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Budget 2006

As expected this year's Budget does not deliver tax cuts for either individuals or companies. Minister of Finance, Dr Cullen, promised no surprises on the tax front and has stuck to his word. In fact this year's Budget sidelines tax – unsurprising given that it falls between two significant tax developments: the radical reforms to the taxation of investment income introduced in yesterday's Bill and the business tax review, which is to commence in earnest in June or July.

Dr Cullen makes no apologies for the fact that Budget 2006 offers more of the same: in his words "more of the same fiscal prudence; more of the same steady management of the economy". Of course it is also more of the same refusal to countenance that tax cuts are affordable and beneficial for the economy.

The Minister's approach can be contrasted with that of his Australian counterpart, Federal Treasurer, Peter Costello. He delivered a Federal Budget last week generous to his electorate – personal income tax cuts worth A\$36.7 billion over four years. The tax rate reductions and threshold adjustments will ensure that from 1 July 2006 over 80% of Australians are on a marginal tax rate of 30% or lower.

The New Zealand Budget confirms that the tax take for 2006 is up – the forecast is for just below \$50 billion (in comparison to last year's \$46 billion) with the share of that figure paid by companies constant (compared to last year) at 18%. In the Government's view the increased tax take and a higher than expected operating surplus (forecast at \$8.5 billion) do not provide room for tax cuts. Dr Cullen focuses instead on the need for fiscal prudence and emphasises forecast cash deficits totalling approximately \$7.4 billion over the next four years.

Expenditure increases follow from the Labour Party's pre-election pledges and its post-election confidence and supply agreements with United Future and New Zealand First. The expansion of the Working for Families package (so that 350,000 families are receiving "targeted tax relief"), the pledge to remove interest from student loans for New Zealand residents and the increase in the rate of New Zealand superannuation (agreed with New Zealand First) account for a significant portion of the increases in expenditure. The Government is also increasing police numbers, raising capital spending on transport, particularly roads, and providing some targeted assistance for businesses that export and undertake research and science activities.

Tax rates

In last year's Budget, dubbed the "chewing gum" Budget by some, Dr Cullen announced small increases in the marginal tax rate thresholds that would come into effect in April 2008. Those increases are not confirmed in this year's Budget.

There has been some speculation that the threshold adjustments might not eventuate given the loss of revenue that will result from the decision not to proceed with a carbon tax. More likely is that the personal tax rate thresholds will be considered in the context of the business tax review that Ministers Cullen and Dunne are conducting.

There are some pitfalls in comparing New Zealand's personal marginal tax rates with those of Australia given that each

country has different family assistance programmes, different accident or medical levies (ACC vs Medicare) and that Australia imposes some taxes such as state payroll taxes and stamp duty which New Zealand does not impose. Nevertheless we believe there is some merit in comparing the personal marginal tax rates and thresholds that apply in each country.

The figures in the tables below do not take into account ACC and Medicare levies and the New Zealand Working for Families programme and its Australian equivalent. The Australian data is based on the rates and thresholds that will apply from 1 July 2006 (ie they take into account the changes announced in the Australian Federal Budget last week).

Marginal rates comparison			
New Zealand		Australia	
Income \$	Marginal Rate %	Income \$	Marginal Rate %
0-9,500	15.0	0-6,000	0.0
9,501-38,000	19.5	6,001-25,000	15.0
38,001-60,000	33.0	25,001-75,000	30.0
60,001+	39.0	75,001-150,000	40.0
		150,001+	45.0

Tax payable comparison				
Income \$	Tax payable		Average tax rate	
	NZ	Australia	NZ	Australia
30000	5730	4350	19.1%	14.5%
60000	14670	13350	24.5%	22.3%
80000	22470	19850	28.1%	24.8%
100000	30270	27850	30.3%	27.9%
150000	49770	47850	33.2%	31.9%
200000	69270	70350	34.6%	35.2%

• Excludes ACC, Medicare, family assistance programmes

Tax take

The amount of tax forecast to be collected in 2006 is just under \$50 billion, a 54% increase since 1999 and a \$3 billion increase on the tax collected in 2005.

Tax take 1999-2006					
	1999		2006 forecast		Increase
	\$b	%	\$b	%	%
Corporate	3.69	11.5	9.04	18.2	145.0
Individual	14.94	46.5	23.63	47.6	58.2
GST	8.40	26.0	10.36	20.9	23.3
Other	5.13	16.0	6.58	13.3	28.3
Total	32.16	100.0	49.61	100.0	54.3

Business tax review

The Budget confirms that the Government will undertake a comprehensive business tax review. The review is a result of the Labour-United Future confidence and supply agreement made after last year's election. Officials are preparing a discussion document that will set out a range of possible initiatives for consideration and debate. That document is likely to be released mid-year and any changes that result from the review are expected to be introduced in draft legislation next year and to take effect from 1 April 2008.

Investment and savings

The investment income reforms covered in yesterday's Tax Tips 8/2006 and in Tax Tips 5/2006 and the KiwiSaver work-based savings scheme (refer to Tax Tips 2/2006) are major planks in the Government's tax policy programme.

Other tax initiatives

The Minister's Budget speech makes specific reference to two recent tax initiatives:

- a Government subsidy for the use of payroll agents by employers. The subsidy will be at a flat rate of \$2 per pay period per employee for up to five employees; and
- the alignment of the racing gaming duty with the duty paid by casinos and an acceleration of bloodstock depreciation (part of the Labour-New Zealand First post-election agreement).

Australian Federal Budget

In its Budget last week the Australian Federal Government announced further personal income tax cuts costing A\$36.7 billion over four years (including the reduction in the fringe benefits tax rate to 46.5%) in addition to last year's A\$21.7 billion tax cut package. The Australian Treasurer, Peter Costello, lowered the top two personal income tax rates – from 47% and 42% to 45% and 40% respectively – and increased the thresholds at which the marginal rates apply. The Budget also increased support for lower income families.

Mr Costello also delivered on his long term objective to simplify the tax rules applying to superannuation contributions and benefits. At a cost of A\$6.2 billion over three years from July 2007 the Federal Government is proposing to revolutionise the treatment of superannuation.

Other than improvements to the capital allowance (depreciation) regime and some enhanced capital gains tax concessions for small businesses the Budget included few major tax announcements relevant to the business community.

Tax policy work programme

In addition to the forthcoming business tax review and the investment and savings reforms introduced recently the Government's tax policy work programme includes:

- new tax rebate rules for charities;
- a review of the non resident withholding tax rates in New Zealand's double tax agreements;
- a discussion document on income splitting for families (likely to be in 2008);
- a review of the taxation of partnerships;
- further work on depreciation including depreciation loadings and losses on disposal of buildings;
- work on the tax consequences of International Financial Reporting Standards;
- a review of the rules governing outbound controlled foreign company investments including the foreign dividend withholding payment and conduit tax relief rules;
- a review of the use of imputation credits; and
- completion of the project to rewrite the Income Tax Act.