

The Treasury

Budget 2018 Information Release

Release Document August 2018

<https://treasury.govt.nz/publications/information-release/budget-2018-information-release>

Key to sections of the Official Information Act 1982 under which information has been withheld.

Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

[1]	to prevent prejudice to the security or defence of New Zealand or the international relations of the government	6(a)
[2]	to avoid prejudice the entrusting of information to the Government of New Zealand on a basis of confidence by the Government of any other country or any agency of such a Government	6(b)(i)
[4]	to prevent prejudice to the maintenance of the law, including the prevention, investigation, and detection of offences, and the right to a fair trial	6(c)
[11]	to damage seriously the economy of New Zealand by disclosing prematurely decisions to change or continue government economic or financial policies relating to the entering into of overseas trade agreements.	6(e)(vi)
[23]	to protect the privacy of natural persons, including deceased people	9(2)(a)
[25]	to protect the commercial position of the person who supplied the information or who is the subject of the information	9(2)(b)(ii)
[26]	to prevent prejudice to the supply of similar information, or information from the same source, and it is in the public interest that such information should continue to be supplied	9(2)(ba)(i)
[27]	to protect information which is subject to an obligation of confidence or which any person has been or could be compelled to provide under the authority of any enactment, where the making available of the information - would be likely otherwise to damage the public interest	9(2)(ba)(ii)
[29]	to avoid prejudice to the substantial economic interests of New Zealand	9(2)(d)
[31]	to maintain the current constitutional conventions protecting collective and individual ministerial responsibility	9(2)(f)(ii)
[33]	to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials	9(2)(f)(iv)
[34]	to maintain the effective conduct of public affairs through the free and frank expression of opinions	9(2)(g)(i)
[36]	to maintain legal professional privilege	9(2)(h)
[37]	to enable the Crown to carry out commercial activities without disadvantages or prejudice	9(2)(i)
[38]	to enable the Crown to negotiate without disadvantage or prejudice	9(2)(j)
[39]	to prevent the disclosure of official information for improper gain or improper advantage	9(2)(k)
[40]	not in scope	
[41]	that the making available of the information requested would be contrary to the provisions of a specified enactment	18(c)(i)
[42]	information is already publicly available or will be publicly available soon	18(d)

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) and section 18 of the Official Information Act.



BRIEFING

R&D tax credit: Cabinet Paper on Timing

Date:	29 January 2018	Priority:	Medium
Security classification:	In Confidence	Tracking number:	1862 17-18 T2018/157 IR2018/024

Action sought		
	Action sought	Deadline
Hon Grant Robertson Minister of Finance	Sign and lodge the attached Cabinet paper for consideration at Cabinet Economic Development Committee on 14 February	8 February 2018
Hon Dr Megan Woods Minister of Research, Science and Innovation	Sign the attached Cabinet paper for consideration at Cabinet Economic Development Committee on 14 February	8 February 2018
Hon Stuart Nash Minister of Revenue	Sign the attached Cabinet paper for consideration at Cabinet Economic Development Committee on 14 February	8 February 2018

Contact for telephone discussion (if required)				
Name	Position	Telephone		1st contact
Richard Walley	Manager, Innovation Policy	[39]	[23]	✓
Keith Taylor	Policy Manager, Inland Revenue	[39]	[23]	
Matthew Gilbert	Manager, Business Growth and Innovation, The Treasury	[39]	[23]	

The following departments/agencies have been consulted
Callaghan Innovation

Minister's office to complete:

- | | |
|---|--|
| <input type="checkbox"/> Approved | <input type="checkbox"/> Declined |
| <input type="checkbox"/> Noted | <input type="checkbox"/> Needs change |
| <input type="checkbox"/> Seen | <input type="checkbox"/> Overtaken by Events |
| <input type="checkbox"/> See Minister's Notes | <input type="checkbox"/> Withdrawn |

Comment



BRIEFING

R&D tax credit: Cabinet Paper on Timing

Date:	29 January 2018	Priority:	Medium
Security classification:	In Confidence	Tracking number:	1862 17-18 T2018/157 IR2018/024

Purpose

To provide you with a Cabinet paper to seek Cabinet approval to introduce an R&D tax credit in April 2019.



Recommended action

The Ministry of Business, Innovation and Employment, Treasury and Inland Revenue recommend that you:

	Min. Finance	Min. RSI	Min. Revenue
a Agree to lodge the attached Cabinet paper on 8 February, for consideration at Cabinet Economic Development Committee on 14 February	<i>Agree/ Disagree</i>	<i>Agree/ Disagree</i>	<i>Agree/ Disagree</i>

Matthew Gilbert
Manager, Business Growth and Innovation
The Treasury

29 / 01 / 18

Hon Grant Robertson
Minister of Finance

..... / /

Richard Walley
Manager, Innovation policy
Labour, Science and Enterprise, MBIE

29 / 01 / 18

Hon Dr Megan Woods
Minister of Research, Science and Innovation

..... / /

Keith Taylor
Policy Manager
Inland Revenue

29 / 01 / 18

Hon Stuart Nash
Minister of Revenue

..... / /

Background

1. The Ministers of Finance, Research Science & Innovation, and Revenue, met on 20 December 2017 to discuss the introduction of an R&D tax credit.
2. Your conversation mainly focused on the timing of introduction. In subsequent discussions, you have decided to introduce the tax credit in April 2019.
3. At the December meeting, you asked officials to prepare a Cabinet paper on the timing of the credit, to enable you to consult Cabinet colleagues, coalition partners, and confidence and supply partners.
4. We have drafted a paper for your consideration, which is attached at annex one.

Next Steps

5. We recommend that you sign and lodge the attached paper by 8 February 2018, for consideration at Cabinet Economic Development Committee on 14 February 2018.
6. In the mean time, officials are continuing to progress work on the tax credit. We plan to provide a briefing on key policy decisions in early February. This will in turn inform the content of a public discussion document, which we hope to release in March, following Cabinet consideration.

Annexes

Annex One: Cabinet Paper, 'Timing of an R&D Tax Credit'

Annex One: Cabinet Paper, 'Timing of an R&D Tax Credit'

Office of the Minister of Finance

Office of the Minister of Research, Science and Innovation

Office of the Minister of Revenue

Chair, Cabinet Business Committee

Timing of an R&D Tax Credit

Proposal

- 1 This paper asks Cabinet to approve the timing of the introduction of a Research and Development (R&D) Tax Credit.

Executive Summary

- 2 Building a diverse, sustainable, productive economy is at the heart of what this Government wants to achieve. This will require more innovation, which is driven by R&D, in particular R&D done by business. The current system of government support for business R&D is through grants, advice, training, support in kind, and some smaller research-focused grants. As a major addition to our current system, we have committed to introducing an R&D tax credit.
- 3 Tax credits have strengths and weaknesses. Therefore, the design of a tax credit must proceed with care, and with awareness of the possibility of unintended consequences,
[34]
- 4 We propose to introduce an R&D tax credit from April 2019.
- 5 This is an ambitious timeframe. It leaves us with no space for unexpected delays, and provides limited time for design, consultation, and for businesses to prepare. It therefore carries some risks. In particular, clear and comprehensive transition planning will be important for firms who currently receive grants that will be replaced by the credit. We want to ensure we do not discourage those firms from performing R&D in the short term, and delay progress towards our 2% goal.
- 6 We therefore recommend Cabinet direct the Ministry of Business, Innovation and Employment (MBIE), Inland Revenue (IR) and Callaghan Innovation to begin planning transitional arrangements immediately, as a key part of the design work.

Background

- 7 Building a diverse, sustainable, productive economy is at the heart of what this Government wants to achieve. This will require innovation which is driven by R&D. This is why we have announced a target of increasing R&D expenditure to 2% of GDP by 2027 – a significant increase from our current 1.27%, but still low by international standards (OECD average is 2.6%).

- 8 The majority of this growth will need to come from increased business R&D. To achieve this target we have agreed to provide increased support for business R&D, alongside direct government investment.
- 9 Without government support, businesses will tend to invest less in R&D than is optimal for the country as a whole, as they are unable to capture the full benefits of their investment. The gains from R&D tend to be broadly distributed through, for example, worker mobility, reverse engineering, or product imitation. Our support for business R&D is primarily for the purposes of compensating for those benefits that do not accrue to the firm.
- 10 The current system of government support for business R&D is through grants (non-discretionary Growth Grants which focus on larger R&D performing firms, and smaller Project and Student Grants), advice, training and support in kind, and some smaller research-focused grants. Much of this support is provided through Callaghan Innovation, with some sector-specific elements provided through Crown Research Institutes and the new Regional Research Institutes. There is also a small R&D tax loss cash out available.
- 11 The current outline of business R&D support, and how it fits within the Government's wider economic strategy is set out in Annex A.
- 12 A coordinated package of supports will be critical to raising business R&D. As a major addition to our current system, we have committed to introducing an R&D tax credit. Tax credits offer certainty to businesses, and enable them to plan their investments according to a clearly stated set of rules. ^[34]
- 13 The design of a tax credit must proceed with care, and with awareness of the possibility of unintended consequences, ^[34] The size of this risk could be significant. This risk will never be completely eliminated, as firm growth and behaviour, with regards R&D, is inherently unpredictable.

Comment

- 14 We propose to introduce an R&D tax credit from April 2019. The design of the credit can largely follow the R&D tax credit that was available to New Zealand businesses for the 2008-2009 income year. However, we will want to modify the scheme to reflect changes in international best practice and experiences in other countries. Also, the limited experience from 2008-09 suggested some claims did not represent good value for taxpayer money and we will want to change the scheme to address these issues.
- 15 An April 2019 date is the earliest we could feasibly introduce a tax credit, and is an ambitious timeframe. It will implement a key commitment from our Fiscal Plan, and make a timely start towards our goal to increase R&D expenditure to 2% of GDP. 2027 is a challenging deadline, and we will need to get started early to maximise our chances of getting there. It will also provide confidence for businesses in the longevity and sustainability of the credit. R&D tax credits work because they provide certainty. An early implementation date will give businesses greater confidence to invest in R&D.
- 16 The timeline for April introduction is broadly public consultation in March 2018 on high-level policy design options such as the definition of R&D, with introduction of legislation into the house mid-2018. This means constrained, but achievable, time frames for design

decisions such as the rate, drafting legislation and operational changes necessary to introduce the credit.

- 17 The R&D Growth Grants administered by Callaghan Innovation have a similar function to that of a tax credit, and will likely be replaced by the credit when it is introduced. Ensuring a smooth transition from the existing Growth Grants system to the new tax credit will be essential to provide continuity of support to businesses, and continue to encourage firms to increase their R&D.
- 18 There are likely to be between 250-300 businesses in receipt of Growth Grants at 1 April 2019. Recipients will be at different stages through their first 3-year contract or further 2-year extension. Transitioning from Growth Grants to a tax credit will require businesses to plan and implement some system changes, and potentially adapt to a different payment schedule. In addition, approximately 42% of current Grant recipients are loss making companies, and there may be recipients who cannot benefit fully from the tax credit in the short term because they have low or no profits.

Risks

- 19 There are some risks to an April implementation date, which we will need to monitor carefully and mitigate where possible. These are:
 - 19.1 It is a 'minimum viable' option. There is no space for delay in any element of the process leading to introduction. This will also require decisions on a range of interrelated design choices in a short timeframe.
 - 19.2 It provides limited time for policy and implementation design, impact analysis, and policy decisions. ^[34]
 - 19.3 ^[34]
- 20 In terms of mitigation, early provision of information, and clear, comprehensive transition planning will be important for firms currently in receipt of Growth Grants. In particular, this will be necessary to ensure we do not discourage those firms from performing R&D in the short term, and delay progress towards our 2% goal. In designing the transition, we will need to provide the certainty of funding essential for businesses to have the confidence to invest in R&D, and allow time for business to plan how they transition to the new tax credit and R&D support system.
- 21 We therefore recommend Cabinet direct MBIE, IRD and Callaghan Innovation to begin planning transitional arrangements immediately, as a key part of the design work.

Consultation

- 22 The Department of the Prime Minister and Cabinet and Callaghan Innovation have been consulted on this report.

- 23 Limited initial business consultation indicates a reasonable level of stakeholder comfort with an April 2019 introduction, and informal consultation will be ongoing throughout the design and implementation process. Officials have met with a partner of an accountancy firm that represented many applicants in 2008-09. Her view was that a 2019 start was preferable because of the uncertainty created by the scheme previously starting then being disbanded.

Financial Implications

- 24 No decisions with fiscal implications are being sought through this paper. However, the introduction of an R&D Tax Credit carries both fiscal cost and risk.
- 25 Without design details, the financial implications of introducing a tax credit are unclear. The financial cost and risk of a tax credit will vary significantly depending on the design of the credit specifically the rate, cap and any exclusions.
- 26 Labour's fiscal plan sets out an allowance for introduction of an R&D tax credit in 2019, with \$100m allocated in the 18/19 fiscal year, rising to \$300m in 2021/22. In total, this allows \$850m over the forecast period.
- 27 From 2018/19 to 2021/22 the Growth Grant MYA has \$664m appropriated. [33]

Human Rights

- 28 There are no human rights implications arising from the proposals in this paper.

Legislative Implications

- 29 Depending on the decision arising from this paper, we may seek to introduce legislation into the house in 2018. We will bring any proposed legislation to Cabinet for approval prior to introduction.

Regulatory Impact Analysis

- 30 Regulatory impact analysis is currently underway for the policy noted in this paper. This analysis will be presented to Cabinet at appropriate stages of the legislative process.

Gender Implications

- 31 There are no gender implications arising from the proposals in this paper.

Disability Perspective

- 32 There are no specific disability considerations arising from the proposals in this paper.

Publicity

- 33 We may wish to make an announcement about the timing of the tax credit following the decision in this paper. We recommend that Cabinet delegates further decisions on announcements on timing of the tax credit to the Minister of Research, Science and Innovation, in consultation with the Minister of Finance and the Minister of Revenue.

Recommendations

- 34 We recommend that Cabinet:
- 34.1 **Note** that building a diverse, sustainable, productive economy will require more innovation, which is driven by R&D.
 - 34.2 **Note** that we have announced a target of increasing R&D expenditure to 2% of GDP by 2027.
 - 34.3 **Note** that the current system of government support for business R&D is through grants (larger non-discretionary Growth Grants, and smaller Project and Student Grants), advice, training and support in kind, and some smaller research-focused grants.
 - 34.4 **Note** that we have committed to introducing an R&D tax credit as a major addition to our current system.
 - 34.5 **Note** the Fiscal Plan allocates \$850m from 2018/19 to 2021/22 to an R&D Tax Credit.
 - 34.6 ^[34]
 - 34.7 **Agree** to implement the tax credit in April 2019.
 - 34.8 **Note** that this is the earliest date we can implement a tax credit, and that it will make a timely start to towards our 2% goal, and provide increased confidence for businesses in the longevity and sustainability of the credit.
 - 34.9 ^[34]
 - 34.10 **Note** that clear, comprehensive transition planning from the existing Growth Grant system to the tax credit will be an important mitigation for these risks, and can help ensure firms are not discouraged from performing R&D during the transition.
 - 34.11 **Direct** MBIE, IR and Callaghan Innovation to begin planning transitional arrangements immediately, as a key part of the design work.
 - 34.12 **Agree** to delegate decisions on announcements on timing of the tax credit to the Minister of Research, Science and Innovation, in consultation with the Minister of Finance and the Minister of Revenue.

Authorised for lodgement

Hon Grant Robertson
Minister of Finance

Hon Megan Woods
Minister of Research, Science and Innovation

Hon Stuart Nash
Minister of Revenue

Annex A

Introducing a Research and Development (R&D) Tax Credit

This is the Government's vision as part of its economic and well-being strategy.

R&D is a key input into the innovation needed to provide competitive advantage and increased productivity

The Government measures this growth through expenditure on R&D across the economy. The coalition agreement outlines a target of 2% of GDP in 10 years.

Private R&D can be increased by encouraging; development or migration of new firms that perform R&D; existing firms to perform R&D; and firms that currently perform R&D to perform more R&D.

Public R&D can also be facilitated through these means. However, with Public R&D, the Government has the added lever of ownership and control over what research is done.

The Government provides financial support to businesses performing R&D to account for positive externalities.

An R&D Tax Credit sits within a range of other financial incentives

