. Targets support to firms prioritising R&D, benefiting small businesses and start-ups. May disadvantage capital-intensive or low-margin industries. Premium rates would increase upfront costs and administrative burden but offer more targeted support for high R&D intensity firms or SMEs. Further modelling is needed to assess if these costs could be offset by lowering the base rate.
Min/Max threshold	***Status quo*** The minimum eligible R&D spend is $50,000 per year (waived for ARP use); the maximum eligible R&D spend is $120 million. Ensures stability for businesses. Enhancements to ARP, extended CES support, and reduced compliance costs may sufficiently assist low-expenditure firms without adjusting the threshold.	***Raise the minimum threshold:*** Raising the minimum threshold could reflect inflation and stakeholder views that RDTI is only worthwhile at $150,000–$500,000 annual spend. While this may improve integrity and reduce the administrative burden, it risks higher costs and excluding start-ups and SMEs — especially if ARP uptake remains low.	**Option 3a. Remove the minimum threshold** Removing the minimum threshold entirely, improving access for micro-firms and start-ups conducting in-house R&D. This could increase uptake but would likely result in a surge of low-value claims, placing pressure on IR's administrative capacity and potentially undermining scheme integrity. **Option 3b. Reduce the maximum threshold:** This could deliver fiscal savings but the impact would fall on a small number of large R&D performers, potentially discouraging investment and encouraging offshoring. Removing the ability to exceed the cap would also conflict with the scheme's core objective of lifting business expenditure on R&D.
Refundability	***Status quo*** Refunds are available for loss-making firms or those with excess RDTI credits, but capped by PAYE, FBT, and ESCT paid. We do not recommend changes to the current refundability settings. We consider that the status quo works for most businesses, and that the alternatives present considerable trade-offs for limited improvement.	***Cap based on R&D intensity*** This option would cap RDTI credits based on R&D intensity The simplest way to do this would be to set a threshold, above which a business could have its RDTI credits refunded. This option would target refundability to those most deserving of it. However, different measures of R&D intensity may favour different types of R&D performing firms. Modelling work would need to be undertaken to understand these impacts. Further, this option would create a boundary that creates a perverse incentive. For instance, firms might be disincentivised from growing, or restructure operations to make R&D appear as a larger share of turnover. Finally, though relatively easy to understand, this option would add complexity to compliance and administration.	***Tangible economic presence (TEP) test*** A TEP test would allow a business to confirm that it is real and so have its RDTI credit fully refunded. A TEP test would build on the current refundability cap to broaden refundability by adding alternative pathways that allow all genuine businesses to access refundability. Criteria to satisfy this test could include: • A firm has labour related taxes equal to or greater than their R&D tax credit claim. • A chartered accountant or practicing lawyer has certified that a business has a TEP. • IR completes a review (for example, checking the tax-paying history of a business, visiting a firm's website, confirming the identity of shareholders/directors). A TEP test could reduce fraud, but overseas experience suggests external certification may lack robustness. Requiring IR to conduct further checks could shift resources from R&D approvals to audits, increasing compliance costs. Businesses may choose the least burdensome option, but IR checks could still impose material costs. This approach may also raise fiscal costs by increasing RDTI credits paid out.

**CES = Customer Engagement Team (previously Callaghan Innovation, to be MBIE Te Whakatairanga Service Delivery (TWSD); **RFI = Request for Information; ***ARP = Approved Research Provider*

Annex Four: Operational enhancements

RDTI setting	Enhancements	Implementation	Ministerial Objectives		
			Reduce compliance burden	Improve access for small business	Target genuine R&D; promote integrity
General Approval (GA) application These changes are administratively feasible, require no legislative amendment, and directly address the most pressing pain points for applicants.	Allow multiple small projects to be consolidated into a single GA application.	System update — revise general approval application form (myIR)	Reduces compliance burden for firms with multiple R&D projects not suited to the Significant Performer pathway		
	Retarget free Government services to provide targeted, early intervention	CES*		Reduces compliance burden at application stage; improves costs-benefit ratio for small business	
	Develop AI prompt guide resource to assist business in structuring applications	CES	Reduces compliance burden at application stage for all businesses		
Core and Supporting Activities These changes will ease compliance costs, especially for small businesses with limited capacity to track detailed R&D costs	Remove requirement to itemise expenditure by core and supporting activities on Supplementary Returns	System update - revise supplementary return form (myIR)	Reduce compliance burden at claims stage for all businesses	Reduces compliance burden at claims stage; improves costs-benefit ratio for small business	
	Remove requirement to track spend (record keeping) with a core and supporting activities breakdown	Update record keeping guidance (IR)	Reduces record keeping compliance burden for all businesses	Reduces record keeping compliance burden; improves costs-benefit ratio for small business	
	Maintain core and supporting definitions in general approval application	No change			Continues to support genuine R&D; ensures integrity of the tax system
Claims In response to stakeholder feedback and the evaluation's findings, IR is considering operation changes to improve efficiency and transparency while maintaining integrity	Extend free Government services to post-application support to provide support and resources for filing of claims	CES		Reduces compliance burden at record keeping/claims stage	
	Improved training and QA processes for RFIs** to ensure consistency and proportionality.	IR			Transparency of expectations for claims promotes scheme integrity
	Clearer guidance for firms on common RFIs to reduce unnecessary back-and-forth.	IR core team (CES MBIE in support)	Reduces claims compliance burden for all businesses by reducing need for RFIs	Reduces compliance burden at claims stage for small businesses who are time and resource poor	
	myIR prompts to encourage submission of commonly requested documents upfront.	IR core team (CES MBIE in support)			
Approved Research Providers Despite the limited uptake, the provision is used by some firms to conduct their R&D. Removing the provision is likely to disproportionately negatively impact smaller firms	Upskill ARPs*** to reduce compliance burdens and build collaborative relationships via the regional business partner network.	CES		Improves access for small business <$50,000	
	Create awareness of ARP programme through use of campaigns, engagement & digital tools	CES			
	Review eligibility criteria; review status of current ARPs	IR			Ensures ARPs can deliver eligible R&D

**CES = Customer Engagement Team (previously Callaghan Innovation, to be MBIE Te Whakatairanga Service Delivery (TWSD); **RFI = Request for Information; ***ARP = Approved Research Provider*

Annex Five: Interactions of the N2RD grant, RDLTC and the RDTI

	N2RD – Claim 40% of R&D spend **Introduced in 2022** Still maturing	**RDTI - Claim 15% of spend** **Introduced in 2019** Still maturing and works well	**RDLTC - 28% of R&D spend.** **Introduced in 2016** Needs review/finessing
What is it?	The N2RD grant offers co-funding up to a maximum total combined cost of $1 million ($400,000) for two years. This covers costs associated with the first project and funding to build R&D skills and capabilities within the business, including support for applying for the RDTI in future.	The RDTI offers tax credits on eligible R&D expenditure and can be used to reduce the amount of income tax you pay. In some circumstances, you can receive a cash refund in place of a tax credit.	The RDLTC provides up to $2 million in annual cash support for early-stage R&D firms by converting tax losses into cash. These losses are cancelled, so firms reach profitability sooner but ultimately pay the same total tax.
Definitions of R&D	Uses the Frascati Manual (OECD standard definition). Definition can be difficult to satisfy given the breadth of R&D instruments that are covered.	Uses the Frascati Manual (OECD standard definition). Definition can be difficult to satisfy given the breadth of R&D instruments that are covered.	Uses the standard accounting definition of R&D. This definition is generally considered easier to satisfy than the Frascati Manual definition used in the RDTI.
What spend qualifies and how do you receive the credit?	The N2RD grant is available to both new and established businesses who spent less than $150,000 on R&D in the last three years and received less than $5,000 in Government support for that. Gives you two years of forward approval for regular payments. This is provided as a reimbursement of spend.	If you spend over $150,000 on R&D and don't qualify for the grant, you can claim the RDTI. The initial evaluation of your R&D activity is rigorous but gives you pre-approval for a list of R&D activities over the next three to four years. Once you receive are pre-approval you can then submit expenditure claims at the end of each tax year to receive tax credits or cash refunds.	There is a one stage approval process (there is no general approval stage for the RDLTC), making it less onerous to comply with. The RDLTC can be claimed on expenditure from the self-funded portion of co-funded Crown grants such as the N2RD grant. This same rule does not apply for the RDTI because "double dipping" is not allowed.

If you are new to R&D Note: -You <u>cannot</u> claim the N2RD grant and the RDTI together for the total of the funded + co-funded amount. -You <u>can</u> claim costs above this total amount under the RDTI*. -You <u>can</u> claim the RDLTC on the co-funded amount of the N2RD grant*. **Business and activity eligibility apply*	**Scenario 1 – Using the N2RD Grant** • You start out with $1 million total costs for an R&D project. • The N2RD grant will provide you with a reimbursement of up to $400,000 (40%) grant on eligible spend. • The grant is paid in reimbursements of 40% of eligible spend in each claim. • You must provide up to $600,000 (60%) of co-funding. • Total spend is $1 million, with up to $400,000 back to you.	**Scenario 2 – Using the N2RD + RDLTC** • You start out and spend $1 million and are in a loss-making position • The N2RD grant will provide you with a reimbursement of $400,000 on eligible spend. • The Grant is paid in reimbursements of 40% of eligible spend in each claim – you provide $600,000 of own money. • Of this amount, you are able to receive a cash out refund under the RDLTC of $168,000 (or 28% of $600,000). • Total spend is $1 million and total refund is $568,000 (56.8%).
If you are an established R&D firm Note: -You <u>can</u> claim the RDLTC and the RDTI for the same R&D activities* **Business and activity eligibility apply*	**Scenario 3 – Using the RDTI** • You do not qualify for the N2RD grant, but you are eligible for the RDTI • Your R&D project is $1 million. • You received the RDTI which is $150,000 (or 15%) refund. • Total you pay is $850,000. • You are not eligible for the RDLTC because you are in profit, or do not meet the business-related R&D intensity criteria.	**Scenario 4 – Using the RDTI + RDLTC** • You have $1 million R&D spend and are in a loss-making position • Your project is $1 million. • You receive 15% credit from the RDTI of $150,000*. • You can claim the RDLTC which is $280,000 (28%) cash out. Total potential refund combined is $430,000 (43%). *For loss making companies the RDTI credit refunds are available but capped by PAYE, FBT, and ESCT paid. If you aren't eligible for refundable RDTI credits in this scenario, the $150k credit would be carried forward until you are in profit.

[EXTERNAL IN-CONFIDENCE]

Reference	BN2025/452
Date	20/11/2025
To	Revenue Advisor, Minister of Revenue – Angela Graham Private Secretary, Minister of Revenue – Anna McGuinness
From	Callum Aldiss
Subject	RDTI: Information further to 6 November 2025 report

Purpose

1 In July 2025, the Minister of Revenue's office passed on ideas from the Minister for policy options to inform policy work on the Research and Development Tax Incentive (RDTI). This policy work resulted in a joint Inland Revenue/MBIE report sent to the Minister of Revenue and Minister of Science, Innovation and Technology on 6 November 2025 (BRIEFING-REQ-0019154; IR2025/376 refers)

2 At the meeting with the Minister of Revenue on 11 November 2025, the Minister requested that officials provide him with a table clarifying where his ideas are reflected in the report and how the options we have provided address them. This table is attached to this note (**Annex 1**).

3 We also provide a table that summarises the policy options outlined in the report, including trade-offs, approximate fiscal cost/savings and whether officials recommend further consideration (**Annex 2**).

4 The Minister also requested that officials provide him with information on the RDTI spend over the last five years (actual vs appropriation), whether this correlates with economic conditions, and to consider whether the underspend should be returned to the centre.

Information for Minister of Revenue on RDTI appropriation

5 The table below shows RDTI spend over the last five years versus the amount appropriated in each year (non-departmental only).

Financial Year of Forecast appropriation	Forecast appropriation	Actual spend
30 June 2019	$40 million	$23 million
30 June 2020	$213 million	$104 million
30 June 2021	$313 million	$154 million
30 June 2022	$420 million	$275 million
30 June 2023	$398 million	$344 million
30 June 2024	$461 million	Not available until April 2026
30 June 2025	$593 million	Not available until April 2027

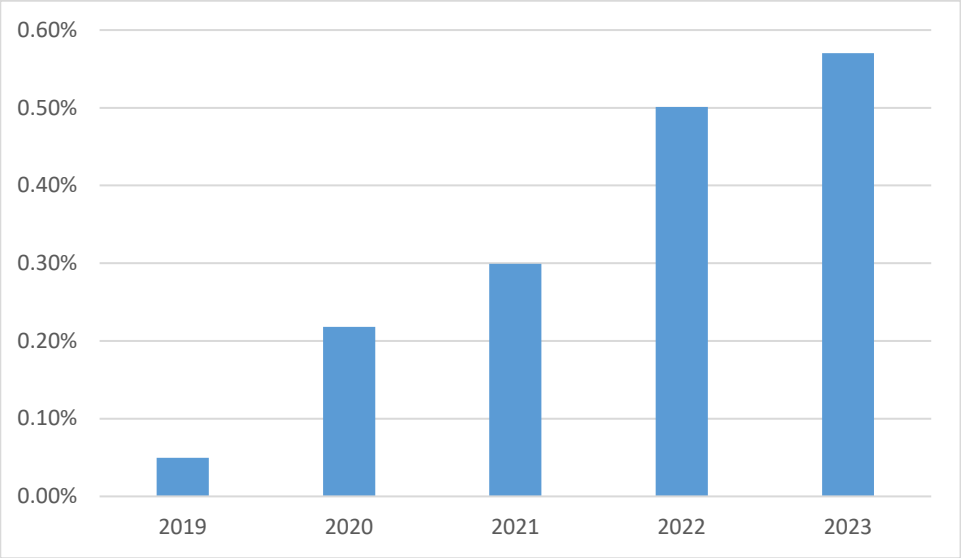
6 There is a long delay between the appropriation as forecasted and actual spend being finalised. This means the actual spend is not known until two years after the forecast, when the next tax year's RDTI claims are due.

7 The Minister also asked whether the actual spend correlates with economic conditions.

8 The forecast appropriation is informed by the Stats NZ R&D survey. This includes changes to gross domestic product (GDP) and business expenditure on R&D. The forecast assumes that all eligible businesses claim the RDTI for their R&D expenditure and receive the full credit.

9 There are not enough data points to determine whether there is a statistical correlation between actual RDTI spend and economic conditions. It is likely that the year-on-year increase also has to do with the scheme being relatively new. However, we have plotted actual RDTI spend against GDP below (noting that the five-year evaluation highlights more informative trends).

10 Figure 1. Eligible RDTI expenditure as a percentage of GDP



11 Finally, the Minister asked about the process for returning the underspend to the centre. When Inland Revenue is confident that all claims for a given year have been paid out, it returns the remaining appropriation to centre by offsetting it against the forecast appropriation for the current year.

Callum Aldiss

Senior Policy Advisor

s 9(2)(a)

Annex 1: Where Minister of Revenue's ideas are reflected in report

Minister of Revenue idea	How it is addressed in the report	Relevant paragraphs
Introduce intensity-based R&D tiering rate	We consider an option to base the RDTI's credit rate on R&D intensity.	Credit rate generally is dealt with in paragraphs 53–62, specifically basing the credit rate on R&D intensity is dealt with in paras 60–61.
Tighten definition of R&D for the purposes of the RDTI: • align definition of R&D with the definition in the OECD's Frascati manual • exclusions (eg, internal process improvements, repeat product testing).	The RDTI's definition of R&D is already based on the Frascati manual. In terms of further exclusions, we identify internal software development and overseas expenditure as viable activities to exclude. The report does not explicitly discuss internal process improvements and repeat product testing, but the former is likely ineligible (unless it can satisfy the main tests by resolving a scientific or technical uncertainty). Currently, pre-production, commercial production and routine testing activities are generally excluded from the RDTI.	• Paragraphs 11–12 discuss the RDTI's definition of R&D based on the Frascati manual. • Paragraphs 25–31 discuss excluding non-administrative internal software development expenditure. • Paragraphs 32–35 discuss excluding overseas expenditure.
Lifetime cap on RDTI credits	The report does not directly address this option. However, we did consider it as part of the options analysis. At a high level, Inland Revenue's analysis is: • Noting that the purpose of the RDTI is to incentivise additional R&D and associated spillovers, we do not consider there is sufficient rationale in this policy intent to distinguish between whether the R&D occurs in a company that has already claimed a certain amount or not. • Moreover, it would create a perverse incentive for firms to structure to maintain RDTI entitlement over time. For instance, a firm that has claimed its maximum	

	lifetime entitlement could wrap up the business and start a "new business" that is substantively the same.	

Administration simplification:
• Light touch pathways when:
  ○ RDTI claim under $x
  ○ certified past claim.
	The report considers various operational changes to reduce complexity. These relate to:
	• the approval process
	• the claims process
	• Approved Research Providers.
	
	The report does not specifically address the options for a simplified pathway for smaller R&D claims or on the basis of past compliance. However, the report discusses the experience of overseas R&D incentives with widespread fraud, which informed the status quo policy settings of the RDTI. This experience suggests that small R&D claims pose a significant fraud risk and loosening integrity mechanisms around claims poses significant fiscal, fraud and integrity risks.
		Operational changes to simplify RDTI application and claims process set out in paragraph 70 (further detail on these options in Annex Four).
		
		Paragraphs 13–17 discuss the policy background current integrity mechanisms, in particular the two-stage approval and claim process.

Refundability cap based on R&D intensity	We consider an option to base the refundability of RDTI credits on R&D intensity.	Paragraphs 66–68 (further detail on options in Annex Three).

Annex 2: Summary of options

Option	Trade-offs	Approx. fiscal cost/saving per annum (based on recent claim data)	Do officials recommend further advice?
Internal software development expenditure			
Reduce the eligible expenditure cap from $25 million to $3 million	• $3 million cap balances support for SMEs, fiscal savings, and reduced administration costs and delays. • A cap reduction may disadvantage larger firms, but the data shows that most businesses would be unaffected by a $3 million cap.	$16.5 million based on RDTI credits paid out in the 2023–24 income year claims	Consider further
Exclude all internal software	• Internal software development tends to generate limited or no spillovers; excluding it from the RDTI would likely increase impact per dollar spent on the RDTI. • Excluding internal software claims reduces integrity risks, administration and compliance costs, and maximises fiscal savings. • While it may lower long-term R&D investment, other support like the R&D Loss Tax Credit remains available for smaller software-focused firms.	$31.5 million based on RDTI credits paid out in the 2023–24 income year claims	Consider further
Overseas expenditure			
Exclude overseas expenditure from the RDTI	• Delivers fiscal, compliance, and administrative savings. • Improves value for money by ensuring support is only provided for economic activities that have a direct benefit within New Zealand. • Reduces support for affected firms (disproportionately large R&D spenders). • May have wider economic impacts. • To the extent that SMEs are affected, it could undermine efforts to improve RDTI access for small businesses	$12.0 million based on RDTI credits paid out in the 2023–24 income year claims	Consider further
In-year payments			
Deliver in-year payments of the RDTI through the tax system Businesses face a significant delay between incurring R&D expenditure and receiving the RDTI.	• Providing in-year payments of the RDTI supports cashflow, especially benefiting SMEs and start-ups. • Supported by several stakeholders in recent consultation. • Applying the refundability cap to in-year payments could be considered to protect the integrity of the tax system, although not applying the cap would ensure SMEs can fully access the benefit. • Delivering in-year payments would be complex and resource-intensive for Inland Revenue, requiring prioritisation against delivering other Government's priorities.	($2.1 million)	Inland Revenue recommends against the in-year payments proposal in favour of implementing the Government's already stated tax system priorities.
Mining exclusions			
Relax mining exclusions To mitigate fiscal risk, only labour costs and the cost of R&D prototypes can be claimed by mining businesses. This disadvantages the sector compared to other industries. The proposal would relax the exclusions broadly in line with other industries.	• Brings the eligibility criteria for the sector in-line with the sector-agnostic design of the RDTI scheme. • Does not address your stated objectives or most of the stakeholder feedback. • Only increases the incentive for a narrow segment of R&D performing businesses.	($0.4 million)	Consider further

Commissioner of Inland Revenue discretion to accept/amend late RDTI filings			
Grant Commissioner of Inland Revenue (CIR) discretion RDTI filing cannot be accepted/amended after the due date. This can result in a firm being denied its RDTI credit. Proposal would allow the CIR discretion to accept/amend in certain circumstances.	• Stakeholders suggest this proposal would reduce the compliance cost of quality assurance for claims and remove a potential disincentive to take-up of RDTI for firms that are denied a credit due to incorrect/late filing. • Limited impact due to the small number of affected firms. • Overall, unlikely to meaningfully address your objectives. Not raised by many stakeholders.	($2.5 million)	Consider further
Credit rate			
Decrease the flat rate	• Decreasing the RDTI credit rate could help achieve your fiscal objectives. • However, this option would decrease the benefit of the scheme for SMEs, thereby reducing take-up. • Further, decreasing the rate of the RDTI would negatively impact on additional R&D and spillovers generated by the scheme and risks creating the perception of policy instability.	Reducing the rate to 12.5% could result in $48 million fewer RDTI credits paid out per annum.	No
Tiered rate based on firm size Higher rate for SMEs, lower for large firms	• Could better reflect access costs and target support where impact is greatest. • However, may incentivise gaming and increase administration complexity due to firm size verification, creating integrity risks. • This “cliff-edge” effect can be mitigated by providing a higher subsidy rate up to a certain level of R&D expenditure and a lower rate for expenditure above that level of expenditure. • This approach generally delivers poor value for money because it provides a higher subsidy for a baseline level of R&D expenditure and a lower subsidy for additional.	Reducing the rate to 12.5% for each dollar of expenditure above $300,000 could result in $40 million fewer RDTI credits paid per year.	No
Tiered rate based on R&D intensity Additional incentive to firms above an R&D intensity threshold	• Additional incentive to firms above an R&D intensity threshold. • Targets support to firms prioritising R&D, benefiting small businesses and start-ups. • Perverse incentive to maximise R&D intensity (eg, disincentivises firms from growing commercial or non-R&D operations). • Adds complexity.	Not currently costed because there are a range of policy design settings that could be considered. Options could be structured to generate fiscal savings.	No
Targeting certain kinds of R&D Provide higher rates to certain kinds of R&D (for example, R&D in sectors or technologies that align with Government priorities).	• We do not consider the RDTI an appropriate tool for targeting specific types of R&D. • If more targeted support is desirable, grant schemes with higher accountability would be more appropriate	Not currently costed because there are a range of policy design settings that could be considered. Options could be structured to generate fiscal savings.	No
Minimum/maximum expenditure thresholds			
Raise the minimum threshold	• Raising the minimum threshold could reflect inflation and stakeholder views that RDTI is only worthwhile at $150,000 to $500,000 annual spend. • While this may improve integrity and reduce the administration burden, it risks excluding start-ups and SMEs, especially if Approved Research Provider uptake remains low.	Not currently costed because there are a range of policy design settings that could be considered. Options likely to generate fiscal savings.	No
Reduce the maximum threshold	• Could deliver fiscal savings but the impact would fall on a small number of large R&D performers. • Removing the ability to exceed the cap would also conflict with the scheme’s core objective of lifting business expenditure on R&D.	Not currently costed because there are a range of policy design settings that could be considered. Options likely to generate fiscal savings.	No

Refundability			
Refundability cap based on R&D intensity Target refundability of RDTI credits at firms that proportionately invest more in R&D.	• Refundability settings are primarily about reducing fraud risk. PAYE is a good indicator of genuine business activity. Self-assessed R&D intensity does not correspond with reduced fraud risk. • Creates perverse incentives (eg, firms might be disincentivised from growing, or restructure operations to make R&D appear as a larger share of turnover). • This option would add complexity to compliance and administration.	Not currently costed because there are a range of policy design settings that could be considered. Options likely to reduce the amount of RDTI credits that are refunded in a given year.	No
Tangible economic presence (TEP) test A TEP test would build on the current refundability cap to broaden refundability by adding alternative pathways that allow all genuine businesses to access refundability. Criteria to satisfy this test could include: 1. A firm has labour-related taxes equal to or greater than their RDTI claim. 2. A chartered accountant or practicing lawyer has certified that a business has a TEP. 3. Inland Revenue completes a review.	• A TEP test could reduce fraud, but overseas experience suggests external certification may lack robustness. • Requiring Inland Revenue to conduct further checks could shift resources from R&D approvals to audits. Further checks would also increase compliance costs. • Businesses may choose the least burdensome option, but Inland Revenue checks could still impose material costs. • This approach may also raise fiscal costs by increasing credits paid out.	Not currently costed because there are a range of policy design settings that could be considered. Options likely to increase the amount of RDTI credits that are refunded in a given year.	No

Briefing note

Reference	BN2025/482
Date	1/12/2025
To	Revenue Advisor, Minister of Revenue - Angela Graham Private Secretary, Minister of Revenue – Melissa Zhen
From	Claire McLellan
Subject	RDTI Ministers' Meeting

Purpose

1 This briefing note sets out additional comments on Inland Revenue's view on options regarding the eligibility of internal software development expenditure, and further information requested on the mining exclusions and the extending refundability.

2 Further, attached to this briefing note is an updated table summarising the options set out in the 6 November RDTI advice (IR2025/376; BRIEFING-REQ-0019154 refers) to support the Minister of Revenue at his meeting with Minister Reti on 3 December.

Internal software development expenditure

3 In our joint report on November 6, agencies identified non-administrative internal software development[1] as an area that could be reviewed to improve value for money and generate fiscal savings. Options presented were reducing the cap to $3 million or excluding all non-administrative internal software development. The Ministry of Business, Innovation and Employment (MBIE) have provided Minister of Science, Innovation and Technology more information on the policy option related to internal software development expenditure. We provide a brief comment on why Inland Revenue considers that making this expenditure ineligible for the RDTI may be one of the better ways to support Ministers' stated objectives.

4 Excluding all internal software development would narrow the eligible activities of RDTI, departing from broad-based principles of the scheme and removing support for the firms who receive support for this expenditure. However, we consider that excluding all internal software development would meet Ministers' stated objectives for the following reasons:

4.1 Internal software development is likely to generate lower spillovers compared to other forms of R&D.

4.2 Determining eligible internal software development has an outsized compliance and administration costs. Related to this are long-standing concerns that internal software development may be prone to reclassification of routine activities as R&D.

[1] Internal software development that is intended for the sole or main purpose of improving the internal administration of a business is excluded from the RDTI. Internal software development that is an integral part of a product being developed by a business is eligible for the RDTI ("non-administrative internal software development"). In practice, these rules seek to exclude internal software development that is likely to be routine business activity (such as running a payroll). Expenditure on non-administrative internal software development is capped at $25 million.

4.3 Inland Revenue considers operational changes are unlikely to materially reduce the burden of assessing eligibility, including changes to current guidance.

4.4 Reducing the cap on eligible expenditure to $3 million does not address the observation that this expenditure is less likely to generate spill overs. Further, it will only partially address the administrative and compliance cost issues identified. The cap is applied only after eligibility is determined, this means that any change to the cap will not impact on the process of determining eligibility; and, while reducing the cap will reduce the amount paid out in claims, we do not necessarily expect it would reduce the volume of claims.

Mining exclusions

5 You have asked for more information on the rationale behind the current mining exclusions. When the RDTI was enacted in 2019, the rules excluded various mining activities on the basis they were unlikely to be R&D. However, there was a concern that the tax regimes for mining may allow RDTI tax credits to be claimed on the upfront costs of assets used by miners. This was not intended and presented fiscal risk, so changes were made in 2021 to limit the eligibility of expenditures that could be incurred by petroleum and mineral miners (mining businesses).

6 While those amendments achieved their intent of preventing significant capital costs of assets used by mining businesses to be claimed, the current expenditure exclusions now disallow mining businesses RDTI tax credits for any expenditure other than labour-related costs and expenditure on prototypes used in R&D.

7 For example, a mining business may trial a new technology that better encourages liquids to rise to the surface of a well. The business would only be able to claim RDTI tax credits for the cost of labour in this trial. It could not claim for expenses like the cost of chemicals, the cost of parts used, the cost of other supporting activities, and overheads. All these expenditures could be claimed by a business undertaking R&D in another industry.

8 The proposal would allow a broader range of costs to be claimed by mining businesses undertaking R&D, including materials, overheads, and repairs and maintenance. The upfront costs of acquisition of assets and large capital expenditures on mining infrastructure would remain ineligible. As would the equivalent of depreciation loss for the mining businesses. This depreciation regime for mining is highly technical and allowing these costs would introduce compliance costs and complexity to the RDTI regime.

Refundability and tangible economic presence

9 You have asked for more information on extending refundability to businesses with little labour-related taxes who may be disadvantaged by the current refundability settings. PAYE is a strong proxy for real business activity because it reflects employment relationships and contributions to the tax system. However, firms with a high proportion of capital costs may not be able to get a large proportion of their credit refunded. Refundable credits support cashflow and are more valuable in present value terms compared to non-refundable credits which are carried forward without interest.

10 The challenge with another test is finding a simple and reliable indicator of tangible economic presence. One idea might be for Inland Revenue to undertake a special review of a firm, looking at whether it is procuring real goods and services for the purpose of R&D. We have not looked into the feasibility of this from an administration perspective yet, but it would likely have high administration costs. We can provide further advice on it if the Minister is interested.

Summary table of options for meeting with Minister Reti on 3 December

11 We have further updated the table summarising the options set out in the 6 November RDTI advice s 9(2)(f)(iv)

Consultation with the Treasury

12 The Treasury was informed about this briefing note.

Claire McLellan

Policy lead

s 9(2)(a)

Research and Development Tax Incentive: summary of options in November 6 advice

Option	Trade-offs	Approx. fiscal cost/saving per annum (based on recent claim data)	Do officials recommend further advice?
Internal software development expenditure			
Reduce the eligible expenditure cap from $25 million to $3 million	• $3 million cap balances support for SMEs, fiscal savings, and reduced administration costs and delays. • A cap reduction may disadvantage larger firms, but the data shows that most businesses would be unaffected by a $3 million cap.	$16.5 million based on RDTI credits paid out in the 2023–24 income year claims	Consider further
Exclude all internal software	• Internal software development tends to generate limited or no spillovers; excluding it from the RDTI would likely increase impact per dollar spent on the RDTI. • Excluding internal software claims reduces integrity risks, administration and compliance costs, and maximises fiscal savings. • While it may lower long-term R&D investment, other support like the R&D Loss Tax Credit remains available for smaller software-focused firms.	$31.5 million based on RDTI credits paid out in the 2023–24 income year claims	Consider further
Overseas expenditure			
Exclude overseas expenditure from the RDTI	• Delivers fiscal, compliance, and administrative savings. • Improves value for money by ensuring support is only provided for economic activities that have a direct benefit within New Zealand. • Reduces support for affected firms (disproportionately large R&D spenders). • May have wider economic impacts. • To the extent that SMEs are affected, it could undermine efforts to improve RDTI access for small businesses	$12.0 million based on RDTI credits paid out in the 2023–24 income year claims	Consider further
In-year payments			
Deliver in-year payments of the RDTI through the tax system Businesses face a significant delay between incurring R&D expenditure and receiving the RDTI.	• Providing in-year payments of the RDTI supports cashflow, especially benefiting SMEs and start-ups. • Supported by several stakeholders in recent consultation. • Applying the refundability cap to in-year payments could be considered to protect the integrity of the tax system, although not applying the cap would ensure SMEs can fully access the benefit. • Delivering in-year payments would be complex and resource-intensive for Inland Revenue, requiring prioritisation against delivering other Government's priorities.	($2.1 million)	Inland Revenue recommends against the in-year payments proposal in favour of implementing the Government's already stated tax system priorities.
Mining exclusions			
Relax mining exclusions To mitigate fiscal risk, only labour costs and the cost of R&D prototypes can be claimed by mining businesses. This disadvantages the sector compared to other industries. The proposal would relax the exclusions broadly in line with other industries.	• Brings the eligibility criteria for the sector in-line with the sector-agnostic design of the RDTI scheme. • Does not address your stated objectives or most of the stakeholder feedback. • Only increases the incentive for a narrow segment of R&D performing businesses.	($0.4 million)	Consider further

Commissioner of Inland Revenue discretion to accept/amend late RDTI filings			
Grant Commissioner of Inland Revenue (CIR) discretion RDTI filing cannot be accepted/amended after the due date. This can result in a firm being denied its RDTI credit. Proposal would allow the CIR discretion to accept/amend in certain circumstances.	• Stakeholders suggest this proposal would reduce the compliance cost of quality assurance for claims and remove a potential disincentive to take-up of RDTI for firms that are denied a credit due to incorrect/late filing. • Limited impact due to the small number of affected firms. • Overall, unlikely to meaningfully address your objectives. • Not raised by many stakeholders.	($2.5 million)	Consider further
Credit rate			
Decrease the flat rate	• Decreasing the RDTI credit rate could help achieve your fiscal objectives. • However, this option would decrease the benefit of the scheme for SMEs, thereby reducing take-up. • Further, decreasing the rate of the RDTI would negatively impact on additional R&D and spillovers generated by the scheme and risks creating the perception of policy instability.	Reducing the rate to 12.5% could result in $48 million fewer RDTI credits paid out per annum.	No
Tiered rate based on firm size Higher rate for SMEs, lower for large firms	• Could better reflect access costs and target support where impact is greatest. • However, may incentivise gaming and increase administration complexity due to firm size verification, creating integrity risks. • This “cliff-edge” effect can be mitigated by providing a higher subsidy rate up to a certain level of R&D expenditure and a lower rate for expenditure above that level of expenditure. • This approach generally delivers poor value for money because it provides a higher subsidy for a baseline level of R&D expenditure and a lower subsidy for additional.	Reducing the rate to 12.5% for each dollar of expenditure above $300,000 could result in $40 million fewer RDTI credits paid per year.	No
Tiered rate based on R&D intensity Additional incentive to firms above an R&D intensity threshold	• Additional incentive to firms above an R&D intensity threshold. • Targets support to firms prioritising R&D, benefiting small businesses and start-ups. • Perverse incentive to maximise R&D intensity (eg, disincentivises firms from growing commercial or non-R&D operations). • Adds complexity.	Not currently costed because there are a range of policy design settings that could be considered. Options could be structured to generate fiscal savings.	No
Targeting certain kinds of R&D Provide higher rates to certain kinds of R&D (for example, R&D in sectors or technologies that align with Government priorities).	• We do not consider the RDTI an appropriate tool for targeting specific types of R&D. • If more targeted support is desirable, grant schemes with higher accountability would be more appropriate	Not currently costed because there are a range of policy design settings that could be considered. Options could be structured to generate fiscal savings.	No
Minimum/maximum expenditure thresholds			
Raise the minimum threshold	• Raising the minimum threshold could reflect inflation and stakeholder views that RDTI is only worthwhile at $150,000 to $500,000 annual spend. • While this may improve integrity and reduce the administration burden, it risks excluding start-ups and SMEs, especially if Approved Research Provider uptake remains low.	Not currently costed because there are a range of policy design settings that could be considered. Options likely to generate fiscal savings.	No
Reduce the maximum threshold	• Could deliver fiscal savings but the impact would fall on a small number of large R&D performers. • Removing the ability to exceed the cap would also conflict with the scheme’s core objective of lifting business expenditure on R&D.	Not currently costed because there are a range of policy design settings that could be considered. Options likely to generate fiscal savings.	No

Refundability			
Refundability cap based on R&D intensity Target refundability of RDTI credits at firms that proportionately invest more in R&D.	• Refundability settings are primarily about reducing fraud risk. PAYE is a good indicator of genuine business activity. Self-assessed R&D intensity does not correspond with reduced fraud risk. • Creates perverse incentives (eg, firms might be disincentivised from growing, or restructure operations to make R&D appear as a larger share of turnover). • This option would add complexity to compliance and administration.	Not currently costed because there are a range of policy design settings that could be considered. Options likely to reduce the amount of RDTI credits that are refunded in a given year.	No
Tangible economic presence (TEP) test A TEP test would build on the current refundability cap to broaden refundability by adding alternative pathways that allow all genuine businesses to access refundability. Criteria to satisfy this test could include: 1. A firm has labour-related taxes equal to or greater than their RDTI claim. 2. A chartered accountant or practicing lawyer has certified that a business has a TEP. 3. Inland Revenue completes a review.	• A TEP test could reduce fraud, but overseas experience suggests external certification may lack robustness. • Requiring Inland Revenue to conduct further checks could shift resources from R&D approvals to audits. Further checks would also increase compliance costs. • Businesses may choose the least burdensome option, but Inland Revenue checks could still impose material costs. • This approach may also raise fiscal costs by increasing credits paid out.	Not currently costed because there are a range of policy design settings that could be considered. Options likely to increase the amount of RDTI credits that are refunded in a given year.	No
s 9(2)(f)(iv)			

MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

Inland Revenue
Te Tari Taake

BRIEFING

RDTI – Options to progress

Date:	10 December 2025	**Priority:**	High
Security classification:	Budget - Sensitive	**Tracking number:**	BRIEFING-REQ-0024980 IR2025/491

Action sought		
	Action sought	**Deadline**
Hon Dr Shane Reti **Minister of Science, Innovation and Technology**	**Agree** to recommendations	15 December 2025
Hon Simon Watts **Minister of Revenue**	**Agree** to recommendations	15 December 2025

Contact for telephone discussion (if required)			
Name	**Position**	**Telephone**	**1st contact**
Claire McLellan	Acting Policy Lead, Policy, IR	s 9(2)(a)	✓
Gina Williamson	Manager, Innovation Policy, MBIE		✓
Callum Aldiss	Senior Policy Advisor, Policy, IR		
Sarah Cordiner	Senior Policy Advisor, Innovation Policy, MBIE		

The following departments/agencies have been consulted
The Treasury

Minister's office to complete:

- ☐ Approved
- ☐ Noted
- ☐ Seen
- ☐ See Minister's Notes
- ☐ Declined
- ☐ Needs change
- ☐ Overtaken by Events
- ☐ Withdrawn

Comments

MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

BRIEFING

RDTI – Options to progress

Date:	10 December 2025	**Priority:**	High
Security classification:	Budget - Sensitive	**Tracking number:**	BRIEFING-REQ-0024980 IR2025/491

Purpose

To provide further information requested by Ministers in relation to the options previously presented for enhancements to the Research and Development Tax Incentive (RDTI) and to confirm your decisions as to which changes to settings you wish to progress.

Recommended action

The Ministry of Business, Innovation and Employment and Inland Revenue recommend that you:

i. **Indicate** in the table below which options you wish to progress:

Option	Minister of Science, Innovation and Technology	Minister of Revenue
a Retain the current internal software cap at $25 million of eligible expenditure, *or*	*Agree/Disagree*	*Agree/Disagree*
b Cap internal software at $3 million of eligible expenditure, *or*	*Agree/Disagree*	*Agree/Disagree*
c Exclude all internal software development expenditure from the RDTI	*Agree/Disagree*	*Agree/Disagree*
d Retain the 10% cap on overseas expenditure.	*Agree/Disagree*	*Agree/Disagree*
e Progress delivering in-year payments of the RDTI through the tax system.	*Agree/Disagree*	*Agree/Disagree*
f Relax mining exclusions to be more aligned with other industries.	*Agree/Disagree*	*Agree/Disagree*
g Progress with granting discretion to the Commissioner of Inland Revenue to accept and amend late filings.	*Agree/Disagree*	*Agree/Disagree*

ii. **Indicate** whether you would like to receive further advice on options s 9(2)(f)(iv)

Minister of Science, Innovation and Technology *Yes/No*

Minister of Revenue *Yes/No*

iii. **Note** that officials will progress operational improvements to the RDTI along the timelines indicated, subject to the cumulative impact of current and proposed initiatives, focussing on the General Approval application process, the claims process and the Approved Research Provider programme.

Minister of Science, Innovation and Technology *Noted*

Minister of Revenue *Noted*

s 9(2)(a)

Gina Williamson
Manager, Innovation Policy
Labour, Science and Enterprise, MBIE

10 / 12 / 2025

s 9(2)(a)

Claire McLellan
Acting Policy Lead
Policy, Inland Revenue

10 / 12 / 2025

Hon Dr Shane Reti
Minister of Science, Innovation and Technology

..... / ..... / .....

Hon Simon Watts
Minister of Revenue

..... / ..... / .....

Background

1. The Ministry of Business, Innovation and Employment (MBIE) and Inland Revenue were commissioned by Going for Growth Innovation, Technology and Science Ministers to provide advice on options for the RDTI that would:

    a. enhance the RDTI's "bang for buck",

    b. ensure the RDTI continues to support genuine R&D,

    c. reduce the compliance burden for businesses and improve access for small business, and,

    d. be fiscally neutral or positive.

2. We provided a joint briefing to Ministers on 6 November 2025 (BRIEFING- REQ-0019154 IR2025/376 refers) noting five settings that Ministers might consider changing to meet the above objectives. These were:

    a. Internal software,

    b. Overseas expenditure,

    c. In-year payments,

    d. Mining exclusions, and

    e. Commissioner of Inland Revenue Discretion.

3. Following Ministerial discussions on 1 and 3 December 2025, we understand Ministers may be considering retaining current settings for internal software and overseas expenditure, subject to ensuring the overall package of changes remains fiscally neutral. You also requested further information regarding in-year payments, mining exclusions and Commissioner of Inland Revenue discretion, including timeframes for implementation.

4. This briefing provides the additional information for the in-year payments, mining exclusions and Commissioner of Inland Revenue discretion settings at **Annex One** and seeks confirmation of your decisions as to what changes, if any, you want to progress.

Proposed policy changes

5. Ministers have previously received advice (including design options) on including a provision for in-year payments of the RDTI through the tax system, relaxing the mining exclusions in the RDTI and a discretionary power for the Commissioner of Inland Revenue to accept and amend late RDTI filings (IR2024/209 refers). Decision making was deferred to allow for the findings of the final five-year evaluation to be considered. These settings were raised by stakeholders in recent consultation as areas of the RDTI that could be improved.

6. The cost over the forecast period (2025/26 – 2029/30) of progressing these options are:

    a. In-year payments - $6.5 million, comprised of $3.1 million for 2026/27 and $1-1.2 million per annum thereafter.

    b. Relaxing mining exclusions - $1.75 million, comprised of $0.7 million for 2026/27 and $0.35 million per annum thereafter.

c. Commissioner of IR discretion - $10 million, comprised of $5 million for 2026/27, $2.5 million for 2027/28, and $1.25 million per annum thereafter.

7. Information regarding cost and implementation timeframes is presented in **Annex One**.

8. In total, progressing these three policy changes will cost $18.2 million total over the forecast period and would need to be offset by savings if you are to ensure that the RDTI options package is fiscally neutral or positive, consistent with the original commissioning from the ITS Ministers meeting.

9. You have three option packages to consider progressing:

   a. Retaining all current policy settings and not progressing proposals for in-year payments, relaxing mining exclusions or Commissioner of IR discretion (MBIE recommended);

   b. Progressing the proposals to relax the mining exclusions and the Commissioner of Inland Revenue discretion, offsetting the fiscal cost of these proposals through changes to internal software development or overseas expenditure settings (IR recommended);

   c. Seek permission from the Minister of Finance to submit a budget bit to progress the proposals for in-year payments, relaxing mining exclusions or Commissioner of IR discretion without cost offsetting.

10. The Minister of Finance has not invited a budget bid for the RDTI and the Minister of Revenue has reiterated the need for this package to be fiscally neutral.

11. The Treasury has advised that given the original commissioning, the current fiscal environment and the very high bar for new spending initiatives, it is unlikely that the RDTI would be invited to submit a budget bid for new spending at this stage of the budget process, unless the proposed spend could be offset with savings from elsewhere in the scheme.

12. Options for changes to settings that would generate savings over the forecast period (2025/26 – 2029/30) are:

   a. Internal software expenditure ($3m cap) - $99 million, comprised of $7 million for 2026/27, then approximately $30 million per annum thereafter.

   b. Internal software expenditure (excluded) - $183 million, comprised of $13 million for 2026/27, then approximately $50-60 million per annum thereafter.

   c. Overseas expenditure (excluded) - $65 million, comprised of $19 million for 2026/27, then approximately $20 million per annum thereafter.

13. These are formal costings based on the 2023 income year projected forward in proportion to the RDTI appropriation growth. They therefore differ from the indicative costings based on the 2024 income year presented in the November briefing (BRIEFING -REQ-0019154 IR2025/376 refers).

14. Details of savings over the forecast period are provided in **Annex Two**. We note that these savings are not necessarily additive. For example, if both savings options were progressed, the total savings may be slightly lower than forecast as some overseas expenditure might be for internal software expenditure.

15. Savings through exclusion of internal software or overseas expenditure can be progressed for the 2026-27 income year through the next Omnibus Tax Bill (August 2026) or budget night legislation. However, because these options reduce the credits available for

R&D firms, we recommend firms are given more time to adjust their R&D investment plans in response these changes. If you progressed these savings options, we recommend that they come into effect for the 2027-28 income year (one year following the new spending options outlined above). Delaying the savings options by a year still results in a fiscally neutral package over the forecast period.

Trade-offs regarding retaining or altering internal software and overseas expenditure settings

16. Administrative internal software, such as HR and payroll, is excluded from the RDTI as it is unlikely to produce wider economic benefits. Non-administrative internal software is eligible but is capped at $25 million to mitigate the risk of misclassification of routine development and acknowledge there are spill over benefits.

17. Excluding all internal software could increase the impact per dollar spent on the RDTI, and reduce administrative and compliance costs (due to the expenditure being ruled ineligible). However, MBIE is concerned this could adversely impact the level of R&D expenditure and the overall spillover benefits of the scheme and may not align with wider Going for Growth objectives, including a push for greater digitisation. Reducing the cap to $3 million - its original level before it was raised prior to introduction to the House in response to stakeholder feedback - would deliver fiscal savings while maintaining accessibility for SMEs.

18. Currently, businesses can claim up to 10 per cent of eligible expenditure for overseas activities that support eligible R&D activities in New Zealand. This balances support for domestic R&D with the reality that some expertise and resources may only be available overseas. However, the overseas expenditure allowance could be viewed to not directly support domestic R&D or generate spillovers in New Zealand. Overseas expenditure can also be difficulty to verify.

Operational enhancements

19. We previously informed you of operational enhancements that would also contribute meaningfully to achieving Ministers' objectives. Improvements to the General Approval application process, the claims process and the ARP programme can continue to reduce compliance burden (BRIEFING-REQ-0019154, IR2025/376 refers).

20. Implementation is subject to operational decisions and priorities, and must be balanced around processing of applications and claims. We note the peak processing times for both MBIE and IR assessors is from March to July.

21. An overview of when operational enhancements could be implemented is provided in **Annex Three.**

22. Agencies are identifying metrics that will help us measure progress of operational improvements and impact in reducing compliance burden and improving access for small businesses.

Consultation

23. The Treasury was consulted in the course of preparing this advice, and provided the comment below:

24. The Treasury notes that the original commission from ITS Ministers required any proposed improvements to the RDTI to be fiscally neutral or deliver savings. Advancing the proposed option set would incur a fiscal cost, which has not been invited into the Budget 2026 process. Given the challenging fiscal environment, there is a high bar for new spending invitations for Budget 26. The proposals outlined do not align with the Government's Budget

2026 spending priorities of addressing outstanding coalition commitments, providing critical and urgent funding to maintain core services, or supporting delivery-ready capital investments approved by Cabinet.

25. Should Ministers wish to proceed with these options, the Treasury recommends offsetting the costs through savings. Additionally, the Treasury advises keeping potential savings options for the RDTI under consideration (such as, s 9(2)(f)(iv) and adjustments to overseas and software expenditure) given the anticipated pressures on the Budget 26 operating allowance.

Next steps

26. For options you agree to progress, MBIE and Inland Revenue will provide design options for your agreement and work with The Treasury to progress options through Budget 2026.

Annexes

Annex One: Further information regarding in-year payments, mining exclusions and Commissioner of Inland Revenue discretion

Annex Two: Forecast savings from changes to internal software or overseas expenditure settings

Annex Three: Indicative timeline for operational enhancements

Annex One: Further information regarding in-year payments, mining exclusions and Commissioner of Inland Revenue discretion

In-year payments

1. Businesses can experience a significant delay between when they incur R&D expenditure and when they receive the associated tax credit. For example, a business that claims RDTI tax credits for the tax year ending 31 March 2026 and files close to all due dates, is likely to receive their credit in May 2027.

2. This mismatch can create cash flow challenges for businesses, particularly SMEs, loss-making businesses and pre-revenue start-ups. It has previously been hypothesised that the mismatch reduces take-up of the RDTI. In 2024, demographic data for the RDTI showed that uptake from businesses in profit has been broadly in line with expectations, but lower amongst businesses in tax loss positions.

3. The in-year payments initiative is intended to improve take-up amongst SMEs and loss-making businesses by providing a quarterly cash payment that is effectively an advance of the RDTI tax credit they expect to receive after the end of the relevant income year. This means that, instead of the tax credit being processed potentially a year after the end of the relevant income year, a business will be getting regular cash payments within the income year.

4. The Research and Development Loss tax Credit (RDLTC) currently exists to support loss making, R&D performing start-ups and SMEs. The RDLTC enables eligible firms to cash out their tax losses,[1] which supports the cashflow of these firms. However, it does not provide support for small profit-making R&D firms.

Integrity and over-payment risk

5. Because in-year payments would disburse RDTI credits before the final entitlement has been approved, there is a risk of paying businesses RDTI credits which they are not entitled to. This risk is exacerbated if certain integrity features, such as the current refundability cap based on labour-related taxes, are not applied to in-year payments. On average, IR reduces amounts claimed by around 5 per cent. However, around ten per cent of firms have their claim reduced by more than twenty per cent. In the 2023-24 tax year, Inland Revenue disallowed $17 million of RDTI credits.

6. The risk of overpayments is an inherent trade-off of making RDTI payments in advance of the claim being finalised. However, if you decide to proceed with this proposal, we will provide you with advice on detailed design settings, including options to mitigate integrity and overpayment risk.

Implementation of in-year payments

7. Introduction of in-year payments will require legislation, which could be enacted by April 2027 in the 2026-27 Taxation Omnibus Bill. The first in-year payments would be available from October 2027 for the 2027-28 income year. Taxpayers with standard balance dates would get payments for first two quarters in October and then once every quarter after that. Taxpayers with early balance dates would receive their first in-year payment in the following quarter.

8. The cost, system development effort, and complexity to build, test, and implement this initiative is relatively large. This initiative will reduce Inland Revenue's change capacity, and resourcing

[1] Eligible expenditure for a given income year is the lesser of a firm's net loss, total R&D spend for the year or 1.5 times its R&D labour costs; this amount is then capped at $2 million.

this initiative will need to be considered when thinking about Inland Revenue's ability to deliver other or new Government priorities.

Fiscal implications

9. The delivery of in-year payments has already been built into RDTI forecasts because those forecasts assume that all eligible businesses will take up the RDTI. This means there are no non-departmental fiscal implications.

10. Implementing and administering RDTI in-year payments would have a $6.500 million departmental cost for which Inland Revenue would need to seek funding through Budget 2026. This cost includes $2.100 million capital and $0.900 million operating for one-off system and process changes, and $3.500 million operating over the forecast period (2025/26 to 2029/30) for administration costs, depreciation, and capital charge, as shown below:

	$m – increase/(decrease)				
In-year payments	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
One-off operating Administration	- -	0.900 0.100	- 1.000	- 1.200	- 1.200
Total operating	**-**	**1.000**	**1.000**	**1.200**	**1.200**
One-off capital -	-	2.100	-	-	-
Total capital expenditure	-	**2.100**	-	-	-

Relaxing the exclusions for mining R&D

11. In 2021, changes were made to the RDTI to limit the eligibility of expenditures that could be incurred by petroleum and mineral miners (mining businesses). This was due to concerns that the tax regimes for mining may have allowed RDTI credits to be claimed on the upfront costs of assets used by mining businesses. This outcome was both unintended and presented fiscal risk.

12. While those amendments achieved their intent, we consider they tightened eligibility too far. Currently, mining businesses cannot claim RDTI tax credits for any expenditure other than labour related costs and expenditure on prototypes used in R&D. This means that most types of R&D expenditures incurred by mining businesses are ineligible for the RDTI. If such expenditure met all other legislative requirements, it would constitute expenditure that would otherwise be eligible for the RDTI but for the mining exclusions.

13. Previous advice recommended relaxing the RDTI mining exclusions so that a broader range of costs can be claimed by mining businesses undertaking R&D including materials, overheads, and repairs and maintenance. The upfront costs of acquisition of assets and large capital expenditures on mining infrastructure would continue to be ineligible for the RDTI.

14. This change would bring eligibility criteria for the sector broadly in line with other industries. This constitutes a broadening of the RDTI's targeting, providing the incentive to a wider range of activities.

Implementation of relaxing mining exclusions

15. This change could be enacted by April 2027 and would apply to expenditure in the 2026-27 income year. Relaxing the mining exclusions will lead to more RDTI tax credits being paid than

would otherwise be the case. The fiscal cost of this change is $1.75 million over the forecast period, as shown below:

	$m – increase/(decrease)				
Vote Revenue Minister of Science, Innovation and Technology	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-departmental Other Expenses: Science, Innovation and Technology: R&D Tax Incentive	0.000	0.700	0.350	0.350	0.350
Total Operating	**0.000**	**0.700**	**0.350**	**0.350**	**0.350**

Commissioner of Inland Revenue discretion

16. Under current law, RDTI applications and returns cannot be accepted or amended once the filing deadline has passed. This could result in a business being denied its RDTI credit for the relevant income year even due to relatively minor errors such as editorial errors or missing filing deadlines due to illness (relevant for small businesses with fewer staff). These settings are unusual as most other parts of the tax system allow for late filing (albeit with interest and penalties).

17. In these cases, RDTI tax credits are not withheld for reasons that improve the scheme's integrity, but instead in a way that reduces its effectiveness as an incentive. Allowing businesses that experience these types of events (and consequently miss an RDTI filing due date) the ability to have their filing processed would be more consistent with the policy intent of the RDTI.

18. Businesses would apply to the Commissioner of Inland Revenue (the Commissioner) to exercise the discretion. The Commissioner would consider the facts of each case and decide if it is appropriate to do so.

Implementation of Commissioner discretion

19. This change could be enacted by April 2027 and would apply for the 2026-27 income year. However, we recommend that this amendment also apply for RDTI filings already submitted for prior years. This would allow existing cases where RDTI tax credits have been denied (or are in review) to be processed where the Commissioner considers it is appropriate to do so.

20. Introducing a discretion for the Commissioner to accept and amend late RDTI filings will lead to more RDTI tax credits being paid than would otherwise be the case, including for cases on hand. The fiscal cost of this change is $10 million over the forecast period, as shown below:

	$m – increase/(decrease)				
Vote Revenue Minister of Science, Innovation and Technology	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Non-departmental Other Expenses: Science, Innovation and Technology: R&D Tax Incentive	0.000	5.000	2.500	1.250	1.250
Total Operating	**0.000**	**5.000**	**2.500**	**1.250**	**1.250**

Annex Two: Forecast savings from changes to internal software or overseas expenditure settings

We note that these savings tables are not necessarily additive. For example, if both options were progressed, there might be a small scaling down of the savings because some overseas expenditure will be internal software expenditure.

Reducing cap for internal software to $3 million

	$m - increase/(decrease)				
Vote Revenue **Minister of Science, Innovation and Technology**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30**
Non-departmental Other Expenses: Science, Innovation and Technology: R&D tax incentive – Software expenditure ($3m cap)	-	(7.000)	(29.000)	(29.000)	(34.000)
Total Operating	**-**	**(7.000)**	**(29.000)**	**(29.000)**	**(34.000)**

Excluding all internal software

	$m - increase/(decrease)				
Vote Revenue **Minister of Science, Innovation and Technology**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30**
Non-departmental Other Expenses: Science, Innovation and Technology: R&D tax incentive – Software expenditure	-	(13.000)	(55.000)	(53.000)	(62.000)
Total Operating	**-**	**(13.000)**	**(55.000)**	**(53.000)**	**(62.000)**

Excluding overseas expenditure

	$m - increase/(decrease)				
Vote Revenue **Minister of Science, Innovation and Technology**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30**
Non-departmental Other Expenses: Science, Innovation and Technology: R&D tax incentive – Offshore expenditure	-	(5.000)	(19.000)	(19.000)	(22.000)
Total Operating	**-**	**(5.000)**	**(19.000)**	**(19.000)**	**(22.000)**

Annex Three: Indicative timeline for operational enhancements

Aspect of scheme	Enhancement	Purpose	Status	Estimated time to implement
The General Approval application process	Allow multiple small projects to be filed as a single application.	Reduce the compliance burden for firms applying through the General Approvals pathway.	Phase one: Customer tool - In progress	6-12 months
	Reorient a portion of free Government advisory services to provide early intervention targeted at SMEs.	Reduce the compliance burden and supporting SME access.	In progress	Ongoing improvement
	Develop an AI prompt resource to guide businesses through applications.	Reduce the compliance burden for all businesses.	In progress	3-6 months
The Claims process	Remove the requirement for a breakdown of expenditure by core and supporting activities.	Reduce the compliance burden for businesses.	Scoping	6-12 months
	Extend free Government advisory services to provide post-application support.	Reduce the compliance burden and supporting SME access.	Scoping	6-12 months
	Improve quality assurance processes and guidance for Requests for Information.	Reduce the compliance burden and promoting transparency and integrity.	In progress	Ongoing improvement
The Approved Research Provider (ARP) programme	Review the eligibility criteria and status of current ARPs	Promote integrity ensuring ARPs can deliver eligible R&D activities.	To start Q1 2026	6 months
	Upskill ARPs to support businesses through applications.	Reduce the compliance burden for businesses.	Pending review of ARPs	6-12 months
	Promote greater awareness of the ARP programme	Improve SME access to the RDTI.	Pending review of ARPs	Ongoing improvement

Tax policy report

MINISTRY OF SOCIAL DEVELOPMENT
TE MANATŪ WHAKAHIATO ORA

Inland Revenue
Te Tari Taake

RDTI options for Budget 2026

Date	18 February 2026	**Priority**	Medium
Security level	Budget sensitive	**Report number**	IR2026/040 BRIEFING-REQ-0027276

Action sought		**Deadline**
Minister of Science, Innovation and Technology	**Note** options agencies recommend to deliver savings and enhance the RDTI s 9(2)(f)(iv) **Refer** this report to the Minister of Finance	20 February 2026
Minister of Finance	**Agree** to initiatives to invite into Budget 2026	26 February 2026
Minister of Revenue	**Note** options agencies recommend to deliver savings and enhance the RDTI s 9(2)(f)(iv)	26 February 2026

Purpose
This report provides a summary of savings and spending options related to the Research and Development Tax Incentive (RDTI) s 9(2)(f)(iv) for consideration in Budget 2026.

Contact for phone discussion, if required			
Name	**Position**	**Phone number**	**First contact**
Michael Contaldo	Manager, Innovation Policy, MBIE	s 9(2)(a)	✓
Claire McLellan	Acting Policy Lead, Policy, IR		✓
Sarah Cordiner	Senior Policy Advisor, Innovation Policy, MBIE		
Adam Carter	Senior Policy Advisor, Policy, IR		

RDTI options for Budget 2026

Executive summary

1. On 9 February 2025, the Minister of Finance wrote to the Minister of Science, Innovation and Technology and the Minister of Revenue requesting officials provide advice on options to maximise savings from the Research and Development Tax Incentive (RDTI) s 9(2)(f)(iv) for Budget 2026, and the trade-offs associated with those options. Specifically, the Minister requested advice by 20 February on:
   a. Internal software expenditure ($3m cap) – saving $99 million over the 2026-2030 forecast period
   b. Internal software expenditure (excluded) – saving $183 million over the 2026-2030 forecast period
   c. Overseas expenditure (excluded) – saving $65 million over the 2026-2030 forecast period
2. s 9(2)(f)(iv)
3. Policy changes to achieve fiscal savings will require trade-offs against impacts to business expenditure on R&D, the wider economy, and business certainty.
4. Internal software expenditure is expected to generate lower spillovers than other R&D. It also incurs relatively higher administrative cost for agencies and compliance costs for businesses than other R&D expenditure categories. Inland Revenue recommends excluding it from the RDTI, while MBIE recommends retaining the current settings.
5. Businesses value being able to claim credits for internal software expenditure and there are a few firms with significant expenditure in this category. An alternative to excluding all internal software expenditure is reducing the cap to $3 million. This would deliver fiscal savings while maintaining accessibility, particularly for SMEs.
6. Overseas R&D expenditure is another category of expenditure that may have fewer direct spillovers for New Zealand. However, while spillovers directly attributable to overseas expenditure may be lower than for domestic expenditure on R&D, this expenditure often enables access to specialised expertise not available domestically and supports firms to retain their broader R&D activity in New Zealand. Agencies do not recommend excluding this expenditure due to the risk of discouraging R&D location in New Zealand.
7. s 9(2)(f)(iv)
8. Savings from the RDTI could be returned to centre or used to fund improvements to the scheme. Subject to funding, the Minister of Science Innovation & Technology and the Minister of Revenue have previously agreed to progress three improvements to the RDTI:
   a. Discretion for the Commissioner of Inland Revenue to accept late or amended filings ($10 million of additional credits over the forecast period)

b. Progressing RDTI In-Year Payments through the tax system ($6.5 million in administrative costs over the forecast period, subject to design decisions which could make the scheme more or less favourable to businesses)

c. Relaxing mining exclusions ($1.75 million in additional credits over the forecast period)

9. These changes are intended to reduce compliance costs for businesses, improve cashflow (a concern raised by SMEs and start-ups during consultation), and strengthen trust in the scheme.

10. A programme of operational improvements is underway to reduce compliance burden for businesses. Further information is included as an annex to this report.

Background

11. In 2025, the first five-year evaluation of the RDTI was delivered (the evaluation).[1] The evaluation found that the scheme overall is functioning as intended and its broad economic impacts compare well with international benchmarks (REQ-0011218, IR2025/147 refers). Specifically:

a. The RDTI has had a positive impact on R&D expenditure, with a 'bang for buck' of $1.40 for every dollar invested, in line with other OECD countries.

b. The economic return is between 2.1 and 6.3 times the amount invested.

c. While there are mixed stakeholder views on the appropriateness of the compliance costs, the scheme strikes an appropriate balance between minimising these costs for businesses and mitigating the risk of fraud.

d. Overall, the RDTI scheme is being administered effectively.

e. The evaluator did not observe anything to suggest that there was not compliance with the legal requirements.

12. Following the evaluation, Going for Growth: Innovation, Technology and Science (ITS) Ministers commissioned advice on fiscally positive or neutral options to enhance the RDTI, that also:

a. enhance the RDTI's "bang for buck",

b. ensure the RDTI continues to support genuine R&D, and

c. reduce the compliance burden for businesses and improve access for small businesses.

13. Officials provided a joint briefing to the Minister of Science, Innovation and Technology and the Minister of Revenue on 6 November 2025 (BRIEFING- REQ-0019154 IR2025/376 refers) on settings in the RDTI that Ministers might consider changing to meet the above objectives. Advice was informed by the evaluation and targeted stakeholder consultation.

14. s 9(2)(f)(iv)

15. On 9 February 2026, the Minister of Finance wrote to the Minister of Science, Innovation and Technology and the Minister of Revenue, inviting savings from the following options into the Budget 2026 process:

a. Research and Development Tax Incentive: Excluding or reducing internal software expenditure

[1] Research and Development Tax Incentive (RDTI) Five-Year Evaluation, prepared by Motu Economic and Public Policy Research & The University of Otago, 15 May 2025

b. Research and Development Tax Incentive: Excluding overseas expenditure

c. s 9(2)(f)(iv)

16. This report provides information on these options and summarises the relevant trade-offs. This report also briefly covers improvements that Ministers are considering that could be offset against the savings options. Advice is due to the Minister of Finance by 20 February.

17. Officials note that operational enhancements also contribute meaningfully to achieving Ministers' objectives. A programme of operational improvements is underway to reduce compliance burden. These are summarised in an annex to this report.

Savings options

Savings from the RDTI

18. The RDTI is a broad-based tax incentive. The savings options officials have identified focus on expenditure categories within the RDTI that may generate lower economic return (or "spillovers") per dollar of cost. This can be due to either relatively lower spillovers from the underlying R&D activity or relatively higher administrative and compliance costs associated with business correctly claiming and agencies processing that expenditure.

19. Officials note that expenditure categories with assumed lower spillovers may still be important for the overall effectiveness of the scheme. The impacts of excluding these kinds of expenditure categories are difficult to quantify and the decisions in this report will ultimately require judgement by Ministers. Ministers may also wish to consider the value of policy stability for supporting confidence in R&D investment in New Zealand.

Internal software expenditure

20. The RDTI makes a distinction between three kinds of software expenditure:

    a. **External software** is software that is developed to be sold or used within a product that is sold. This kind of R&D expenditure is generally treated like other eligible expenditure. We are not proposing any changes to external software eligibility.

    b. **Administrative internal software** is software that is used to run a business (such as HR and payroll systems). This kind of R&D expenditure is excluded from the RDTI.

    c. **Non-administrative internal software** is software that enhances non-digital services to customers. For example, a delivery business might develop a software product to help its customers track their packages. Even though the software may be integrated into the business's internal computer systems, it is primarily customer-facing and not administrative in nature. This kind of expenditure is subject to a cap of $25 million per business per year. The purpose of the cap is to recognise that while there are some spillover benefits, there is a fiscal risk associated with routine development being misclassified as R&D.

21. In practice, distinguishing between administrative and non-administrative internal software is difficult for both claimants and staff assessing RDTI applications. As a result, this category imposes disproportionately high compliance and administrative costs. While process improvements may reduce these costs at the margin, they are unlikely to materially address the underlying complexity.

22. We have identified two savings options for this setting:

    a. Internal software expenditure (excluded) - $183 million, comprised of $13 million for 2026/27, then approximately $50-60 million per annum thereafter.

    b. Internal software expenditure ($3m cap) - $99 million, comprised of $7 million for 2026/27, then approximately $30 million per annum thereafter.

23. Inland Revenue recommends excluding all internal software because it is likely to represent low value for money once administration costs and lower spillovers are accounted for. MBIE recommends retaining the current settings. MBIE is concerned exclusion could adversely impact the level of R&D expenditure and the overall spillover benefits of the scheme and may not align with wider Going for Growth objectives, including a push for greater digitisation.

24. During consultation in 2025, stakeholders supported retaining eligibility for non-administrative internal software development under the RDTI, noting its importance for productivity in highly digitised sectors (such as game development, digital services, and other service-based firms). Stakeholders noted that, in these sectors, internal software is often integral to the products and services they deliver.

25. Ministers could also consider reducing the cap to $3 million per year - its original level before it was raised prior to introduction to the House in response to stakeholder feedback. This option could deliver fiscal savings while maintaining accessibility, particularly for SMEs. Ninety per cent of businesses claiming some credits for internal software would be unaffected by the change. However, we note there are at least three firms with expenditure greater than $20 million in this area, indicating there is significant R&D investment in this space. Inland Revenue note that this option would not reduce administrative costs very much as expenditure still needs to be identified before a credit cap is put on it.

Overseas expenditure

26. Overseas expenditure is currently capped, with a business able to claim 10 per cent of their total R&D expenditure for overseas activities that support eligible R&D activities in New Zealand. The RDTI aims to incentivise R&D activities performed in New Zealand. However, allowing some overseas expenditure recognises that activities or expertise in certain fields may only be available overseas. New Zealand's cap on overseas expenditure is more restrictive than Australia's, where the cap is effectively 50 per cent of eligible expenditure.

27. Excluding overseas expenditure would realise savings of $65 million over the forecast period (comprised of $5 million for 2026/27, then approximately $20 million per annum thereafter).

28. Excluding overseas expenditure was identified as a possible area to realise savings as this expenditure could be viewed to not directly support domestic R&D or generate spillovers in New Zealand. However, while spillovers directly attributable to overseas expenditure may be lower than for domestic expenditure on R&D, it supports businesses' access to critical expertise and capabilities not available domestically, enabling retention of their broader R&D activity in New Zealand. Given New Zealand's size and distance from international markets, officials judge there is a risk that some businesses could relocate some of their R&D programmes elsewhere if overseas expenditure were excluded, reducing overall economic benefit to New Zealand.

29. Both agencies do not recommend excluding overseas expenditure.

s 9(2)(f)(iv)



s 9(2)(f)(iv)



Improvements to the scheme

36. In 2024, Ministers received advice on including a provision for (1) a discretionary power for the Commissioner of Inland Revenue to accept and amend late RDTI filings, (2) in-year payments through the tax system, and (3) revising the mining exclusions in the RDTI (IR2024/209 refers). Decisions were held off until the results of the five-year evaluation were available. These settings were raised by stakeholders in recent consultation as areas of the RDTI that could be improved.

37. The Minister of Science, Innovation and Technology and the Minister of Revenue have previously agreed to progress work on three improvements to the RDTI (REQ-0024980, IR2025/491 refers). The costs to progress are relatively small and would be offset by the savings options. These settings were raised by stakeholders in recent consultation as areas of the RDTI that could be improved.

Discretion for the Commissioner of Inland Revenue

38. Under current law, RDTI applications and returns cannot be accepted or amended once the filing deadline has passed. This can result in a business being denied its RDTI credit for the relevant income year, even due to relatively minor errors such as editorial errors or missing filing deadlines due to illness. Feedback indicates that the absence of discretion also currently leads to excessive time spent on claim preparation, which can increase compliance costs. This change could also strengthen business trust in the scheme.

39. Both agencies recommend granting discretion to the Commissioner to accept claims affected by minor errors or exceptional circumstances (e.g., natural disasters). Designing a narrow scope for discretion would mitigate the risk of businesses using this opportunity to re-characterise prior R&D expenditure.

In-Year Payments

40. Businesses currently experience a delay between incurring R&D expenditure and receiving the associated tax credit. This delay can create cash flow challenges for businesses, particularly loss-making businesses and pre-revenue start-ups. In-Year Payments would address this challenge by paying out the credit in instalments throughout the year.

41. Targeted consultation in 2025 indicated there is some support from the business community for implementing In-Year Payments (particularly from SMEs). The previous Government agreed to implement In-Year Payments of the RDTI through the tax system. However, due to the long lead-in time, a loan scheme was introduced in March 2023 as a temporary measure to provide in-year payments. This scheme was closed in January 2024 on the basis that it was costly to administer with significant operational risks, had low uptake (only 203 loans were issued compared to a forecast of 3,650 loans over three years) and was overall not delivering value for money.

42. MBIE recommends In-Year Payments be progressed due to the cashflow support it can provide to start-ups, helping them invest in their R&D programmes earlier than they can currently. We anticipate that this will contribute to economic growth and align with Going for Growth objectives.

43. Inland Revenue does not recommend implementing In-Year Payments through the tax system because of the cost to implement, the higher cost to administer, and the risk of overpayments leading to debt and additional debt activities. Inland Revenue also understands businesses may have become more comfortable with the annual RDTI claims and payment process. It sees greater value in decreasing processing times through operational changes.

44. In-year payments are expected to have a departmental cost of around $6.5 million over the forecast period. Detailed design decisions on In-Year Payments would need to be made promptly if this option is progressed. There may be further non-departmental costs depending on how Ministers wish to balance integrity of the scheme and accessibility. If this option is progressed officials will report back on these design features and any associated fiscal costs.

Relaxing mining exclusions

45. In 2021, changes were made to the RDTI to limit the eligibility of expenditures that could be incurred by mining businesses (including minerals, petroleum, natural gas and geothermal) due to concerns that settings at the time may allow R&D tax credits to be claimed on the upfront costs of assets used by miners. While those amendments achieved their intent, officials consider they tightened eligibility too far. Currently, mining businesses cannot claim RDTI tax credits for any expenditure other than labour related costs and expenditure on prototypes used in R&D. This puts these businesses at a disadvantage compared with other businesses enrolled in the RDTI.

46. Relaxing mining exclusions would broaden the scheme to align the mining sector with other industries eligible for the RDTI, in-line with the sector-agnostic design of the RDTI scheme. This constitutes a broadening of the RDTI's targeting, providing the incentive to a wider range of activities. Officials recommend changing this setting to align with the sector agnostic intent of the RDTI, however, note it only increases the incentive for a narrow segment of R&D performing businesses and does not address Ministers' stated objectives.

Financial implications

Non-departmental impact

47. The following table summarises the non-departmental fiscal impacts of the potential options over the forecast period. The savings would apply to the non-departmental

Science, Innovation and Technology: R&D Tax Incentive Other Expenses appropriation within Vote Revenue.

	$m - increase/(decrease)					
Options - Non-departmental Other Expenses	2025/26	2026/27	2027/28	2028/29	2029/30 & Outyears	Total
Reducing internal software to $3 million	-	(7.000)	(29.000)	(29.000)	(34.000)	(99.000)
Excluding all internal software	-	(13.000)	(55.000)	(53.000)	(62.000)	(183.000)
Excluding overseas expenditure	-	(5.000)	(19.000)	(19.000)	(22.000)	(65.000)
Discretion for Commissioner	-	0.500	2.500	1.250	1.250	10.000
Relaxing mining exclusions	-	0.700	0.350	0.350	0.350	1.750
In-year payments	-	-	-	-	-	-

48. s 9(2)(f)(iv)

Administrative impact

49. The following table summarises the departmental impacts for Inland Revenue to implement and administer the potential options over the forecast period. These costings are high level and will be refined based on policy and design decisions. We note that the two internal software options are mutually exclusive.

	$m - increase/(decrease)					
Options – Departmental administration cost	2025/26	2026/27	2027/28	2028/29	2029/30 & Outyears	Total
Operating						
Reducing cap for internal software to $3 million	-	0.100	-	-	-	0.100
Excluding all internal software	-	0.100	-	-	-	0.100
Excluding overseas expenditure	-	0.100	-	-	-	0.100
Discretion for Commissioner	-	-	-	-	-	-
Relaxing mining exclusions	-	0.100	-	-	-	0.100
In-year payments[2]	-	1.000	1.000	1.200	1.200	4.400
Capital						
In-year payments	-	2.100	-	-	-	2.100

Consultation

50. The Treasury has been informed of this report.

[2] There may be further non-departmental costs of implementing an In-Year Payment scheme however this will depend on design decisions. In particular, how integrity risks are balanced against the level of accessibility for businesses. This will be detailed in future reporting.

Next steps

51. Officials will prepare budget bids for Budget 2026 as directed.

52. Officials will continue to monitor the status of the work programme to deliver operational improvements and report on their impact against the objectives set out by the Going for Growth Ministers as data becomes available.

Recommendations

We recommend you:

1. **Note** Inland Revenue recommends:
   a. excluding internal software
   b. allowing Commissioner discretion and relaxing mining exclusions
   c. s 9(2)(f)(iv)

2. **Note** MBIE recommends:
   a. retaining current internal software and overseas expenditure settings
   b. s 9(2)(f)(iv)
   c. progressing In-Year Payments through the tax system to support Going for Growth objectives and allowing Commissioner discretion

3. **Refer** a copy of this report to the Minister of Finance

   Refer - yes / no

   Minister of Science, Innovation, and Technology

4. **Indicate** which of the following items you would like to invite for Budget 2026:

   Indicate preferred options below.

   Minister of Finance

Reducing the RDTI's internal software expenditure cap from $25 million to $3 million	Yes/no
Excluding internal software expenditure from RDTI eligibility	Yes/no
Excluding overseas expenditure from RDTI eligibility	Yes/no
s 9(2)(f)(iv)	
Progressing In-Year Payments through the tax system	Yes/no
Giving discretion for the Commissioner of Inland Revenue to accept late or amended filings	Yes/no
Relaxing mining exclusions	Yes/no

s 9(2)(a)

Michael Contaldo
Manager
Innovation Policy | MBIE
18/02/2026

Claire McLellan
Acting Policy Lead
Policy | Inland Revenue
18/02/2026

Hon Nicola Willis
Minister of Finance
/ /2026

Hon Shane Reti
Minister of Science, Innovation and Technology
/ /2026

Hon Simon Watts
Minister of Revenue
/ /2026

Annex: Indicative timeline for operational enhancements

Aspect of scheme	Enhancement	Purpose	Status	Estimated time to implement
The General Approval application process	Allow multiple small projects to be filed as a single application.	Reduce the compliance burden for firms applying through the General Approvals pathway.	Phase one: Customer tool - In progress	6-12 months
	Reorient a portion of free Government advisory services to provide early intervention targeted at SMEs.	Reduce the compliance burden and supporting SME access.	In progress	Ongoing improvement
	Develop an AI prompt resource to guide businesses through applications.	Reduce the compliance burden for all businesses.	In progress	3-6 months
The Claims process	Remove the requirement for a breakdown of expenditure by core and supporting activities.	Reduce the compliance burden for businesses.	Scoping	6-12 months
	Extend free Government advisory services to provide post-application support.	Reduce the compliance burden and supporting SME access.	Scoping	6-12 months
	Improve quality assurance processes and guidance for Requests for Information.	Reduce the compliance burden and promoting transparency and integrity.	In progress	Ongoing improvement
The Approved Research Provider (ARP) programme to support very small claimants	Review the eligibility criteria and status of current ARPs	Promote integrity ensuring ARPs can deliver eligible R&D activities.	To start Q1 2026	6 months
	Upskill ARPs to support businesses through applications.	Reduce the compliance burden for businesses.	Pending review of ARPs	6-12 months
	Promote greater awareness of the ARP programme	Improve SME access to the RDTI.	Pending review of ARPs	Ongoing improvement

Briefing note

Inland Revenue
Te Tari Taake

Reference	BN2026/073
Date	5/03/2026
To	Revenue Advisor, Minister of Finance – Carl Harris Revenue Advisor, Minister of Revenue – Angela Graham Private Secretary, Minister of Science, Innovation and Technology – Emily Robinson
From	Adam Carter
Subject	**RDTI and internal software**

Purpose

1 The Minister of Revenue requested additional information on the distributional impacts of limiting internal software expenditure and examples of such expenditure. He has also asked for more information on the size and nature of the firms accessing the Research and Development Tax Incentive (RDTI) more generally.

Non-administrative internal software

Policy under consideration

2 Firms can claim up to $25 million of expenditure per year on non-administrative internal software development. Fifteen percent of this gives a maximum credit value of $3.75 million.

3 Ministers are considering whether to change the RDTI settings for non-administrative internal software. The two policy options being considered are: (1) exclude internal software entirely, or (2) reduce the expenditure cap from $25 million to $3 million. Changes would apply from 1 April 2027. The estimated savings from these options are:

Options – Non-departmental Other Expenses	2025/26	2026/27	2027/28	2028/29	2029/30 & Outyears	Total
Reducing cap to $3 million	-	(7.000)	(29.000)	(29.000)	(34.000)	(99.000)
Excluding all internal software	-	(13.000)	(55.000)	(53.000)	(62.000)	(183.000)

4 Officials have identified this expenditure category as representing lower value for money than other expenditure categories. This is primarily due to:

- some evidence that internal software development has lower spillovers than other kinds of research and development (R&D) expenditure (although there are high levels of uncertainty), and
- this expenditure category has relatively high administrative costs for Inland Revenue and compliance costs for customers when compared to other expenditure categories.

Inland Revenue has recommended excluding internal software from the RDTI, while the Ministry of Business, Innovation and Employment (MBIE) has recommended retaining the current settings.

5 Removing non-administrative internal software has risks. MBIE is concerned that excluding non-administrative internal software expenditure from the RDTI could adversely impact the level of R&D expenditure and the overall spillover benefits of the scheme and may not align with wider Going for Growth objectives, including a push for greater digitisation. Removing this expenditure may also put more pressure at the boundary with external software because firms will now have an incentive to classify non-administrative internal software as external software. Ministers may also wish to consider the value of policy stability in supporting investment certainty.

Definition of internal software expenditure

6 The RDTI makes a distinction between three kinds of software expenditure:

- **External software** is software developed to be sold itself or used within a product that is sold. An example is accounting software that is sold to other businesses. This kind of R&D expenditure is generally treated like other eligible expenditure. We are not proposing any changes to external software eligibility.
- **Administrative internal software** is software used to run a business (such as HR and payroll systems). This kind of R&D expenditure is excluded from the RDTI.
- **Non-administrative internal software** is software that enhances non-digital services to customers. For example, a delivery business might develop a software product to help its customers track their packages. Even though the software may be integrated into the business's internal computer systems, its primary purpose is to support customers rather than support delivery drivers. This kind of expenditure is subject to a cap of $25 million per business per year. The cap partly recognises the risk of administrative internal software being recharacterised as non-administrative internal software.

7 Due to similarities between administrative and non-administrative internal software activities, determining legitimate activity is difficult and causes administrative burden for agencies and compliance costs for businesses (for example, through responding to requests for information). The Motu evaluation observed that "internal software claims almost always require specialist tax/technical advisors due to complexity, adding material cost". Disproportionate time spent assessing software claims is observed in other countries too.

Examples of administrative internal software expenditure

8 Officials are unable to provide detailed information about specific R&D projects for which non-administrative internal software expenditure is claimed because this could disclose sensitive revenue information. However, the following stylised examples give a sense of core activities involving non-administrative internal software:

- Integrating data held across different parts of the business to provide customers with financial insights.
- Improving image recognition software for early detection of diseases in horticulture.
- Enhancing tracking systems for certain goods, including allowing customers to monitor the progress of goods or services in transit.

Firms currently claiming internal software expenditure

Number of claimants and size of *expenditure*

9 Most firms have filed their supplementary returns for the 2024 income year. Credits of $350 million have been claimed to date, with 12.5% ($43 million) of these claimed for internal software (henceforth "internal software").

10 As shown in Table 1, 13.5% of firms accessing the credit (135 of 995) have claimed for internal software. Only a small number of firms exceeded the $25 million expenditure cap, each claiming credits valued at $3.75 million. Most firms who claim some internal software claim less than $1 million of expenditure with a credit value of up to $150,000.

Table 1: Firms claiming internal software expenditure by expenditure/credit bands (provisional data for 2024)

Expenditure ($)	Credit value ($)	Number of firms
10 million+	1.5 million+	8[1]
1 million–9 million	0.15 million–1.35 million	41
Less than 1 million	Less than 0.15 million	86
0	0	860
Total		**995**

11 A total of 21 firms claimed internal software expenditure exceeding $3 million with a credit value of $450,000 or greater.

Sectors claiming internal software expenditure

12 Firms with the largest claims are concentrated in the financial services industry. However, firms claiming more than $3 million of expenditure span manufacturing, transport, energy, and entertainment industries. These firms are often large service-sector incumbents. It is worth noting that there has been considerable variability year-to-year in the expenditures of firms making the largest claims, generally reflecting the life cycle of particular software projects.

13 Smaller firms claiming internal software are more concentrated in the software, digital services, analytics, and creative-technology sectors.

Internal software development major type of R&D claimed by these firms

14 Firms claiming internal software expenditure are claiming most of their credits from this expenditure category. Of the 135 firms that claim some internal software expenditure, 91 firms claim over half of their credits from this expenditure category. Sixty-eight firms claimed credits solely for internal software development.

International context

15 It is common for expenditure on non-administrative internal software to be eligible for R&D tax incentives. For example, Australia, Canada, Ireland and the United Kingdom allow non-administrative internal software expenditure provided it meets their definition of R&D. Australia is more restrictive in terms of what kinds of software expenditure can be eligible as a core activity but relatively less restrictive in terms of what can be claimed as a supporting activity. New Zealand is unique in having a separate cap for non-administrative internal software.

Broader distributional analysis

16 This section provides information about the firms claiming the RDTI more generally. The average amount of all eligible R&D expenditure across all firms is $2.25 million with a credit value of $337,000. The median amount of eligible R&D expenditure is lower.

[1] We have created an above $10 million band because the number of taxpayers exceeding the cap is too small, risking disclosure of sensitive revenue information.

Half of firms claim less than $700,000 of expenditure with a credit value of $105,000. Table 2 shows the number of firms by credit bands.

Table 2: **Firms claiming RDTI by expenditure/credit bands (provisional data for 2024)**

Eligible expenditure ($)	Credit value ($)	Number of firms
0–333,333	0–49,999	274
333,333–666,660	50,000–99,999	184
666,667–1,666,660	100,000–249,999	283
1,666,667–3,333,327	250,000–499,999	121
3,333,333–6,666,660	500,000-999,999	66
6,666,667–13,333,327	1,000,000–1,999,999	33
13,333,333–33,333,327	2,000,000–4,999,999	28
33,333,333+	5,000,000+	6
Total		**995**

17 We do not have any information on whether firms are owned in New Zealand. Access to the RDTI is determined by a firm's New Zealand presence and the location of its R&D activity, rather than ownership or nationality. To be eligible, a claimant must be a New Zealand tax resident or a non-resident with a fixed establishment in New Zealand, and must undertake its core R&D activities in New Zealand. Firms do not need to be New Zealand-owned, and resulting intellectual property does not need to be held in New Zealand, provided the claimant owns or has the right to use the R&D outcomes.

18 Inland Revenue is required to publish the names of R&D tax credit recipients and the amount of their tax credit (in dollar bands), at least two years after the end of the tax year to which the credit relates.[2] The list gives a sense of which companies have accessed the RDTI in previous years.

Compliance costs

19 Low R&D expenditure firms face disproportionately higher compliance costs, making the scheme less attractive and, in some cases, financially unattractive. The Motu evaluation noted that there was consensus across interviewed stakeholders that firms needed to be spending at least $300,000–$500,000 on eligible R&D expenditure for the RDTI to be financially beneficial. It also found that around half (51%) of all firms that exited the scheme had an average annual R&D spend less than $300,000.

20 We note that a programme of operational changes is currently underway aimed at reducing compliance costs. As well as simplifying the claims process, some action points are particularly targeted at small businesses. For example, improving the Approved Research Provider (ARP) programme, which allows firms to access the RDTI even if they have R&D expenditure below the $50,000 minimum threshold.

Consultation

21 MBIE has been consulted on this briefing note. The Treasury has been informed.

[2] https://www.ird.govt.nz/research-and-development/tax-incentive/contractors-certifiers-approved-research-providers-and-rdti-credit-recipients/list-of-rdti-credit-recipients

Next steps

22 The Minister of Finance is meeting with the Minister of Revenue on Monday, 9 March 2026. Ministers may wish to discuss this policy item.

Adam Carter

Senior Policy Advisor

s 9(2)(a)

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: Fringe benefit tax review update

Date:	27 May 2025	**Priority:**	High
Security level:	Sensitive - Budget	**Report number:**	IR2025/220

Action sought

	Action sought	Deadline
Minister of Finance	**Discuss** preferred option with officials OR **Agree** to recommendations	6 June 2025
Minister of Revenue	**Discuss** preferred option with officials OR **Agree** to recommendations	6 June 2025

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Bary Hollow	Principal Policy Advisor	s 9(2)(a)	☒

27 May 2025

Minister of Finance
Minister of Revenue

Fringe benefit tax review update

Purpose

1. This report updates you on submissions from the officials' issues paper "Fringe benefit tax – options for change" (the issues paper) and recommends which proposals to progress (depending on any availability of funding) for the upcoming omnibus taxation bill (the Bill).

2. There are various reform packages which Ministers could progress, and these depend on Ministers preferred timelines and whether Ministers would still prefer a fiscally neutral package.

Issues paper

3. The issues paper was released on 1 April 2025 for five weeks of public submissions. The paper focused on simplifying the fringe benefit tax (FBT) rules and reducing compliance costs. The FBT proposals mainly focused on how the rules apply to motor vehicles and unclassified benefits, as well as a proposal to include the entertainment expenditure deduction limitation rules within the FBT regime.

4. The issues paper gained feedback on each proposal separately, however, to proceed with a fiscally neutral package some proposals will need to be combined.

5. The main proposals are summarised as:

    5.1 **Motor vehicles**: updating the rates for calculating the value of a motor vehicle and simplifying the process for calculating a motor vehicles value for FBT by removing day counts and exemptions and introducing categories to determine the rate of FBT.

    5.2 **Unclassified benefits**: two options to reduce compliance costs, either exempting certain benefits from the current test by way of a limited list or reforming the test and exempting benefits less than $200 that are not in lieu of remuneration.

    5.3 **Entertainment expenditure rules**: simplifying the rules and including them as part of FBT instead of the current deduction limitation.

    5.4 **Data and filing**: introducing new data requirements and enabling electronic filing of FBT returns.

Issues paper feedback and summary of submissions

6. We received 39 submissions on the issues paper.[1] Overall, submitters commented that the issues paper was a good step forward to reforming the rules. The 'close

[1] Of those, six submissions were considered out of scope as they dealt with items not raised in the issues paper, such as the FBT exemption for charities and the application of FBT on health insurance premiums.

enough is good enough' principle[2] in particular, received positive feedback. The submissions provided detailed feedback on the various proposals. We have provided a high-level summary below.

7. Some submitters noted there would need to be consideration of how any transitional rules would work when implementing the changes.

Motor vehicles

8. The proposals aimed to simplify how FBT is paid on motor vehicles. This area was identified by the regulatory stewardship review as the most common area where misconceptions arise.

9. The paper proposed updating the values of a motor vehicle for FBT purposes based on external sources, as these were last updated in 2006.[3] The recalculation resulted in increased values of motor vehicle, and we proposed three different values based on fuel type (standard, hybrid and plug-in electric vehicles). We also proposed an ongoing review every four years. Most submitters were in favour of setting the values based on external sources and agreed they should be updated regularly (submissions on how long varied).

10. The paper also proposed a change in the application of FBT to motor vehicles. This is currently based on counting the days a vehicle is available for private use. The proposal would remove counting days and instead apply three categories depending on the private use of the vehicle.

11. Submitters were largely in favour of the category approach and commented this would reduce compliance costs. One submitter suggested that this change could reduce compliance time by 750 hours per annum, when factoring in the time required to request, complete, follow up vehicle logbooks. There were examples where some taxpayers overpay to avoid the compliance costs and risk under the current rules, so in these cases there would not necessarily be a reduction in compliance costs.

12. There were many submissions about refining and modifying the categories to capture weekend private use at a lesser rate. We have revised the categories based on submissions and the updated proposal is in **Appendix 1**.

13. There were many submissions around widening the definition of emergency vehicle, which would be a new exemption under the category approach. We have engaged with some of these submitters and have also made changes to this definition, which are reflected in **Appendix 1**.

Unclassified benefits

14. The issues paper proposed two options to reform the rules relating to unclassified benefits:

    14.1 **Remuneration approach:** exclude benefits under $200 that are not provided in lieu of remuneration; or

    14.2 **List approach:** retain the current test but include a list which exempts certain non-remunerative benefits such as flowers provided for life events.

[2] Close enough is good enough is based on getting near enough to an approximation of the benefit rather than determining precisely the actual benefit. This should lead to rules that are easier to understand and comply with.
[3] This follows the same methodology Inland Revenue uses to calculate tax free mileage reimbursement rates. This was calculated using the up-to-date costs of running a motor vehicle issued by the New Zealand Automobile Association (costs excluding fuel cost) and the Ministry of Business, Employment and Innovation (fuel costs).

15. Overwhelmingly submitters preferred the remuneration approach, many commenting that it would significantly reduce compliance costs and was sensible to apply. Some suggested also raising the test to $300 per benefit to align with Australia.

16. One submitter said capturing and tracking these unclassified benefits is one of the biggest sources of compliance costs when preparing FBT calculations. They commented that the proposed remuneration approach would substantially decrease current compliance costs and ease the FBT filing process.

17. The list approach was not preferred, as this would not resolve the issue of capturing and tracking benefits. Some submitters commented that a list would actually increase their compliance costs, as it would require extra analysis of the benefits. As the list would still apply to the current tests, there were submissions about the issues with this test (such as the thresholds).

Entertainment

18. Submitters had reservations about changes to these rules without further consultation. While some commented that these rules are complex and should be reviewed, many did not support the proposal in the issues paper and suggested not proceeding with this at this point in time. The common points of feedback were:

    18.1 The changes would negatively impact loss-making companies (FBT would be payable in cash rather than just an adjustment to losses) and non-for-profit organisations as they do not have a FBT exemption and there would be an adverse cash impact to them.

    18.2 It would require businesses that only have one event a year to submit a FBT return.

    18.3 It may increase tax payable because of the differing FBT rate compared to the company tax rate for no saving in compliance costs.

Data, filing and integrity

19. Submitters mostly supported the proposed data requirements, provided these aligned to data that was already created. Many were supportive of being able to file returns through software. These are operational matters which can be progressed without the need for legislative change.

s 9(2)(f)(iv)



24. s 9(2)(f)(iv)

Miscellaneous proposals

25. We also received submissions relating to other minor proposals raised in the issues paper. These are not covered in this report as they are immaterial compared to the motor vehicles and unclassified benefits proposals. These will be addressed in the final proposals for consideration by Cabinet but again these were generally well received.

Way forward

26. Based on the feedback received from submitters, we recommend that Ministers progress:

26.1 **The category approach to motor vehicles**

26.1.1 The motor vehicle changes had positive feedback from submitters, and we have made changes to the categories following submissions which we have positively tested with some submitters. The final motor vehicle proposal is outlined in **Appendix 1**; and

s 9(2)(f)(iv)

26.3 **The data, filing, integrity and miscellaneous proposals**

26.3.1 Regardless of the package progressed, we recommend progressing these proposals as they have an immaterial fiscal cost and were supported by submitters.

27. Based on the feedback of submitters however, we would not recommend progressing the proposed changes to **entertainment expenditure** until further consultation can be completed.

28. As a result, there are multiple options for taking forward a package of amendments to the FBT rules that depend on Ministers preferred timelines and whether Ministers would still prefer a fiscally neutral package.

Larger reform, neutral fiscal cost, defer package introduction

29. As noted, we do not recommend progressing proposed changes to the entertainment expenditure rules until further consultation can be undertaken. However, this would mean deferring the fiscal benefit of these changes.

30. As a result, if Ministers want to progress a fiscally neutral larger package of reforms including changes to motor vehicles, s 9(2)(f)(iv) and changes to entertainment we would recommend deferring that package beyond the timeline for inclusion in the upcoming omnibus Bill.

Larger reform, net fiscal cost, earlier legislation in August tax Bill

31. It would be possible to progress changes with a net fiscal cost in the upcoming omnibus Bill if Ministers would prefer (i.e., progressing motor vehicle changes and s 9(2)(f)(iv)). However, doing so would require additional funding, as the Budget 2025 contingency assumes a fiscally neutral package.

32. Doing so will require funding pre-committing the s 9(2)(f)(iv) cost of these reforms against Budget 2026 as follows:

	$ million increase / (decrease)				
Vote Revenue **Minister of Revenue**	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29 & Outyears**
Tax Revenue:					
FBT new Motor Vehicle Categories		3.950	15.800	15.800	15.800
Company tax on deductibility	-	(1.100)	(4.400)	(4.400)	(4.400)
Total tax impact of Motor Vehicle proposal	**-**	2.850	11.400	11.400	11.400
s 9(2)(f)(iv)					

33. It is not possible to charge the fiscal cost of these reforms against the tax policy scorecard, given its current balance.

34. We note that it would still be possible to progress consultation on the entertainment expenditure changes while progressing a package with a net fiscal cost. If Ministers later decide to progress the entertainment expenditure changes, it would be possible to neutralise the fiscal cost of the overall package of reforms in future years.

35. These fiscal costings take no account of the substantial reduction in compliance costs for taxpayers which will result from these proposals.

Smaller reform, fiscally neutral, earlier legislation in August tax Bill

36. If you wish to progress a fiscally neutral package in time for the upcoming omnibus Bill, we recommend you progress the motor vehicle changes s 9(2)(f)(iv) This option has a fiscal benefit of s 9(2)(f)(iv)

	$ million increase / (decrease)				
Vote Revenue **Minister of Revenue**	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29 & Outyears**
Tax Revenue:					
FBT new Motor Vehicle Categories		3.950	15.800	15.800	15.800
Company tax on deductibility	-	(1.100)	(4.400)	(4.400)	(4.400)
Total tax impact of Motor Vehicle proposal	**-**	2.850	11.400	11.400	11.400
s 9(2)(f)(iv)					

s 9(2)(f)(iv)

37. s 9(2)(f)(iv)

38.

39.

Consultation

40. The Treasury has been consulted on the contents of this report, and agrees with Inland Revenue that Ministers should progress the package that best meets their fiscal and compliance-cost reduction objectives.

Recommended action

We recommend that you:

1. **Discuss** which option you would like to progress with officials; **OR**

2. **Agree** to progress **ONE** of the following **FOUR** options:

    2.1 **Larger reform, neutral fiscal cost, later introduction** - Motor vehicle category change, s 9(2)(f)(iv) , entertainment deduction limitation changes but defer introduction to allow more consultation on the entertainment changes.

    Agreed/Not Agreed Agreed/Not Agreed

    OR

    2.2 **Larger reform, net fiscal cost, introduction in August tax Bill** - Motor vehicle category change, s 9(2)(f)(iv) , inclusion in the August tax Bill. *(Officials preferred option subject to funding)*

    Agreed/Not Agreed Agreed/Not Agreed

    OR

    2.3 **Smaller reform, neutral fiscal cost, introduction in August tax Bill** - Motor vehicle category change, s 9(2)(f)(iv) , inclusion in the August tax Bill.

    Agreed/Not Agreed Agreed/Not Agreed

OR

2.4 **Smaller reform, fiscal benefit, introduction in August tax Bill** - Motor vehicle category change inclusion in the August tax Bill, s 9(2)(f)(iv)

Agreed/Not Agreed Agreed/Not Agreed

2.5 **Note** if you agree to any of options 2.2-2.4 above officials will prepare a Cabinet report for inclusion in the August tax Bill.

Noted Noted

s 9(2)(a)

Bary Hollow
Principal Policy Advisor
Policy

Hon Nicola Willis
Minister of Finance
/05/2025

Hon Simon Watts
Minister of Revenue
/05/2025

Appendix 1

Motor vehicles – revised categories

1. This proposal implements new categories to apply to motor vehicles depending on the permitted private use of the vehicle. The aim of this option is to bring the calculation of FBT on motor vehicles closer to the remuneration aspect of the benefit. The issues paper proposed three categories:

Table 1: Preferred categories of vehicle use

Category	Limitations on use	Rate[4]
1	Vehicles predominantly available for employee's unrestricted private use (i.e., perk vehicles). The provision of the vehicle is generally reflected in the employee's remuneration package.	100%
2	Vehicles predominantly for business use, with restricted private use (i.e., tools of trade). The employee may use the vehicle for travel to and from work (work generally being the same workplace), but not at other times. Generally, the vehicle will be allocated to a single employee (although other employees may use the vehicle during business hours).	35%
3	Vehicles solely for business use with no personal usage other than for commuting to and from work (multiple workplaces/worksites) with no personal usage (other than incidental use).	0%

2. Submitters were largely happy with the category approach. Many of the submissions focused on the details and boundaries of the categories. For example, they raised the treatment of pool vehicles, vehicles that are available for business use but not allocated to an employee. Another common submission was whether the categories were able to encompass the vehicles that are work-related for 5 days a week and available for private use for 2 days a week. These vehicles would likely be paying FBT at a rate of 28%-37% of the motor vehicle value, but were likely to be taxed at 100% in the proposed categories.

3. The revised categories feature two extra categories to make clear where these types of arrangements would fall. It also makes clear that we consider commuting to and from work personal use and taxable (this would be ignored when employers consider whether the vehicle is mainly used for business use). These categories would be set once the vehicle is acquired (provided to the employee).

Table 2: Revised categories of vehicle use

Category	Limitations on use	Rate
1	**Vehicle <u>mainly</u> for private use** (i.e., perk vehicles). The provision of the vehicle is generally reflected in the employee's remuneration package. For determining whether a vehicle is mainly for private use, the fact that other employees have access to the vehicle or not during business hours is ignored.	100%

[4] The rate is the percentage of the fringe benefit taxable value that FBT will be payable on.

2	**Vehicle <u>mainly</u> for business use, restricted private use** during rostered days off, public holidays and/or statutory leave days and commuting to and from work.	35%
3	**Vehicle <u>only</u> for business use and commuting** to and from work (**same workplace**). The vehicle is generally taken home by the same employee.	20%
4	**Vehicle <u>only</u> for business use and commuting** to and from work (**multiple workplaces**).	0%
4b	**Vehicles <u>only</u> for business use, no private use** (other than incidental use). Vehicle does not need to be sign written (i.e., pool vehicles). These vehicles are not allocated to a single employee.	0%

4. Incidental use would be permitted in all categories. Branding would be required for categories 2, 3 and 4 (excluding 4b).

5. In the issues paper we proposed that where a major shareholder-employee of a close company has a vehicle used for private use and this exceeds $80,000, this would automatically be a category one vehicle (100% FBT). The purpose would be to prevent them from purchasing luxury vehicles and being able to claim a lower rate of FBT. Submitters suggested this limit was too low, so we have adjusted this to a higher value of $100,000.

6. Submitters provided feedback that the proposed emergency vehicle exemption did not capture all emergency services, so we have widened the definition (bolded) as follows:

   Any vehicle owned by:

   - *an ambulance service (including air ambulance services),*
   - *the New Zealand Police,*
   - *Fire and Emergency New Zealand,*
   - ***New Zealand Defence Force,***
   - ***A local authority that is required by section 64 of the Civil Defence Emergency Management Act 2002 to provide civil defence emergency management,***
   - ***A volunteer organisation which has a service level agreement with the New Zealand government for the provision of emergency services,***

   that is used for the provision of emergency services to the New Zealand public and is:

   - *visibly marked on the exterior of the vehicle that it is used for that purpose,* ***and/or***
   - *is fitted with flashing warning lights or other similar warning devices.*

   would be exempt from FBT."

7. The changes above to the motor vehicle proposals have slightly changed the fiscal impact that we previously reported to you on. The updated fiscal impact is as follows:

	$ million increase / (decrease)				
Vote Revenue **Minister of Revenue**	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29 & Outyears**
Tax Revenue:					
FBT new Motor Vehicle Categories		3.950	15.800	15.800	15.800
Company tax on deductibility	-	(1.100)	(4.400)	(4.400)	(4.400)
Total tax impact of Motor Vehicle proposal	**-**	2.850	11.400	11.400	11.400
Total operating	**-**	(2.850)	(11.400)	(11.400)	(11.400)

Tax policy report

Inland Revenue
Te Tari Taake

Fringe benefit tax review – options to progress

Date	5 March 2026	**Priority**	Medium
Security level	Budget sensitive	**Report number**	IR2026/069

Action sought		**Deadline**
Minister of Finance	**Discuss** preferred option with officials; OR **Agree** to recommendations.	20 March 2026
Minister of Revenue	**Discuss** preferred option with officials; OR **Agree** to recommendations.	20 March 2026

Purpose

We understand that, subject to your overall Budget priorities, Ministers want to progress s 9(2)(f)(iv) proposals from the FBT review as part of Budget 2026. This report seeks your agreement to final options, the approach and the sequencing of delivery.

We have previously reported to you on submissions from the officials' issues paper "Fringe benefit tax – options for change" (the issues paper)[1] and recommended to you which proposals to progress (dependent on any availability of funding) (IR2025/220 refers).

Final decisions on that report were deferred pending discussions with certain stakeholders and refinement of the final fringe benefit tax (FBT) proposals. We reported to you on feedback from that stakeholder engagement in August 2025 (BN2025/366 refers).

s 9(2)(f)(iv)

Contact for phone discussion, if required

Name	**Position**	**Phone number**	**First contact**
Bary Hollow	Principal Policy Advisor	s 9(2)(a)	✓
Natisha Jones	Senior Policy Advisor		☐

[1] This was released on 1 April 2025 and received 39 submissions.

Fringe benefit tax review – options to progress

Progressing FBT reform

1 The FBT reform policy options aim to simplify the rules and reduce compliance costs. There are various reform packages which Ministers could progress, and these depend on Ministers preferred timelines and whether you prefer a largely fiscally neutral package or if there is scope for funding to progress all the proposals. The detailed options are discussed in more detail in **appendix one**, but the summarised policy options are:

FBT Policy proposal	Fiscal cost	Stakeholder feedback	Impacts to progression
Changes to motor vehicle rules - Category approach: simplifying how FBT is paid on motor vehicles - Miscellaneous updates to the rules	Low fiscal cost of $544,000[2] over the forecast period.	The motor vehicle changes had positive feedback from submitters, and the further changes we have made have been positively tested at various forums such as the Chartered Accountants Australia and New Zealand tax conference, and directly with certain stakeholders including Federated Farmers and the Taxpayers Union.	As these proposals are a low cost which can be charged to the tax policy scorecard there is no financial impediment to progression. Taxpayers would receive significant compliance cost savings from these changes. We have been working with the stakeholders who raised concerns regarding the proposals and believe their concerns have been addressed in these final proposals, so see the risk of adverse reaction to the final proposals as low but not zero.
s 9(2)(f)(iv)			

[2] There is a very small fiscal cost to these changes which can be managed through the tax policy scorecard.

2 Once Ministers have decided which options to progress there are two possible timelines to progress these:

- Pre-Budget or Budget announcement and inclusion in the upcoming omnibus bill for 2026–27 ***(officials preferred approach)***, or
- Budget 2026 announcement and budget night legislation.

3 Our preferred timeline will allow us to continue to engage with stakeholders to ensure that an optimal product is ultimately progressed. With your agreement to lift Budget secrecy on the project we can continue to work with stakeholders on the basis we are still working on the proposals to get optimal proposals provided to Ministers. No timeline for delivery needs to be provided to stakeholders during this process.

4 This will also allow us to go back to those stakeholders who originally had concerns over the proposals to ensure that there is unlikely to be any repeat of the negative press coverage that occurred last year.

5 In addition, progressing any changes in an upcoming omnibus bill will allow for wider stakeholder consultation through the bill process. This would enable us to ensure the new legislation is workable in practice. Budget night legislation will not permit this and because this is the rewrite of the rules relating to a major part of the New Zealand tax system, we would not advise this.

6 Regardless of the legislative vehicle, it is likely these changes would only apply from 1 April 2027 at the earliest to allow Inland Revenue and businesses to update their administrative systems. We consider that Budget night legislation will not provide any benefit other than the changes are legislated prior to the election. However, since the legislation would be budget sensitive we would not be able to consult on legislative changes, meaning further, potentially significant, remedial changes would likely be required to the rules, which could create uncertainty.

Previous work with stakeholders

7 When the negative media coverage surrounding the original proposals arose last year, we directly engaged with those stakeholders who had raised issues. As previously reported these concerns were not entirely based on a correct understanding of the proposals although there were some valid concerns raised.

8 As part of that engagement, we have modified some of the proposals to address those concerns. These modifications do not result in a material change in the policy of the prior proposals but are more related to clarification ensuring that particular situations are explicitly covered within the rules.

9 We have socialised those modified proposals with the stakeholders who raised them and they have provided confirmation they are comfortable with those modified proposals as we outlined to you previously (BN2025/366 refers).

10 While we cannot guarantee there will not be future negative reaction to the proposals the main groups who raised concerns previously appear to be supportive of the modified proposals, so we see the risk of further negative reaction to be reduced.

11 In addition, to mitigate this, we will be engaging directly with some of the individuals who were active in the media last year as part of our stakeholder engagement process to identify any other issues that may get raised.

12 s 9(2)(f)(iv)

s 9(2)(f)(iv)

Options to progress

Package to progress

19 Subsequent to feedback from submissions on the issues paper and further discussions with stakeholders we consider that, barring any technical changes, the policy work (other than legislative drafting) for both the motor vehicles s 9(2)(f)(iv) is largely complete. s 9(2)(f)(iv)

20 Based on stakeholder feedback, we recommend that ultimately Ministers progress, either:

The motor vehicle changes (very low fiscal cost):

- The motor vehicle changes had positive feedback from submitters, and we have made changes to the categories following submissions which we have positively tested with some stakeholders. For your information the final motor vehicle proposals are outlined in detail in **appendix one.**

[3] This was not covered in the FBT officials' issues paper – *options for change*, but in the February 2025 officials' issues paper, *Taxation and the not-for-profit sector*.

21 The fiscal impact of the motor vehicle changes are:

	$m - increase/(decrease)				
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Crown Revenue and Receipts:					
Tax Revenue –					
FBT		(0.060)	(0.250)	(0.250)	(0.250)
Company tax	-	0.020	0.070	0.070	0.070
Net tax impact	-	(0.040)	(0.180)	(0.180)	(0.180)
Total Operating	**-**	**0.040**	**0.180**	**0.180**	**0.180**

22 This fiscal impact can be absorbed within the tax policy scorecard.

s 9(2)(f)(iv)

30 s 9(2)(f)(iv)

Timing of decisions

31 In terms of delivery timelines of Ministers preferred option above, there are two options:

- Pre-Budget or Budget announcement and inclusion in the upcoming omnibus bill for 2026–27 ***(officials preferred approach)***, or
- Budget announcement and budget night legislation.

32 For the reasons noted above we recommend an option where legislative changes are progressed as part of the omnibus tax bill for 2026-27 which will give us an opportunity to work with stakeholder outside of the budget secrecy process.

Financial implications - administration

Motor vehicle changes s 9(2)(f)(iv)

33 Based on an initial design assessment of the motor vehicle policy change option, Inland Revenue estimates the cost to implement and administer this initiative would be $0.300 million operating over the forecast period. s 9(2)(f)(iv)

34 s 9(2)(f)(iv) estimates will be refined and included for consideration as part of the proposed Budget initiative.

Consultation

35 The Treasury has been consulted on the contents of this report, and agrees with Inland Revenue that Ministers should progress the package that best meets their fiscal and compliance-cost reduction objectives.

Recommendations

We recommend that you:

1. **Discuss** which option you would like to progress with officials (e.g., at Joint Ministers meeting on Monday 9 March).

   OR:

2. **Agree** to progress one or more of the following changes:

   a. **Motor Vehicle Changes**

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

and/or:

s 9(2)(f)(iv)

Agree / Disagree
Minister of Finance

Agree / Disagree
Minister of Revenue

Financial Recommendations

IF you agree to recommendation 2a – motor vehicle changes:

3. **Note** the following fiscal impact as a result of progressing the proposed motor vehicle changes, with a corresponding impact on the operating balance and net core Crown debt:

	$m - increase/(decrease)				
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Crown Revenue and Receipts					
Tax Revenue:					
FBT	-	(0.060)	(0.250)	(0.250)	(0.250)
Company tax	-	0.020	0.070	0.070	0.070
Total tax revenue	-	(0.040)	(0.180)	(0.180)	(0.180)
Total Operating	**-**	**0.040**	**0.180**	**0.180**	**0.180**

4. **Agree** to charge this fiscal impact to the tax policy scorecard.

Agree / Disagree
Minister of Finance

Agree / Disagree
Minister of Revenue

5. **Note** the following departmental impact as a result of progressing the proposed motor vehicle changes, with a corresponding impact on the operating balance and net core Crown debt:

	$m - increase/(decrease)				
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Departmental:					
Implementation and administration costs	-	0.200	0.050	0.050	-
Total Operating	**-**	**0.200**	**0.050**	**0.050**	**-**

6. **Agree** to invite the departmental impacts as a result of progressing the proposed motor vehicle changes into the Budget process.

Agree / Disagree
Minister of Finance

Agree / Disagree
Minister of Revenue

s 9(2)(f)(iv)

8. **Agree** to the legislative timing for changes agreed to in recommendation 2:

   a. Pre-Budget/Budget announcement and inclusion in the taxation omnibus bill for 2026–27 **(Officials preferred option)**.

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

or

   b. Budget announcement and inclusion in budget night legislation.

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

9. **Agree** for officials to continue to engage with stakeholders on the detail of potential changes notwithstanding the Budget process (i.e., lift Budget secrecy in the design of final changes).

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

s 9(2)(f)(iv)

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

s 9(2)(a)

Bary Hollow
Principal Policy Advisor
Policy | Inland Revenue
5 March 2026

Hon Nicola Willis	Hon Simon Watts
Minister of Finance	**Minister of Revenue**
/ /2026	/ /2026

Appendix One

Motor vehicles

1. The motor vehicle proposals aim to simplify how FBT is paid on motor vehicles. This area was identified by the regulatory stewardship review as the most common area where misconceptions arise. These can be divided into the 'category approach' and 'hygiene' changes.

Motor vehicles – category approach

2. The main proposal simplifies the way FBT applies to motor vehicles. This is currently based on counting the days a vehicle is available for private use. The proposal would remove counting days and instead require a taxpayer to choose a category (depending on the private use of the vehicle) and use that rate when calculating their FBT liability.

3. The aim of this approach is to bring the calculation of FBT on motor vehicles closer to the remuneration aspect of the benefit. The issues paper proposed three categories which have been further developed to reflect stakeholder feedback into five categories. The revised categories are:

Table 1: Revised categories of vehicle use

Category	Limitations on use	Rate
1 – full private use	**Vehicle <u>mainly</u> for private use** (i.e., perk vehicles). The provision of the vehicle is generally reflected in the employee's remuneration package. For determining whether a vehicle is mainly for private use, the fact that other employees have access to the vehicle or not during business hours is ignored. Vehicle does not have to be branded.	100%
2 – partial private use	**Vehicle <u>mainly</u> for business use. Private use is permitted** during rostered days off, public holidays and/or statutory leave days and commuting to and from work. Vehicle must be branded.	35%
2b – limited private use farm vehicles	**Vehicle <u>mainly</u> for business use on farmland and used to support farming operations. Private use is permitted when not working.** Vehicle must be owned by a closely held company in the business of farming and used by a shareholder employee. Vehicle does not have to be branded.	35%
3 – minor private use	**Vehicle for business use. The only private use permitted is commuting** to and from work by the same employee (to the **same worksite**). The vehicle can be used for business use by others at work. Vehicle must be branded.	20%
4 – minor private use	**Vehicle for business use. The only private use permitted is commuting** to and from home to work where "work" requires travel across **multiple worksites**. The vehicle can be used for business use by others at work. Vehicle must be branded.	0%
4b – no private use pool car	**Vehicles <u>exclusively</u> for business use. No private use** (other than incidental use). Vehicle does not need to be sign written (i.e., pool vehicles). These vehicles are not allocated to a single employee.	0%

	Cat 1	Cat 2	Cat 2b	Cat 3	Cat 4	Cat 4b
Private use allowed on non-workdays	✓	✓	✓	✗	✗	✗
Extensive business use	✗	✗	✓	✗	✓	✓
Regular commuting permitted	✓	✓	✓	✓	✓	✗
Branding required	✗	✓	✗	✓	✓	✗
Incidental use permitted	✓ All categories					

4. The revised categories consider a range of feedback to include categories of vehicles that were missing from the original proposal and make the boundaries clearer. It also makes clear that we consider commuting to and from work personal use and taxable (this would be ignored when employers consider whether the vehicle is mainly used for business use). These categories would be set once the vehicle is acquired (provided to the employee).

5. The new categories also use the definition of "multiple worksites". This includes travel within the same business premises required for delivery of the services to the employer, examples:

   5.1 a farm worker takes a vehicle to work on a farm and uses it to travel around the farm to deliver services all day.

   5.2 a forestry worker drives from home to the forest and uses the vehicle around the forestry block all day to provide services to the employer.

6. We have generally had positive feedback on the category approach, mainly that it would save compliance costs. For example, one submitter on the original proposal in the issues paper suggested that this change could reduce compliance time by 750 hours per annum, when factoring in the time required to request, complete, and follow up vehicle logbooks.

7. Other changes to support the categories (and stakeholder feedback) are outlined below:

Proposal in the issues paper	Updated proposal	Rationale for change
Introduce a concept of "incidental travel" to ensure one-off non-remunerative use of a vehicle is ignored for FBT purposes.	Amended to allow for regular non-remunerative private use on the way to and from work (akin to the current permitted private use on work related vehicles).	Feedback was that there were some regular private use on the way to and from work that was not material that would not be covered by the proposed definition.
Remove the current work-related and emergency call exemptions.	No change	Submitters were in general agreement that the category and new exempt vehicle definition would account for these.
Exemption for vehicles providing emergency services to the New Zealand public.	Widen the types of vehicles that can use this exemption to capture a wider range of emergency vehicles.	Submitters raised organisations that did not originally feature in the definition that should have been captured.

Proposal in the issues paper	Updated proposal	Rationale for change
Major shareholder–employees of close companies would only be able to use category 2 or 3 when the cost base of the vehicle is less than $80,000.	Ministers decided not to proceed with this change.	Submitters suggested the value should have been $100,000 but per instruction this change will not proceed.
Commissioner can exempt certain motor vehicles from branding requirements.	Slightly widened exemption power.	Widened to capture other scenarios where branding isn't appropriate/necessary.

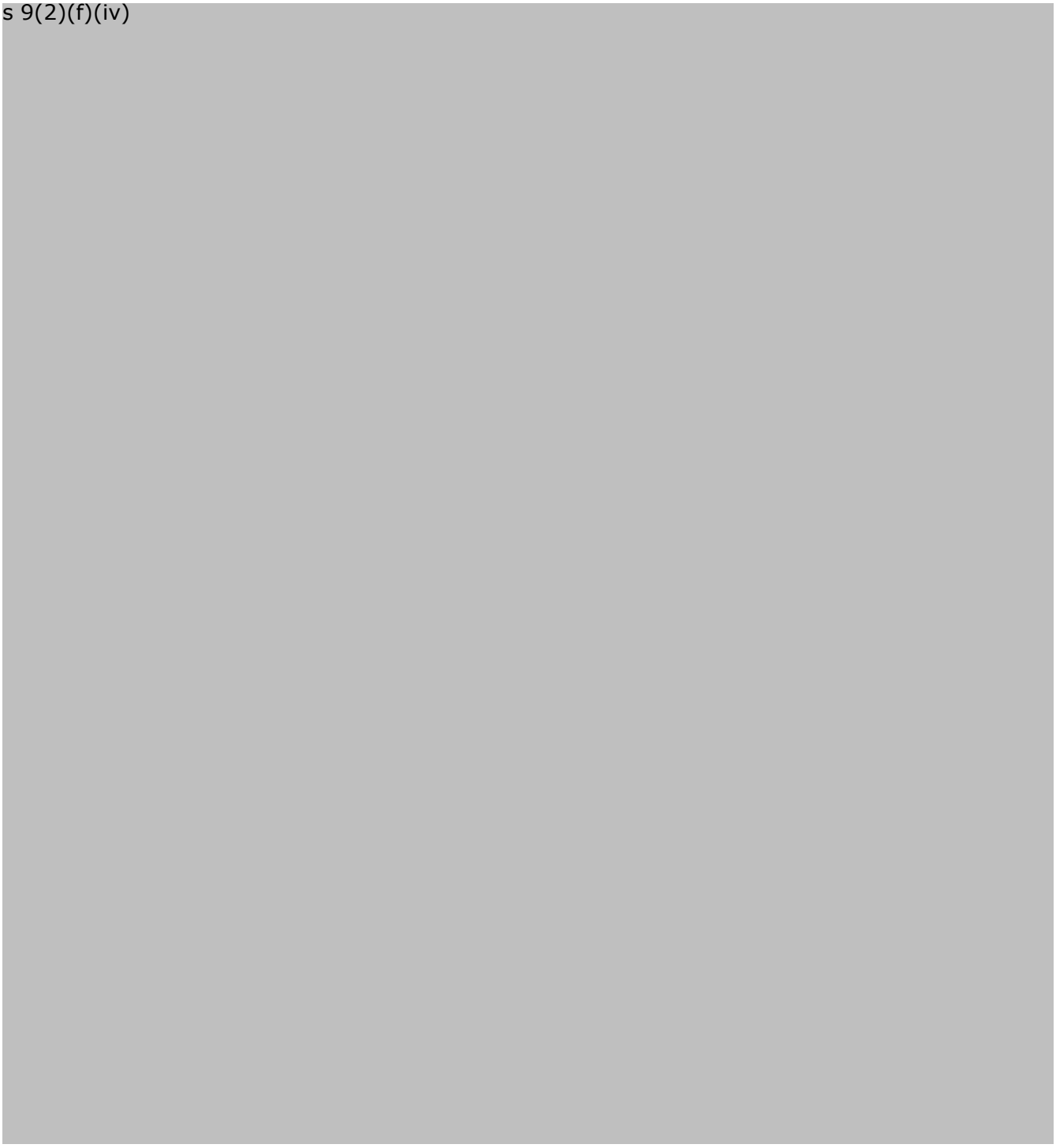
Hygiene changes

8. Other proposals in the issues paper modified and updated various areas of the motor vehicle rules. The updated proposals (and stakeholder feedback) are reflected below:

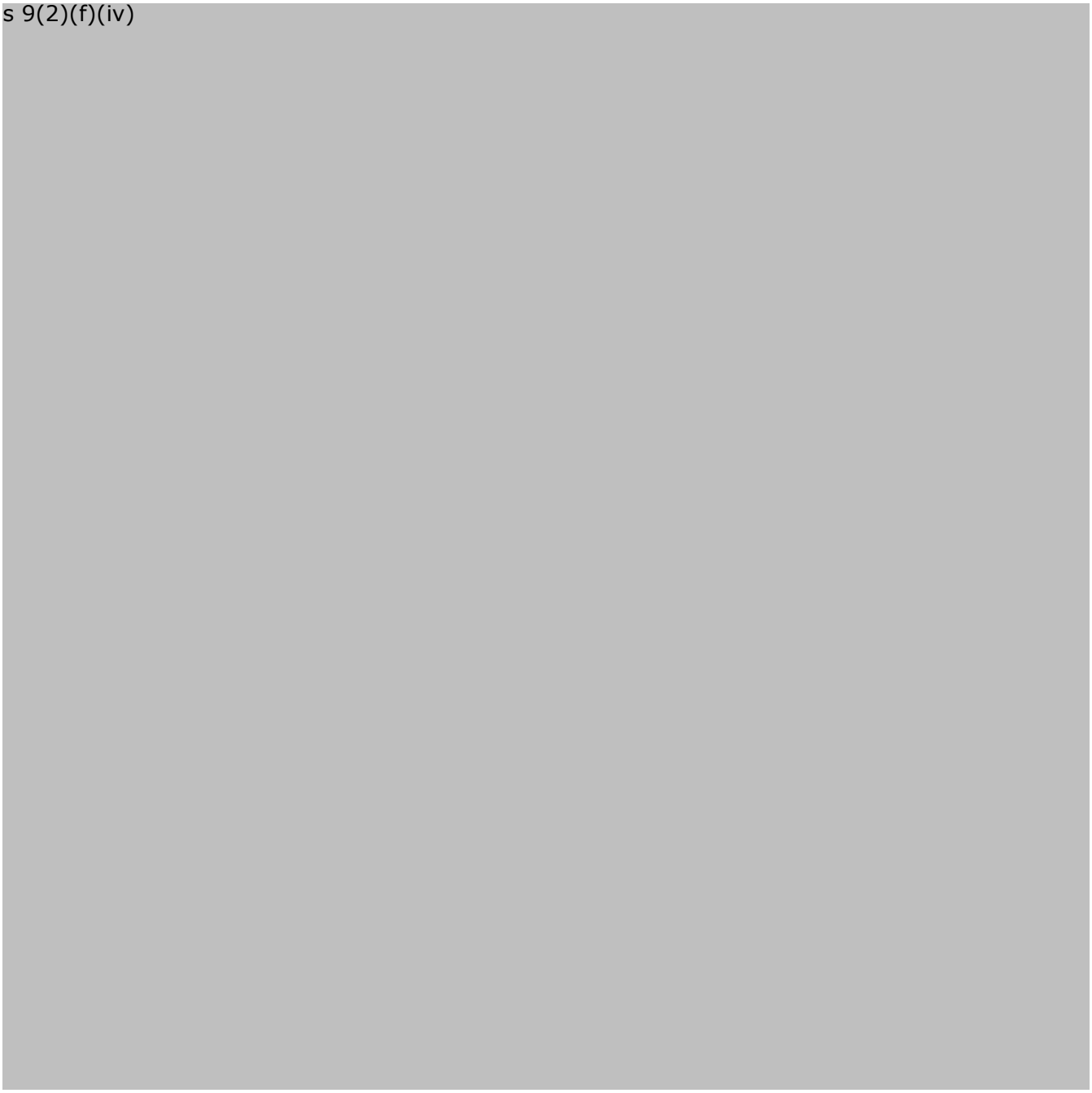
Proposal in the issues paper	Updated proposal	Rationale for change
Increase the weight limit for vehicles subject to FBT from 3,500kg to 4,500kg.	Increase to 6,000kg.	A higher weight limit was preferred by submitters.
Remove the ability to use tax book value as an option for valuing a motor vehicle.	Not proceeding.	Submitters preferred this option be retained and the removal would not materially reduce compliance costs.
New valuation calculation • Calculate the value of a motor vehicle with reference to external sources • Introduce an optional valuation basis depending on fuel type • Recalculate values every four years	No change.	Submitters were supportive of these changes.
New rates for calculating the value of a motor vehicle for FBT purposes (based on cost price of the vehicle): • standard default rate: 26% annually or 6.5% quarterly • hybrid vehicle: 22.4% annually or 5.6% quarterly • electric vehicles: 19.4% annually or 4.8% quarterly.	New rates (including a discount of 12.5%) **Cost base** • standard default rate: 22.8% annually or 5.7% quarterly; • hybrid vehicle: 19.6% annually or 4.9% quarterly; and • electric vehicles: 17.0% annually or 4.25% quarterly; **Tax book value option** • standard default rate: 40.25% annually or 10.1% quarterly; • hybrid vehicle: 34.13% annually or 8.53% quarterly; and	The discount built into the rates is to reflect the non-availability of the vehicle for private use due to mechanical issues etc.

Proposal in the issues paper	Updated proposal	Rationale for change
	• electric vehicles: 29.75% annually or 7.44% quarterly.	
No longer require taxpayers to maintain logbooks or day counts to count days the vehicle is unavailable for private use • Major-shareholders can still apply an alternate regime to account for the private use of the vehicles as a dividend (CX 17) instead of FBT.		This is a feature of the category approach which simplifies the regime, logbooks can still be used for certain taxpayers if desired under CX 17 (major shareholder employees). Amendments to section CX 17 are also proposed to make it more workable.

s 9(2)(f)(iv)



s 9(2)(f)(iv)



Inland Revenue
Te Tari Taake

POLICY

Tax policy report: Determining Funding Costs of Permanent Establishments of Foreign Banks

Date:	9 April 2025	**Priority:**	Medium
Security level:	Sensitive - Budget	**Report number:**	IR2025/100

Action sought

	Action sought	**Deadline**
Minister of Finance	**Agree** to recommendations	30 April 2025
Minister of Revenue	**Agree** to recommendations	30 April 2025

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**	**Suggested first contact**
Sam Rowe	Policy Lead	s 9(2)(a)	☐
Haydn Clark	Technical Specialist		☒

9 April 2025

Minister of Finance
Minister of Revenue

Determining Funding Costs of Permanent Establishments of Foreign Banks

Executive summary

Purpose

1. This report outlines some possible changes that the Government could make to how funding costs are calculated for permanent establishments[1] (PEs) of foreign banks to reduce profit shifting and seeks your approval to consult on them. These changes are based on OECD guidance and would be compatible with our Double Tax Agreements (DTAs).

Background

2. In 2024 you commissioned a review of the income tax settings of banks. In our initial report in October 2024 (IR2024/403) we advised that there are no significant issues with the taxation of the general operations of the banks, but reforms could be considered to address technical issues relating to the structure of equity and debt provided by foreign parents to their branches in New Zealand.

3. You indicated interest in further work on the attribution of funding to New Zealand branches (ie PEs) of foreign banks. On 19 February, you confirmed verbally at a Joint Ministers meeting that this work should continue on a Budget 2026 timeline.

Context

4. When an entity that is tax resident in another country operates in New Zealand through a PE, the Income Tax Act (ITA) provides New Zealand with the right to tax profits that are attributable to that PE. New Zealand's DTAs also give New Zealand the right to tax the profits to the extent they are attributable to that PE. As a PE is a part of an entity and not a separate legal entity, determining what income and expenditure is attributable to a PE is not a straightforward exercise.

5. The process of attributing income and expenditure to a PE presents tax planning opportunities. One example of this is that under current tax rules, foreign bank entities can increase funding costs for their New Zealand PEs by allocating them their most expensive tax deductible funding, thus reducing the PE's tax liability here.

6. The OECD issued guidance for determining funding costs of a PE in the 2008 and 2010 OECD Profit Attribution Reports. This guidance outlines different approaches that can be adopted, including one which would address the issue of expensive funding being allocated to PEs.

[1] Permanent establishment or PE is the term for an entity's fixed place of business in another country. A PE is often referred to as a branch of an entity. Double Tax Agreements give a country the right to tax profits attributable to a PE located there.

Materiality

7. There are currently s 6(c) foreign bank entities with PEs in New Zealand s 6(c) [2]. These PEs hold assets of approximately $60b.[3] Our initial estimate is that these changes would raise approximately $100m of tax revenue per year from these PEs, although this will depend somewhat on the final design details.

8. While the changes would increase the tax paid by foreign bank entities in New Zealand, they would not increase the total tax paid by each foreign bank entity worldwide, provided the head office country accepts the determination of funding costs in New Zealand ie the changes would generally only affect where taxes are paid but not the total amount of tax paid by affected foreign bank entities (except to the extent taxes in New Zealand are higher than in the bank's home jurisdiction there would be an increase, or to the extent they are lower there would be a decrease)[4].

9. A determination of funding costs in New Zealand based on the changes should generally be acceptable in a head office country as it would follow an approach outlined in OECD guidance. There is though, a risk of double taxation (or non-taxation) if the head office country requires the bank to adopt an alternative approach in its jurisdiction. It is not uncommon for countries to have different approaches[5] and DTAs provide a mechanism for working through differences via a process called the mutually agreed procedure. However, in cases where differences cannot be resolved via this process, the reform could in practice increase the global tax paid by banks to some extent. s 6(a) .[6]

Problem definition

10. Under current tax rules, a foreign bank entity can increase the funding costs of a PE in New Zealand by allocating expensive funding to the PE. The current approach also allows a PE to be 100% debt funded (which generates more tax deductions) although the entity of which it is a part is partially funded by equity (which does not generate tax deductions). As a result, a portion of profits generated in New Zealand can effectively be shifted to an entity's head office country.

Officials' currently preferred approach to address the problem

11. The guidance in the 2008 and 2010 OECD Profit Attribution Reports provides different approaches for determining a bank's funding costs. However, there is only one approach that will address the policy problem. That is to determine a bank PE's funding cost deductions based on the Fungibility Approach.

s 6(c)

[3] Banking businesses in New Zealand are largely operated by New Zealand resident entities (including local subsidiaries of foreign bank entities). PEs account for less than 10% of the New Zealand bank system total assets.
[4] Provided the home country rules exempt the PE income (as is the case in Australia, which has a 30% corporate tax rate), or provides a refundable tax credit for foreign income taxes.
[5] For example, Australia has an optional regime for determining funding costs of bank PEs in Australia based on the London Interbank Offer Rate or LIBOR which was a benchmark interest rate used to determine the average rate at which major banks lend to each other. This does not follow OECD guidance and therefore is unlikely to align with the approach in head office countries of foreign banks operating there (new benchmark rates are being considered due to the cessation of LIBOR).
s 6(a)

12. This approach recognises that a bank's pool of funds is fungible with respect to how those funds are applied, and that management has a great deal of flexibility in its application. As new borrowing will generally free other funds for other purposes, a portion of the bank's aggregated borrowing is attributed to each asset under the Fungibility Approach, resulting in a PE's funding costs being determined based on the average interest rate for the entity. If you would like to address the policy problem, our current thinking is that changes could be introduced requiring bank PEs to apply this approach.

13. There are potentially two ways that the Fungibility Approach could be implemented in practice[7]. One method could be to apportion an entity's total funding costs for financial reporting purposes based on the proportion of total debt held by the PE compared to the bank as a whole. We prefer this method because it is straightforward, and it faithfully reflects the fungibility concept. However, it is a significant change from the current framework (as it does not tax any individual debt funding instruments). Another method could be to determine a PE's interest costs, based on the average interest rate for the entity and the debt instruments attributed to the PE under the current approach. This approach is more complex but aligns with the current framework more closely.[8] The main difference between the two approaches is how foreign currency gains and losses are calculated.

14. To align the changes with the OECD guidance, funding costs should also include a markup on treasury costs that are allocated to PEs (to fairly allocate profit in relation to treasury services performed offshore). Funding costs should also be determined based on an allocation of an entity's equity capital (or "free capital")[9] to a PE, on a pre-determined basis.

15. Some consequential updates to the thin capitalisation rules and approved issuer levy rules for banks may also need to be made, depending on the design of the substantive changes.

16. These are initial conclusions, and they would benefit from consultation with banks to increase our understanding the potential impacts and practical challenges.

Next steps

17. If you would like to progress work on the changes, we recommend consulting with foreign banks that have PEs in New Zealand as well as their advisors and advocacy bodies as a next step. We should also consult with the Reserve Bank of New Zealand (RBNZ) on the changes.

18. s 6(c) , we recommend that consultation be initiated by officials issuing a targeted letter to each of these interested parties. However, we could issue a Government discussion document or official's consultation paper if you would prefer a wider public consultation.

19. Following consultation, we will report back to you with our recommendations. If we recommend changes and you agree, you could seek Cabinet approval for the changes as part of Budget 2026. If agreed, the changes could be included in the 2026 Omnibus Tax Bill.

[7] While there are technical differences, they would both raise approximately the same amount of revenue.
[8] This approach also has similarities with Australia's optional regime for Australian PEs (except Australia's regime uses LIBOR as the rate).
[9] Free capital refers to funding that is free of funding costs. Allocating free capital to a PE is important because it effectively deems a portion of a PE's funding to be 'equity like' so that it does not create income tax deductions.

Background

Current law

New Zealand Has a Right to Tax Profits of a Permanent Establishment

27. When an entity that is tax resident in another country operates in New Zealand through a PE, the Income Tax Act 2007 (ITA) provides New Zealand with a right to tax profits that are attributable to that PE. New Zealand's DTAs also give New Zealand the right to tax the entity's profits, but only to the extent they are attributable to that PE.

28. As a PE is a part of an entity and not a separate legal entity, determining what income and expenditure is attributable to a PE is not a straightforward exercise. Detailed guidance regarding how income and expenditure should be attributed to a PE is provided by the OECD in the commentary on its model tax treaty (the OECD Commentary) and in other published reports.

The Relevant Business Activity Approach

29. An approach to profit attribution that was previously endorsed by the OECD is referred to as the Relevant Business Activity (RBA) Approach. This approach is still applied by numerous countries, including New Zealand and Australia.

30. Under this approach, the profits attributable to a PE are determined based on the functions actually performed (taking into account assets used) by the PE. Based on this analysis, a portion of the income actually derived and expenditure actually incurred by the entity is attributed to a PE. This can allow an entity to allocate to the PE an entire loan from a third party, so that all the deductions for the resulting interest are claimed by the PE (for example where the funds raised are on-lent out of the PE). In addition, a bank PE can claim deductions for notional lending to it from the overseas part of the entity. This presents banks with tax planning opportunities. One example of this is that foreign bank entities can increase funding costs for their PEs by allocating them their most expensive funding, thus reducing the PE's New Zealand tax liability.

31. The OECD (and many jurisdictions) also consider that, when determining a PE's funding costs, the RBA Approach allows for the allocation of a portion of the entity's free capital[10] to a PE. The allocation of free capital to a PE is important because it can reduce a PE's interest expense by effectively deeming a portion of a PE's funding to be 'equity like' so that it does not create income tax deductions. However, New Zealand does not currently require free capital to be allocated to PEs. This means the PE can be treated as being 100% funded by interest bearing debt, even though the entity of which it is part is partially funded by equity and other non-interest bearing capital.

The Authorised OECD Approach

32. An alternative approach to profit attribution that is now preferred by the OECD is the Authorised OECD Approach or "AOA". The AOA seeks to more closely (but not completely) align the taxation of multinationals operating through PEs with the taxation of multinationals operating through subsidiaries. This is primarily achieved by requiring a PE's profits to be determined on the basis that it is a separate entity from the other parts of the entity of which it is a part. All internal 'dealings' between a PE and other parts of the entity must then be recognised for tax purposes and

[10] Free capital refers to funding that does not create income tax deductions, like share capital.

priced based on arm's length principles. The key distinction here is that this approach allows the entity to charge a profit margin on its non-core supplies to the PE.[11] In addition, it allows for things like deemed royalties and interest to be charged, but does not allow the source country to charge the withholding tax that would be payable if actual royalties and interest were charged.

33. We considered that this approach would create more tax planning opportunities and pose a risk to our tax base. For this reason New Zealand, along with many other countries (including Australia), has not adopted the AOA. However, we consider that the guidance on determining funding costs in the more recent AOA publications can be used under our RBA Approach[12] (as this guidance does not rely on us treating a PE as a separate entity, which is the key difference between the RBA Approach and the AOA).

34. The OECD guidance outlines different approaches that can be adopted, including one which would address the issue of expensive funding being allocated to PEs. The guidance leaves it open for countries to choose to adopt one or a mixture of the approaches. Legislative changes will need to be made to adopt a specific approach in New Zealand. These changes should be compatible with our DTAs.

Problem definition

35. Under current tax rules, a foreign bank can increase a New Zealand PE's funding costs by allocating expensive funding to the PE. The current rules also do not require any of the underlying's entity's free capital to be allocated to the PE, thus increasing its deductible interest costs. As a result, a portion of profits generated by a PE in New Zealand can effectively be shifted to an entity's head office country.

Risks

36. Banks may try to resist change to address this problem by saying that an increase in tax costs for their PEs will increase borrowing costs for New Zealanders. However, if the head office country accepts the determination of funding costs in New Zealand, an increase in the amount of tax paid in New Zealand due to the changes should generally result in an equivalent decrease in the amount of tax paid offshore (eg in Australia) with no net increase in a bank's costs worldwide.[13]

37. As the determination of funding costs in New Zealand would follow an approach in OECD issued guidance, it should be acceptable in a head office country. However, there is a risk of double taxation (or non-taxation) if the head office country requires the bank to adopt an alternative approach in its jurisdiction. It is not uncommon for countries to have different approaches and DTAs provide a mechanism for working through differences via a process called the mutually agreed procedure. An example of how differences can arise is Australia's optional regime for determining funding costs of bank PEs in Australia based on the London Interbank Offer Rate.[14] This optional regime does not follow OECD guidance and therefore is unlikely to align with the approach in head office countries of the foreign banks operating there.

[11] The AOA also allows a profit margin to be charged on the entity's core supplies to the PE, but the RBA Approach also allows this so it is not a point of distinction.
[12] We note that the Netherlands has taken a similar position where its tax treaties require the RBA Approach.
[13] Banks that have no increase in total taxes paid will create competitive pressure where a bank does experience an increase.
[14] The London Interbank Offer Rate or LIBOR was a benchmark interest rate used to determine the average rate at which major banks lend to each other. New benchmark rates are being considered because of the cessation of LIBOR.

38. In practice this means that a portion of the additional profit taxed by the measure could potentially also be taxable in other countries in some cases. While we do not expect this portion to be large, it would result in some double taxation. Accordingly, we expect this measure to be resisted by the banking sector, particularly Australian banks.

Options analysis

The Fungibility Approach

39. The OECD guidance in the 2008 and 2010 OECD Profit Attribution Reports outlines three approaches for calculating funding costs of a PE. They are:

- The Fungibility Approach. This involves determining an entity's total interest cost and allocating some of that cost to the PE, on a pre-determined basis.
- The Tracing Approach (which is similar to our current approach). This involves attributing specific funding to the PE and setting an interest rate by tracing the funding back to the original provider and using the interest rate charged by that person. The actual interest expense of the entity is allocated to the PE with no mark-up added.
- Pricing by reference to arm's length data. This involves recognising internal dealings between the PE and other parts of the entity where there is an "owner" of a financial asset (determined based on where significant related people functions are carried out). Interest is charged on these dealings at an arm's length price (with no credit rating differential margin as the dealing is between two parts of the same legal entity).

40. The only approach that will address the problem of banks allocating expensive funding to PEs is the Fungibility Approach. Under this approach a PE's funding costs are determined based on the average interest rate for the entity. The other approaches would allow high-cost funding to continue to be allocated to a PE to the detriment of the tax base.

41. In addition to addressing the policy problem, we think the Fungibility Approach is the most appropriate way to determine the funding costs of a bank PE and it will therefore improve coherence of the tax system. In this regard, it is helpful to consider what is meant when the OECD refers to the 'Fungibility' Approach. The fungibility concept is not intended to convey the idea that a bank's funding as a pool of debt liabilities is fungible, since debts are not fungible. An on-demand deposit is not the same as a bank certificate of deposit or bond for example. Rather the concept is intended to convey that the funds raised, irrespective of the source, are fungible. This means that any funds can be applied to generate any form of asset in any location the bank chooses.

42. In other words, the combination of short-term deposits and term loans raised by the bank can be applied to generate both long term mortgages or short-term corporate loans both domestically, and in the bank's foreign branches. In this sense the bank's pool of funds is fungible with respect to how those funds are applied, and management has a great deal of flexibility in its application. As new borrowing will generally free other funds for other purposes, it is appropriate to broadly attribute a portion of all borrowing to all assets, and to determine a PE's funding costs based on the average interest rate for the entity.

43. There are two ways that the Fungibility Approach could be implemented in practice. One way could be to apportion an entity's total funding costs for financial reporting purposes to the PE based on the proportion of debt held by the PE. We currently prefer this method because it is the simplest, and it most faithfully reflects the fungibility concept. However, it is more of a departure from current rules.[15][16]

44. Another method could be to determine the PE's interest costs based on the debt allocated to it under the current approach, but using the average interest rate for the entity as a whole (rather than the actual interest charged on the debt instruments allocated to the PE). This approach is more complex but aligns with current rules more closely. It also has similarities with Australia's optional regime for determining PE funding costs (except that a PE's average interest rate would be used instead of LIBOR). We think it would be useful to consult on both approaches before we recommend one.

Allowing a Markup on Treasury Costs

45. Normally, under the Relevant Business Activity (or RBA) Approach, other parts of an entity may be allocated a profit on supplies of core goods and services to the PE (such as loans in the case of a bank). However, the Fungibility Approach only allocates a portion of an entity's actual funding costs to a PE. This approach does not allocate any profit to other parts of the entity in relation to the bank's internal borrowing and lending activity. However, some profit allocation may be warranted where another part of the bank carries out treasury functions for the branch (such as raising the loans from third parties). This is allowed under the OECD guidance for the AOA.[17]

46. While New Zealand has not adopted the AOA, to increase alignment with the OECD guidance, an offshore treasury function markup could be included in the funding costs of a bank PE in addition to the funding costs allocated under the Fungibility Approach. We have identified two options for calculating a treasury function markup. They are:

- A treasury cost markup. This involves increasing the interest cost by a percentage of the actual treasury costs allocated to the PE ie a margin on the allocated treasury costs. Based on comparable markups in bank subsidiaries, 10% may be appropriate.
- An interest rate markup. This involves increasing the interest cost by a percentage of the allocated actual interest cost ie a margin on the allocated interest cost.

47. Our currently preferred approach for allocating profit on treasury functions is to include a markup on treasury costs in funding costs. This will mean that the markup is based on the level of treasury services provided to the PE offshore. A markup on funding costs is not preferred because there is not always a correlation between the treasury service provided and the level of funding. However, we think it would be useful to consult on both approaches before we recommend one.

[15] The current rules apply to individual debt instruments and require foreign currency gains or losses to be determined based on movements against the New Zealand dollar, whereas this method would apportion funding costs on total debt and foreign currency gains or losses would be determined based on movements against the entity's functional currency for financial reporting purposes (eg for Australian banks this would be the Australian dollar).

[17] This is because a PE can be charged the offshore treasury costs plus a markup under the AOA.

Allocating Free Capital

48. The OECD guidance outlines three approaches for allocating free capital to a PE. They are:

    - The Capital Allocation Approach. This involves allocating the actual free capital of the entity, on a predetermined basis (e.g. based on the PE's share of the entity's assets or assets and risks).
    - The Thin Capitalisation Approach. This involves allocating free capital based on what an independent entity would have if it were carrying on the same business as the PE by reference to data from comparable independent entities.
    - The Safe Harbour Approach. This involves allocating free capital based on regulatory requirements for an independent banking entity.

49. Our currently preferred approach for allocating free capital to a PE is the Capital Allocation Approach because this ensures that free capital is allocated based on the entity position and in line with industry norms. However, we think it is also worthwhile to consult on the other measures before we recommend one to you.

Consequential Changes

50. Depending on the design of the substantive changes, some consequential updates may need to be made to the thin capitalisation rules to account for free capital allocated to PEs, and to the approved issuer levy rules to account for changes to PE funding costs. We can provide further advice on these matters in our next report.

Consultation with Treasury

51. Treasury has been consulted and agrees with the advice in this report.

Financial implications

52. Our initial estimate is that the changes would raise additional revenue of approximately $100 million a year. This will depend on the final design.

Administrative implications

53. Implementation and on-going administration costs can be met through baseline funding.

Next steps

54. If you would like to progress work on the changes, we recommend consulting with foreign banks that have PEs in New Zealand as a next step. Given the high level of complexity s 6(c) of these changes, we recommend that consultation be initiated by officials issuing a targeted consultation letter to each of the 12 banks as well as their advisors and advocacy bodies. We also recommend consulting with the RBNZ. As the reforms are likely to be opposed by most banks, details of the targeted consultation may become widely public.

Recommended action

We recommend that you:

1. **agree** to progress work on potential changes that will require bank PEs to apply a Fungibility Approach for determining their funding costs;

   Agreed/Not agreed Agreed/Not agreed

2. **agree** that consultation on the potential changes should take place as a next step;

   Agreed/Not agreed Agreed/Not agreed

3. **agree** that consultation should cover methods for practically determining funding costs in accordance with the Fungibility Approach, proposals to include a markup on treasury costs in funding costs and to allocate a portion of an entity's actual free capital to a PE, and consequential updates to the thin capitalisation and approved issuer levy rules;

   Agreed/Not agreed Agreed/Not agreed

4. **agree** that consultation should be initiated by officials issuing a targeted consultation letter to bank PEs, related advisors and advocacy bodies and the RBNZ rather than the Government issuing a public discussion document or officials issuing a public issues paper;

   Agreed/Not agreed Agreed/Not agreed

5. **indicate** if you would like to see a copy of the targeted consultation letter before it is issued; and

   Yes/No Yes/No

6. **agree** that work on the changes should progress to timeframes that would allow for their inclusion in the 2026 Omnibus Tax Bill and for estimated revenue to be included in Budget 2026 forecasts.

   Agreed/Not agreed Agreed/Not agreed

s 9(2)(a)

Sam Rowe
Policy Lead
Policy

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

The Appendix is withheld in full under section 9(2)(g)(i) of the OIA

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **Determining Funding Costs of Branches of Foreign Banks**

Date:	31 July 2025	**Priority:**	Medium
Security level:	Sensitive - Budget	**Report number:**	IR2025/331

Action sought

	Action sought	**Deadline**
Minister of Finance	**Agree** to recommendations	15 August 2025
Minister of Revenue	**Agree** to recommendations	15 August 2025

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**	**Suggested first contact**
Sam Rowe	Policy Lead	s 9(2)(a)	☐
Haydn Clark	Technical Specialist		☒

31 July 2025

Minister of Finance
Minister of Revenue

Determining Funding Costs of Branches of Foreign Banks

Executive summary

Purpose

1. This report outlines some possible changes that the Government could make to how funding costs are calculated for permanent establishments[1] of foreign banks to reduce profit shifting and seeks your approval to consult on them. These changes are based on OECD guidance and would be compatible with our Double Tax Agreements (DTAs). Permanent establishments are commonly referred to as branches. We have used this common term in the remainder of the report.

Background

2. In 2024 you commissioned a review of the income tax settings of banks. In our initial report in October 2024 (IR2024/403) we advised that there are no significant issues with the taxation of the general operations of the banks, but reforms could be considered to address technical issues relating to the structure of equity and debt provided by foreign parents to their branches in New Zealand.

3. You indicated interest in further work on the attribution of funding to New Zealand branches of foreign banks. On 19 February, you confirmed verbally at a Joint Ministers meeting that this work should continue on a Budget 2026 timeline.

Context

4. When an entity that is tax resident in another country operates in New Zealand through a branch, the Income Tax Act (ITA) provides New Zealand with the right to tax profits that are attributable to that branch. New Zealand's DTAs also give New Zealand the right to tax the profits to the extent they are attributable to that branch. As a branch is a part of an entity and not a separate legal entity, determining what income and expenditure is attributable to a branch is not a straightforward exercise.

5. The process of attributing income and expenditure to a branch presents tax planning opportunities. One example of this is that under current tax rules, foreign bank entities can increase funding costs for their New Zealand branches by allocating them their most expensive tax deductible funding, thus reducing the branch's tax liability here.

6. The OECD issued guidance for determining funding costs of a branch in the 2008 and 2010 OECD Profit Attribution Reports. This guidance outlines different approaches that can be adopted, including one which would address the issue of expensive funding being allocated to branches.

[1] Permanent establishment is the term for an entity's fixed place of business in another country. Double Tax Agreements give a country the right to tax profits attributable to a permanent establishment located there.

Materiality

7. There are currently s 6(c) foreign bank entities with branches in New Zealand that would be affected by the changes. s 6(c) [redacted]

8. These branches hold assets of approximately $60 billion and as such account for less than 10% of the New Zealand bank system total assets.[2] Our initial estimate is that the changes proposed in this report would raise approximately $100 million of tax revenue per year from these branches, although this will depend somewhat on the final design details.

9. While the changes would increase the tax paid by foreign bank entities in New Zealand, they would not increase the total tax paid by each foreign bank entity worldwide, provided the head office country accepts the determination of funding costs in New Zealand i.e. the changes would generally only affect where taxes are paid but not the total amount of tax paid by affected foreign bank entities (except to the extent taxes in New Zealand are higher than in the bank's home jurisdiction there would be an increase, or to the extent they are lower there would be a decrease)[3]. For this reason, the changes outlined in this report should not cause any economic barriers for existing bank branches or new ones.

10. A determination of funding costs in New Zealand based on the changes should generally be acceptable in a head office country as it would follow an approach outlined in OECD guidance. There is though, a risk of double taxation (or non-taxation) if the head office country requires the bank to adopt an alternative approach in its jurisdiction. It is not uncommon for countries to have different approaches[4] and DTAs provide a mechanism for working through differences. However, in cases where differences cannot be resolved, the reform could in practice increase the global tax paid by foreign banks with New Zealand branches to some extent. s 6(a) [redacted]

11. In New Zealand, branches are almost entirely engaged in wholesale business. This is because of restrictions imposed on them by the Reserve Bank of New Zealand (RBNZ) which limit their ability to undertake retail business[5]. As wholesale customers are typically able to secure funding from a range of sources, including from locally incorporated entities and directly from domestic or foreign wholesale debt capital markets, competitive forces will mean that it is unlikely that branches can pass on any increased tax costs to their customers.

[2] Banking businesses in New Zealand are largely operated by New Zealand resident entities (including local subsidiaries of foreign bank entities).
[3] Provided the home country rules exempt the branch income (as is the case in Australia, which has a 30% corporate tax rate), or provides a refundable tax credit for foreign income taxes.
[4] For example, Australia has an optional regime for determining funding costs of bank branches in Australia based on the London Interbank Offer Rate (LIBOR) which was a benchmark interest rate used to determine the average rate at which major banks lend to each other. This does not follow OECD guidance and therefore is unlikely to align with the approach in head office countries of foreign banks operating there. New benchmark rates are being trialled due to the cessation of LIBOR.
[5] The RBNZ completed a review of its policy for branches in 2023. As a result of this review, the RBNZ's new policy is that branches will be completely prohibited from engaging in retail business. This new policy is expected to take effect in 2028.

Problem definition

12. Under current tax rules, a foreign bank entity can increase the funding costs of a branch in New Zealand by allocating expensive funding to the branch. The current approach also allows a branch to be 100% debt funded (which generates more tax deductions) although the entity of which it is a part is partially funded by equity (which does not generate tax deductions). As a result, a portion of profits generated in New Zealand can effectively be shifted to an entity's head office country.

Officials' currently preferred approach to address the problem

13. The guidance in the 2008 and 2010 OECD Profit Attribution Reports provides different approaches for determining a branch's funding costs. However, there is only one approach that will address the policy problem. That is to determine a bank branch's funding cost deductions based on the Fungibility Approach.

14. This approach recognises that a bank's pool of funds is fungible with respect to how those funds are applied, and that management has a great deal of flexibility in its application. As new borrowing will generally free other funds for other purposes, a portion of the bank's aggregated borrowing is attributed to each asset under the Fungibility Approach, resulting in a branch's funding costs being determined based on the average cost of funds rate for the entity. If you would like to address the policy problem, our current thinking is that changes could be introduced requiring bank branches to apply this approach.

15. There are potentially two ways that the Fungibility Approach could be implemented in practice.[6] One method could be to apportion an entity's total funding costs for financial reporting purposes based on the proportion of total debt held by the branch compared to the bank as a whole. We prefer this method because it is straightforward, and it faithfully reflects the fungibility concept. However, it is a significant change from the current framework (as it does not tax any individual debt funding instruments). Another method could be to determine a branch's interest costs, based on the debt instruments attributed to the branch under the current approach but to limit funding cost deductions each year based on the average rate that interest was incurred by the entity as a whole (rather than allow a deduction for all the actual interest charged). This approach is more complex but aligns with the current framework more closely.[7] The main difference between the two approaches is that the first approach would determine a single deduction for total funding costs while the second would cap funding cost deductions for actual debt instruments allocated to a branch, on an instrument-by-instrument basis.

16. Requiring a specific approach should help to develop a level playing field for banks by ensuring that branches determine their funding cost deductions in a uniform way, and by more closely aligning the funding costs of bank branches with bank entities.

17. To align the changes with the OECD guidance, funding costs should also include a markup on treasury costs that are allocated to branches (to fairly allocate profit in relation to treasury services performed offshore). Funding costs should also be determined based on an allocation of an entity's equity capital (or "free capital")[8] to a branch, on a pre-determined basis.

[6] While there are technical differences, they would both raise approximately the same amount of revenue.
[7] This approach also has similarities with Australia's optional regime for Australian branches (except Australia's regime uses LIBOR as the rate).
[8] Free capital refers to funding that is free of funding costs. Allocating free capital to a branch is important because it effectively deems a portion of a branch's funding to be 'equity like' so that it does not create income tax deductions.

18. Some consequential updates to the thin capitalisation rules and approved issuer levy rules for banks may also need to be made, depending on the design of the substantive changes.

19. These are initial conclusions, and they would benefit from consultation with banks to increase our understanding the potential impacts and practical challenges.

Next steps

20. If you would like to progress work on the changes, we recommend consulting with foreign banks that have branches in New Zealand as well as their advisors and advocacy bodies as a next step. We should also consult with the RBNZ on the detailed design.

21. As the changes are complex s 6(c) , we recommend that consultation be initiated by officials issuing a targeted letter to each of these interested parties. We have attached a draft targeted consultation letter. However, we could issue a Government discussion document or official's consultation paper if you would prefer a wider public consultation.

22. Following consultation, we will report back to you with our recommendations. If we recommend changes and you agree, you could seek Cabinet approval for the changes as part of Budget 2026. If agreed, the changes could be included in the 2026 Omnibus Tax Bill.

Background

Current law

New Zealand Has a Right to Tax Profits of a Branch

27. When an entity that is tax resident in another country operates in New Zealand through a branch, the Income Tax Act 2007 (ITA) provides New Zealand with a right to tax profits that are attributable to that branch. New Zealand's DTAs also give New Zealand the right to tax the entity's profits, but only to the extent they are attributable to that branch.

28. As a branch is a part of an entity and not a separate legal entity, determining what income and expenditure is attributable to a branch is not a straightforward exercise. Detailed guidance regarding how income and expenditure should be attributed to a branch is provided by the OECD in the commentary on its model tax treaty (the OECD Commentary) and in other published reports.

The Relevant Business Activity Approach

29. An approach to profit attribution that was previously endorsed by the OECD is referred to as the Relevant Business Activity (RBA) Approach. This approach is still applied by numerous countries, including New Zealand and Australia.

30. Under this approach, the profits attributable to a branch are determined based on the functions actually performed (taking into account assets used) by the branch. Based on this analysis, a portion of the income actually derived and expenditure actually incurred by the entity is attributed to a branch. This can allow an entity to allocate to the branch an entire loan from a third party, so that all the deductions for the resulting interest are claimed by the branch (for example where the funds raised are on-lent out of the branch). In addition, a bank branch can claim deductions for notional lending to it from the overseas part of the entity. This presents banks with tax planning opportunities. One example of this is that foreign bank entities can increase funding costs for their branches by allocating them their most expensive funding, thus reducing the branch's New Zealand tax liability.

31. The OECD (and many jurisdictions) also consider that, when determining a branch's funding costs, the RBA Approach allows for the allocation of a portion of the entity's free capital[9] to a branch. The allocation of free capital to a branch is important because it can reduce a branch's interest expense by effectively deeming a portion of a branch's funding to be 'equity like' so that it does not create income tax deductions. However, New Zealand does not currently require free capital to be allocated to branches. This means a branch can be treated as being 100% funded by interest bearing debt, even though the entity of which it is part is partially funded by equity and other non-interest bearing capital.

The Authorised OECD Approach

32. An alternative approach to profit attribution that is now preferred by the OECD is the Authorised OECD Approach or "AOA". The AOA seeks to more closely (but not completely) align the taxation of multinationals operating through branches with the taxation of multinationals operating through subsidiaries. This is primarily achieved by requiring a branch's profits to be determined on the basis that it is a separate entity from the other parts of the entity of which it is a part. All internal 'dealings' between a branch and other parts of the entity must then be recognised

[9] Free capital refers to funding that does not create income tax deductions, like share capital.

for tax purposes and priced based on arm's length principles. The key distinction here is that this approach allows the entity to charge a profit margin on its non-core supplies to the branch.[10] In addition, it allows for things like deemed royalties and interest to be charged, but does not allow the source country to charge the withholding tax that would be payable if actual royalties and interest were charged.

33. We considered that this approach would create more tax planning opportunities and pose a risk to our tax base. For this reason, New Zealand, along with many other countries (including Australia), has not adopted the AOA. However, we consider that the guidance on determining funding costs in the more recent AOA publications can be used under our RBA Approach[11] (as this guidance does not rely on us treating a branch as a separate entity, which is the key difference between the RBA Approach and the AOA).

34. The OECD guidance outlines different approaches that can be adopted, including one which would address the issue of expensive funding being allocated to branches. The guidance leaves it open for countries to choose to adopt one or a mixture of the approaches. Legislative changes will need to be made to adopt a specific approach in New Zealand. These changes should be compatible with our DTAs.

Problem definition

35. Under current tax rules, a foreign bank can increase a New Zealand branch's funding costs by allocating expensive funding to the branch. Branches of foreign banks consistently earn significantly lower net interest income margins compared with the entities of which they are a part which indicates that this problem is ingrained and widespread. The current rules also do not require any of the underlying entity's free capital to be allocated to the branch, thus increasing its deductible interest costs. As a result, a portion of profits generated by a branch in New Zealand can effectively be shifted to an entity's head office country.[12]

Risks

36. Banks may try to resist change to address this problem by saying that an increase in tax costs for their branches will increase borrowing costs for New Zealanders. However, if the head office country accepts the determination of funding costs in New Zealand, an increase in the amount of tax paid in New Zealand due to the changes should generally result in an equivalent decrease in the amount of tax paid offshore (e.g. in Australia) with no net increase in a bank's costs worldwide.[13]

37. As the determination of funding costs in New Zealand would follow an approach in OECD issued guidance, it should be acceptable in a head office country. However, there is a risk of double taxation (or non-taxation) if the head office country requires the bank to adopt an alternative approach in its jurisdiction. It is not uncommon for countries to have different approaches and DTAs provide a mechanism for working through differences. An example of how differences can arise is Australia's optional regime for determining funding costs of bank branches in Australia based on the London Interbank Offer Rate.[14] This optional regime does not follow OECD guidance

[10] The AOA also allows a profit margin to be charged on the entity's core supplies to the branch, but the RBA Approach also allows this so it is not a point of distinction.
[11] We note that the Netherlands has taken a similar position where its tax treaties require the RBA Approach.
[12] s 6(a)
[13] Banks that have no increase in total taxes paid will create competitive pressure where a bank does experience an increase.
[14] The London Interbank Offer Rate or LIBOR was a benchmark interest rate used to determine the average rate at which major banks lend to each other in the money market, i.e. short term generally overnight or out to 3 months. New benchmark rates are being trialled because of the cessation of LIBOR.

and therefore is unlikely to align with the approach in head office countries of the foreign banks operating there.

38. In practice this means that a portion of the additional profit taxed by the measure could potentially also be taxable in other countries in some cases. While we do not expect this portion to be large, it would result in some double taxation. Accordingly, we expect this measure to be resisted by the banking sector, s 6(a)

39. In New Zealand, branches of foreign banks are almost entirely engaged in wholesale business due to restrictions imposed on them by RBNZ which limit their ability to undertake retail business[15]. It is unlikely that any increased tax costs can be passed on to their wholesale customers, as these customers can typically secure funding from a range of sources.[16]

Options analysis

The Fungibility Approach

40. The OECD guidance in the 2008 and 2010 OECD Profit Attribution Reports outlines three approaches for calculating funding costs of a branch. They are:

- The Fungibility Approach. This involves determining an entity's total interest cost and allocating some of that cost to the branch, on a pre-determined basis.
- The Tracing Approach (which is similar to our current approach). This involves attributing specific funding to the branch and setting an interest rate by tracing the funding back to the original provider and using the interest rate charged by that person. The actual interest expense of the entity is allocated to the branch with no mark-up added.
- Pricing by reference to arm's length data. This involves recognising internal dealings between the branch and other parts of the entity where there is an "owner" of a financial asset (determined based on where significant related people functions are carried out). Interest is charged on these dealings at an arm's length price (with no credit rating differential margin as the dealing is between two parts of the same legal entity).

41. The only approach that will address the problem of banks allocating expensive funding to branches is the Fungibility Approach. Under this approach a branch's funding costs are determined based on the average cost of funds rate for the entity. The other approaches would allow high-cost funding to continue to be allocated to a branch to the detriment of the tax base.

42. In addition to addressing the policy problem, we think the Fungibility Approach is the most appropriate way to determine the funding costs of a bank branch and it will therefore improve coherence of the tax system. In this regard, it is helpful to consider what is meant when the OECD refers to the 'Fungibility' Approach. The fungibility concept is not intended to convey the idea that a bank's funding as a pool of debt liabilities is fungible, since debts are not fungible. An on-demand deposit is not the same as a bank certificate of deposit or bond for example. Rather the concept is intended to convey that the funds raised, irrespective of the source, are

[15] The RBNZ completed a review of its policy for branches in 2023. As a result of this review, the RBNZ's new policy is that branches will be completely prohibited from engaging in retail business. This new policy is expected to take effect in 2028.
[16] Including from locally incorporated entities and directly from domestic or foreign wholesale debt capital markets.

fungible. This means that any funds can be applied to generate any form of asset in any location the bank chooses.

43. In other words, the combination of short-term deposits and term loans raised by the bank can be applied to generate both long term mortgages or short-term corporate loans both domestically, and in the bank's foreign branches. In this sense the bank's pool of funds is fungible with respect to how those funds are applied, and management has a great deal of flexibility in its application. As new borrowing will generally free other funds for other purposes, it is appropriate to broadly attribute a portion of all borrowing to all assets, and to determine a branch's funding costs based on the average interest rate for the entity.

44. There are two ways that the Fungibility Approach could be implemented in practice[17]. One way could be to apportion an entity's total funding costs for financial reporting purposes to the branch based on the proportion of debt held by the branch. We currently prefer this method because it is the simplest, and it most faithfully reflects the fungibility concept. However, it is more of a departure from current rules.[18]

45. Another method could be to determine the branch's interest costs based on the debt allocated to it under the current approach, but to limit funding cost deductions each year based on the average rate that interest was incurred by the entity as a whole for the year (rather than allow a deduction for all the actual interest charged on the debt instruments allocated to the branch). This approach is more complex but aligns with current rules more closely. [19] It also has similarities with Australia's optional regime for determining branch funding costs (except that Australia's regime imposes a cap based on a benchmark rate).

46. The main difference between the two approaches is that the first approach would determine a single deduction for total funding costs while the second would cap funding cost deductions for actual debt instruments allocated to a branch, on an instrument-by-instrument basis. We think it would be useful to consult on both approaches before we recommend one.

Allowing a Markup on Treasury Costs

47. Normally, under the Relevant Business Activity (or RBA) Approach, other parts of an entity may be allocated a profit on supplies of core goods and services to the branch (such as loans in the case of a bank). However, the Fungibility Approach only allocates a portion of an entity's actual funding costs to a branch. This approach does not allocate any profit to other parts of the entity in relation to the bank's internal borrowing and lending activity. However, some profit allocation may be warranted where another part of the bank carries out treasury functions for the branch (such as raising the loans from third parties). This is allowed under the OECD guidance for the AOA.[20]

48. While New Zealand has not adopted the AOA, to increase alignment with the OECD guidance, an offshore treasury function markup could be included in the funding costs of a bank branch in addition to the funding costs allocated under the Fungibility Approach. We have identified two options for calculating a treasury function markup. They are:

[17] While there are technical differences, they would both raise approximately the same amount of revenue.
[18] The current rules apply to individual debt instruments and require foreign currency gains or losses to be determined based on movements against the New Zealand dollar, whereas this method would apportion funding costs on the entity's total debt and foreign currency gains or losses would be determined based on movements against the entity's functional currency for financial reporting purposes (e.g. for Australian banks this would be the Australian dollar).
[19] This is because funding costs would be determined based on the debt instruments actually allocated to the branch, on an instrument-by-instrument basis.
[20] This is because a branch can be charged the offshore treasury costs plus a markup under the AOA.

- A treasury cost markup. This involves increasing the interest cost by a percentage of the actual treasury costs allocated to the branch i.e. a margin on the allocated treasury costs. Based on comparable markups in bank subsidiaries, 10% may be appropriate.

- An interest rate markup. This involves increasing the interest cost by a percentage of the allocated actual interest cost i.e. a margin on the allocated interest cost.

49. Our currently preferred approach for allocating profit on treasury functions is to include a markup on treasury costs in funding costs. This will mean that the markup is based on the level of treasury services provided to the branch from offshore. A markup on funding costs is not preferred because there is not always a correlation between the treasury service provided and the level of funding. However, we think it would be useful to consult on both approaches before we recommend one.

Allocating Free Capital

50. The OECD guidance outlines three approaches for allocating free capital to a branch. They are:

- The Capital Allocation Approach. This involves allocating the actual free capital of the entity, on a predetermined basis (e.g. based on the branch's share of the entity's assets or assets and risks).

- The Thin Capitalisation Approach. This involves allocating free capital based on what an independent entity would have if it were carrying on the same business as the branch by reference to data from comparable independent entities.

- The Safe Harbour Approach. This involves allocating free capital based on regulatory requirements for an independent banking entity.

51. Our currently preferred approach for allocating free capital to a branch is the Capital Allocation Approach because this ensures that free capital is allocated based on the entity position and in line with industry norms. However, we think it is also worthwhile to consult on the other measures before we recommend one to you.

Consequential Changes

52. Depending on the design of the substantive changes, some consequential updates may need to be made to the thin capitalisation rules to account for free capital allocated to branches, and to the approved issuer levy rules to account for changes to branch funding costs. We can provide further advice on these matters in our next report.

Consultation with the Treasury, the RBNZ and s 6(a)

53. The Treasury has been consulted and agrees with the advice in this report. We have talked with the RBNZ about the proposals, and they have no concerns with the changes being considered.

54. s 6(a)

Financial implications

55. Our initial estimate is that the changes would raise additional revenue of approximately $100 million a year. This will depend on the final design. We will provide an updated estimate when we report back with recommendations following the consultation process.

Administrative implications

56. Implementation and on-going administration costs can be met through baseline funding.

Next steps

57. If you would like to progress work on the changes, we recommend consulting with foreign banks that have branches in New Zealand as a next step. Given the high level of complexity s 6(c) of these changes, we recommend that consultation be initiated by officials issuing a targeted consultation letter (attached) to each of the s 6(c) banks as well as their advisors and advocacy bodies. We also recommend consulting with the RBNZ further on the detailed design. As the reforms are likely to be opposed by most banks, details of the targeted consultation may become widely public.

Recommended action

We recommend that you:

1. **agree** to progress work on potential changes that will require bank branches to apply a Fungibility Approach for determining their funding costs;

   Agreed/Not agreed Agreed/Not agreed

2. **agree** that consultation on the potential changes should take place as a next step;

   Agreed/Not agreed Agreed/Not agreed

3. **agree** that consultation should cover methods for practically determining funding costs in accordance with the Fungibility Approach, proposals to include a markup on treasury costs in funding costs and to allocate a portion of an entity's actual free capital to a branch, and consequential updates to the thin capitalisation and approved issuer levy rules;

   Agreed/Not agreed Agreed/Not agreed

4. **agree** that consultation should be initiated by officials issuing a targeted consultation letter to bank branches, related advisors and advocacy bodies and the RBNZ rather than the Government issuing a public discussion document or officials issuing a public issues paper;

   Agreed/Not agreed Agreed/Not agreed

5. **indicate** if you have any feedback on the draft targeted consultation letter; and

   Yes/No Yes/No

6. **agree** that work on the changes should progress to timeframes that would allow for their inclusion in the 2026 Omnibus Tax Bill and for estimated revenue to be included in Budget 2026 forecasts.

Agreed/Not agreed

Agreed/Not agreed

Sam Rowe
Policy Lead
Policy

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

The Appendix is withheld in full under section 9(2)(g)(i) of the OIA

Inland Revenue
Te Tari Taake
Policy
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New Zealand

T. 04 890 1500

Briefing note

Reference: BN2025/347

Date: 3 September 2025

To: Revenue Advisor, Minister of Finance – Carl Harris
Revenue Advisor, Minister of Revenue – Angela Graham
Private Secretary, Minister of Revenue – Helen Kuy

From: Haydn Clark and Rory Tait

Subject: **Communications Plan for Consultation on Determining Funding Costs of Permanent Establishments of Foreign Banks**

Context

1. The Government has authorised officials to consult with relevant stakeholders on possible changes to how funding costs are calculated for permanent establishments of foreign banks [IR2025/331 refers]. The consultation seeks to inform formative thinking on possible changes that would seek to reduce profit-shifting behaviour while being consistent with OECD guidance.

2. The consultation has the potential to generate interest from the public, s 6(c) The Minister of Finance also asked us to consider proactive communications. This briefing note sets out our communications plan for the targeted consultation.

Communications plan for consultation

3. We plan to take a light-touch approach to communications as these policy issues are technical and specific. Officials are still early in the policy process where we would like to test stakeholder views on the problem while developing possible solutions. As such, we've decided to use a targeted and limited communications strategy instead of something broad or high profile. If following consultation, the Government chooses to make a legislative change, there will be an opportunity for further stakeholder engagement via the select committee process.

Targeted consultation letter to be circulated

4. We intend to share the targeted consultation letter [IR2025/331 refers] s 6(c) related advisors, industry associations, the RBNZ, selected tax academics and s 6(a) . This is broader than originally planned as this will produce a wider range of feedback and views, especially if there is media interest in the issue.

Reactive engagement

5. s 9(2)(g)(i)

s 9(2)(g)(i)

6. s 6(c)

Consultation with the Treasury and the RBNZ

7. The Treasury and the RBNZ have been consulted on the issues being considered.

8. The Treasury was not informed about this briefing note.

Sam Rowe
Policy Lead
s 9(2)(a)

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **Determining Funding Costs of Branches of Foreign Banks**

Date:	27 November 2025	**Priority:**	Medium
Security level:	Sensitive - Budget	**Report number:**	IR2025/464

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to recommendations	11 December 2025
Minister of Revenue	**Agree** to recommendations	11 December 2025

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Sam Rowe	Policy Lead	s 9(2)(a)	☒
Haydn Clark	Principal Policy Advisor		☐

27 November 2025

Minister of Finance
Minister of Revenue

Determining Funding Costs of Branches of Foreign Banks

Executive summary

Purpose

1. This report sets out feedback from stakeholders on potential changes to how funding costs are calculated for permanent establishments[1] of foreign banks, advice on how the proposals could be revised to address the feedback, and recommended next steps. Permanent establishments are commonly called branches. We've used this common term in the rest of the report.

Context

2. In our July 2025 report (IR2025/331) we asked for approval to consult on possible changes to how funding costs are calculated for branches. The report outlined initial conclusions that needed further input from stakeholders and noted a double taxation risk. You asked us to progress this work to a Budget 2026 timeline.

Materiality

3. There are s 6(c) foreign bank entities with branches in New Zealand. These branches hold about $60 billion of assets[2] and account for less than 10% of the New Zealand bank system total assets. Branches mainly do wholesale business because of restrictions set by the Reserve Bank of New Zealand (RBNZ) that limit their participation in retail activities.

Problems and solutions consulted on

4. We consulted on two problems. Current tax rules do not require an entity's free capital[3] (e.g. its share equity) to be allocated to its branch. This allows a branch to be allocated more debt which increases its tax deductions. An entity can also fund its branch entirely with more expensive long-term debt, which also increases its tax deductions. As a result, a portion of profits generated in New Zealand can effectively be reported in an entity's head office country.

5. The solutions we consulted on were based on guidance in the 2010 OECD Profit Attribution Report ("the OECD guidance"). We consulted on three approaches for allocating free capital to a branch. They involve allocating an entity's capital to its branch based on either the branch's share of the entity's risk weighted assets, data from comparable independent entities, or regulatory requirements for an independent banking entity. We preferred the first approach because this would ensure an allocation based on the entity's actual position, and in line with industry norms.

[1] Permanent establishment is the term for an entity's fixed place of business in another country.
[2] s 6(c)
[3] Free capital refers to capital that does not result in tax deductions such as equity and retained earnings.

6. We consulted on two practical methods for allocating funding costs to a branch based on a fungibility approach (that is, an entity's average cost of funds). The first involves apportioning an entity's total funding costs for financial reporting purposes based on the proportion of total debt held by the branch compared to the entity as a whole. The second involves limiting a branch's funding cost deductions each year based on the average rate that interest was incurred by the entity as a whole.

Feedback from stakeholders

7. Stakeholders had mixed views on the capital allocation problem. Some thought that there was no problem because the thin capitalisation rules already address capital allocation concerns, some were unsure if there was one, and some thought that making changes in this area would not be unreasonable.

8. Stakeholders were broadly concerned about allocating an entity's actual capital to a branch on a proportional basis because this would mean that branches and entities would have different tax capital requirements, which could disrupt commercial decision making. The stakeholders who thought that changes could be made preferred raising the thin capitalisation threshold to address the problem (the third of three approaches we consulted on). This would preserve the neutral tax treatment of entities and branches, and stakeholders felt it would be less complex.

9. Stakeholders unanimously disagreed that branches being funded entirely with long-term funding was a policy problem. Only two stakeholders gave reasons for their view. They thought that transfer pricing principles already require an appropriate mix of funding in a branch. Additionally, as matching the term of a branch's debt funding with the term of its assets (which are typically long-term loans) is common commercial practice for managing liquidity risk, they considered that the current approach results in an appropriate mix of funding.

10. Stakeholders also did not support the solutions. They were concerned that:

    - The solutions would not allocate any of the costs of raising short-term funding to a branch, but it would use that short-term funding in calculating its interest deductions.
    - The solutions also did not appropriately account for differences in interest rates associated with currencies – the solutions would effectively use the currency of the headquarter country to calculate the borrowing costs, but interest rates might be different when borrowing in the headquarter country's currency than in New Zealand dollars. As a result the true New Zealand dollar borrowing costs would be misstated.
    - The solutions were a significant departure from common commercial practice for pricing internal funding, which is widely accepted for tax purposes, and they ignored actual third-party transactions entered by a branch.

11. Stakeholders thought that these problems would cause a significant risk of material double taxation which would potentially drive businesses to either incorporate or provide lending offshore instead of using branches, increase interest rates charged to customers, or exit New Zealand altogether.

Officials' responses

12. We still think that there is a problem with the current rules not requiring capital to be allocated to a branch. Prudential capital requirements have risen globally to levels that substantially exceed the current tax thin capitalisation ratio; for example, the Tier 1 capital ratio plus the prudential capital buffer[4] for systemically important

[4] This is a cushion of capital that banks must hold above their minimum Tier 1 capital requirements.

New Zealand banking entities is 12.5%, compared to a thin capitalisation ratio of 6%. Consequently, branches can hold additional debt (effectively using the difference between the regulatory capital required and the capital required under the thin capitalisation rules), thereby increasing their tax deductions.

13. However, we acknowledge that allocating capital to a branch on a proportional basis could disrupt the neutral treatment of entities and branches, potentially leading to undesirable commercial impacts and affecting competition. We agree with stakeholders that the problem could better be addressed by raising the thin capitalisation threshold. This would resolve concerns about tax neutrality.

14. We recommend progressing work on changes to the thin capitalisation rules to address the problem.[5] Raising the thin capitalisation threshold would increase the amount of aggregate capital that a foreign owned New Zealand banking group is required to hold, so it would apply to a group's New Zealand branches, banking entities and any holding company on a consolidated basis (which is a broader scope than the original proposal). This will also protect the tax base from more debt being loaded into banking groups via holding companies.

15. We also still think there is a problem with branches being funded mostly with long-term debt, which is more expensive. This is because when a branch is funded in this way, the profits it is allocated do not reflect the results that would usually be expected from maturity transformation – this is the normal money-making process of a conventional bank.[6]

16. We do agree with stakeholders though that the proposals we consulted on could over allocate profits to a branch (overcorrect the problem) causing a double taxation risk. The issues raised by stakeholders are genuine shortcomings with the OECD's approved approach, particularly their concerns around the interest rate differential between currencies, which have not been identified in the OECD guidance.

17. From discussions with officials in other countries, we understand that our funding problem is unique. New Zealand branches are funded mostly with internal long-term debt, whereas branches in most other OECD countries are funded with a mix of deposits, debt raised in the local market and internal dealings. There are some other variations of the fungibility approach in the OECD guidance which could avoid the issues raised by stakeholders and potentially be modified to address the problem. However, as addressing the problem would require a more bespoke solution, we do still have concerns about potential double taxation risks.

Next steps

18. If you would like to progress work on changes to the thin capitalisation rules, we recommend another round of targeted consultation on proposals. We can start a brief consultation in mid-January if you would like to progress these changes to the Budget timeline. Our preference would be to begin this consultation after businesses resume next year because of the significance of the changes for the industry. But this would mean the proposals would not be ready in time for the Budget.

19. If you would like to progress work on the long-term funding issue, we recommend proceeding on an extended timeline to provide time to work through the problem and potential solutions s 9(2)(f)(iv) . Following this, we would report back on our findings and recommendations before you decide whether to initiate further consultation with local stakeholders.

[5] In our October 2024 report [IR2024/402] we recommended progressing changes to the thin capitalisation rules as a low priority measure. However, stakeholder feedback indicates that more substantial reforms may be considered, which would justify elevating the priority of this work.

[6] This is the practice by which short-term funding is used to fund long-term loans. Banks earn profits from this process by making a higher return on long-term loans compared to the interest they pay on short-term deposits.

First problem: free capital

Problems we consulted on

27. We consulted on two problems with the current approach. The first problem is that the current tax rules don't require an entity's equity capital (referred to as "free capital") to be allocated to its branch and instead allow it to have a higher proportion of debt funding than the entity it's part of. This increases the amount of interest deductions attributable to the branch. While we do have thin capitalisation rules for banks, they apply on a consolidated banking group basis, and the banking thin capitalisation threshold of 6%[7] sits materially below current prudential capital requirements in New Zealand (effectively around 12.5%) and overseas. As a result, excess free capital in a group's locally incorporated bank entities can be used to shelter branches from the thin capitalisation rules. And where there is only a branch in a group, as the thin capitalisation threshold is materially lower than the actual level of capital in the entity it is part of, more debt can be allocated to the branch on a proportional basis to increase interest deductions.

Solutions we consulted on

28. We consulted on three approaches for allocating free capital to a branch based on OECD guidance. They involved allocating the capital of the entity, based on either the branch's share of the entity's risk weighted assets, data from comparable independent entities, or regulatory requirements (the Safe Harbour Approach).

29. Our preferred approach for allocating capital in the consultation was based on risk weighted assets because this would ensure that capital is allocated based on the entity's actual position and in line with industry norms.

Feedback from stakeholders

30. Stakeholders had mixed views on the policy problem:

    - Deloitte and the Corporate Taxpayers Group did not think there was a problem. They felt the current thin capitalisation rules adequately address concerns about capital allocation.
    - Chartered Accountants Australia New Zealand felt it was not clear if there was a problem because the thin capitalisation rules already set minimum requirements for subsidiaries as well as branches of foreign banks. The New Zealand Banking Association was also uncertain if there was a problem, and if there was one, how it should be defined.
    - Westpac thought that an allocation of free capital may potentially already be required based on guidance released the OECD.
    - The Commonwealth Bank and Citibank noted that bank regulators globally have been increasing prudential requirements, and that the current thin capitalisation requirements for tax have not kept up.

31. Stakeholders also had mixed views on the solutions:

    - All stakeholders were concerned that our preferred approach would result in branches and entities being treated differently and that this would distort commercial decision-making.

[7] There are special thin capitalisation rules for banks. The ordinary thin capitalisation rules do not apply to them.

- The stakeholders who thought there was no policy problem did not support any solutions.
- Westpac suggested that capital allocation requirements might be clarified by simply issuing guidelines on the application of the OECD guidance in New Zealand.
- The Commonwealth Bank and Citibank thought that the problem could be addressed by raising the thin capitalisation threshold from 6%:
    - Both stakeholders thought the threshold for tax could be aligned with the RBNZ requirements for New Zealand incorporated banks. The Commonwealth Bank suggested using the current Tier 1 capital ratio, plus the prudential capital buffer. Citibank said that this approach would be less complex than the proposals consulted on, resulting in lower compliance costs.
    - As an alternative, Citibank suggested that the threshold could be aligned with a bank's own publicly disclosed capital ratio (which is already subject to prudential regulation).
    - The Commonwealth Bank said that further consideration should also be given to allow for situations where the RBNZ lowers requirements when a banking group is under stress.
    - The Commonwealth Bank also noted that the RBNZ is currently reviewing its capital requirements and suggested that the tax thresholds should be reviewed regularly to align with prudential requirements.

Officials' responses

32. We still think that there is problem with the current rules and agree with the feedback from the Commonwealth Bank and Citibank. Prudential capital requirements have increased globally to a point where they are much higher than the thin capitalisation ratio eg the Tier 1 capital ratio plus the prudential capital buffer for systemically important bank entities is currently 12.5% and for other bank entities is 10.5%, while the banking thin capitalisation ratio for tax is 6%. As a result, additional debt can be added to branches which increases their deductions for tax. We do agree with stakeholders, though, that allocating capital based on risk weighted assets would affect the neutral treatment of entities and branches which could have undesirable commercial impacts and weigh on competition.

33. We do not think that Westpac's suggestion of addressing the problem by issuing guidelines on the application of the OECD guidance is workable. This is because the OECD guidelines do not prescribe a particular approach but instead set out options countries can choose from, and the current guidelines issued by Inland Revenue state that New Zealand does not require a capital allocation. On this basis we consider that any change in approach should be made legislatively, so that our position is clear in our law and to allow stakeholders to submit on proposed changes through the legislative process.

34. We agree with the Commonwealth Bank and Citibank that the problem could be addressed by raising the thin capitalisation threshold – this is the OECD's Safe Harbour Approach we consulted on along with our preferred method. This approach would also address the risk of extra debt being added to banking groups via holding companies (which is a broader scope than the original proposal). This would resolve concerns raised by stakeholders about branches being treated differently from entities and it should not raise any double taxation issues or tax treaty issues.

35. The thin capitalisation rules were introduced in 2005 to address the problem of banks using cross-border financing to reduce tax paid in New Zealand. These rules are applied at the level of the New Zealand group, which includes holding companies and branches. However, holding companies and branches are ignored for New Zealand prudential regulation purposes[8]. The narrower scope of the prudential requirements means that the thin capitalisation ratio of the New Zealand banking group can be much lower than the regulatory capital ratio for the banking entity if banking groups take on extra debt at the holding company level (such debt is then typically used to capitalise the local operating bank entity). This creates a tax planning opportunity for banks to increase their New Zealand interest deductions.

36. The thin capitalisation rules were designed to ensure that a foreign-owned banking group operating in New Zealand held a minimum percentage of tax equity. The first minimum percentage in 2005 was set at 4%. This equalled the then-current Tier 1 regulatory capital requirement. The ratio was raised to 6% in 2011, which coincided with plans to raise the Tier 1 regulatory requirement to 6%. Although the rate was aligned, it was never explicitly linked because this would tie the government's hands in responding to changes in the banking environment.

37. A new feature of prudential regulatory settings since the introduction of the bank thin capitalisation rules in 2005 is the prudential capital buffer. This is a cushion of capital that banks must hold above their minimum Tier 1 capital requirements to absorb unexpected losses and enhance stability. Banks that fall below the buffer face restrictions, such as on paying dividends, rather than full sanctions. The current Tier 1 capital requirement is 7% and the buffer requires additional common equity over above that of 5.5% for systemically important banks and 3.5% for other banks.

38. The buffer requirement has become an important part of bank prudential regulation, and it is very uncommon for banks to not comply with it as this affects their ability to distribute earnings to shareholders. This can be seen from the capital ratios of all banks operating in New Zealand in Appendix 1 – the average common equity ratio of these banks is 14.2% and the average Tier 1 ratio is 15.42%.

39. We think it would be sensible to align the thin capitalisation ratio closer to the Tier 1 capital requirements plus the prudential capital buffer, in line with the feedback from the Commonwealth Bank, as this setting reflects commercial reality. The actual common equity (which is like tax equity) of most banks sits above this requirement.

40. We do not recommend a ratio based on a bank's publicly disclosed prudential capital ratio, as was suggested by Citibank. A concern with this approach is that linking tax to actual capital held, rather than to a fixed benchmark, may incentivise banks to maintain lower levels of capital to maximise their interest deductions. In effect, sound management could increase tax costs, which could undermine stability.

41. It's likely that some banks will resist aligning the thin capitalisation ratio closer with the Tier 1 capital requirements plus the prudential capital buffer. One of the possible concerns with this approach is that the purpose of the buffer is to provide a cushion which a bank can absorb if it is under stress. Another potential concern is that a portion of the prudential capital buffer is made up of a counter cyclical buffer which the RBNZ can reduce or remove during periods of systemic stress to encourage all banks to continue lending. We think these concerns could be addressed by providing for temporary variations to the thin capitalisation ratio where a bank is under stress, or there is broader systemic stress, in line with the feedback from the Commonwealth Bank.

42. Another issue that needs consideration is whether there should be different thresholds for systemically important banks and other banks, as there is for regulatory capital purposes. A single threshold would need to be set at a suitable

[8] Although the RBNZ does not impose capital obligations on branches, it does require the entity of which a branch is a part to comply with its home regulator's requirements.

level for non-systemically important banks, but this would leave headroom for more debt to be loaded into holding companies of systemically important banks and into branches of banks that are systemically important in their head office countries. These problems could be addressed by setting different thresholds, in line with the Commonwealth Bank's suggestion, but it would be useful to consult further on this.

43. The RBNZ is currently reviewing capital requirements for banks, and it would also be useful to know the outcome of their review before consulting on proposals, particularly because Tier 1 capital requirements may be lowered. We understand that the RBNZ is planning to release final decisions by mid-December.

44. The tax ratios of approximately half of the banking groups are above the current Tier 1 Capital requirements plus the prudential capital buffer (including two of the big-4 banking groups). This means that raising the threshold closer to the Tier 1 Capital requirements will affect about half of foreign-owned banks. For those that do have lower tax ratios, there would only be a modest difference, so the impact of raising the threshold would not be significant on a group-by-group basis. As only some banks would be affected, and the impact would not be significant on a group-by-group basis, we think that competitive forces would mean it is unlikely that any increased tax costs could be passed on to customers, and if they were any passthrough would likely be partial and small.

Next steps

45. These issues would benefit from stakeholder input, so we recommend another round of targeted consultation if you would like to make changes to the thin capitalisation rules. We could run a short consultation process from mid-January if you would like to progress proposals to a Budget timeline. As the changes being considered are significant, and there are likely to be staff absences in January, our preference would be to start the consultation after businesses are back to full capacity next year and allow the standard six weeks. However, this would mean that the proposals would not be ready for the next Budget, so you may not prefer this option. We do not recommend progressing changes without consultation because of the complexity of the measures being considered.

Financial implications

46. The estimated tax revenue from increasing the thin capitalisation ratio will depend on final decisions about the thresholds for systematically important banks versus other banks, and how branches are classified between these categories (eg this could be based on the New Zealand banking group classification or the head office country classification). Our initial estimate is that raising the thin capitalisation ratio to 12.5% for banking groups that include a systemically important New Zealand bank and to 10.5%[9] for other groups would raise $80m over the forecast period[10]:

	$m - increase/(decrease)				
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & outyrs**
Crown Revenue and Receipts: Company tax	-	5.600	22.700	25.700	25.100
Total Operating	**-**	**-5.600**	**-22.700**	**-25.700**	**-25.100**

47. The forecast would increase to $90m over the forecast period if branches were classified as systemically important based on the head office country classification.

[9] These are the current minimum requirements for Tier 1 capital plus the prudential capital buffer. The RBNZ may lower these requirements following their review – this would reduce the revenue estimate.
[10] Assuming changes apply from the beginning of the 2027 income year.

Second problem: long-term interest-bearing funding

Problem we consulted on

48. The second problem is that the current tax rules allow branches in New Zealand to be primarily funded with internal long-term loans from the head office, and in some cases, external long-term loans allocated to the branch. Long-term loans are an expensive form of funding which increases interest deductions.

Solutions we consulted on

49. We consulted on a single solution for allocating funding costs to a branch based on OECD guidance. This would involve determining a branch's funding costs based on the average cost of funds for the entity. We sought feedback on two ways that this could be done in practice. One would be to apportion an entity's total funding costs for financial reporting purposes to a branch based on the proportion of debt held by the branch. The other, would be to limit a branch's interest costs based on the average rate that interest was incurred by the entity as a whole for the year.

50. The main difference between the two approaches is that the first would determine a single deduction for total funding costs while the second would cap funding cost deductions for actual debt instruments allocated to a branch, on an instrument-by-instrument basis. Our preferred approach was to allocate a portion of total funding costs for financial reporting purposes.

Feedback from stakeholders

51. Stakeholders unanimously disagreed that branches being funded entirely with long-term funding was a policy problem. Only Citibank and the New Zealand Banking Association gave reasons for their view. They said that transfer pricing principles, which require arm's length funding conditions, already require an appropriate mix of short-term and long-term debt to be allocated to a branch. Further, in their view, it is appropriate to match the term of a branch's funding with the term of its assets to manage liquidity risk.

52. Stakeholders also did not agree with the solutions:

- All stakeholders were concerned that the solutions would not allocate any costs of raising short-term funding to a branch. These costs make up a significant proportion of a bank's operating expenses, and as a result profits would be over allocated to a branch causing a high risk of double taxation.
- Stakeholders were worried that the solutions would not appropriately account for differences in interest rates associated with currencies. This could cause an over allocation of profits (if head office country rates are lower) or an under allocation (if head office country rates are higher), raising the risk of double tax.
- Stakeholders noted that the solutions are a significant departure from common commercial practice for pricing internal funding. They said that this practice is widely accepted for tax purposes and departing from it in such a big way would increase the risk of double taxation and be very complex.
- Citibank and the New Zealand Banking Association were also concerned that the solutions ignore a branch's third-party transactions which could further raise the double taxation risk.
- Stakeholders thought that the risk of double taxation would potentially drive businesses to either incorporate or lend offshore instead of using branches, increase interest rates charged to customers, or exit New Zealand altogether.

Officials' responses

53. We agree with the feedback from stakeholders that the proposals would over allocate profit to New Zealand because they don't account for differences in interest rates associated with currencies or allocate any of the costs of raising funding in the head office. The solution proposed was based on an approved approach in the OECD guidance, but we think that the issues raised by stakeholders are genuine shortcomings with the approach which have not been identified in the OECD guidance, and they would cause a significant double taxation risk. Accordingly we do not recommend fully adopting either of the consulted upon options.

54. However, we do still think there is a policy problem that warrants further consideration. The consultation process has been helpful in refining our thinking on this. Conventional bank businesses make profits from maturity transformation. This is the practice by which lower interest short-term liabilities, such as customer deposits, are used to fund higher interest long-term assets, like loans. Interest rates typically increase with the term of the loan.

55. We understand s 6(a) that branches of conventional banking businesses in most other OECD countries are funded with a mix of customer deposits, loan capital raised in the local market and internal long-term match-funding from the head office. Therefore, the profits allocated to these branches reflect the results that would ordinarily be expected from maturity transformation in a stand-alone entity. New Zealand branches of international banks appear to be unique when compared with branches in other countries because almost all their liabilities are internal long-term match-funding from the head office. As a result, the profits allocated to these branches do not reflect what would ordinarily be expected from maturity transformation in a stand-alone entity.

56. Match-funding is an internal funds transfer pricing approach that is widely used by banks. A bank's treasury acts as a central funding unit, providing notional funding to business units for their assets. For example, if a branch issues a 3-year loan, it's funded by a notional 3-year liability from the treasury unit. The internal match-funding transfer pricing is determined by the market-based rate for that specific maturity. This is further explained in the example in Appendix 2.

57. When a branch is almost entirely funded in this way, the profits it is allocated do not reflect the results that would ordinarily be expected from maturity transformation. This is because all the returns the banking entity as a whole makes from maturity transformation are effectively transferred to the treasury unit in the head office country. However, those returns actually arise partly because of the external lending function in the branch and are managed through the rates negotiated with customers by the branch. In essence, maturity transformation arises from the combination of two activities – the bank borrowing short term funds and then lending them out long-term. The branch performs the long-term lending side, but all the profits are allocated to the short-term borrowing side.

58. As funding a branch almost entirely with match-funding is contrary to the conventional banking model, it would not produce an arm's length result overall. Our understanding is that it would not be commercially feasible for a standalone bank to be entirely funded by matched term debt, due to the lower lending margins it would produce. This means the current match-funding approach produces lower profits than would be commercially possible for a standalone entity.

59. However, match-funding is accepted by other countries for pricing internal bank funding dealings with branches. The problem appears to be a New Zealand specific one, due to the unique funding make-up of local branches, so resolving it would require a bespoke solution which could increase the risk of double taxation. The OECD guidance does address a similar problem though. One unique feature of banks is their long-term debt often forms part of regulatory capital, which benefits the whole entity. The guidance concludes that it is not correct for one part of a bank to

bear all the interest expense in respect of expensive debt that benefits the whole entity. It outlines different ways to address this problem which are variations of the fungibility approach that could be modified to address our problem.[11]

Conclusion and next steps

60. We consider that a solution to this issue would still be within OECD guidance. However it would need to be a bespoke solution, and so we do still have concerns about double taxation risks. If you would like us to progress work on this issue, we recommend that this is done on an extended timeline, to allow time to work through the problem and possible solutions s 9(2)(f)(iv) as a next step. We could then report back to you with recommendations based on the outcomes of that work before you decide whether to progress with another round of consultation. Alternatively, weighing up the mix of bank measures you choose to progress, you may decide that you do not wish to progress work on this issue.

61. Provided the double tax risks can be addressed, making changes would not increase the total tax paid by each foreign bank entity worldwide i.e. this would only affect where taxes are paid, not the total amount of tax paid by affected entities (except to the extent taxes in New Zealand are higher than in the bank's home jurisdiction there would be an increase, or to the extent they are lower there would be a decrease). As a result, making changes should not cause any economic barriers for existing bank branches or new ones or increase funding costs in New Zealand.

Financial implications

62. Our initial estimate is that addressing the issue could raise approximately $120m over the forecast period[12]. The actual revenue gain will depend on final design decisions including the application date of any changes.

	$m - increase/(decrease)				
Vote Revenue Minister of Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & outyrs**
Crown Revenue and Receipts: Company tax	-	8.400	33.900	39.100	37.500
Total Operating	**-**	**-8.400**	**-33.900**	**-39.100**	**-37.500**

Consultation with the Treasury and the RBNZ

63. The Treasury and the RBNZ were consulted regarding this report.

Administrative implications

64. Implementation and on-going administration costs can be met through baseline funding.

[11] The US applies a variation of the fungibility approach which accounts for differences in interest rates associated with currencies. It treats borrowing in each currency as a separate fungible pool which is used to fund assets of the same currency. This approach works for the US because branches operating there will always hold a large pool of USD since they can raise deposits, and the USD is world's reserve currency. We don't think this approach will work in a New Zealand context.

[12] Assuming changes apply from the beginning of the 2027 income year.

Recommended action

We recommend that you:

1. **agree** to progress work on changes to the thin capitalisation rules to address the risks with how capital is allocated to branches and, more broadly, to banking groups;

   Agreed/Not agreed Agreed/Not agreed

2. **indicate** if you would like to progress this work to a Budget 2026 timeline;

   Yes/No Yes/No

3. **agree** that consultation should take place as a next step;

   Agreed/Not agreed Agreed/Not agreed

4. **agree** that the consultation should cover raising the thin capitalisation ratio closer to the Tier 1 capital ratio plus the capital buffer, different thresholds for systemically important banks and others, and whether to provide for cases of financial stress;

   Agreed/Not agreed Agreed/Not agreed

5. **agree** that consultation should be initiated by officials issuing a targeted consultation letter to foreign-owned banking groups, related advisors and advocacy bodies and the RBNZ rather than the Government issuing a public discussion document or officials issuing a public issues paper;

   Agreed/Not agreed Agreed/Not agreed

6. **indicate** if you would like to review the consultation letter before it is issued;

   Yes/No Yes/No

7. **indicate** if you would like progress work on changes to address the problem of branches being funded almost entirely with more expensive long-term debt;

   Yes/No Yes/No

8. **agree** that this work should not progress to a Budget 2026 timeline;

   Agreed/Not agreed/NA Agreed/Not agreed/NA

Sam Rowe
Policy Lead
Policy

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

Appendix 1: Capital ratios of banks operating in New Zealand

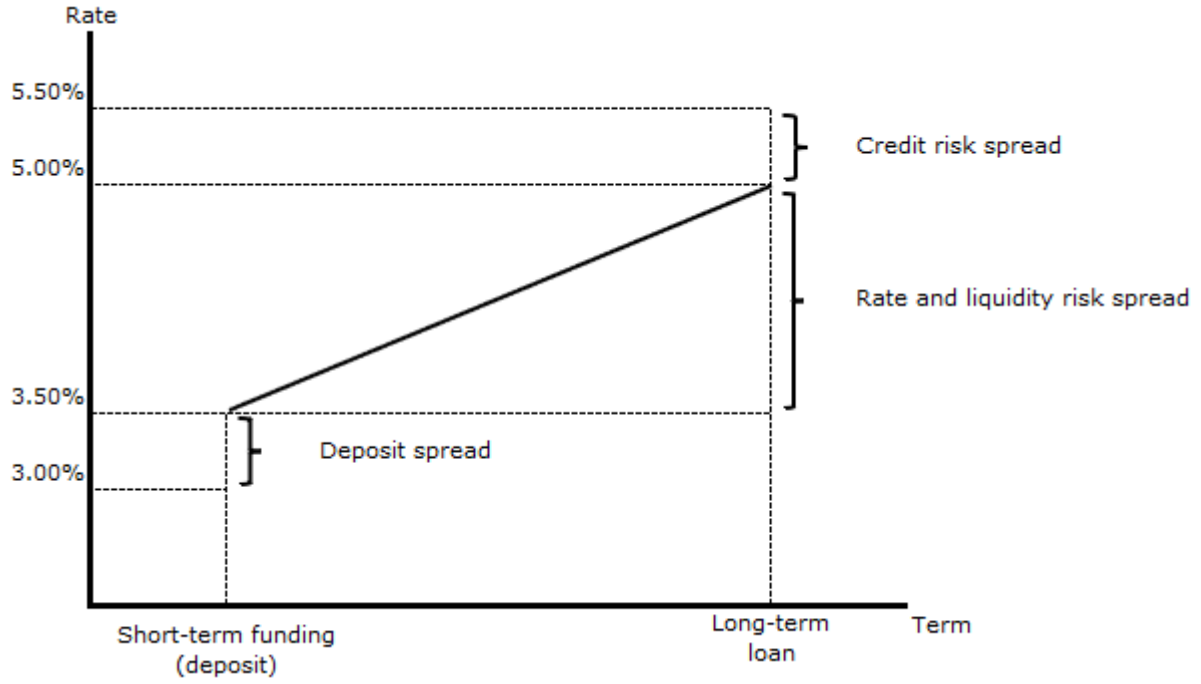
s 6(c)

Table 2: Average common equity and Tier 1 ratios of banks operating in New Zealand

Averages	
Common equity ratio s 6(c)	
Foreign entities	14.42%
Local entities	13.66%
All entities	14.20%
Tier 1 ratio s 6(c)	
Foreign entities	15.66%
Local entities	14.84%
All entities	15.42%

Appendix 2: Example of bank funds transfer pricing for match-funding

Diagram: Example of bank funds transfer pricing



In the above diagram, a bank is funded by short-term funding (a deposit) at 3%. This short-term funding is transferred to the bank's treasury unit at 3.5%. The deposit spread (of 0.5%) is allocated to the unit that manages the short-term funding to cover its costs plus a profit margin. The bank's treasury unit uses the funds to provide long-term funding to its branch at 5%, the market-based rate for the specific term. The interest rate and liquidity risk spread (of 1.5%) is allocated to the treasury unit to cover its costs plus a profit margin. The branch uses this funding to make a long-term loan at 5.5%. The credit risk spread (of 0.5%) is allocated to the branch to cover its costs plus a profit margin.

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: **Approval to consult on changes to taxation rules for foreign-owned New Zealand banking groups**

Date:	12 December 2025	**Priority:**	Medium
Security level:	Sensitive - Budget	**Report number:**	IR2025/493

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to recommendations	12 January 2026
Minister of Revenue	**Agree** to recommendations	12 January 2026

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Sam Rowe	Policy Lead	s 9(2)(a)	☒
Haydn Clark	Principal Policy Advisor		☐

12 December 2025

Minister of Finance
Minister of Revenue

Approval to consult on changes to taxation rules for foreign-owned New Zealand banking groups

Purpose

1. This report seeks your agreement for officials to circulate the attached consultation letter on changes to the tax rules for foreign-owned New Zealand banking groups.

Background

2. We recently consulted with stakeholders on two problems related to the taxation of branches of foreign-owned banking groups in New Zealand. In both cases, the existing rules mean a portion of profits generated in New Zealand can effectively be reported in an entity's head office country. These problems are:

    2.1 **Capital allocation:** current rules do not require an entity's free capital to be allocated to its branch. This allows a branch to be allocated more debt, increasing its tax deductions. We propose that this could be addressed by making changes to the thin capitalisation rules for banks.

    2.2 **Long-term funding:** current rules allow an entity to fund its branch entirely with more expensive long-term debt, increasing its tax deductions. This problem is unique to New Zealand, and a solution requires further design work to mitigate double taxation risks and ensure consistency with OECD guidance.

3. In our November report (IR2025/464), we provided advice on these issues and recommended that you authorise officials to engage in further consultation to develop a workable capital allocation solution on a Budget 2026 timeline. You indicated that you wish to progress a solution to the long-term funding issue for Budget 2026 as well. We have prepared a consultation letter canvassing these two issues.

Next steps

4. Following your feedback on the attached consultation letter, officials will begin targeted consultation on changes to address both the capital allocation and long-term funding problems. To meet a Budget timeline this consultation will take place from mid-January for four weeks, then we will report back on stakeholder feedback and policy design recommendations. As with the previous consultation, we anticipate a negative reaction from the banks to these changes. This is particularly true for the long-term funding issue, which banks are likely to regard as novel internationally and at risk of creating double taxation.

5. We will continue to consult with the Reserve Bank of New Zealand and the Treasury on these issues.

Recommended action

We recommend that you:

1. **agree** for officials to circulate the attached consultation letter with relevant stakeholders

Agreed/Not agreed

Agreed/Not agreed

s 9(2)(a)

Sam Rowe
Policy Lead
Policy

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

Inland Revenue
Te Tari Taake

Policy
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12 January 2026

[Name]
[Organisation]
[Address]

Dear [stakeholder]

Changes to Tax Rules for Foreign-Owned New Zealand Banking Groups

1. Officials have been considering changes to the tax rules for foreign-owned New Zealand banking groups. Given your interest in this topic, we are sending this letter to you to get your views.

2. This letter sets out issues that we are aware of with the current rules along with some possible solutions. It is important to note this is a letter from officials and represents our initial thinking on proposed changes, it does not set out the Government's views. Any future work in this area will be subject to the normal Government approval process and prioritisation.

3. We welcome your views on any aspects of the topics covered in this letter. We would be grateful if you could respond to us in writing by 13 February 2025. In addition to any response you provide in writing, we would be happy to meet to discuss your views.

4. Although we are consulting in a targeted way, the consultation is not confidential. As with any correspondence with officials, your response may be the subject of a request under the Official Information Act 1982 which could result in its release or publication unless there are grounds for it to be withheld (in whole or part). Withholding responses on the grounds of privacy, or for any other reason, will be determined in accordance with the Official Information Act 1982. If you think that any part of your submission should be withheld, please clearly indicate this.

Background

5. In September 2025, we consulted on two policy problems. Current tax rules do not require a foreign bank's free capital (e.g. its share equity) to be allocated to its branch[1]. This allows a branch to be allocated more debt on a proportional basis when compared with the entity it's a part of, which increases its tax deductions. An entity can also fund its branch entirely with more expensive long-term debt, which also increases its tax deductions. As a result, a portion of profits generated in New Zealand can effectively be reported in an entity's head office country.

6. This letter outlines updated problem definitions and solutions taking into account the feedback that we received.

[1] While New Zealand does have thin capitalisation rules, they apply on a New Zealand banking group basis, and the threshold is generally materially lower than the actual capital in the entity a branch is part of, so more debt can be allocated to the branch on a proportional basis.

Capital allocation

Summary of previous consultation

7. Stakeholders had mixed views on the capital allocation problem. Some thought that there was no problem because the thin capitalisation rules already address capital allocation concerns, some were unsure if there was a problem or if it had been defined correctly, and some thought that making changes in this area would not be unreasonable.

8. We consulted on three approaches for allocating free capital to a branch. They involved allocating an entity's capital to its branch based on either the branch's share of the entity's risk weighted assets, data from comparable independent entities, or regulatory requirements for an independent banking entity. We preferred the first approach because this would ensure an allocation based on the entity's actual position, and be in line with industry norms.

9. Stakeholders were broadly concerned about allocating an entity's actual capital to a branch on a proportional basis because this would mean that branches and entities would have different tax capital requirements, which could disrupt commercial decision making. The stakeholders who thought that changes could be made preferred raising the thin capitalisation threshold to address the problem. This would preserve the neutral tax treatment of entities and branches, and stakeholders felt it would be less complex.

10. We've broadened the scope of the capital allocation problem definition to consider New Zealand banking groups, based on feedback from stakeholders about maintaining neutral tax equity settings for entities and branches.

Updated problem summary

11. Prudential capital requirements have increased globally to a point where they are now much higher than New Zealand's thin capitalisation ratio for banks. For example, in New Zealand, the Tier 1 capital requirement plus the prudential capital buffer for domestic systemically important banks is currently 12.5% and for other banks is 10.5%, while the thin capitalisation ratio is 6%.

12. As a result, additional debt can be added to New Zealand banking groups via holding companies which increases the group's tax deductions. And where there is a branch in a group, as the thin capitalisation threshold is generally materially lower than the actual level of capital in the entity it is part of, more debt can be allocated to the branch on a proportional basis, which increases tax deductions.

Questions

- Do you think we have defined the problem accurately?

Where to set the thin capitalisation threshold

13. The thin capitalisation rules were introduced in 2005 to address the problem of banks using cross-border financing to reduce tax paid in New Zealand. These rules are applied at the level of the New Zealand group, which includes holding companies and branches. However holding companies and branches are ignored for New Zealand prudential regulation purposes[2]. The narrower scope of the prudential requirements means that the tax capital ratio of the New Zealand group can be much lower than the

[2] Although the RBNZ does not impose capital obligations on branches, it does require the entity of which a branch is a part to comply with its home regulator's requirements.

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regulatory capital ratio of the bank when the group takes on extra debt at the holding company level to place equity in the local operating bank entity, or at the branch level to fund lending.

14. The thin capitalisation rules were designed to ensure that a foreign-owned banking group operating in New Zealand holds a minimum percentage of tax equity. While the tax ratio could differ from the regulatory ratio, there is commercial sense in alignment to an external prudential benchmark as this connects tax with commercial settings. The first minimum percentage in 2005 was set at 4%. This equalled the then-current Tier 1 capital requirement. The ratio was raised to 6% in 2011, which coincided with plans to raise the Tier 1 requirement to 6%. Although the rate was aligned, it was never explicitly linked because this would tie the government's hands in responding to changes in the banking environment.

15. A new feature of prudential regulatory settings since the introduction of the bank thin capitalisation rules in 2005 is the prudential capital buffer. This is a cushion of capital that banks must hold above their minimum Tier 1 capital requirements to absorb unexpected losses and enhance financial stability. Banks that fall below the buffer face restrictions, such as on dividend payouts, rather than full sanctions. The buffer requirement has become an important part of bank prudential regulation, and it is very uncommon for banks to not comply with the requirement as it affects their ability to distribute earnings to shareholders.

16. [There are some technical variances between tax equity and Tier 1 capital due to differences in tax and regulatory objectives. However, on [X] December 2025, the RBNZ announced changes to the Tier 1 capital requirements which will reduce these variances. From [Date], Tier 1 capital must be made up entirely of common equity, which is the prudential regulatory concept that most closely corresponds to tax capital.

17. The RBNZ also announced that from [Date] the new Tier 1 capital requirement will be [X]% and the buffer will require additional common equity over above that of [X]% for systemically important banks and [X]% for other banks.]

18. We think it would be sensible to increase the thin capitalisation ratio to align with the RBNZ's Tier 1 capital requirements plus the prudential capital buffer, as this setting lines up closely with local and overseas commercial settings for banks. This would be a straightforward way to ensure that branches, and New Zealand banking groups more generally, are treated as holding a commercial level of equity for tax purposes.

Question

- Do you think that increasing the thin capitalisation threshold would address the risk of under allocation of capital to foreign-owned New Zealand banking groups?
- Do you have any comments on the proposal to increase the threshold to line up with the Tier 1 capital requirements plus the prudential capital buffer announced by the RBNZ?

Cases of financial stress

19. One of the possible concerns with this approach is that the purpose of the prudential capital buffer is to provide a cushion which a bank can absorb if it is under stress. Another potential concern is that a portion of the buffer is made up of a counter cyclical buffer which the RBNZ can reduce or remove during periods of systemic stress to encourage all banks to continue lending.

20. These concerns could be addressed in the thin capitalisation rules by allowing for situations where a bank is under stress, or there is broader systemic stress. For

example, the rules could provide an Order in Council power to temporarily vary the thin capitalisation threshold for a single bank when it is under financial stress, and automatically vary the threshold for all banks when the RBNZ lowers the prudential capital buffer because of systemic stress.

21. The determination of whether a bank is under stress should be based on criteria. For example, this could be where a bank falls below the prudential capital buffer requirement, and this is caused by a trading loss in the same period that equals or exceeds the capital shortfall. The variation period could align with the bank's own buffer shortfall for a limited time (eg based on the bank's buffer reinstatement plan) not exceeding a fixed period eg 12 months.

22. In cases where the RBNZ lowers the prudential capital buffer, the variation could align with the RBNZ's buffer reduction.

Questions

- Do you think that the thin capitalisation rules should allow for situations where a bank is under stress?
- Do you have any comments on how this could be provided for?
- Do you have any comments on the criteria for determining whether a bank is under stress?
- Do you have any comments on what the time period for a threshold variation for a bank should be?
- Do you think that the thin capitalisation rules should allow for situations where there is broader systemic stress?
- Do you have any comments on how this could be provided for?

Different thresholds for systemically important banks and other banks

23. Another issue that needs consideration is whether there should be different thin capitalisation thresholds for systemically important banks (SIBs) and other banks. If a single threshold was used, it would need to be set at a suitable level for non-SIBs which could, depending on the rate, leave headroom for more debt to be taken on by holding companies and branches of banks that are SIBs in their head office country.

24. These problems could be addressed by setting different thresholds for SIBs and non-SIBs. For example, the SIB threshold could apply to banking groups that include any SIB (which would include a branch of a bank that is a SIB in its head office country), and the non-SIB threshold could apply to all other banking groups. This is our preferred approach because it would line up the threshold more closely with commercial settings for each group. Alternatively, the SIB threshold could apply to banking groups that include a domestic SIB.

Questions

- Do you have any comments on the proposal to set different thresholds for SIBs and non-SIBs?
- Do you have any comments on how to classify banking groups for this purpose?

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Long-term debt funding

Summary of previous consultation

25. Stakeholders disagreed that branches being funded entirely with long-term debt was a policy problem. Stakeholders thought that transfer pricing principles already require an appropriate mix of debt funding in a branch. Additionally, as matching the term of a branch's debt funding with the term of its assets (which are typically long-term loans) is common commercial practice for managing liquidity risk, they considered that the current approach results in an appropriate mix of debt funding.

26. We consulted on two practical methods for allocating funding costs to a branch based on an entity's average cost of funds. The first involves apportioning an entity's total funding costs for financial reporting purposes based on the proportion of total debt held by the branch compared to the entity as a whole. The second involves limiting a branch's funding cost deductions each year based on the average rate that interest was incurred by the entity as a whole.

27. Stakeholders did not support either of these solutions. They were concerned that the solutions would not allocate any of the costs of raising short-term debt funding to a branch, but it would use that short-term funding in calculating its interest deductions. They were also concerned that the solutions did not appropriately account for differences in interest rates associated with currencies – the solutions would effectively use the currency of the headquarter country to calculate the borrowing costs, but interest rates might be different when borrowing in the headquarter country's currency than in New Zealand dollars. As a result, the true New Zealand dollar borrowing costs would be misstated. Stakeholders were also concerned that the solutions were a significant departure from common commercial practice for pricing internal debt funding, which is widely accepted for tax purposes, and that they ignored genuine third-party transactions entered by a branch.

28. Stakeholders thought that these problems would cause a significant risk of material double taxation which would potentially drive businesses to either incorporate or provide lending offshore instead of using branches, increase interest rates charged to customers, or exit New Zealand altogether.

29. We agree with the feedback from stakeholders that the original proposals would over allocate profit to New Zealand because they don't account for differences in interest rates associated with currencies or allocate any of the costs of raising short term debt funding in the head office. However, we do still think there is a policy problem that warrants further consideration. The consultation process has been helpful in refining our thinking on this.

Updated problem summary

30. Conventional bank businesses make profits from maturity transformation. This is the practice by which lower interest short-term liabilities, such as customer deposits, are used to fund higher interest long-term assets, like loans. Interest rates typically increase with the term of the loan.

31. We understand that branches of conventional banking businesses in most other OECD countries are funded with a mix of customer deposits, debt raised in the local market and internal long-term match-funding from the head office. Therefore, the profits allocated to these branches reflect the results that would ordinarily be expected from maturity transformation in a stand-alone entity. New Zealand branches of international banks appear to be unique when compared with branches in other countries because often almost all their liabilities are internal long-term match-funding from the head office. As a result, the profits allocated to these branches do not reflect what would ordinarily be expected from maturity transformation in a stand-alone entity.

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32. Match-funding is an internal funds transfer pricing approach that is widely used by banks. A bank's treasury acts as a central funding unit, providing notional debt funding to business units for their assets. For example, if a branch issues a 3-year loan, it's funded by a notional 3-year liability from the treasury unit. The internal match-funding transfer pricing is determined by the market-based rate for that specific maturity. This is further explained in the example in the appendix.

33. When a branch is almost entirely funded in this way, the profits it is allocated do not reflect the results that would ordinarily be expected from maturity transformation. This is because all the returns the banking entity as a whole makes on interest rate and liquidity risks connected with the branch's lending are effectively transferred to the treasury unit in the head office country. However, those returns actually arise partly because of the external lending function in the branch and are managed partly through the rates negotiated with customers by the branch. In essence, maturity transformation arises from the combination of two activities – the bank borrowing short term funds and then lending them out long-term. The branch performs the long-term lending side, but all the profits in relation to interest rate risk and liquidity risk are allocated to the short-term borrowing side.

34. As funding a bank almost entirely with match-funding is contrary to the conventional banking model, allowing a branch to be funded in this way would not produce an arm's length result overall. For example, our understanding is that it would not be commercially feasible for a standalone bank to be entirely funded by matched term debt, due to the lower lending margins it would produce. This means the current match-funding approach produces lower profits than would be commercially possible for a standalone entity.

35. However, match-funding is accepted by other countries for pricing internal bank debt funding dealings with branches. The problem appears to be a New Zealand specific one, due to the unique debt funding make-up of local branches, so addressing it would require a bespoke solution.

Questions

- Do you think we have defined the problem accurately?

Consideration of principles in OECD guidance

36. New Zealand applies the relevant business activity (RBA) approach to allocate profits to branches. New Zealand has not adopted the Authorised OECD Approach (AOA). However, the OECD's 2010 Report on the Attribution of Profits to Permanent Establishments, which sets out the AOA, contains some principles for determining an arm's length profit allocation in certain bank industry specific situations which are still relevant to our approach. This is because arm's length profit allocation is a common goal of both approaches, and the relevant comments do not rely on the adoption of the AOA's separate entity approach.

37. Paragraphs 117 to 121 in Part II of the report discuss an issue involving the overallocation of long-term debt funding to a branch. While it is a different issue to the New Zealand branch funding problem outlined above, there are some similarities. One unique feature of banks is that their long-term debt often forms part of regulatory capital, which benefits the whole entity. The report concludes that it is not appropriate for one part of a bank to bear all the interest expense in respect of this expensive debt.

38. Paragraphs 120 to 121 explain a couple of the different ways this issue can be addressed. Banks raise funds from a variety of sources with varying interest rates. Some funds are free or give rise to very low interest rates, whilst others give rise to high interest rates, such as subordinated debt. Paragraph 120 says that one way to address the issue is for the rate charged on internal dealings to be based on an appropriately "blended" rate, to reflect the proportions of debt funding at different interest rates and maturities.

39. Paragraph 121 says that under other internal debt funding pricing approaches, an adjustment will be needed because the approach used doesn't appropriately account for higher interest rate debt. For example, where internal dealings are priced by reference to market wholesale interbank interest rates, an adjustment may be needed to reflect the actual debt funding mix of the bank of which the PE is a part.

40. As New Zealand has not adopted the AOA and the policy problem outlined above is unique, we think a bespoke legislative solution will be required. However, the principles in the OECD's report that overallocation of long-term debt can lead to an inappropriate profit allocation in certain circumstances and that this can be addressed by making a profit allocation adjustment are helpful.

Internal long-term debt funding profit reallocation

41. We think an adjustment is appropriate in cases where a branch has a high proportion of internal long-term match-funding priced at market rates. This is because match-funding allocates all the returns generated by a branch to cover interest rate and liquidity risks to the head office treasury unit (as discussed above). While internal match-funding isolates interest rate and liquidity risks in the treasury unit for management accounting purposes, the actual risk to the entity does still arise in part from the branch's lending to external customers. This lending is partly managed by the branch in negotiating appropriate interest rates with customers, and the loans sit on the branch's balance sheet and therefore in the branch. However, the risks also partly originate from the short-term debt funding raised in the head office country and are partly managed by the treasury function in the head office country, so a portion of the profits should also be allocated there. Our initial, high-level, thinking on a possible solution is outlined below.

42. The problem could be addressed by introducing new rules which apply to internal long-term debt funding in a branch that is priced based on market rates. The rules would require a profit reallocation adjustment where the proportion of internal long-term debt funding[3] in a branch is greater the proportion of long-term debt funding in the entity it's part of minus the proportion of external long-term debt funding in a branch[4]. This reduction of the entity's proportion of long-term debt funding would result in a branch's external long-term debt proportion being matched with the entity's long-term debt proportion first. Any excess long-term debt funding proportion remaining in the entity as a whole would then be offset against the internal long-term debt funding proportion in the branch. The amount remaining after this offset would then be subject to an adjustment. For this purpose, long-term debt funding would include all debt funding with a term greater than [18] months and be determined based on the average of the opening and closing funding balances for the year.

Example 1

Bank A has an average of 30% long-term debt funding for the year. Bank A's branch has an average of 90% internal long-term debt funding for the year and an average of 10% external long-term debt funding for the year. The branch's proportion of internal

[3] To total debt funding.
[4] Where the proportion of long-term debt funding in the entity minus the proportion of external long-term debt funding in the branch is less than zero, this would be treated as zero.

long-term debt funding for the year (90%) exceeds the proportion of long-term debt funding in Bank A minus the proportion of long-term external debt funding in the branch (20%, being 30% - 10%) by 77.78% (100% – 20%/90%).

43. To the extent a branch has a higher proportion of long-term internal debt funding, the adjustment would reallocate a portion of a treasury unit's profit before tax from internal long-term lending to a branch. We think 50% is an appropriate portion given the important role that a branch plays in the maturity transformation process.

Example 2

Continuing example 1, the Bank A treasury unit's net profit before tax from funding provided to the branch is $10m. The adjustment would reallocate $3.9m of profit to the branch ($10m x 77.78% x 50%).

44. Alternatively, to simplify compliance, the rules could provide for a formula-based profit adjustment. For example, this could be based on 50% (half) of a fair treasury net profit before tax margin (being the percentage profit on each dollar of interest received from a branch) based on conservative benchmarking eg 15%[5]. This would mean the reallocated profit could equal a fixed percentage of the relevant portion of a branch's match-funding cost eg 7.5% (50% of 15%).

Example 3

Continuing examples 1 and 2, Bank A's branch incurs $67m of internal long-term funding costs for the year. The adjustment would reallocate $3.9m of profit to the branch ($67m x 77.78% x 7.5%).

Questions

- Do you have any comments on the proposed approach for identifying long-term debt funding, and the process for determining the proportion of long-term debt funding each year?
- Do you have any comments on the proposal to reallocate a portion of the actual net profit before tax earned by a treasury unit on long-term debt funding provided to a branch, including on the appropriate profit percentage?
- Do you have any comments on the alternative proposal to reallocate an amount based on a legislative formula, including on the appropriate profit percentage and a fair treasury net profit before tax margin?
- Do you have a preferred approach?

External long-term debt funding profit allocation

45. We think a profit reallocation adjustment is also appropriate in cases where a branch has a high proportion of external long-term debt funding. This would address integrity risks arising from the internal long-term debt funding profit reallocation proposal ie the risk of external long-term debt funding being allocated to a branch instead of

[5] We understand that this may be a conservative benchmark net profit before tax margin, but we invite further feedback on this.

internal long-term debt funding. It would also address the risk highlighted in the OECD's report, of long-term debt that is regulatory capital being overallocated to a branch.

46. These risks could be addressed by rules which apply to external long-term debt funding in a branch. The rules would require a profit reallocation adjustment where the proportion of external long-term debt funding in a branch is greater the proportion of long-term debt funding in the entity it's part of. Long-term debt funding and the relevant proportions would be determined in the same way described above.

Example 4

Bank B has an average of 30% long-term debt funding for the year. Bank B's branch has an average of 50% external long-term debt funding for the year. The branch's proportion of external long-term debt funding for the year (50%) exceeds the proportion of long-term debt funding in Bank B by 40% (100% – 30%/50%).

47. An allocation of external long-term debt funding directly to a branch is in essence similar to an allocation of internal long-term match-funding. It results in an increase in the head office treasury function profit due to a direct allocation of expensive debt funding costs to the branch instead of the treasury unit. To the extent a branch has a higher proportion of external long-term debt funding, an adjustment could be made to reallocate a fair treasury net profit before tax margin based on a formula.

48. There may be a case for excluding long-term debt funding from the adjustment where it is raised by a branch in the local market, in New Zealand dollars, to fund its own lending and is not regulatory capital. That's because this funding has a connection with activities of the branch and does not provide a regulatory capital benefit to the entity as a whole. One concern with this, though, would be that it could allow banks to undermine the rules by loading New Zealand dollar debt into a branch.

Questions

- Do you have any comments on the proposal to reallocate a portion of profit earned by a treasury unit based on a legislative formula where certain external long-term debt funding is allocated directly to a branch instead of the treasury unit?
- Do you have any comments on whether external long-term debt funding should be excluded from the adjustment where it is raised by a branch in the local market, in New Zealand dollars, to fund its own lending, and it is not regulatory capital?

Bank special purpose funding vehicles

49. Another integrity risk is that banks might transfer activities currently performed by branches to special purpose funding vehicles that are funded with long-term match-funding. If the proposals proceed, further consideration will need to be given to this risk and potential solutions. This could, for example, involve extending measures like those outlined above to bank's special purpose funding vehicles.

Questions

- Do you have any comments on this integrity risk and how it could be addressed?

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Double tax risk

50. As the proposals above outline bespoke solutions to a unique New Zealand problem, there is some risk of double taxation. We will be discussing the problem and proposals with other countries to understand their views on this. We also note that, while any rules introduced relating to long-term debt funding would establish a default New Zealand position on funding costs, where another country disagrees with the overall amount of profit allocated to a New Zealand branch, any double tax concerns could still be addressed by competent authorities via the mutually agreed procedure (MAP) process.

Questions

- Do you have any comments on the double tax risk or whether any such double tax could be addressed by competent authorities via the MAP process?

Next steps

51. As mentioned, we look forward to receiving your written views on the issues raised in this letter and are happy to meet with you as well if that would be of any help. If you would like to arrange a meeting, please contact Haydn Clark, Principal Policy Advisor on s 9(2)(a)

52. We will update Ministers on this topic once we have considered feedback on this letter. Following that, any next steps will be subject to decisions by Ministers.

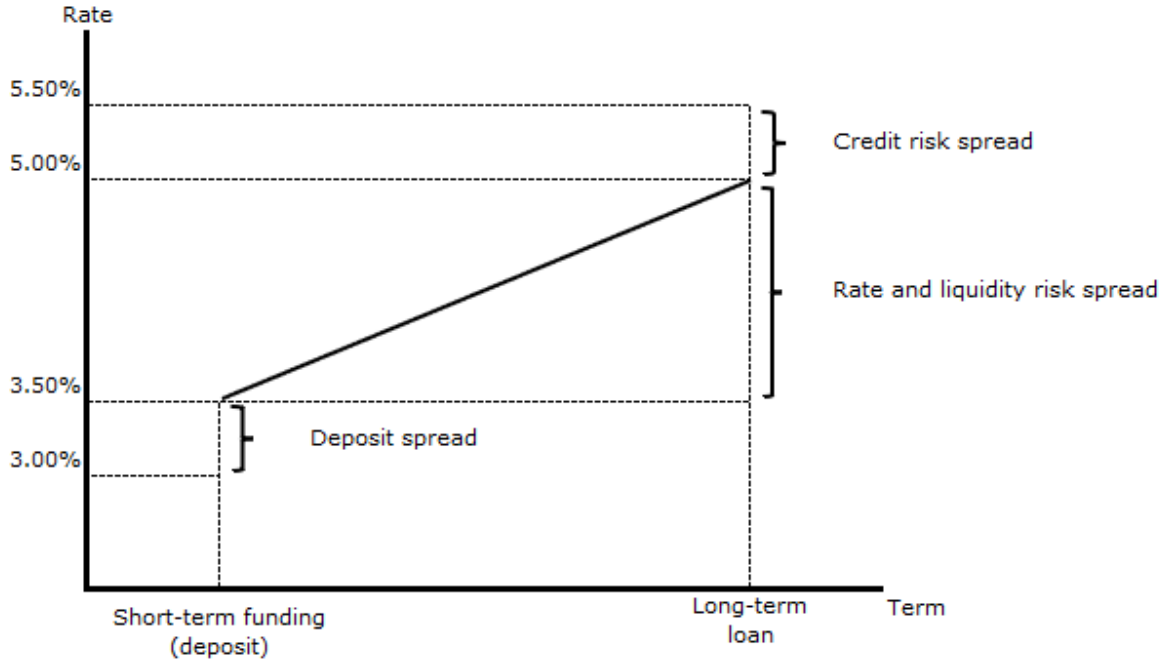
Yours sincerely

Sam Rowe
Policy Lead

DRAFT

Appendix: Example of bank funds transfer pricing for match-funding

Diagram: Example of bank funds transfer pricing



In the above diagram, a bank is funded by short-term debt funding (a deposit) at 3%. This short-term funding is transferred to the bank's treasury unit at 3.5%. The deposit spread (of 0.5%) is allocated to the unit that manages the short-term funding to cover its costs plus a profit margin. The bank's treasury unit uses the funds to provide long-term debt funding to its branch at 5%, the market-based rate for the specific term. The interest rate and liquidity risk spread (of 1.5%) is allocated to the treasury unit to cover its costs plus a profit margin. The branch uses this funding to make a long-term loan at 5.5%. The credit risk spread (of 0.5%) is allocated to the branch to cover its costs plus a profit margin.

Tax policy report

Inland Revenue
Te Tari Taake

Changes to tax rules for foreign-owned New Zealand banking groups

Date	13 March 2026	**Priority**	Medium
Security level	Budget sensitive	**Report number**	IR2026/066

Action sought		**Deadline**
Minister of Finance	**Agree** to recommendations	27 March 2026
Minister of Revenue	**Agree** to recommendations	27 March 2026

Purpose
This report summarises stakeholders' feedback on proposed changes to tax rules for foreign-owned New Zealand banking groups and seeks a decision from Ministers on next steps.

Contact for phone discussion, if required

Name	**Position**	**Phone number**	**First contact**
Sam Rowe	Policy Lead	s 9(2)(a)	☐
Haydn Clark	Principal Policy Advisor		✓

Changes to tax rules for foreign-owned New Zealand banking groups

Executive summary

1 This report addresses two policy issues regarding the tax treatment of foreign-owned New Zealand banking groups.

2 Firstly, it considers increasing the thin capitalisation threshold to align with updated prudential capital requirements announced by the Reserve Bank. This would protect New Zealand's tax base by limiting the overall level of debt funding in banking groups. Stakeholder feedback on this proposal was mixed – some questioned the need for change while others supported alignment with prudential standards. Our key recommendation is to adopt new thresholds based on the Reserve Bank's recently announced prudential requirements. If implemented from 1 April 2027, these changes would raise $45 million over the forecast period.

3 The second issue concerns the mix of debt funding in New Zealand bank branches, particularly high proportions of long-term debt funding that we consider does not produce an arm's length profit attribution. While all stakeholders opposed the proposed changes, we still think there is a policy problem that warrants further consideration. However, s 6(a) s 9(2)(f)(iv)

Background

4 In our November 2025 report (IR2025/464) we asked for approval to consult on proposed changes to how funding costs are calculated for foreign banks. These revised proposals took account of feedback received from stakeholders during consultation in October 2025. You asked us to progress this work to a Budget 2026 timeline.

Problem 1: Outdated capital requirements

Problem consulted on

5 The first problem is that prudential capital requirements have increased globally to a point where they are now much higher than New Zealand's thin capitalisation ratio for banks. For example, in New Zealand, the Tier 1 capital requirement plus the prudential capital buffer for domestic systemically important banks is currently 12.5% of risk weighted assets, and for other banks is 10.5%[1], while the thin capitalisation threshold is 6%. As a result, additional debt can be added to New Zealand banking groups via holding companies, which increases the group's tax deductions. And when there is a branch in a group, more debt can be attributed to the branch proportionally than the actual level of debt in the entity it is part of, which increases tax deductions.

Context

6 The thin capitalisation rules for banking groups were introduced in 2005 to address the problem of banks using cross-border financing to reduce tax paid in New Zealand. The rules are intended to ensure that a foreign-owned banking group operating in New Zealand holds a commercially realistic level of equity for tax purposes. Unlike prudential settings, the Government can choose where to set the thin capitalisation threshold.

[1] In December 2025 the Reserve Bank announced that these requirements would change to 12% and 11% respectively from December 2028.

7 In determining a commercially realistic level for the current thin capitalisation threshold, consideration was given to various factors. These included local and worldwide prudential requirements, the potential for disruption to the banking industry if further capital was required to support the New Zealand business, and the economic and revenue impacts. The main focus was on preventing excessive interest deductions from cross-border financing, to prevent the loss of revenue. These factors remain relevant today, however, because the bulk of New Zealand's banking is now conducted via local entities,[2] greater emphasis should be given to local prudential requirements versus worldwide requirements.

8 While the tax ratio could differ from prudential requirements, alignment connects tax with commercial settings. The minimum percentage started at 4% in 2005, matching contemporary Tier 1 capital requirements, then increased to 6% in 2012 alongside plans to raise Tier 1 requirements to 6%. Despite this alignment, the rate was never formally linked to Tier 1 to maintain Government flexibility in policy changes.

9 Since the introduction of the thin capitalisation rules, a new prudential regulation tool has been developed called the prudential capital buffer. This is a cushion of capital that banks must hold above their minimum Tier 1 capital requirements to absorb unexpected losses. Banks that fall below the buffer face restrictions, such as on dividend payouts, but not full sanctions. It is very uncommon for banks to not comply with the buffer requirement because it affects their ability to distribute earnings. Based on the most recently published annual reports, all banks operating in New Zealand[3] satisfied their buffer requirements. The average common equity ratio was approximately 14% and the average Tier 1 capital ratio was approximately 15%.

Solution consulted on

10 We consulted on a proposal to increase the thin capitalisation threshold to align with the Tier 1 prudential capital requirements that were announced by the Reserve Bank in December 2025 (including the prudential capital buffer requirements), that is, 12% for group 1[4] deposit takers and 11% for group 2[5] deposit takers. This would set the thin capitalisation threshold based on a commercially realistic benchmark. Different thin capitalisation thresholds would apply for different sized banks in line with the approach to prudential regulation, and the changes would provide for temporary variations to the requirements when banks are under stress or when the Reserve Bank makes changes to the countercyclical buffer[6] requirements in times of broader systemic stress. Feedback was also sought on the implementation approach.

Feedback from stakeholders

11 We received feedback from 12 banks, advisors and advocacy bodies. Chartered Accountants Australia and New Zealand (CA ANZ) and KPMG did not comment on the merits of the problem definition or proposed solution. They submitted that consultation on proposals that affect banks is very important to understand the impacts.

12 ANZ, Bank of China, China Construction Bank, Industrial and Commercial Bank of China, Westpac, the Corporate Taxpayers Group, the New Zealand Banking Association and Deloitte did not support the proposals. They submitted:

- There is no evidence that New Zealand banks' interest deductions are demonstrably high relative to the group that they are part of and it is therefore not clear that there is a problem. Westpac did however note that a significant amount of time has passed since the thin capitalisation threshold was last updated and it may be sensible to review whether it remains fit for purpose.

[2] When the rules were introduced, a greater proportion of banking was conducted through branches.
[3] This includes locally incorporated entities and foreign bank entities operating through branches.
[4] Systemically important deposit takers holding $100 billion or more of assets.
[5] Deposit takers holding more than $2 billion and less than $100 billion of assets.
[6] A portion of the prudential capital buffer that the Reserve Bank can adjust in response to market conditions.

- If proposals are to progress, the thin capitalisation threshold should be set below prudential requirements to provide for the differences in prudential and tax capital calculations. For example, there are differences in the basis for adjusting for deferred tax and expected credit losses in calculating the amount of capital held.
- Alignment creates the risk of tax settings interfering with prudential regulation. For example, aligning the thin capitalisation threshold with the prudential requirements including the prudential capital buffer could undermine the ability for a bank to return to the required buffer ratio due to an increased tax liability.
- The thin capitalisation threshold should not take account of the prudential capital buffer requirements or, if they do, should provide for cases of financial stress.
- There should not be different requirements for banks depending on their size. The same thin capitalisation threshold should apply to all New Zealand banking groups because this would provide a simpler framework and a level playing field.
- Any banks that do not currently meet the new thin capitalisation threshold should be given a reasonable timeframe to adjust capital levels. For example, the tax changes could coincide with the application of the prudential changes.

13 Commonwealth Bank of Australia (the parent of ASB) and Citibank supported the proposals. They submitted:

- The thin capitalisation threshold could be aligned with prudential capital requirements including the prudential capital buffer. Commonwealth Bank of Australia noted that alignment represents sensible tax policy.
- Commonwealth Bank of Australia supported the proposal to set different requirements for banks depending on their size, in line with prudential settings. Citibank did not support this proposal because it would increase complexity and potentially discourage growth. They preferred a single threshold for all banks, however, they were open to the tax threshold being aligned with the highest prudential requirement that applies to systemically important banks.
- Commonwealth Bank of Australia supported the proposal to provide for situations when a bank falls below the prudential capital requirements because of commercial stress or because there is broader systemic stress, though it noted that this will happen rarely. Citibank did not support this proposal because it would increase complexity. It noted that the thin capitalisation rules do not require banks to hold equity, instead they disallow interest deductions when a bank falls below the threshold, so banks are already free to choose to hold insufficient equity for tax purposes and make an adjustment under the thin capitalisation rules.
- The changes could be implemented as a single increase to the threshold on a prospective basis because impact on the industry will likely be limited.

Officials' responses

14 We think that the policy problem has been defined accurately. While we agree with stakeholders that banks have generally not taken full advantage of the mismatch in prudential and tax requirements, there is a risk that their behaviour could change in the future if current thin capitalisation settings remain as they are. Therefore, we agree with the Commonwealth Bank of Australia that increasing the thin capitalisation threshold to align with prudential capital requirements would be sensible tax policy.

15 We do not agree with the opposing stakeholders that the thin capitalisation threshold needs to provide for differences in the makeup of prudential capital and tax capital. This is because the differences are relatively minor and banks already hold capital management buffers over and above prudential requirements. These buffers should generally be sufficient to ensure any variances between prudential capital and tax capital do not result in interest denial under the thin capitalisation rules. On the two previous occasions when the thin capitalisation threshold was set, it was aligned with the Tier 1 capital requirements and there were greater variances in prudential and tax

capital at those times. The Tier 1 capital requirements announced in December 2025 will reduce the variances by removing "Additional Tier 1 capital" from Tier 1 capital.

16 We also do not agree with the opposing stakeholders that aligning with the prudential capital buffer requirements will interfere with prudential regulation. As Citibank noted, the thin capitalisation rules do not require banks to hold equity, they simply disallow interest deductions when a bank falls below the threshold, so banks are already free to choose to hold less equity than the threshold for tax purposes and some do so. We think aligning with the prudential capital buffer requirement would generally have the opposite effect, as the parents of banks that fall below it would be incentivised to reinstate the buffer quickly by recapitalising their New Zealand subsidiaries.

17 We received feedback from the Reserve Bank that it does not support the proposal to provide for a reduction to the thin capitalisation threshold when a single bank falls below the buffer requirement because this could send a negative market signal that could potentially trigger or worsen a liquidity stress event. We agree with this feedback and therefore do not consider that the changes should provide for this.

18 However, we consider that the changes should provide for a reduction to the thin capitalisation threshold in line with any changes announced by the Reserve Bank to the countercyclical capital buffer.[7] This would maintain alignment of the thin capitalisation threshold with regulatory requirements and therefore commercial settings, and should address some of the concerns raised by opposing stakeholders about aligning the tax requirements with the prudential buffer requirement. The Reserve Bank did not raise any concerns with this proposal from a market regulation perspective.

19 We do not agree with opposing stakeholders that a single thin capitalisation threshold is necessary to level the playing field. The different prudential capital requirements for group 1[8] deposit takers and group 2[9] deposit takers may enhance competition. This is because the lower prudential requirements for group 2 deposit takers allows for a lower weighted average cost of capital so they can compete more effectively with large established market participants in group 1. Aligning the thin capitalisation requirements for both group 1 and group 2 deposit takers would undermine this market setting.

20 We also do not agree with Citibank that setting different thin capitalisation threshold requirements for group 1 and group 2 deposit takers would be a barrier to growth in practice. We understand the theoretical concern, however New Zealand's group 2 deposit takers are all far below the group 1 threshold, allowing room for significant growth before the higher tax settings would apply. The four systemically important banks in group 1 are all much larger than the other market participants.

21 We consider that setting different thin capitalisation thresholds based on the size of a bank's New Zealand operations, in line with the Reserve Bank's criteria, will ensure that the thin capitalisation threshold is set at a commercially realistic level for banking groups of the relevant size (which is determined by prudential settings). Distinguishing banking groups depending on whether they include a domestic systemically important bank would be an effective way to align with local prudential settings. This approach will maintain tax neutrality between entities and branches of the same size, which is something that stakeholders considered important in the previous consultation.

22 At present, the thin capitalisation rules for banking groups do not apply to other smaller deposit takers such as finance companies. However, the Reserve Bank is considering changes to how market participants are named, which could result in these other deposit takers coming within scope of the thin capitalisation rules from December 2028. This could increase the smaller deposit takers' compliance costs and have a negative impact on competition. Therefore, if the Reserve Bank's changes affect the scope of the thin capitalisation rules, we consider they should be updated to retain the current scope. We will report to you further on this if necessary.

[7] The portion of the buffer that the Reserve Bank can adjust in response to market conditions.
[8] Systemically important deposit takers holding $100 billion or more of assets.
[9] Deposit takers holding more than $2 billion and less than $100 billion of assets.

23 The tax ratios of approximately half of the banking groups are above the current Tier 1 capital requirements plus the prudential capital buffer s 6(c) . This means that raising the threshold to align with these requirements will affect about half the foreign-owned banks. For all but one of those that do have lower tax ratios, there would only be a modest difference, so the impact of raising the threshold would generally not be significant on a group-by-group basis. As a result, we think that competitive forces would mean it is unlikely that any increased tax costs could be passed on to customers, and if any costs were passed on, they would likely be partial and small.

24 We agree with stakeholders that banking groups should be given a reasonable time to adjust capital levels. However, because the proposals would not have a significant impact, we recommend they are implemented as a single prospective threshold increase from 1 April 2027. The Reserve Bank noted that this would mean there is a misalignment with regulatory settings during their transition period, with the new settings applying in December 2028, but it does not consider this an issue for financial stability. If you would prefer to provide a longer period for banks to adjust, the changes could apply from 1 January 2029 to align with the Reserve Bank's changes. We recommend that the changes are included in the next omnibus taxation Bill.

25 Although these proposals would not raise significant amounts of revenue, they would provide an additional benefit in protecting the existing tax base from erosion (we estimate they will protect approximately $240 million of tax a year). s 9(2)(f)(iv)

Conclusions and next steps

26 In summary, we consider:

- The thin capitalisation threshold should be increased to align with the Tier 1 capital requirements plus the buffer requirements announced in December 2025.
- The rules should provide for a reduction to the threshold in line with any changes announced by the Reserve Bank to the countercyclical capital buffer.
- Different thresholds should apply depending on whether a banking group includes a domestic systemically important bank. The thin capitalisation threshold should be set at 12% for banking groups with a domestic systemically important bank and at 11% for all other banking groups.
- The scope of the thin capitalisation rules should not be changed.
- The proposals should apply from 1 April 2027, or alternatively 1 January 2029 if you would prefer to align the timing with the Reserve Bank's changes.

27 Subject to your approval the changes will be included in the next omnibus taxation Bill.

Impacts

28 If implemented from 1 April 2027, these proposals are forecast to raise $45 million over the forecast period and $15 million per year thereafter.

	$m - increase/(decrease)				
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Crown Revenue and Receipts:					
Tax Revenue – company tax	-	3.200	13.100	14.400	14.500
Total Operating	**-**	**(3.200)**	**(13.100)**	**(14.400)**	**(14.500)**

29 If a single threshold is retained, and it is raised to 12%,[10] the forecast would increase to $52 million over the forecast period and $17 million for outyears. If it is raised to 11%[11], the forecast would decrease to $29 million over the forecast period and $9 million for outyears. If it is raised to 10%, the forecast would further decrease to $24 million over the forecast period and $8 million for outyears.

30 We recommend that the positive impact of thin capitalisation rules changes be managed against the Tax Policy Scorecard. This is consistent with Inland Revenue and the Treasury's recommendation in the recent Scorecard Update report (T2026/261; IR2026/075 refers). You may alternatively choose to manage the increase in tax revenue against the Budget 2026 operating allowance, or to defer a decision until later in the Budget cycle.

31 We do not anticipate a material change in compliance costs due to these proposals because they involve changing a rate in a regime that taxpayers already comply with. There may be one-off costs for some taxpayers to adjust their capital levels.

32 There are no non-departmental operating costs or departmental administrative impacts.

Problem 2: High levels of long-term debt funding in branches

Problem consulted on

33 The second problem is that New Zealand branches of foreign banks are typically funded with a high proportion of long-term debt,[12] which is contrary to the conventional bank profit-making model. The result is it does not produce an arm's length profit overall.

34 Conventional banks (which primarily undertake deposit-taking and lending) generate profits from maturity transformation. This is the practice by which lower interest short-term liabilities, such as customer deposits, are used to fund higher interest long-term assets, like loans. Interest rates typically increase with the term of the loan.

35 Branches of conventional banking businesses are typically funded with a mix of customer deposits, debt raised in the local market and internal funding from the head office. Therefore, the profits attributed to these branches reflect the results that would ordinarily be expected from maturity transformation in a stand-alone entity. However, New Zealand branches of international banks are generally not funded in this way – often almost all their liabilities are internal long-term funding from the head office (this is partly because of the deposit-taking restrictions imposed on branches by the Reserve Bank and the lack of available capital in New Zealand).

36 When a branch is funded with a high proportion of long-term debt, all returns the banking entity makes from maturity transformation[13] are effectively transferred to the head office country. The branch is only attributed returns for managing credit risk.[14]

37 However, the maturity transformation returns arise partly because of the client relationship management, negotiation and lending functions in the branch. In essence, maturity transformation arises from two activities – the bank borrowing short-term funds and then lending them out long term. The branch performs the long-term lending side in New Zealand, but all the profits are attributed to the head office's short-term borrowing side offshore.

Context

38 Often, almost all the liabilities of New Zealand branches of international banks are internal long-term match-funding loans from the head office. Match-funding is an

[10] Aligning with the new prudential requirements for group 1 deposit takers.
[11] Aligning with the new prudential requirements for group 2 deposit takers.
[12] Compared with the entity they are part of.
[13] The term premium.
[14] The credit risk premium.

internal funds transfer pricing approach that is widely used by banks. A bank's treasury acts as a central funding unit, providing notional debt funding to business units for their assets (the debt funding is notional because the head office and the business units are both part of the same legal entity). For example, if a branch issues a three-year loan, it is funded by a notional three-year liability from the treasury unit. The internal match-funding transfer pricing is determined by the market-based rate for that specific maturity. This is further explained in the example in the appendix.

Solution consulted on

39 We consulted on a proposal intended to encourage branch debt funding to be more reflective of the funding mix in the entity a branch is part of. When a branch is attributed a high proportion of long-term funding, it would be attributed a portion of the notional profit made by the head office in respect of that long-term funding over a certain threshold. We also consulted on supporting integrity measures that would apply to external long-term funding and bank special purpose vehicles.

Feedback from stakeholders

40 We received consistent feedback opposing the problem statement and proposed solution. Submissions from stakeholders who provided feedback on this issue included:

- Maturity transformation does not occur in the New Zealand branch. Many risks including interest rate, currency and liquidity risks are managed offshore, usually in the head office. Therefore, it would not be appropriate to attribute profit to the branch for activities it does not undertake. This difference in functions also means the New Zealand branch cannot be compared to the entity as a whole.
- Branches of foreign-owned banking groups are restricted in their ability to take cheaper short-term retail deposits in New Zealand, and therefore they must source funding elsewhere. s 9(2)(b)(ii)
- The proposed solution is a departure from international norms, which means that there is a risk of double taxation should officials not obtain agreement from overseas tax authorities on the proposed solution.
- Increasing the tax costs to operate branches in New Zealand could increase borrowing costs or encourage foreign-owned banking groups to reconsider the structures through which they conduct their wholesale and institutional business in New Zealand. This could harm competition in that market and ultimately reduce tax payable in New Zealand relative to the status quo.

41 Most submitters did not provide detailed comments on specific design features of the proposed solution. However, the views of those that did are summarised below:[15]

- Treasury units themselves do not have a profit of their own, they are cost centres that distribute funding within the group such that they do not make a profit. Therefore, it would not be possible to reallocate profit from the treasury unit.
- It could also be challenging to identify what represents "long-term debt" for the global bank as a whole, and for New Zealand. Any classification of debt should be consistent with already reported metrics (for example, as used in financial statements).

[15] CitiBank, Bank of China, China Construction Bank, Industrial and Commercial Bank of China, Commonwealth Bank of Australia, Deloitte, KPMG, and the New Zealand Banking Association.

- Citibank agreed it may be helpful to limit the scope of the proposal to specific circumstances when a branch has high levels of long-term debt.
- Relying on a competent authority mechanism to address double taxation risks may not provide sufficiently timely or certain resolution because it still relies on other jurisdictions accepting New Zealand's position.
- Consideration would be given to other structures if the proposed solution were to be implemented. For example, banks could transfer their loan books to special purpose vehicles or lend directly from offshore (which could erode the tax base).

Officials' comments

42 We think that the problem has been defined accurately. We do not agree with stakeholders that maturity transformation does not occur in the branch. We consider that the client relationship management, negotiation and lending functions performed by a branch, which are critical for managing risks relating to customer retention, play a role in maturity transformation and therefore should be attributed some of the profit arising from it. The stakeholders' positions also overlook the reality that profits from maturity transformation arise from the head office borrowing short and the branch (which is simply a part of the head office) lending long. The lending by the branch is the activity that in fact produces the revenue. Accordingly, it is not commercially or economically reasonable to contend that none of the profit from maturity transformation is attributable to the branch.

43 In addition, a stand-alone entity funded primarily with long-term debt would be less efficient than normal banks (because it could not generate sufficient profit) and would be unable to compete with them. Therefore, we consider that funding a branch in this way does not produce an arm's length result overall. A portion of the returns from maturity transformation should sit in the branch. We think the feedback s 9(2)(b)(ii) upports the view that high levels of long-term debt do not produce an arm's length result for a branch.

44 However, there is uncertainty around whether other countries will agree with our position. If they disagree, this could result in double taxation. s 6(a) This uncertainty means there is a high risk of double taxation from a unilateral legislative solution, and we recommend not progressing one because of this risk. Although our double taxation agreements contain dispute settlement procedures, given the technical issues identified by countries we have spoken with, we think there is a strong risk that settlement would not be in our favour. This would result in tax refunds.

45 We accept the feedback from stakeholders that the adjustment mechanism we proposed in the consultation would be difficult to apply in practice because some banks do not calculate profit for their treasury unit or on the specific lines of funding provided to a branch. Therefore, if you would still like us to progress work on a unilateral legislative solution, alternative adjustment mechanisms will need to be considered.

46 We recommend that alternatives are considered and discussed with other countries as a first step. Following this, we would report to you about alternative adjustment mechanisms and likely recommend officials undertake detailed targeted consultation with banks on the proposals. While stakeholders are unlikely to support them given their opposition to the problem statement, it would be useful to understand their views

on whether they are practically workable. This means there is no viable unilateral option for Budget 2026.

47 s 9(2)(f)(iv) s 6(a) s 9(2)(f)(iv) We also recommend that New Zealand only progresses a unilateral solution in common with other countries, rather than by ourselves. Moving with other countries would mean New Zealand could follow existing pathways for resolving the problem, which would increase the acceptability of a unilateral solution, and so reduce the risk of double taxation.

48 We have not provided updated forecasts for a unilateral solution because there is uncertainty about the design of an alternative adjustment mechanism and the degree of risk that taxes ultimately may be refunded through settlement procedures in our double tax agreements.

Conclusions and next steps

49 In summary, we consider that, for the long-term debt issue:

- The problem statement has been defined accurately.
- There is a significant risk of double taxation with a unilateral legislative solution, and we do not recommend progressing one because of this risk.
- If, notwithstanding the above, you would like us to progress a unilateral solution, alternative adjustment mechanisms will need to be considered to address practical implementation concerns raised by stakeholders. We also recommend more targeted consultation on these alternatives.
- s 9(2)(f)(iv) , and that a unilateral solution should only be progressed in common with other countries.

50 s 9(2)(f)(iv)

Consultation

51 The Reserve Bank and the Treasury were consulted in preparing this report and their feedback has been incorporated above.

Recommendations

We recommend you:

1 **Agree** to increase the thin capitalisation threshold for banking groups that include a systemically important bank to 12%.	
Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

2 **Agree** to increase the thin capitalisation threshold for other banking groups to 11%.	
Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

3 **Note** that an application date of 1 April 2027 will result in these tax changes applying before the prudential changes announced by the Reserve Bank in December 2025 apply (in December 2028).

4 **Agree** that the changes to the thin capitalisation rules should apply from:

a. 1 April 2027

Agree / Disagree — Agree / Disagree

Minister of Finance — *Minister of Revenue*

OR

b. 1 January 2029 if you would prefer to align with the timing of the Reserve Bank's changes

Agree / Disagree — Agree / Disagree

Minister of Finance — *Minister of Revenue*

5 **Agree** to include the thin capitalisation changes in the next omnibus taxation Bill.

Agree / Disagree — Agree / Disagree

Minister of Finance — *Minister of Revenue*

6 **Note** we will report to you about how to retain the current scope of the thin capitalisation rules for banking groups if naming convention changes being considered by the Reserve Bank affect this.

Financial Recommendations

7 **Note** the following forecast changes as a result of the decisions in recommendations 1 to 4 above (with a 1 April 2027 application date), with a corresponding impact on the operating balance and net core Crown debt:

	$m - increase/(decrease)				
Vote Revenue	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30 & Outyears**
Crown Revenue and Receipts:					
Tax Revenue – company tax	-	3.200	13.100	14.400	14.500
Total Operating	**-**	**(3.200)**	**(13.100)**	**(14.400)**	**(14.500)**

8 **Agree** to one of the following for managing the increase in tax revenue in recommendation 7:

a. manage the increase in tax revenue against the Tax Policy Scorecard (officials' recommendation)

Agree / Disagree — Agree / Disagree

Minister of Finance — *Minister of Revenue*

OR

b. manage the increase in tax revenue against the Budget 2026 operating allowance

Agree / Disagree — Agree / Disagree

Minister of Finance — *Minister of Revenue*

OR

c. defer the decision on the fiscal management of the increase in tax revenue until later in the Budget 2026 process.

Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

9 **Note** there is a high risk of double taxation with a unilateral solution to the problem of bank branches being funded with a high proportion of long-term debt.

10 s 9(2)(f)(iv)

11 s 9(2)(f)(iv)

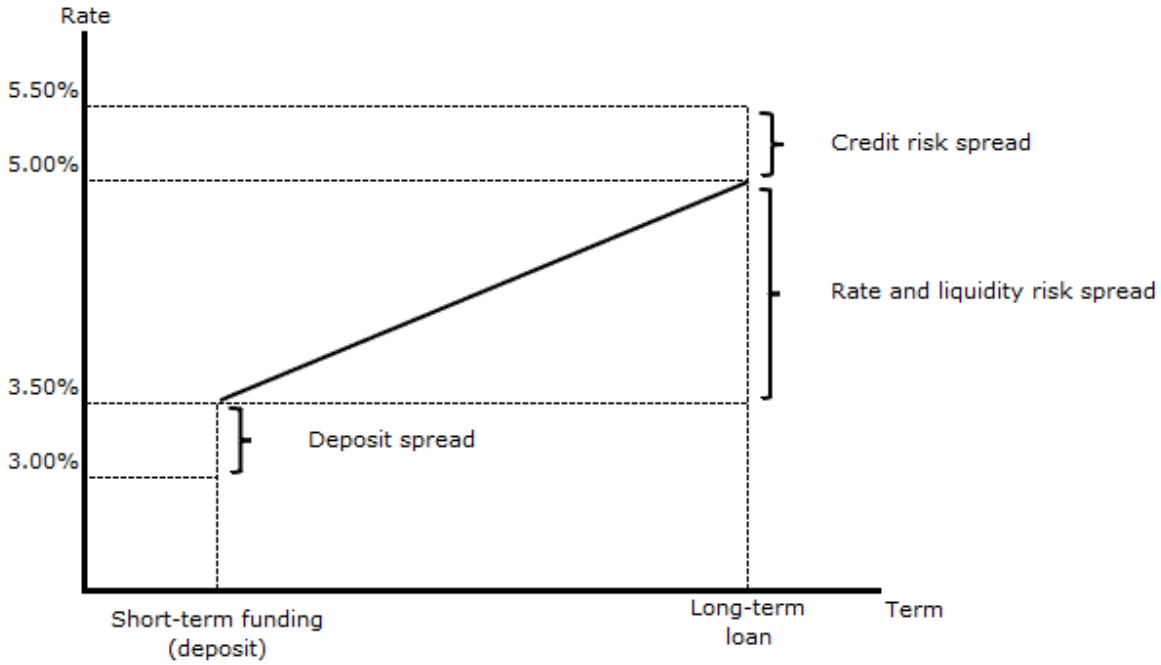
Agree / Disagree	Agree / Disagree
Minister of Finance	*Minister of Revenue*

Sam Rowe
Policy Lead
Policy | Inland Revenue
13 / 03 / 2026

Hon Nicola Willis	Hon Simon Watts
Minister of Finance	**Minister of Revenue**
/ /2026	/ /2026

Appendix: Example of bank funds transfer pricing for match-funding

Diagram: Example of bank funds transfer pricing



1 In the above diagram, a bank is funded by short-term debt funding at 3%. This short-term funding is transferred to the bank's treasury unit at 3.5%. The deposit spread (of 0.5%) is allocated to the unit that manages the short-term funding to cover its costs plus a profit margin.

2 The bank's treasury unit uses the funds to provide long-term debt funding to its branch at 5%, the market-based rate for the specific term. The interest rate and liquidity risk spread (of 1.5%) is allocated to the treasury unit to cover its costs plus a profit margin.

3 The branch uses this funding to make a long-term loan at 5.5%. The credit risk spread (of 0.5%) is allocated to the branch to cover its costs plus a profit margin.

Inland Revenue
Te Tari Taake

Te Tūāpapa Kura Kāinga
Ministry of Housing and Urban Development

POLICY

Tax policy report: Extending Investment Boost to certain residential buildings

Date:	11 September 2025	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2025/348 HUD2025-007930

Action sought

	Action sought	Deadline
Minister of Finance	**Note** the contents of this report **Indicate** whether you want to progress further work on extending Investment Boost to new high-density residential buildings for possible inclusion in Budget 2026	25 September 2025
Minister of Housing		25 September 2025
Minister of Revenue		25 September 2025

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Felicity Barker	Policy Lead – IRD	s 9(2)(a)	☐
Matt Pilkinton	Senior Policy Advisor – IRD		☒
Claire Leadbetter	Policy Manager – HUD		☒
Paul Bruere	Principal Policy Advisor – HUD		☐

11 September 2025

Minister of Finance
Minister of Housing
Minister of Revenue

Extending Investment Boost to certain residential buildings

Purpose

1. This report seeks direction on whether to undertake further work on extending Investment Boost to certain residential buildings for possible inclusion in Budget 2026.

Executive Summary

2. New commercial and industrial buildings are eligible for Investment Boost, but new residential buildings are not. This may be distorting investment away from residential buildings and towards commercial buildings in some circumstances.

3. Taxes are most distorting when there are close substitutes receiving different tax treatment. Commercial and residential buildings are likely to be highly substitutable when:

    3.1 They compete for the same parcel of land. Competition for land between commercial and residential buildings is most apparent in areas zoned for high-density such as city centres and walkable catchments of rapid transit stops.

    3.2 They are of a similar form or use similar construction methods (e.g. a 10-storey apartment block and a similarly constructed 10-storey office block).

4. Current Investment Boost settings are therefore likely to be most distortionary through favouring the development of commercial buildings over high-density residential buildings (e.g. apartments). This may limit the expected impact on new housing supply of the Government's Going for Housing Growth reforms. However, current Investment Boost settings are less likely to be distorting investment away from low and medium density housing (e.g. standalone houses and townhouses).

5. Given the distortion created by current settings, there may be a case to extend Investment Boost to new high-density residential buildings. We estimate extending Investment Boost to new high-density residential buildings in Budget 2026 would have a fiscal cost of around $158 million over the forecast period.

6. Officials consider that extending Investment Boost to new high-density residential buildings is a worthwhile initiative; however, the fiscal cost needs to be weighed against other budget priorities. Should you wish to progress further work, we will provide you with further advice on extending Investment Boost to high-density residential buildings for possible inclusion in Budget 2026. This will include advice on whether extending Investment Boost is the most cost-effective way to support the Government's housing and productivity objectives.

Background

7. Investment Boost was introduced in Budget 2025 as a tax incentive for businesses to invest in assets such as machinery, tools and equipment. It allows businesses to immediately deduct 20 per cent of the value of a new asset in the income year the asset is first available for use.

8. New commercial and industrial buildings are eligible for Investment Boost, but residential buildings are not. A residential building is generally considered to be a place that a person can be expected to live with a degree of permanence. The Income Tax Act classifies buildings such as hotels, motels, serviced apartments and assisted living units in retirement villages (but not independent living units) as commercial buildings.

9. Since enacting Investment Boost, officials have become concerned that the exclusion of residential buildings may be distortionary at the margin in some circumstances. In particular, where land is highly substitutable between commercial or residential uses, Investment Boost may incentivise the construction of commercial buildings over residential buildings. The Property Council has also suggested that Investment Boost be extended to build-to-rent.[1]

Rationale for excluding residential buildings

10. The original policy rationale for excluding residential buildings was that Investment Boost should be targeted towards assets that have a high cost of capital. There is significant uncertainty about the cost of capital for residential buildings, although the cost of capital is likely to be lower on average than other assets eligible for Investment Boost such as machinery and commercial buildings.

11. A key factor that influences estimates for an asset's cost of capital is the rate of economic depreciation (the rate an asset falls in value over time). International evidence suggests that industrial buildings depreciate the fastest, followed by commercial buildings and multi-unit residential buildings respectively. Stand-alone residential buildings seem to depreciate the slowest at a rate close to 0%.

12. While multi-unit buildings will generally depreciate at a slower rate than commercial buildings, there is likely to be significant variability within each category. For example, two-storey terraced housing and 12-storey apartment blocks are both multi-unit residential buildings but are unlikely to depreciate at the same rate. As such, some multi-unit residential buildings may depreciate at the same rate or faster than some commercial buildings.

13. Local government rates may also contribute to commercial buildings having a higher cost of capital on average than residential buildings. Rates for commercial buildings are typically higher than rates for residential buildings with the same capital value. For example, in major cities, commercial rates are 1.5 to 3.7 times higher than residential rates.

Substitutability between residential and commercial buildings

14. Taxes are most distorting when there are close substitutes receiving different tax treatment. Commercial and residential buildings are likely to be highly substitutable when:

[1] For tax purposes, build-to-rent is defined as a development consisting of 20 or more units (in one or multiple buildings) all held in common ownership and used for long-term rental accommodation.

14.1 The buildings compete for the same parcel of land. Competition for land between commercial and residential buildings is most apparent in areas zoned for high-density such as city centres and walkable catchments of rapid transit stops. In these areas, landowners are more likely to have legitimate choices between developing commercial or residential buildings.

14.2 The buildings are of a similar form or use similar construction methods. For example, a 10-storey apartment building and a 10-storey office block could have almost identical construction and only differ in internal fit-out.

15. Given this, current Investment Boost settings are likely to be most distortionary in favouring development of commercial buildings over high-density residential buildings such as apartments.

16. Current settings are less likely to be distorting investment away from low and medium density housing (e.g. standalone houses and townhouses). This type of housing is likely to depreciate at lower rates than commercial buildings and therefore have a lower cost of capital. In addition, there is less competition for land between residential and commercial buildings in lower density zones as:

16.1 Lower population densities limit the amount of demand and labour necessary to support significant amounts of commercial activity; and

16.2 Zoning rules limit the types and extent of commercial activities that can take place in these areas.

Impact on Government's housing objectives

17. Current Investment Boost settings may lead to less new high-density residential buildings, and more commercial buildings, than would have otherwise been the case. In the case of mixed-use buildings, Investment Boost may lead to a lower proportion of the building being used for residential purposes. At the margins, this distortion could limit the expected impact on new housing supply of the Government's Going for Housing Growth programme and resource management reforms. For example, the recently enacted requirements to enable building heights of up to 15 stories around some City Rail Link stations may not have the anticipated housing impact if investment is distorted towards commercial buildings.

Extending Investment Boost to high-density residential buildings

18. Given the distortion created by current settings, there may be a case to extend Investment Boost to high-density residential buildings such as apartments. This would enable property investors purchasing new rental apartments to deduct 20 per cent of the cost (excluding land). Owner-occupiers purchasing new apartments would not be able to claim Investment Boost as they are not using the property to derive income.

Benefits

19. In addition to increasing neutrality, extending Investment Boost to high-density residential buildings would have a few other potential benefits:

19.1 **Increased productivity** – High-density residential buildings are more likely to have a higher cost of capital. As such, extending Investment Boost to these buildings would support the Government's productivity objectives. Housing growth is also an enabler of economic growth due to the agglomeration benefits of cities. If extending Investment Boost leads to additional housing growth, there will be related productivity gains.

19.2 **Integrity benefits** – There is currently some uncertainty around the boundary between eligible commercial buildings and ineligible residential buildings. This is particularly the case with serviced apartments which are eligible for Investment Boost but can easily be converted to long-term residential rental use. Extending Investment Boost to high-density residential buildings would reduce these boundary issues between eligible and ineligible buildings.

Risks

20. As discussed in paragraphs 26-30, extending Investment Boost to high-density residential buildings would have a significant fiscal cost. Other risks of extending Investment Boost include:

20.1 **Subsidisation** – Extending Investment Boost may result in subsidisation of some investments in residential buildings, reducing economic efficiency. Subsidisation of investment is an existing risk of Investment Boost; however, this risk is reduced by targeting investments with higher costs of capital. Extending Investment Boost to high-density residential buildings (but not other housing) is therefore unlikely to create a significant risk of subsidisation.

20.2 **Integrity risks** – Current tax settings look at the use of a building to determine whether it is eligible for Investment Boost. Extending Investment Boost to high-density residential buildings would instead require looking at the structure of the building to determine eligibility. This may give rise to some unintended impacts. Extending Investment Boost may also create some boundary issues between rental apartments and owner-occupied apartments.

Definition of high-density residential buildings

21. Extending Investment Boost to high-density residential buildings would require robust criterion for what qualifies as high-density. Criteria based on building height would likely be a clear and simple way to ensure Investment Boost is only extended to high-density residential buildings.

22. A potential option for defining a high-density residential building is a dwelling in a multi-unit building that is at least four storeys tall. This definition would target residential buildings most likely to have high construction costs and most likely to be competing for land with commercial buildings as:

22.1 Buildings four or more storeys tall are typically much more expensive to build owing to engineering requirements; and

22.2 Four storey buildings are typically not permitted in areas zoned for low-medium density.

23. Further advice on how to define a high-density residential building can be provided if you agree to progressing work on extending Investment Boost.

Build-to-rent

24. As an alternative to extending Investment Boost to all new high-density residential buildings, it could instead be extended to just new build-to-rent developments. For tax purposes, build-to-rent is defined as a development consisting of 20 or more units (in one or multiple buildings) all held in common ownership and used for long-term rental accommodation. Build-to-rent developments will typically consist of high or medium density housing. However, a development of 20 or more stand-

alone houses can qualify as build-to-rent. Current Investment Boost settings are less likely to distort investment in less dense types of build-to-rent because depreciation is likely to be lower.

25. Extending Investment Boost to only build-to-rent would have a lower fiscal cost than extending it to all new high-density residential buildings. However, it is not clear that supporting build-to-rent over other residential rental business models is the best use of Investment Boost. Extending Investment Boost to build-to-rent may be distortionary (i.e. by making developments with less than 20 units or with dispersed ownership relatively less attractive) and create integrity risks as build-to-rent units can easily be changed to standard rental units. Furthermore, the distortionary impact of current Investment Boost settings moving investment away from high-density residential buildings would also largely remain.

Fiscal implications

26. Investment Boost as enacted had an estimated fiscal cost of around $6.6 billion over the Budget 2025 forecast period.

27. We estimate the cost of extending Investment Boost to new high-density residential buildings is around $158 million over the forecast period. For the purposes of this estimate, we have assumed high-density residential buildings are only eligible if they are first available for use on or after Budget Day 2026.

Table 1: Fiscal impact of extending Investment Boost to new high-density residential buildings

	$m – increase/(decrease)			
Vote Revenue **Minister of Revenue**	**2025/26**	**2026/27**	**2027/28**	**2028/29 & Outyears**
Crown Revenue and Receipts: Tax Revenue – company tax	(10.300)	(43.400)	(42.700)	(61.100)
Total Operating	**10.300**	**43.400**	**42.700**	**61.100**

28. There is significant uncertainty in this estimate as there has been significant volatility in the number of new apartments constructed each year and predicting future delivery trends is difficult. Since the Auckland Unitary Plan became operative, we estimate a long-run average of around 3,250 new apartments completed per annum. However, consents for new apartments between 2018 and 2023 were around 4,000 per annum but dropped to 1,942 in the year to June 2024. They have subsequently recovered 12 percent to 2,178 in the year to June 2025.

Build-to-rent

29. By way of comparison, extending Investment Boost to build-to-rent would have an estimated cost of around $77 million over the forecast period. As above, this assumes build-to-rent units are only eligible if they are first available for use on or after Budget Day 2026.

Table 2: Fiscal impact of extending Investment Boost to build-to-rent

	$m – increase/(decrease)			
Vote Revenue **Minister of Revenue**	**2025/26**	**2026/27**	**2027/28**	**2028/29 & Outyears**
Crown Revenue and Receipts: Tax Revenue – company tax	(5.000)	(21.100)	(20.700)	(29.800)
Total Operating	**5.000**	**21.100**	**20.700**	**29.800**

30. There is significant uncertainty around the growth of build-to-rent. Our estimate is based on optimistic construction delivery trends of around 1,000 new units per annum.

Recommendation

31. Officials consider that extending Investment Boost to new high-density residential buildings is a worthwhile initiative, given the potential to improve neutrality between commercial and residential investment, support housing supply objectives, and reduce boundary issues in the tax system. However, we note that the fiscal cost of such an extension is not insubstantial and needs to be weighed against other budget priorities.

Consultation

32. The Treasury has been consulted on this report.

Next steps

33. Should you wish to progress further work, we will provide you with further advice on extending Investment Boost to high-density residential buildings for possible inclusion in Budget 2026. This will include advice on whether extending Investment Boost is the most cost-effective way to support the Government's housing and productivity objectives.

34. We recommend discussing with officials if you would like further work to be undertaken on extending Investment Boost to a different subset of residential buildings (e.g. just build-to rent or all new residential).

Recommended action

We recommend that you:

1. **Indicate** whether you want to progress further work on extending Investment Boost to new high-density residential buildings for possible inclusion in Budget 2026.

   Yes/No

2. **Note** the following estimated fiscal impacts of extending Investment Boost to new high-density residential buildings.

	$m – increase/(decrease)			
Vote Revenue **Minister of Revenue**	**2025/26**	**2026/27**	**2027/28**	**2028/29 & Outyears**
Crown Revenue and Receipts: Tax Revenue – company tax	(10.300)	(43.400)	(42.700)	(61.100)
Total Operating	**10.300**	**43.400**	**42.700**	**61.100**

   Noted

3. **Indicate** whether you want officials to undertake further work on extending Investment Boost to a different subset of residential buildings (e.g. just build-to-rent or all new residential buildings).

   Yes/No

s 9(2)(a)

Felicity Barker
Policy Lead – IRD

s 9(2)(a)

Claire Leadbetter
Policy Manager – HUD

Hon Nicola Willis
Minister of Finance
/ /2025

Hon Simon Watts
Minister of Revenue
/ /2025

Hon Chris Bishop
Minister of Housing
/ /2025

Te Tūāpapa Kura Kāinga
Ministry of Housing and Urban Development

Inland Revenue
Te Tari Taake

Briefing

Extending Investment Boost to build-to-rent developments			
To Minister	Hon Nicola Willis	**Portfolio**	Finance
	Hon Chris Bishop	**Portfolio**	Housing
	Hon Simon Watts	**Portfolio**	Revenue
Date	10/12/2025	**Priority**	High
Tracking number	IR2025/468; HUD2025-008735		

Action sought	
Action sought	Indicate whether to submit a Budget bid for extending Investment Boost to build-to-rent.
Deadline	17/12/2025 to allow for a Budget bid to be submitted to the Treasury by the 19 December deadline.

Contact for discussion			
Name	**Position**	**Telephone**	**First contact**
Claire Leadbetter	Policy Manager - HUD	s 9(2)(a)	✓
Paul Bruere	Principal Advisor - HUD		
Felicity Barker	Policy Lead – IRD		
Matt Pilkinton	Senior Policy Advisor – IRD		✓

Other agencies consulted
The Treasury

Recommended actions	
It is recommended that you:	
1. Note the Minister of Finance and Minister of Housing requested advice on extending Investment Boost to build-to-rent (IR2025-348; HUD2025-007930 refers).	*Noted*
2. Indicate whether to submit a Budget bid for extending Investment Boost to build-to-rent.	*Yes* | *No*
3. Note the Ministry of Housing and Urban Development (HUD) recommends extending Investment Boost to build-to-rent; however, Inland Revenue and the Treasury do not.	*Noted*

4. Note the estimated fiscal impacts of extending Investment Boost to build-to-rent:

	$m – increase/(decrease)				
Vote Revenue Minister of Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & Outyears
Crown Revenue and Receipts: Tax Revenue – company tax	(5.000)	(21.100)	(20.700)	(29.800)	(27.500)
Total Operating	5.000	21.100	20.700	29.800	27.500

If a Budget bid for extending Investment Boost to build to rent is submitted

5. Agree that Investment Boost is only extended to build-to-rent developments in high-density residential buildings (recommended by HUD and Inland Revenue). — *Agree* | *Disagree*

s 9(2)(a)

Claire Leadbetter
Policy Manager - HUD
10 / 12 / 2025

s 9(2)(a)

Felicity Barker
Policy Lead - IRD
10 / 12 / 2025

Hon Nicola Willis
Minister of Finance
..... / ..... / .....

Hon Chris Bishop
Minister of Housing
..... / ..... / .....

Hon Simon Watts
Minister of Revenue
..... / ..... / .....

[SENSITIVE]

Purpose

1. This report seeks decisions on submitting a budget bid to extend Investment Boost to cover newly completed build-to-rent developments, for potential inclusion in a tax package for Budget 2026.

Executive summary

2. Build-to-rent housing is playing a growing role in the provision of housing at scale and density in New Zealand. Build-to-rent is likely to benefit from changes the Government is making to the planning system, land supply and infrastructure settings, and supports housing and urban development objectives. It can attract additional institutional investment and provide counter-cyclical construction activity when build-to-sell development is more challenging.

3. Current Investment Boost settings may, at the margins, be distorting investment away from high density residential buildings (including build-to-rent) and towards commercial buildings, as residential buildings are not eligible for Investment Boost. However, current settings are unlikely to be distorting investment away from low and medium density housing. In previous advice, HUD and Inland Revenue agreed there may be a case to extend Investment Boost to high-density residential buildings to address this distortion. Extending Investment Boost to build-to-rent would partially address this distortion; however, it would create a new distortion favouring build-to-rent over other residential rental business models.

4. HUD recommends providing Investment Boost for high-density build-to-rent to remove a potential barrier to additional housing and countercyclical construction activity and partially address a distortion against high-density residential buildings. High-density build-to-rent developments can provide hundreds of units, and any additional housing would have more security of tenure for tenants and be of higher quality relative to the general stock of rental housing.

5. Inland Revenue does not recommend extending Investment Boost to build-to-rent as this is unlikely to stimulate significant additional supply and would largely provide windfall gains to developments that would go ahead under current settings. As such, Inland Revenue considers extending Investment Boost to build-to-rent is unlikely to justify the estimated fiscal cost of $104 million over the forecast period.

6. Noting agencies' differing views, HUD and Inland Revenue both agree that if Investment Boost is extended to build-to-rent, it should be limited to just build-to-rent developments in high-density residential buildings. This will avoid providing tax concessions to build-to-rent developments consisting of low and medium-density buildings that are not affected by the distortion.

7. If you wish to consider extending Investment Boost to build-to-rent as part of Budget 2026, further advice will be provided in early 2026 on the detailed design of the policy. In the interim, a placeholder Budget 2026 initiative will be submitted to the Treasury by the Friday 19 December 2025 deadline.

Background

8. Officials have previously provided advice seeking direction on whether to extend Investment Boost to certain residential buildings (IR2025-348; HUD2025-007930 refers). Investment Boost provides a one-off deduction for 20 percent of the cost of new capital assets, including new commercial and industrial buildings. The report noted there may be a case to extend Investment Boost to high-density residential buildings (e.g. apartments) as residential buildings are not eligible for Investment Boost. At the margins, this may be distorting investment away from these residential buildings and towards commercial buildings.

9. The Minister of Finance and Minister of Housing indicated they did not want further work undertaken on extending Investment Boost to high-density residential buildings. However, further advice on the extension of Investment Boost to build-to-rent alone was requested.

What is build-to-rent?

10. Build-to-rent in New Zealand is a small but growing type of purpose built rental where owners hold and run a contiguous group of dwellings as rentals over the long term. Build-to-rent is characterised by larger-scale development, long-term tenancies (e.g. fixed-terms of up to ten years) and unified property ownership and tenancy management. Build-to-rent development opportunities are typically high-density apartments within or close to urban transport corridors and amenities, for tenants who value the access and convenience these locations provide.

11. Build-to-rent developments were excluded from the subsequently repealed rules limiting the tax deductibility of interest for residential property investors. For the purposes of this exclusion, build-to-rent land was defined as a development consisting of 20 or more units (in one or multiple buildings) all held in common ownership and used for long-term rental accommodation. In addition, to qualify for the exemption, build-to-rent operators were required to offer ten-year fixed-term tenancies that tenants can terminate with 56 days' notice, and tenancy agreements that expressly refer to the ability of tenants to personalise the dwelling.

Role that build-to-rent plays in the housing system

12. The build-to-rent sector can help support the Government's housing and urban development priorities, including increased density in urban centres and along major transit corridors, and improved quality of rental housing stock. The current rental housing stock is generally older so, at the margins, increasing build-to-rent provision will increase the supply of new built rentals.

13. Increasing build-to-rent supply also provides choice for some renters who value tenure stability e.g. people with school age children who don't expect to buy a home in the short-term, or older renters who wish to stay connected to a particular community. Children can benefit significantly from secure tenure, which stabilises

schooling and friendships, frequent contact with health professionals, and community participation. Similarly, for older people tenure stability contributes to health and wellbeing, supporting ageing in place.

14. Build-to-rent is likely to deliver additional housing as it is financed by institutional investors who may not invest in residential property in New Zealand otherwise, and it is less likely to crowd out delivery of homes for owner occupation. Build-to-rent can play a counter-cyclical role in supporting housing construction at times when securing buyers and finance for build-to-sell developments is more challenging.

Build-to-rent is enabled by a set of actions the Government is taking

15. The Government's current work programme will support the sector through removing regulatory barriers to build-to-rent. Changes the Government is making through the Going for Housing Growth and RMA reforms are likely to enable the delivery of build-to-rent alongside other housing types. The recent addition of the large rental asset test to the Overseas Investment Act 2005 will also enable more overseas investment in build-to-rent.

16. Forecasting build-to-rent delivery trends is difficult. As with apartment construction more generally, there is significant volatility in the number of new build-to-rent units constructed each year (including high, medium and low-density build-to-rent):

    - Analysis commissioned by HUD from PwC in 2023 estimated build-to-rent could deliver between 7,200 and 11,500 units by 2033 under regulatory settings prior to the introduction of Investment Boost. This analysis noted different depreciation treatment of residential and commercial buildings and fitouts can create barriers to build-to-rent development.
    - The Property Council has a public build-to-rent tracker that shows, as of 30 September 2025, there are 1,106 units under construction and 3,899 "in the pipeline".[1] The units under construction are concentrated in Auckland, and both Auckland and Otago regions (predominantly Queenstown) have over 1,000 units in the pipeline.

Analysis on extending Investment Boost to build-to-rent

17. New Zealand's tax system is intended to support economic efficiency through minimising distortions on taxpayers' behaviour. Our previous advice noted that current Investment Boost settings may be distortionary in favouring development of commercial buildings over high-density residential buildings such as apartments. This is because high-density residential buildings will often compete for the same parcel of land as commercial buildings and may be of a similar form or use similar construction methods. However, current settings are less likely to be distorting

[1] This could include developments that are at the final pre-construction phases, to announced developments that have not secured consents or financing.

investment away from low and medium density housing (e.g. standalone houses and townhouses).

18. At the margins, Investment Boost may be distorting investment away from build-to-rent developments in high-density buildings and towards commercial buildings. Build-to-rent developments will typically be high density; however, some developments are medium density. A development of 20 or more contiguous standalone houses held in single ownership may also be build-to-rent. Investment in medium and low-density build-to-rent developments is unlikely to be distorted by Investment Boost.

19. Extending Investment Boost to build-to-rent would reduce the distortion favouring investment in commercial buildings over high-density build-to-rent developments. However, as currently defined it would also:

    - **Create a new distortion** by favouring build-to-rent over other residential rental business models. Rental developments with fewer than 20 units or with dispersed ownership would be relatively less attractive if build-to-rent was eligible for Investment Boost.
    - **Provide tax concessions** for a small number of low and medium density build-to-rent developments as current settings are not distorting investment away from these developments. We propose to mitigate this by extending Investment Boost to only build-to-rent developments in high-density residential buildings (such as apartment blocks).
    - **Create integrity risks** for Crown revenue as build-to-rent units could be easily converted to a standard rental unit after an Investment Boost deduction has been claimed.

20. Inland Revenue advises there is not a strong case under standard tax policy considerations for extending Investment Boost to build-to-rent (even if limited to just high-density build-to-rent). This is because:

    - Extending Investment Boost would create a new distortion favouring build-to-rent over other residential rental businesses.
    - The existing distortion favouring investment in commercial buildings is likely to only have a marginal impact on the delivery of new build-to-rent developments. Reducing this distortion by extending Investment Boost to build-to-rent may therefore not justify the significant fiscal cost of approximately $104 million over the forecast period.

Extending Investment Boost to build-to-rent could have positive, but uncertain impacts for the sector

21. HUD considers there is still a case for extending Investment Boost to high-density build-to-rent, as partially fixing the existing distortion removes a barrier for a sector that provides supply, scale and diversity in the rental market. Each high-density

build-to-rent project can provide over 100 units,[2] and, at the margins, extending Investment Boost to build-to-rent could lead to additional units in a development and/or additional build-to-rent developments being constructed within the forecast period. Addressing part of the distortion against high-density residential buildings is preferred to taking no action, and builds on reforms elsewhere that remove barriers to investment in and construction of build-to-rent.

22. Inland Revenue notes that any impacts on supply from extending Investment Boost to build-to-rent may also be limited owing to policy uncertainty around whether Investment Boost will be an enduring feature of the tax system. Some stakeholders have raised that businesses are discounting the benefit of Investment Boost when making investment decisions on long-term projects (such as construction projects) because of a concern that a future Government will repeal Investment Boost before the project is complete, and the deduction can be claimed. This suggests much of the benefit of extending Investment Boost to build-to-rent will be a windfall gain to investment that would have occurred anyway, rather than stimulating new investment. Inland Revenue has separately provided advice to the Minister of Revenue on increasing policy certainty around Investment Boost for long-term projects (IR2025/455 refers).

Financial implications

23. The estimated cost to extend Investment Boost to build-to-rent is around $104 million over the forecast period.[3] The fiscal impact of the extension to build-to-rent developments is shown below:

	$m – increase/(decrease)				
Vote Revenue Minister of Revenue	2025/26	2026/27	2027/28	2028/29	2029/30 & Outyears
Crown Revenue and Receipts: Tax Revenue – company tax	(5.000)	(21.100)	(20.700)	(29.800)	(27.500)
Total Operating	5.000	21.100	20.700	29.800	27.500

24. Costings are based on approximately 1,000 build-to-rent units completed per year, which is above the midpoint of estimates from PwC analysis (935 per year for ten years). In practice, the amounts claimed in deductions for build-to-rent would vary significantly from year-to-year.

Recommendation

25. Inland Revenue and HUD agree that Investment Boost is creating a distortion that, at the margins, favours commercial building construction over high-density residential buildings. Extending Investment Boost to high-density build-to-rent developments

[2] For context, Resido (Sylvia Park) the largest completed build-to-rent complex in New Zealand, has 295 units.
[3] The previous advice estimated costs of $77 million out to 2028/29. This advice extends the forecast period to 2029/30.

would partially remove this distortion but has a significant fiscal cost. Furthermore, the effects of extending Investment Boost to build-to-rent are difficult to assess and may be offset or less material than other action to encourage housing supply.

26. Inland Revenue does not recommend extending Investment Boost to build-to-rent (even if limited to just high-density build-to-rent developments). The cost of such an extension is not justified as it would likely only lead to minor impacts on the supply of new build-to-rent developments. In addition, it would create a distortion favouring build-to-rent over other residential rental business models. If the Government wishes to support the build-to-rent sector, reducing regulatory barriers or providing targeted funding is likely to be more effective.

27. HUD recommends extending Investment Boost to high-density build-to-rent buildings to partially remove the distortion that potentially favours commercial building development over high-density residential development at the margins. HUD also supports the extension on the grounds that it could remove a disincentive to housing investment from institutional investors, and provide countercyclical construction activity.

Consultation

28. The Treasury was consulted on this advice. The Treasury agreed with previous advice that there may be a case to extend Investment Boost to new high-density residential buildings, given the potential distortion Investment Boost created between commercial and high-density residential buildings (IR2025/348 HUD2025-007930 refers). However, the Treasury does not recommend extending Investment Boost to build-to-rent, as this would not address the existing distortion and would create a new distortion favouring build-to-rent over other residential developments.

Next steps

29. We have asked for joint decisions by 17 December 2025, so that if Ministers agree to the proposal, it can be incorporated into the Budget bid process.

30. If you wish to consider extending Investment Boost to build-to-rent as part of Budget 2026, further advice will be provided in early 2026 on the detailed design of the policy. In the interim, a placeholder Budget 2026 initiative will be submitted to the Treasury by the Friday 19 December 2025 deadline.

Inland Revenue
Te Tari Taake

POLICY

Tax policy report: Software subsidy for small businesses

Date:	10 December 2025	**Priority:**	High
Security level:	Sensitive - Budget	**Report number:**	IR2025/475

Action sought

	Action sought	Deadline
Minister of Revenue	**Agree** to recommendations	15 December 2025

Contact for telephone discussion (if required)

Name	Position	Telephone	Suggested first contact
Claire McLellan	Acting Policy Lead	s 9(2)(a)	☒
Talia Harvey	Senior Policy Advisor		☐

10 December 2025

Minister of Revenue

Software subsidy for small businesses

Executive summary

1. This report seeks your decision on whether to request a Budget invitation for a subsidy for business software aimed at improving tax compliance outcomes for small businesses and reducing administration costs for Inland Revenue.

2. We previously committed to doing more work on a software subsidy to encourage taxpayers to use software, to be potentially included in Budget 2026. We have completed this work and do not recommend progressing it.

3. While it would likely save some compliance costs for businesses, cost does not appear to be the main barrier for uptake. In recent informal consultation a software subsidy to encourage software use was not well supported.

4. Furthermore, initial analysis suggests administrative savings for Inland Revenue are modest and do not justify a subsidy.

5. However, if you do wish to consider an option for Budget 2026, we have identified two alternative mechanisms which could deliver this: a super-deduction or a direct subsidy.

6. The fiscal cost of the super-deduction proposal is $326 million over the forecast period. This level of cost and uncertainty of impact means that investment is likely to be better used elsewhere.

Background

7. Inland Revenue has been considering policy options that could be progressed for Budget 2026 to support tax compliance for small businesses. At the officials meeting on 16 September, you expressed interest in further advice on a subsidy to encourage taxpayers to use software.

8. Accounting and payroll software is widely regarded as best practice for accurate recordkeeping and financial management as long as they are deployed and used correctly.

9. Despite Inland Revenue's Business Transformation programme, small businesses can face compliance costs that are disproportionately high relative to their size. One of the reasons for this may be a failure to use software when it is available.

10. Inland Revenue has a longstanding commitment to understanding and addressing SME tax compliance challenges, with regular surveys and research dating back several years. These efforts have included a series of compliance surveys—including the 2025 SME Compliance Survey (2025 Survey), which focused on businesses with 0–20 employees, including sole traders. The 2025 Survey asked a range of questions about businesses' use of software.

11. Inland Revenue is actively working to address compliance challenges through two initiatives: Simplifying Small Business Tax (SSBT) and Improving Business Tax (IBT).

Problem definition

12. It is generally accepted that accounting and payroll software can reduce compliance costs for small businesses and administration costs for Inland Revenue.

13. Despite the potential for software to reduce compliance effort, uptake remains low among the smallest businesses. The 2025 Survey found that for those with 6-19 employees around 80% use accounting software for record-keeping and filing purposes. For smaller businesses with 0-5 employees, this falls to just under 60%. Similar gaps exist for GST.

14. Because larger SMEs (businesses with 6-19 employees) already have high adoption rates, any intervention to improve compliance efficiency should focus on smaller businesses, where the need and potential impact are greatest. We recommend such interventions, if progressed, target small businesses with 0-10 employees.

15. The 2025 Survey found that 70% of small businesses not currently using software believe they have the skills and tools needed without using software and more than half believe their business is too small to justify adopting software.

16. However, one third of those businesses not currently using software, do cite cost as a factor, and so possible levers to encourage uptake could include subsidies (such as an upfront subsidy/voucher or super-deductions).

Analysis

17. Subsidies can be used to encourage taxpayers to adopt business software for tax compliance. These mechanisms have been used in other contexts to influence behaviour, but their effectiveness for business software is uncertain.

18. We have undertaken work to assess the likely effectiveness of a subsidy for improving taxpayer compliance outcomes and reducing Inland Revenue's administrative costs. This includes reviewing recent engagements with businesses and analysing Inland Revenue administrative data. In summary we found:

    - for business software, given cost is not the most significant barrier for businesses to take up software, it may be of only limited influence and deliver benefits only to those who do use or would have used software in any case.

    - informal engagement with stakeholders, gave an indication that external software providers did not favour a direct subsidy due to concerns that it may encourage a race to the bottom. It could encourage new entrants with lower quality products to enter the market.

    - because we expect taxpayers to weigh up the cost of their time as compared with the cost of software, the fact that some choose to spend their time on manual compliance rather than have software do this for them does not, in itself, justify intervention to subsidise software.

    - some evidence that software use does reduce administration costs for Inland Revenue. In particular, the proportion of GST and Employers returns that can completed without manual intervention is higher when taxpayers use software, but the difference is not significant when compared to those who use MyIR.

19. In conclusion, having completed further analysis, Inland Revenue's recommendation is to not progress with a software subsidy for Budget 2026. We consider the investment that would be required would be better allocated to other projects.

Options

20. If you do wish to consider an option for Budget 2026, we have identified two alternative mechanisms which could deliver this: a super-deduction or a direct subsidy. If progressed, we would recommend that the options be targeted at smaller businesses where survey data shows uptake of business software is lowest (0-10 employee businesses)[1].

Option one: Super-deduction

21. This option would introduce a super-deduction of 200% for eligible business software costs[2], which could be capped, for example at $3,000[3] per business per year and time-limited to three years. This would reduce the net expense for businesses. For example:

    - If a business spends $1,000 on approved software and faces a 28% company tax rate:
        - Normal deduction: $1,000 × 28% = $280 tax benefit
        - 200% deduction: $2,000 × 28% = $560 tax benefit
    - This would give the business a $280 benefit of the subsidy[4].

22. This would be a self-assessed approach that minimises administrative complexity.

23. It is challenging to target this policy towards eligible businesses who are not currently using software. This means that the super-deduction would be available for all eligible businesses. This results in a high fiscal cost of approximately $100 million p.a. for design settings described in paragraph 21. If applicable from the 2026-27 tax year, this is estimated to cost $326 million within the forecast period. While the cost can be scaled by reducing the cap or the time-limit, doing so would also reduce the incentive effect of any subsidy.

Option two: Direct subsidy

24. This option would provide a subsidy directly to the software providers based on the number of customers who are eligible businesses.

25. The delivery mechanism makes this option more complex and less efficient. Unlike a super-deduction, which can be implemented through existing tax processes, an upfront subsidy would require Inland Revenue to engage directly with numerous software providers. This introduces a substantial administrative overhead for eligibility checks, payment processing, and monitoring.

26. Experience with similar incentive schemes shows that uptake can be limited when claiming requires additional steps outside normal processes. Under a direct subsidy model, software businesses would need to complete an application and verification processes, which adds friction compared to incentives embedded in routine tax filings for the taxpayers receiving the benefit.

s 6(c)

[1] While survey data showed uptake was lowest for businesses with 0-5 employees, we would suggest a higher upper bound.
[2] This would be limited to the purchase or subscription to a software package that was specifically designed to provide a double entry accounting system, point of sale or payroll software to an eligible business.
[3] The $3,000 limit ensures that all major software costs should qualify each year. The costing assumes most business will be under that limit.
[4] Taxpayers in a tax loss position may not derive an immediate benefit from this option.

28. We have not costed this option as it would depend heavily on specific design.

Financial implications

29. If progressed, a super-deduction for businesses with 0-10 employees, with a $3,000 cap and 3-year time-limit applying from 1 April 2026 is estimated to have a fiscal cost of $326 million over the forecast period. This is set out in the table below by June year ($million):

	$m - increase/(decrease)				
Vote Revenue **Minister of Revenue**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30**
Crown Revenue and Receipts: Tax Revenue – income tax*	(26.000)	(104.000)	(110.000)	(86.000)	-
Total Operating	**26.000**	**104.000**	**110.000**	**86.000**	**-**

*Split 88% company tax, 12% other persons

30. The detailed design for delivering a direct subsidy would need to be determined if this is the preferred option. A new appropriation would likely be required to fund the subsidy. We would need to do further work to develop a fiscal estimate for the subsidy once the design is established.

Administrative implications

31. If a super-deduction is progressed, the implementation costs and ongoing administration costs are estimated to be $0.200 million over the forecast period.

32. However, if a direct subsidy is progressed, the implementation costs are estimated at $2.000 million and the preliminary administration costs are estimated at $26.250 million over the forecast period, subject to design.

33. If progressed, Inland Revenue will seek funding for the administration cost of this initiative as the cumulative impact of all Budget initiatives for Vote Revenue exceeds Inland Revenue's ability to fund, without directly impacting core service delivery, tax revenue, or tax debt.

Consultation

34. The Treasury has been consulted on this report and agrees with Inland Revenue's conclusions. Given the significant Crown investment required for the proposal, there would need to be strong evidence of the positive externalities arising to justify the subsidy. The Treasury has not been presented with such evidence to date.

35. Advancing the proposed option set would incur a significant fiscal cost. Given the challenging fiscal environment, there is a high bar for new spending for Budget 2026. The proposal outlined does not align with the Government's Budget 2026 spending priorities of addressing outstanding coalition commitments, providing critical and urgent funding to maintain core services, or supporting delivery-ready capital investments approved by Cabinet.

Next steps

36. Progressing either option would require Budget funding. As this work is not on the Tax and Social Policy Work Programme, it is not currently invited into the Budget process.

Specific approval from the Minister of Finance would be needed to submit a bid, and Budget bid submissions are due by 19 December.

37. If you wish to progress work on a super-deduction or direct subsidy, we recommend discussing its inclusion into the Budget process with the Minister of Finance before 19 December. We can prepare a placeholder bid in the interim, and submit this by the deadline, subject to your decision in this paper and the outcome of your discussion with the Minister of Finance.

Recommended action

We recommend that you:

1) Agree to one of the following options:

a) Not to progress further work on a super-deduction or direct subsidy for business software **(recommended)** Agreed/Not agreed	b) **Super-deduction:** 200% deduction for eligible software to businesses with less than 10 employees and $20m turnover for a time limited 3-year period and up to a maximum of $3,000 per business per year. Agreed/Not agreed	c) **Direct Subsidy:** to eligible software providers and products based on new customers signed up within three years commencing 1 April 2026. Agreed/Not agreed

2) **Note** that the fiscal cost of option b is estimated to be $326 million over the forecast period (subject to design decisions) with a corresponding impact on the operating balance and net core Crown debt:

	$m - increase/(decrease)				
Vote Revenue **Minister of Revenue**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30**
Crown Revenue and Receipts: Tax Revenue – income tax*	(26.000)	(104.000)	(110.000)	(86.000)	-
Total Operating	**26.000**	**104.000**	**110.000**	**86.000**	**-**

*Split 88% company tax, 12% other persons

Noted

3) **Note** that the mechanism for a direct subsidy would still need to be determined but it is expected that a new appropriation would be required to fund the subsidy.

Noted

4) **Note** that if you agree to either option b or c, then **agree** to seek approval from the Minister of Finance to invite the fiscal impacts of this initiative into the Budget 2026 process.

Noted and Agreed/Noted and not agreed

s 9(2)(a)

Claire McLellan
Acting Policy Lead
Policy

Hon Simon Watts
Minister of Revenue
Date: