MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

# COVERSHEET

| **Minister** | Hon Grant Robertson | **Portfolio** | Finance |
|---|---|---|---|
| **Title of Cabinet paper** | New Zealand Income Insurance: decisions on outstanding policy questions | **Date to be published** | 28 April 2023 |

| **List of documents that have been proactively released** | | |
|---|---|---|
| **Date** | **Title** | **Author** |
| November 2022 | New Zealand Income Insurance: decisions on outstanding policy questions | Office of the Minister of Finance |
| 7 November 2022 | New Zealand Income Insurance: Decisions on Outstanding Policy Questions<br>CAB-22-MIN-0484 Minute | Cabinet Office |

**Information redacted** **YES / NO** *[select one]*

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**In confidence**

Office of the Minister of Finance

Office of the Minister for Social Development and Employment

Office of the Minister for ACC

Office of the Minister for Workplace Relations and Safety

Cabinet Business Committee

# New Zealand Income Insurance: decisions on outstanding policy questions

## Proposal

1 This paper seeks Cabinet Business Committee's (CBC) agreement to policy proposals for key outstanding decisions on the New Zealand Income Insurance (NZII) design.

## Relation to government priorities

2 NZII arose out of the Government's work with its Future of Work Tripartite Forum partners[1], and our commitment to a more productive, sustainable, and inclusive economy. Our proposals for a NZII Scheme support the Government's goals for:

2.1 working New Zealanders and their families to be better prepared for the unpredictable economic and health shocks that can reduce their ability to earn through no fault of their own

2.2 working people to be confident of their place in the future of work and open to taking jobs in dynamic but potentially risky sectors

2.3 addressing the current inequity, where a person who experiences an accident can receive much more support than a person with a non-accident-related health condition or disability despite a similar loss of ability to work, and

2.4 improving skill matching and employer's access to skilled workers.

## Executive Summary

3 On 4 July 2022, Cabinet agreed to proceed with NZII and made decisions on the detailed design of the Scheme. Cabinet invited Ministers with delegated authority to report back on a set of outstanding policy questions by October 2022. **Annex A** presents the final proposed design of the Scheme.

1 Business New Zealand and the New Zealand Council of Trade Unions.

4 Decisions on key outstanding policy questions are necessary prior to an announcement of the Government's intention to introduce NZII. The key outstanding questions, and our recommendations, are as follows:

4.1 *The income replacement rate and levy structure.* We propose retaining an income replacement rate of 80 percent and a flat rate levy structure, to be shared equally between employers and employees.

4.2 *Coverage of self-employment*. We propose to exclude self-employed workers from the Scheme to focus on establishing the main Scheme for employees, but to signal our intention to cover some groups of self-employed in the future.

4.3 *Bridging payments: eligibility, and interaction between bridging and contractual redundancy payments.* We are proposing that the bridging payment (and notice period) should be applicable to all workers (as agreed by Cabinet in July 2022) and employers can satisfy the bridging payment requirement by paying contracted redundancy compensation that meets or exceeds the bridging requirement.

5 We propose adopting an indicative levy rate of 2.0 percent (of salary and wages) when announcing the Scheme, lower than the 2.77 percent indicated in previous consultation. We consider that an indicative rate of 2.0 would strike an appropriate balance of risk between the Crown, workers, and businesses.

6 We propose to continue modelling work and undertake a public consultation on a proposed levy following passage of the legislation and ahead of the Scheme going live.

7 There are several further areas where policy work is progressing. These includes Te Tiriti o Waitangi/Treaty of Waitangi provision(s) and second-order policy covering NZII's role in responding to economic crises, application to non-standard work, use of offences, penalties and enforcement, and information sharing. We will update Cabinet on decisions on these issues in December 2022 when we seek approval to introduce the Bill to the House.

8 The expected launch date for the Scheme is 1 April 2025. This aligns to the tax year and provides sufficient time for a quality build and implementation, designed in partnership with Māori.

## Background

9 On 4 July 2022, Cabinet agreed to introduce NZII and made decisions on the detailed design of the Scheme [CAB-22-MIN-0250.02 refers], including coverage, entitlements, claimant and employer obligations, funding and delivery, dispute resolution, and governance. Work is now underway to produce a NZII Bill that reflects these policy decisions.

10 Cabinet invited the Ministers of Finance, Social Development and Employment, ACC, Revenue, and Workplace Relations and Safety to report

back to the Cabinet Economic Development Committee by October 2022 on outstanding policy questions relating to:

10.0 further options for reducing the impact of the NZII levy on low-income workers

10.1 further coverage choices for self-employed workers

10.2 NZII's role in responding to economic crises

10.3 further advice on enforcement, offences, and penalties

10.4 arrangements for obtaining and sharing personal information required to administer NZII, and

10.5 coverage for non-standard workers (fixed-term, seasonal, and casual).

11 Cabinet also agreed to do further work on whether the bridging payment is in addition to any contractual entitlement to redundancy compensation [CAB-22-MIN-0250.02 paragraph 35 refers].

12 Cabinet authorised Ministers to make additional policy decisions, minor and technical changes, and related matters of detail to the policy decisions agreed by Cabinet, consistent with the general policy intent, on issues that arise in drafting the Bill and its passage through the House, in consultation with relevant Ministers as appropriate [CAB-22-MIN-0250.02 paragraph 84 refers].

13 The Government has run a tripartite process with Business New Zealand and the New Zealand Council of Trade Unions to develop proposals for the outstanding policy questions covered in this paper.

14 The Government also committed to a close partnership between the Crown and the National Iwi Chairs Forum in designing and delivering NZII. Officials have met regularly with the Pou Tangata Skills and Employment Iwi Leaders Group (the SE ILG).[2]

## Setting an updated indicative levy rate, based on new modelling

*We consulted on a levy rate at the upper end of the range, to reflect the modelling uncertainty and ensure New Zealanders understood the potential for a higher levy*

15 Consultation on the Scheme earlier in the year set out an indicative levy rate of 2.77 percent of salary and wages up to the maximum income cap, split equally between employers and workers at 1.39 percent each.[3]

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2 In-depth workshops were held with the SE ILG representatives on 7 and 8 September and 13 October, on the outstanding policy questions covered in this paper and the implications for Māori, including levy relief, the inclusion of self-employed workers, information sharing, and Te Tiriti o Waitangi/Treaty of Waitangi provision.

3 Original modelling estimated 112,300 people with prior annual earnings averaging $49,488 will claim NZII for an average duration of 4.9 months per year due to economic displacement, and 135,300 people with prior annual earnings averaging $57,072 will claim NZII for an average duration of 2.7 months per year due to a health condition or disability.

16 The modelling that underpinned this indicative levy rate was based on one of several potential scenarios developed by officials alongside Business New Zealand and the New Zealand Council of Trade Unions. Each scenario was based on a different set of assumptions about:

16.1 **Policy parameters for the Scheme**, which the government can control through the design process. These include the scope of leviable income, eligibility requirements such as the residency rule and the contribution period required to claim, the replacement rate and maximum claim duration, and Scheme administration costs.

16.2 **Expected behavioural response to the Scheme**, which is less controllable, but can have a significant impact on Scheme costs. This includes applicant numbers, along with the average length and value of claims, which are fundamentally uncertain at the outset and will require flexibility to adapt to actual experience over time.

17 The rate adopted for consultation was at the upper midpoint of the modelled options developed by the tripartite working group. This reflected, among other things, the level of uncertainty around the detailed policy design of the NZII and the accuracy of the assumptions used for all the modelling options. Officials are continuing to work on improving the modelling.

18 The economic environment and labour market context will continue to change ahead of the implementation of the NZII. The initial levy rate for the NZII is highly likely to differ from the figure used for consultation, even if the underlying methodology used to set it is the same. We included a levy rate in the discussion paper towards the upper end of the range, and clearly communicated the uncertainty involved in levy setting, to ensure New Zealanders understood the potential for a higher levy rate and fed back on the proposal accordingly.

*We will need to communicate an updated indicative initial levy rate alongside final decisions on the detailed design of the Scheme*

19 The indicative levy rate used for consultation was set at that time for that particular purpose, as discussed above. Officials have continued to work on the range of modelled levy rate options to make adjustments that reflect where policy settings have settled since consultation. This has resulted in upward adjustments to the indicative rate previously consulted on, and the ongoing refinement of the modelling will continue to change the required levy rates under different demand assumptions.

20 We will therefore need to communicate an updated indicative initial levy rate to New Zealanders when we announce final decisions on the detailed design of the Scheme. This rate should strike a balance between mitigating the financial impact of the levy on New Zealand workers and businesses, and the risks associated with underfunding the Scheme. Communicating the initial rate allows workers and businesses to plan as best as possible for the actual cost impost of the Scheme.

*We can set an indicative initial levy rate within the range of 1.7 to 3.0 percent, but lower rate options come with more risk for Scheme funding*

21 Given the uncertainty over how much demand will emerge over time, it is not possible to precisely estimate the actual cost of the Scheme when it is introduced and therefore the levy required to meet costs. However, officials' advice is that there is a range of feasible levy rate options for Ministers to choose from, based on risk preference. The rate set out in the discussion document (which has been adjusted to 3.0 percent) is at the higher end of the range. A rate as low as 1.7 percent could be set to reflect a desire for the government to take on more risk at the outset and adjust levies as experience beds in.[4]

22 The level of behavioural response the Scheme will generate is highly uncertain. However, officials' advice is that it will gradually increase and become clearer over time as people respond to the change in policy. We can change the levy rate over time as these impacts become apparent. This allows us to take a starting position for levies that reflects trade-offs between short-term and long-term costs for the Crown and levy payers.

23 Adopting a lower initial levy would minimise the initial financial impact of the introduction of the Scheme on businesses and workers. Public consultation showed the amount of the levy is a concern for New Zealanders, in particular those on lower incomes, and on balance it is our view that there is not a good levy relief option to address this. Given the Crown has greater financing flexibility than individuals as the Scheme is introduced, it may be better placed to carry the risk associated with any initial financial impact.

24 There is also scope to phase in the levy over time, although this would come with many of the risks associated with setting the initial levy at the lower end of this range (depending on the shape of the phase-in path relative to actual demand on the Scheme).

25 Taking this approach to levy setting comes with a risk that the levy is set too low and would need to adjust to repay any under-funding over time. This may involve greater overall cost to levy payers due to financing costs. To correct for any under-collection, we anticipate there would be a period where future levies are set higher than costs, which would raise concerns about intergenerational inequity. It would be important to carefully monitor claims cost to avoid financial liabilities accumulating rapidly if claims are much higher than anticipated.

26 Any shortfalls may require a claim against the Crown's current liquidity holdings ($15 billion). However, there is the ability to accommodate short periods of under-funding. The Cabinet agreed funding policy will allow the Crown flexibility to reset levies in line with actual claims experience within 2

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4 For example, officials have advised that a levy rate of 1.7 percent could be feasible based on revised modelling assumptions of 90,500 people with prior annual earnings averaging $46,956 claiming NZII for an average duration of 4.2 months per year due to economic displacement, and 103,400 people with prior annual earnings averaging $33,370 claiming NZII for an average duration of 2.8 months per year due to a health condition or disability.

years if it quickly becomes apparent that levies are either significantly low or high to limit any operational impacts on liquidity holdings.

27 Adopting a higher levy rate at the outset runs a higher risk of unnecessarily burdening individuals in the short term but could be more efficient for levy payers over time and would position the Scheme to be more resilient to economic shocks. A higher levy is more likely to enable the Scheme to embed a small surplus position for long-term Scheme financial efficiency, as financing charges are more expensive than investment returns for a short-tail Scheme.

*There are ways to mitigate any mismatch between levy revenue and the true cost of claims*

28 Once the Scheme is introduced it is most likely that experience will differ from assumptions, and the Scheme will require levy adjustments to be made. The updated indicative initial levy rate should also reflect the choices Government will have as to how to correct for any deviations and return the Scheme to a sustainable funding track.

28.1 In a situation where there is a substantial **deficit**, Government it will have choices as to the timing and spread of levy adjustments, and it could consider in exceptional circumstances grants to enable the Scheme to adopt a sustainable levy track without the need to additionally make up any initial underfunding.

28.2 In a situation where there is a substantial **surplus**, the Government will again have choices as to the timing and spread of levy adjustments and could choose to provide a one-off levy reduction.

29 **Annex B** outlines scenarios where experience differs from expectations at different levy rates from the lower to the upper limit of the preferred range:

29.1 1.7 percent aligns with the lower feasible initial levy rate set out in the modelling methodology. This initial rate would minimise the financial impact of the Scheme on workers and businesses but carries the highest tolerable risk for Scheme funding.

29.2 3.0 percent aligns with the upper feasible initial levy rate set out in the modelling methodology. This initial rate would increase the financial impact of the introduction of the Scheme on workers and businesses from the levy rate we consulted on but lowers the risk that the Crown may need to underwrite the unfunded cost of the Scheme.

30 To illustrate the choices within this range, the table also sets out some illustrative mid-points:

30.1 2.0 percent, which would significantly reduce the cost impost of the Scheme on workers and businesses from the levy we consulted on but still comes with a high level of risk for the Crown and levy-payers.

30.2 2.5 percent, which would reduce the financial impact of the introduction of the Scheme on levy payers and increase the risk to the Crown and levy-payers to some extent, relative to the levy we consulted on.

31 The modelling shows that small levy differences, of up to 0.5 percentage points, could tolerably be managed with relatively small adjustments within the first ten years. However, if the difference in experience from expectations are in the order of over 1.0 percentage points, large funding shortfalls could accumulate quickly, and the Scheme could deviate from a sustainable funding track in a way that makes a return more challenging.

32 For instance, a modelled scenario where a 1.7 percent levy is adopted, whereas experience would have required a 2.7 percent levy (an additional 1.0 percentage point), the Scheme's funding requirement could face a shortfall of $6 billion despite sustained levy increases. At the other end of the spectrum, a modelled scenario where a 3.0 percent levy is adopted, whereas experience would have required a 2.0 percent levy (a 1.0 percentage point difference), the Scheme would accumulate a surplus of $5.5 billion.

33 **Annex B** further outlines responses that the Government could adopt to the various scenarios, which include mixes of levy increases and decreases over varying time horizons. It also highlights how varying levels of funding grants could influence the levy track under various scenarios.

*We recommend that CBC adopt an indicative initial levy rate of 2.0 and undertake public consultation on a proposed levy rate following passage of the legislation*

34 In the light of the above, we are proposing that CBC adopt an indicative levy rate of 2.0 percent to communicate to New Zealanders alongside decisions on the final design of the Scheme. We consider that this strikes an appropriate balance of interest between the Crown, workers, and businesses.

35 Subject to the change in timeframe for the Scheme going live from what was consulted on (from December 2023 to 1 April 2025), we propose to continue to advance the modelling work to improve understanding of the relative risks and undertake a public consultation on a proposed levy following passage of the legislation.

36 This would enable modelling to take full account of the most up to date data, the final Scheme design, and appropriately weigh the risks for the Crown and levy payers of over or underfunding the Scheme at the outset. A consultation process on the initial levy rate would:

36.1 convey transparency and contribute to public confidence in the Scheme

36.2 enable the government to canvas the modelling and trade-offs involved with a preferred levy rate, and the mitigations that are available if the actual costs are substantially higher or lower than the revenue generated by the levy, and

36.3 be a key mitigation for managing uncertainty and public expectations concerning the funding requirement for the scheme.

## Setting the levy structure

*Cabinet noted our intention in July 2022 to do further work to explore options for levy relief for lower-income earners*

37 In July 2022, Cabinet agreed that income insurance will provide a replacement rate of 80 percent of prior income up to an indexed maximum cap which aligns with ACC's maximum cap, currently $136,544 per annum.

38 In our advice to Cabinet in July 2022, we noted that we intended to do further work on whether changes to the scheme's replacement rate could help fund a reduction in the levy rates or offset the cost of a progressive levy rate.

39 We indicated that a change to the proposed replacement rate and flat-rate levy structure would be preferred if an option could be identified that:

39.1 meets the scheme objectives, including a sufficiently high level of income smoothing,

39.2 provides effective levy relief to low-income workers who would struggle to meet the cost of the levy,

39.3 does not require Crown funding, and

39.4 is operationally feasible.

*We do not recommend funding levy relief for lower-income earners by reducing the Scheme's replacement rate below 80 percent*

40 Any replacement rate balances providing claimants with adequate income support while they search or train for a good job and reducing moral hazard risk by incentivising a return to work to restore their full prior income.

41 We have considered a range of options for providing levy relief for low-income workers. Key options for funding a reduction in the levy rates included:

41.1 a reduced replacement rate to 70 percent, or

41.2 a stepped-down replacement rate based on Scheme duration (claimants receive an 80 percent replacement rate for three months and a 60 percent replacement rate for the remaining three months).

42 Modelling undertaken by the Treasury indicates that reducing the replacement rate to 70 percent would generate reasonably large savings, indicating an increased pressure for claimants to return to work.

43 It is important to note that the potential savings from a reduction in the replacement rate, and hence the funding available for levy relief, are highly dependent on how people respond to a lower replacement rate. These behavioural changes are challenging to estimate.

44 The Scheme is intended to shift behaviours in the economy and allow workers an opportunity to engage in considered job search. The reduction in

replacement rates could significantly impact the scheme's ability to support people back into good work and reduce wage scarring. Behavioural impacts of this size indicate that people would feel greater pressure to return to a job, rather than undertaking a considered job search for a good job.

45 Further, we expect lower-income workers would be more impacted by the reduced replacement rate, as they are more likely to benefit from the additional financial support to return to a good job.

46 Reducing the replacement rate will have flow-on impacts for the welfare system. As income insurance decreases, welfare may increase for eligible people to offset this (depending on a person's circumstances). Reducing the replacement rate will therefore mean low-income families receive relatively less gain from the introduction of NZII.

47 We propose retaining the 80 precent replacement rate as this balance best supports the Scheme's goal to support people back into good work and reduce wage scarring.

*We considered alternative settings, including whether a levy-free threshold could be introduced through higher employee levy rates above that threshold*

48 There are a range of options to introduce greater progressivity to the levy, and we consider a levy-free threshold to be the best option for doing so.[5]

49 Our proposed initial levy rate of 2.0 percent would lead to an employee levy of 1.0 percent. If we introduced a levy-free threshold of $14,000, the employee levy rate above that threshold would increase to 1.34 percent to offset the reduced revenue, using 2018/19 data. **Annex C** includes options for levy-free thresholds on each of the indicative employee levy rates discussed in the previous section.

50 Compared to a flat rate 1.0 percent employee levy, introducing a $14,000 levy-free threshold would mean workers earning below $55,000 per year would pay lower levies, and those earning above $55,000 would pay more.

51 Providing relief through the levy is not always well targeted:

51.1 There are many low-income earners in high-income families (e.g., teenagers working part-time and living with high-income parents), and vice versa (e.g., higher-income sole breadwinners in large families). Levy relief would therefore go to high income families in some cases and may miss some low-income families.

51.2 A levy free threshold would mean some workers receive the Scheme's entitlements without paying a levy (e.g. part-time workers).

5 We also considered a lower levy rate under $48,000, rather than a levy-free zone, and structures with multiple rates and thresholds. However, the lower-levy rate does not address the concerns around casual workers, and multi-threshold options add considerable administrative complexity.

51.3 A higher levy rate on income above the threshold would mean larger families would pay a higher levy, despite being eligible for welfare (e.g. working for families).

52 Progressive levies increase compliance and administrative burdens on employers, agencies, workers, and Scheme administrators. Employers do not collect data on whether their employee has multiple jobs and real-time tracking of individual incomes is not practical, therefore it is likely that individuals with multiple jobs or inconsistent income will pay an incorrect levy during the year.

53 Aligning the threshold with income tax thresholds (with the lowest threshold currently being $14,000) creates significant administrative efficiencies compared to creating new thresholds, particularly for those paying secondary tax, who would be less likely to be over or under levied.

54 Alternatively, we could maintain the 1.39 percent headline levy (which aligns with the employee portion of the 2.77 levy rate that was consulted on) and fund a levy-free threshold that is not aligned with the income tax thresholds. maintaining the 1.39 percent headline employee levy would fund a levy-free threshold of just over $15,000, based on 2018/19 data.

55 This would allow a higher levy-free threshold but be more administratively burdensome and increase compliance costs for employees, employers, and payroll providers.

56 It is important to note that a levy-free threshold will have different long-term implications than a flat rate levy. For a flat-rate levy, wage growth affects both the cost of the Scheme and the levy base, meaning the estimated levy rate would remain broadly the same even as wages grow. A levy-free threshold will raise more revenue over time, as wage growth pushes more income into the higher-levy threshold (often referred to as 'fiscal drag'). To illustrate this, maintaining the 1.39 percent headline employee levy and using the expected 2023/24 data (which incorporates forecasted wage growth), a threshold of $19,000 could be funded.

57 The key decisions for CBC are therefore whether to introduce a flat rate or progressive levy, and if the latter is preferred, whether to align with existing income tax thresholds.

*On balance, we recommend confirming Cabinet's decision on a flat-rate levy*

58 Undertaking further work on options for levy progressivity was grounded in our desire to mitigate the impact of the levy on lower-income earners and ensure they are benefitting proportionately from their input into the Scheme.

59 We consider the decision on a flat-rate or progressive levy (e.g. through a levy-free threshold) to be finely balanced but recommend retaining the flat-rate levy. Overall, the proposed NZII Scheme (with an 80 percent replacement rate and flat-rate levy) is expected to progressive and redistribute income to lower-income families.

60 Using the indicative 2.77 percent levy in the discussion document, the Treasury's modelling indicates that the Scheme is expected to redistribute income from high-income to low-income families. Workers in low-income families are likely to have more triggering events (displacement and health conditions and disabilities) and will access the Scheme more often than workers from higher-income families. This means people on low incomes will benefit disproportionately from NZII.

61 If the levy were reduced, we would expect the scheme would still be redistributive. However, as the revenue raised by the scheme would be lower, there would be less income to redistribute.

62 Further, a progressive levy increases administrative burden for employers, workers, and Scheme administrators. A flat-rate levy will reduce compliance and administrative costs.

63 We are therefore not proposing a change to the earlier Cabinet decision in July 2022 on a flat-rate levy structure for the Scheme.

## Coverage of self-employed workers

64 The inclusion of self-employed workers in NZII has been the subject of significant consideration throughout the Scheme's development.

65 International experience shows that self-employed workers are amongst the most challenging to include effectively in income insurance schemes. Overseas schemes take different approaches, but no comparable scheme has full, compulsory cover for the self-employed, which reflects the difficulty of covering this group of workers.

65.1 Some countries (e.g. Canada), cover self-employed for health events but not for economic displacement. Other countries, allow self-employed to opt-in to a scheme, but they then face difficult conditions for triggering cover and/or tough stand-down rules.

65.2 COVID-19 has resulted in some countries bringing the self-employed into aspects of their schemes, but this has largely been done on a high-trust basis, with mixed results.

66 A central tension is that excluding self-employed workers from coverage may incentivise the reclassification of work arrangements to avoid paying levies. Conversely, including self-employed workers – especially for displacement – creates integrity risks, as many self-employed can control over income and arrange their affairs to access insurance payments. Covering self-employment also risks distorting business decisions by shifting business risks from the self-employed to the Scheme. Opt-in arrangements magnify this risk.

67 In our advice to Cabinet in July, we noted clear benefits to including some self-employed workers in the Scheme, particularly those who closely resemble employees. Cabinet noted further work would be undertaken to consider whether and how self-employed workers could be included and invited Ministers to report back on this issue [CAB-22-MIN-0250.02 refers].

*We have considered additional options for covering groups of self-employed workers*

68 Extending NZII coverage to self-employed workers who resemble employees (e.g. couriers) is desirable as they are more likely to be more vulnerable (have low bargaining power, lack financial reserves, be impacted by market shifts) and therefore more susceptible to a displacement type event.

69 The options canvassed in the NZII discussion document for including self-employed groups focussed on their degree of dependency (e.g. self-employed workers with fewer than five clients/counterparties), but size of operation could be a more definitive criterion of vulnerability. Accordingly, we looked at options for covering self-employed workers based on turnover or number of employees, as well as whether there are existing groups of self-employed workers (e.g. occupations listed on Inland Revenue's list of scheduled payment activities) that could form a sensible basis for NZII coverage.

70 Across all options, the overarching concern is the boundary issues created in attempting to define sub-groups of self-employed workers. A key risk is that workers with similar operations may end up on different sides of a boundary. Boundaries also increase the risk of excluding vulnerable workers and creating opportunities for some workers to adapt their business to be in or out as they please. These factors, and the administrative complexity required to design and administer workable Scheme settings for each sub-group, may reduce the overall coherence and integrity of the Scheme.

71 Legal professional privilege

*We recommend excluding self-employed workers from the Scheme, but signalling our intention to cover some groups of self-employed in the future*

72 Covering self-employed remains challenging and could complicate or delay the introduction of the Bill. We therefore propose to exclude the self-employed from NZII initially, to focus on establishing the main Scheme for employees.

73 We intend, however, to continue to explore avenues to bring vulnerable groups of self-employed workers into the Scheme. We will draw on work currently underway in overseas countries who brought self-employed workers into aspects of their Schemes during COVID-19, supported by the

6 Groups could be selected based on occupational groupings, and coverage could be limited to either displacement or a health condition or disability (HCD), or it could include both.

7 Legal professional privilege

Organisation for Economic Cooperation and Development, to bring these workers back in on an ongoing basis.

74 We are also proposing to signal in our public communications that Government has a strong intention of bringing self-employed workers in to the Scheme, once the main Scheme has been established, the effects of excluding the self-employed are apparent, and the impact of the Better Protections for Contractors interventions are clearer (see below).

*There is other work underway that may mitigate the impact of excluding self-employed workers from the Scheme at this stage on some of these workers*

75 Confidentiality [redacted]

76 While further analysis is undertaken to explore options for including self-employed people in the Scheme, this programme of work may help to reduce the impact of excluding self-employed people who are substantively working as employees and should benefit from the Scheme.

## Eligibility for bridging payments and notice period

77 Cabinet agreed in July that employers would provide a four-week bridging payment when making an employee's position redundant, whether or not the person is eligible for NZII [CAB-22-MIN-0250.02 paragraph 34 refers].

78 Since July, we have sought further advice on whether to limit the bridging payment to only those employees who are eligible for NZII. A targeted approach where the bridging payment is provided only if an employee is eligible for NZII would be aimed at deterring spurious redundancies for the purpose of the Scheme.

79 As the bridging payment is, first and foremost, a Scheme setting to deter spurious redundancies, imposing this setting on employers with workers who are not eligible for NZII may be seen as outside of the scope of the NZII. These broader protections may be more appropriately addressed through improvements in the Employment Relations and Employment Standards (ERES) system.

80 Cabinet also previously agreed that the bridging payment obligation would be accompanied by a four-week notice period. We propose that settings for the notice period (i.e. whether this applies to all displaced employees or just those eligible for the Scheme) should align with Cabinet's decisions on bridging payment eligibility, for simplicity, consistency, and operational efficiency.

81 Providing the notice period and bridging payment to all workers made redundant would create a new employment standard and mean that all workers would receive some protection in the event of redundancy. It would

also ensure all workers made redundant are treated equally (rather than some being eligible for notice and bridging payment and others not).

82 NZII eligibility settings such as the contribution history or residency criteria might be sufficient to act as a deterrent to spurious redundancies and pushing up costs of the Scheme. If a person is not eligible for NZII because, for example, they do not meet eligibility criteria such as the contribution history or residency criteria then the incentive for unnecessary or sham redundancies disappears.

83 The targeted approach would also have impacts for the Scheme's implementation and add operational complexity for both ACC and employers. Employers may not know whether an employee is eligible for the notice period and bridging payment until ACC has made a determination on eligibility. It will also have implications for the Scheme's penalties, offences, and enforcement, as detailed later in this paper (see paragraphs 101 to 103).

84 We propose to maintain Cabinet's previous position, to provide the notice period and bridging payment to all workers made redundant.

## Interaction between bridging and contractual redundancy payments

85 In July, Cabinet agreed to further work on whether the bridging payment is in addition to any contractual entitlement to redundancy compensation. The NZII discussion document proposed that bridging would be payable in addition to any contractually negotiated redundancy compensation, given that existing contractual provisions may reflect an express or implicit wage sacrifice.

86 There are arguments both ways, but on balance we propose allowing employers to satisfy the bridging payment requirement by paying contracted redundancy compensation that meets or exceeds the bridging requirement. Where the contracted redundancy provision is less than four-weeks, the employer would need to pay the difference to the employee.

87 This approach would:

87.1 still achieve the policy intent for NZII of discouraging unwarranted redundancies, and

87.2 reduce costs for employers who have agreed to contractual redundancy.

88 Although some employees who have traded-off wages or other benefits for redundancy provisions may feel that they do not gain anything additional in the event of a redundancy, some will receive redundancy entitlements above the bridging payment as well as their income insurance entitlement.

89 This will create some challenges for how bridging payments and redundancy payments are treated in the welfare system, as bespoke rules apply to redundancy payments compared to other forms of income. Ministers will receive further advice on this issue.

90 Ultimately, we consider this is a transitional issue. Collective agreements will be renegotiated, with the bridging payment serving as a new minimum floor and parties free to negotiate around this.

## Te Tiriti o Waitangi/Treaty of Waitangi provision

91 We have committed to a close working relationship with SE ILG on the Scheme's policy and legislative design to ensure it meets the needs, interests, and aspirations of Māori, considers the impacts for Māori, and ensures the Crown gives effect to Te Tiriti o Waitangi/Treaty of Waitangi.

92 Cabinet has agreed to include a Tiriti o Waitangi/Treaty of Waitangi provision in the Bill to recognise and respect the Crown's responsibilities, with reference to specific provisions within the Bill [CAB-22-MIN-0250.02 refers]. Cabinet also noted that officials will work with the SE ILG, Crown Law Office and the Treaty Provisions Oversight Group (TPOG) to develop a well-balanced and workable Tiriti/Treaty provision.

93 Officials have been, and will, continue to closely work with the SE ILG and engage with TPOG and other relevant agencies ahead of an update to Cabinet in December.

94 To support the close working relationship with the SE ILG on this work, MBIE officials have recommended seeking a waiver from the Attorney General to share drafting instructions and the draft Bill. We are supportive of this approach given the significance of the proposal and the need to ensure the Scheme is responsive to the needs of Māori and ensures the Crown gives effect to Te Tiriti o Waitangi/Treaty of Waitangi.

## Update on further policy work underway

95 There are several further areas where second order policy work is progressing. We intend to update Cabinet on decisions taken on these issues in December 2022 when we seek approval to introduce the Bill to the House but provide some interim updates below.

*The role of NZII in responding to economic crises*

96 In July, Cabinet noted its intention for the Scheme to have the flexibility to provide additional Crown-funded support during a crisis.

97 The key risk in building a dedicated crisis response function into NZII is that the function may not be suitable to the nature of the crisis, and the preferred response. It would be useful, however, to specify in legislation that Ministers can direct ACC to use NZII's administrative capabilities to support responses to economic crises (e.g. ACC could use its payments engine and data sharing arrangements with other agencies to deliver response payments).

98 The provisions would make clear that:

98.1 any payments outside the usual eligibility conditions would be a cost to the Crown, and

98.2 the Scheme would likely be participating in partnership with other agencies in responding to an economic crisis.

*Non-standard work*

99 Cabinet agreed that NZII will cover those in non-standard employment arrangements (fixed-term, seasonal and casual) for loss of work. Given the challenges in determining when a loss of work has occurred for these employees – especially for casual employment – Cabinet agreed that NZII will take a principles-based approach: income insurance will cover the loss of income from reasonably anticipated work, with entitlements based on a person's established pattern of work [CAB-22-MIN-0250.02 refers].

100 It is difficult to identify a clear test for an expectation of future work, but:

100.1 primary legislation could set out a list of verifiable factors (based on employment case law considerations) for considering if a person had a reasonable expectation of future work[8], and

100.2 regulations could also specify circumstances ('safe harbours') under which a person would automatically be deemed to have met the 'reasonable expectation of future work' standard.

*Offences, penalties, and enforcement*

101 Many of the existing penalty and offence provisions in the Accident Compensation Act 2001 can be replicated for NZII. These include penalties related to overpayments and unpaid levies, offences related to misleading and not providing information to the Corporation, and limitation periods.

102 Once the Scheme is established, employers will need to provide a notice period and bridging payment (where applicable) to their employees and notify the Scheme of any redundancies. These are new employer obligations where there are no existing offences, penalties, or enforcement mechanisms.

103 Officials are continuing to work through aspects of enforcement, and the intersection between the ERES system and NZII.

*Information sharing arrangements: privacy issues still to be resolved*

104 Effective operation of the Scheme requires personal information for accurate levying and assessment and management of claims. Scheme information will also be important for determining full and correct entitlements from other government services.

105 Officials have engaged with the Office of the Privacy Commissioner (OPC) and the Legislation Design and Advisory Committee (LDAC) on the approach to the Scheme's information sharing requirements and propose to proceed with a combination of legislative provisions and individual authorisation

8 These would likely include whether an employer gave an express commitment of future work, duration with the employer, and evidence provided of a regular and consistent pattern of work.

(informed consent from individuals). MBIE officials are comfortable that any negative impacts on individual's privacy are proportionate to the benefits.

106 There are a number of important privacy issues still requiring consideration in terms of the overall policy design of the scheme, and any future implementation. This includes full consideration of the appropriate information sharing mechanism, which potentially could involve legislative provisions and informed consent from individuals, but should be considered as part of a broader analysis of the privacy impacts of the scheme.

107 Agencies have committed to working with the Office of the Privacy Commissioner to resolve those issues in a timely way, and ensure that a privacy-by-design approach is reflected in the policy design and operational aspects of the scheme.

## Next steps and commencement of the Scheme

108 We intend to seek Cabinet approval to introduce the Bill to the House in December. The Bill has a category 4 priority on the 2022 Legislation Programme (to be referred to select committee in 2022). Cabinet has agreed that the legislation should be passed no later than July 2023 [CAB-22-MIN-0250.02 refers].

109 The expected launch date for the Scheme is 1 April 2025. This is aligned to a tax year and provides sufficient time for a quality build and implementation, designed in partnership with Māori. Implementation is expected to commence soon after the Bill is enacted in July 2023.

110 The proposed timeline is set out in the table below.

***Table: Legislation timeline***

| ***Step*** | ***Proposed date*** | ***Consistency assurance*** |
|---|---|---|
| Date by which the Bill will be provided to the Ministry of Justice for an assessment of consistency with the New Zealand Bill of Rights Act 1990 (BORA) | 24 November 2022 | An initial draft of the Bill is expected to be provided to Ministry of Justice for NZBORA vetting in October, so that changes as a result of vetting can be included in the Bill before it is circulated for Ministerial consultation. In accordance with the Cabinet manual, the last date for submission of a near final draft of the Bill for NZBORA vetting is 24 November (two weeks before Cabinet Committee). |
| Cabinet Legislation Committee (LEG) approval to introduce the Bill | Thursday 8 December | This is the latest possible date to enable introduction of the Bill this year. |
| Cabinet approval to introduce the Bill and Introduction to the House | Monday 12 December | This is the latest possible date to enable the Bill to undergo a full select committee process and be passed in mid-2023. |
| First reading and referral to select committee | Thursday 15 December | 15 December is the first day that the Bill can receive its first reading and referral to |

| Step | Proposed date | Consistency assurance |
|---|---|---|
| | | select committee if it is introduced on 12 December. It is the last sitting day for the year. |
| Report back from select committee | Mid-June 2023 | This allows for a 6-month Select Committee process. |
| Date of enactment | June – July 2023 | Before Parliament rises in 2023. |
| Commencement | All parts commenced by 1 April 2025 | Parts would be commenced as operationally required, with all parts commenced for go-live 1 April 2025. |

## Impact Analysis

*Regulatory Impact Statement and Climate Implications of Policy Assessment*

111 A final Regulatory Impact Statement (RIS) combining the decision to proceed with the Scheme and the detailed design choices will be submitted to Cabinet when the Bill is considered for introduction. Publication of the RIS will coincide with the introduction of the Bill to the House.

112 The Climate Implications of Policy Assessment (CIPA) team was consulted on the proposal to proceed with NZII and confirmed that the CIPA requirements do not apply to the Scheme as the threshold for significance is not met.

## Financial Implications

113 The financial implications of the Scheme were covered in *Cabinet Paper 1: New Zealand Income Insurance – Agreement to Proceed*, considered by Cabinet in July 2022.

114 The Scheme was estimated to cost $3.54 billion if commenced in December 2023, funded by an estimated levy of 2.77 percent, using 2018/19 data. The Treasury's Budget Economic and Fiscal Update 2022 estimates that this will increase to $4.7 billion per annum with the Scheme beginning in 2025/26, reflecting projected wage growth.

115 Officials continue to refine the tripartite working group's modelling of the NZII cost and levy requirements. The proposed 2.0 percent indicative levy would generate a funding requirement of approximately $3.4 billion for forecast costs for the initial levy year of 2025/26. Further work is being undertaken to refine the cost and levy assumptions, which will support a levy consultation following the passage of legislation.

116 ACC, MSD, and Inland Revenue are working on refined costings for establishing Scheme infrastructure for a Budget 2023 initiative, currently estimated at approximately $600 million over four years.

117 Free and frank opinions [redacted]

Free and frank opinions [redacted]

## Population Implications

118 The population impacts of the Scheme were considered by Cabinet in July 2022 when it agreed to proceed with the Scheme. The proposals in this paper have additional implications for the following populations.

*Self-employed workers*

119 Self-employed workers are a diverse group and include business owners, sole traders, platform workers, contractors, and freelancers. Self-employed workers are more likely to be men (60 percent), older (40 percent are aged over 55 years) and to identify as New Zealand European (75 percent). Māori and Pacific peoples are disproportionately unlikely to be self-employed (8.2 percent and 2.4 percent of self-employed people respectively). The cohort has a wide income range and a disproportionately large number of low earners.

120 Although self-employed workers might generally be expected to have accounted for business risks in their pricing and private insurance arrangements, we know that a proportion of self-employed workers are relatively dependent on a small number of clients/counterparties and have similar vulnerabilities to employees.

121 Excluding the self-employed from NZII, at least initially, means that they will not have the protections and support of the Scheme at its onset. However, self-employment cover in some form could be reviewed following the go-live of the Scheme when the effects of excluding the self-employed are clearer.

*Māori, young people and migrants*

122 The proposal in this paper that the bridging payment should only apply to those employees who are eligible for the Scheme has implications for:

122.1 temporary visa holders who have not been continuously resident in New Zealand for at least two years at the time of trigger event, and

122.2 New Zealand citizens and residents who do not meet the six-month contribution requirement.

123 International experience suggests that contribution requirements are more difficult to meet for people in non-standard working arrangements, new to the workforce, and with relatively long but interrupted contribution histories (e.g. due to caregiving or studying).

124 The Household Labour Force Survey data provides a broad indication of the percentage of people made ineligible by the contribution history requirement (and therefore would not receive a bridging payment), showing a significant

disproportionate effect on young people. The disproportionate effect on Māori should also be noted. This raises an equity concern as, due to the roles and occupations that Māori work within, there will be a large portion of Māori who contribute but do not benefit from the Scheme.

| | Percentage of workers unlikely to meet contribution history |
|---|---|
| **Overall population** | 12% |
| **Māori** | 17% |
| **Pacific peoples** | 13% |
| **Women** | 13% |
| **15 – 17-year-olds** | 41% |

## Human Rights

125 The proposals in this paper are consistent with the New Zealand Bill of Rights Act 1990 (NZBORA) and the Human Rights Act 1993.

126 [Legally privileged] Crown Law advice was sought on the exclusion of temporary visa holders who have been continuously resident in New Zealand for less than two years from NZII. Crown Law concluded that NZII does not unjustifiably limit section 19 of the NZBORA and considers the Scheme's treatment of temporary migrants to be reasonable, and that it can be justified in a free and democratic society.

## Consultation

127 *Cabinet Paper 1: Agreement to Proceed*, considered by Cabinet on 4 July 2022, set out the consultation undertaken on NZII.

128 The Council of Trade Unions, Business New Zealand, and the SE ILG were consulted on the proposals in this paper.

129 This paper was prepared by MBIE. MSD, ACC, the Treasury, the Ministry for Primary Industries, Inland Revenue, Te Puni Kokiri, the Ministry for Education, the Ministry for Ethnic Communities, the Ministry for Women, the Ministry of Health, and PCO were consulted. The Department of Prime Minister and Cabinet was informed.

## Communications

130 We seek CBC's direction on when the Government should announce its intention to proceed with NZII. A joint Ministerial media release and other communications collateral will be prepared to support the announcement.

## Proactive Release

131 We intend to proactively release this paper and other NZII Cabinet papers, along with a range of underpinning policy advice documents, at the time the Government announces its decision to proceed with NZII. Documents will be published on the MBIE website.

## Recommendations

The Ministers of Finance, Social Development and Employment, ACC, and Workplace Relations and Safety recommend that the Cabinet Business Committee:

1 **note** that on 4 July 2022 Cabinet agreed to proceed with New Zealand Income Insurance and made decisions on the detailed design of the Scheme [CAB-22-MIN-0250.02 refers].

2 **note** that Cabinet invited the Ministers of Finance, Social Development and Employment, ACC, Revenue, and Workplace Relations and Safety to report back to the Cabinet Economic Development Committee by October 2022 on outstanding policy questions relating to:

2.1 further options for reducing the impact of the NZII levy on low-income workers

2.2 further coverage choices for self-employed workers

2.3 NZII's role in responding to economic crises

2.4 further advice on enforcement, offences, and penalties

2.5 coverage for non-standard workers (fixed-term, seasonal, and casual)

2.6 arrangements for obtaining and sharing personal information required to administer NZII.

3 **note** that Cabinet agreed to do further work on whether the bridging payment is in addition to any contractual entitlement to redundancy compensation [CAB-22-MIN-0250.02 paragraph 35 refers].

*Levy modelling update*

4 **note** that previous public consultation earlier this year referenced a levy rate of 2.77 percent of salary and wages, which was based on behavioural assumptions set towards the upper end of the range of modelled methods.

5 **note** that an updated indicative initial levy rate will need to be communicated as part of any announcement of final decisions on the detailed design of the Scheme, to allow New Zealand workers and businesses to plan as best as possible for the actual cost impost of the Scheme.

6 **note** that subsequent work policy and risk analysis modelling work (which remains a work in progress) indicates that the initial levy could be set within a range of 1.7 to 3.0 percent of salary and wages (split evenly between workers and employers).

7 **note** that there are trade-offs in the balance of financial risk to be borne by levy-payers and the Crown in the early years of the Scheme, and Cabinet's risk appetite should guide where the levy is initially set within the range of 1.7 to 3.0 percent.

8 **agree** to adopt an updated indicative initial levy rate of 2.0 percent of salary and wages for the purposes of announcing the Government's intention to introduce the Scheme.

9 **agree** that subject to the change in timeframe for the Scheme going live (from December 2023 to 1 April 2025), levy modelling work should continue to be advanced and that the initial levy rate be agreed following a round of public consultation on the levy following passage of the legislation.

*Income replacement rate*

10 **agree** to retain a replacement rate of 80 percent of prior income up to a maximum cap, consistent with Cabinet's decision on 4 July 2022 [CAB-22-MIN-0250.02 paragraph 14 refers].

11 **note** that Cabinet agreed that the levies be equally shared by workers and employers at the outset of NZII, but that this could be adjusted over time by regulation as is deemed equitable [CAB-22-MIN-0250.02 paragraph 56 refers].

*Levy structure*

12 **agree** to a flat rate levy structure which, together with an 80 percent replacement rate, is expected to be redistributive in favour of lower-income families and provide greater support than welfare alone.

13 **note** that alternative progressive levy structures were considered, with the best alternative being a levy-free threshold, though this is not well targeted.

14 **note** that the following progressive levy structures would raise the same amount of revenue as the flat-rate 2.0 percent levy:

14.1 a levy-free threshold of $14,000, with a levy rate of 1.34 percent above that (up to the maximum cap).

14.2 a levy free threshold of between $14,000 – $19,000, with a levy rate of 1.39 percent above that (up to the maximum cap).

*Coverage of self-employed workers*

15 **agree** to exclude self-employed workers from NZII initially, to focus on establishing the main Scheme for employees.

16 **note** that we will communicate our intent to explore avenues to bring vulnerable groups of self-employed workers into the Scheme and mitigate the risk of employees being reclassified as contractors to avoid NZII levies.

*Bridging payments*

17 **note** that Cabinet agreed in July that employers would be required to provide a four-week notice period and a four-week bridging payment when making an employee's position redundant, whether or not they are eligible for income insurance [CAB-22-MIN-0250.02 refers].

18 **note** that we sought further advice on options to provide a four-week bridging payment when making an employee's position redundant only if an employee is eligible for the NZII Scheme but have not recommended this approach.

19 **agree** that employers can satisfy the bridging payment requirement by paying contracted redundancy compensation that meets or exceeds the four-week bridging requirement.

*Other areas of ongoing policy work*

20 **note** that there are a number of further areas where policy work is progressing, and delegated Ministers intend to update Cabinet on these issues when we seek approval to introduce the Bill to the House.

21 **note** that Cabinet authorised us to make additional policy decisions, minor and technical changes, and related matters of detail to the policy decisions agreed by Cabinet, consistent with the general policy intent, on issues that arise in drafting of the Bill and its passage through the House, in consultation with relevant Ministers as appropriate [CAB-22-MIN-0250.02 paragraph 84 refers].

*Next steps*

22 **note** that the Bill should be introduced no later than mid-December 2022.

23 **note** that Cabinet has agreed that the legislation should be passed no later than July 2023 [CAB-22-MIN-0250.02 refers].

24 **agree** that the expected launch date for the Scheme is 1 April 2025, to align with a tax year and provide sufficient time for a quality build and implementation, designed in partnership with Māori.

Authorised for lodgement

Hon Grant Robertson

Minister of Finance

Hon Carmel Sepuloni

Minister for Social Development and Employment

Minister for ACC

Hon Michael Wood

Minister for Workplace Relations and Safety

## Annex A: Final proposed design of the NZII Scheme

Proposals covered in this paper are *italicised*.

| **NZII: Summary of final proposed design** |
|---|
| **Coverage for economic displacement** |
| 1. Would cover displacement (loss of work, due to the disestablishment of a job) |
| 2. Would not cover job loss due to poor employee performance, gross misconduct, or resignation |
| 3. Would cover complete job loss only (including full loss of a part-time job where a person remains engaged in other employment) |
| **Coverage provided for most employee working arrangements** |
| 4. Full- and part-time permanent employees |
| 5. Fixed-term, seasonal and casual employees (where displacement prevents completion of time-limited employment agreements, with entitlements covering the remainder of the employment agreement) |
| *6. Self-employed workers would be excluded from NZII initially* |
| **Coverage dependent on minimum contributions, with limits for subsequent claims** |
| 7. Workers would need to have contributed to the Scheme for six months or more over the 18 months preceding the claim (transitional arrangements for determining worker eligibility will apply in the Scheme's establishment phase, based on a minimum of six months' earnings in the 18-month period preceding commencement) |
| 8. Statutory parental leave (paid and unpaid) would be included in the qualifying period |
| 9. A limit would apply so workers could only claim up to a total of six months of entitlements every 18 months |
| **Coverage provided for New Zealand citizens and residents** |
| 10. Insurance payments would be available to eligible New Zealand citizens and residents |
| 11. Temporary migrants would need to meet the contribution history requirement and have resided in New Zealand continuously for at least two years at the time they experience a trigger event to access the Scheme |
| **Entitlements for displaced workers** |
| 12. *Provide a replacement rate of 80% of prior income* (up to ACC's maximum cap, currently $136,544) for a maximum of six months (see 'employer support' and 'help to return to work' for bridging payment) |
| 13. Where a person loses a part-time job and continues to earn income from another part-time job, the Scheme would 'top up' the workers income to 80% of the total pre-loss level |
| 14. Insurance payments would be calculated on an individual basis (with no asset-testing or partner income assessment) and would abate (reduce) dollar for dollar (a 100% abatement rate) once the combination of personal exertion income and insurance reached 100% of pre-loss income |
| **Entitlements generally treated as income for social security payments** |

| NZII: Summary of final proposed design |
|---|
| 15. MSD, ACC and Inland Revenue would generally treat insurance payments as income, for welfare and tax purposes |
| **Employers to support the Scheme's operation** |
| 16. Employers would be required to give at least four-weeks' notice to the insurer and to the employee pre-displacement and pay a bridging payment to meet the cost of a worker's initial period of unemployment for up to four-weeks. *Bridging payments could be to all displaced employees, or limited to those eligible for NZII*<br>*17. Employers would be able to satisfy the bridging payment requirement by paying contracted redundancy compensation that meets or exceeds the four-week bridging requirement* |
| **Coverage and entitlements for loss of work capacity due to a health condition or disability (HCD)** |
| **Similar provisions for displacement and loss of work capacity due to a HCD** |
| 18. Would provide the same entitlements as for displacement. The replacement rate, abatement rate, length of coverage, contribution requirements, limits on subsequent claims, citizenship or residence requirements, and interactions with other payments would be the same |
| **Coverage provided for any HCD that leads to a significant reduction in work capacity, and coverage for all working arrangements** |
| 19. Would cover any HCD that results in a reduction in capacity to work of at least 50% and that is expected to last no less than four working weeks |
| 20. Would cover most forms of working arrangements |
| **Health practitioners and employer to certify the effect of the HCD on work capacity** |
| 21. Worker would need to provide a work capacity assessment (in form of medical certificate) and where appropriate and required supporting evidence from their employer about their capacity to undertake the job. Any additional independent work capacity assessment would be undertaken as needed |
| 22. Timing of any reviews of a claimant's work capacity would be guided by advice from the claimant's health practitioner and progress made towards returning to work, where appropriate |
| **Employers to help workers return to work and keep jobs open** |
| 23. Employers would take reasonable steps to support an employee to continue working (including workplace changes or redeployment where possible) before the employee stops work |
| 24. Employers would make reasonable efforts to protect the job where a reasonable prognosis is made of a return to work within six months |
| **Insurance claimants' obligations** |
| **Claimants to search for work, with payments suspended in cases of serious non-compliance** |
| 25. Expected to be based in NZ, to search for suitable employment or to prepare for employment (with deferrals for those in certain circumstances, e.g. approved training, participating in an ALMP, recuperating from acute phase of health condition), |

| NZII: Summary of final proposed design |
|---|
| 26. Expected to accept suitable offers of employment. Not required to accept non-suitable offers of employment such as those that do not offer pre-displacement wages and conditions |
| **Health condition and disability claimants obliged to participate in work capacity assessments, and return-to-work services, where appropriate** |
| 27. Expected to provide subsequent work capacity medical certificates (similar to those used by ACC or MSD) if required |
| 28. Expected to engage in return-to-work activities where relevant and required |
| 29. Work obligations could be deferred on guidance by health practitioner |
| **Delivering Income Insurance** |
| **Scheme to be administered by ACC** |
| 30. Employers or workers could lodge claims with ACC, which would administer the Scheme |
| 31. Governance of the Scheme would include tripartite and Māori representation |
| **Scheme would help people return to good jobs** |
| 32. Would operate a case management system and connect people with support to find or prepare for work |
| 33. Partner agencies could provide support to claimants to search or prepare for work, where appropriate |
| 34. Where needed and appropriate, Scheme would refer people to employment and health services to enable them to return to work |
| **Disputes would be handled effectively** |
| 35. Would operate an efficient and independent dispute resolution process, with multiple escalation steps where needed |
| **Scheme would take enforcement action where necessary** |
| 36. Would take appropriate action to collect levy payments, and to deter and respond to misrepresentation |
| 37. New offences, penalties and enforcement mechanisms will be established for the new employer obligations (notice period and bridging payment (where applicable)) |
| **ACC would require high quality and timely information to deliver the Scheme effectively and efficiently** |
| 38. ACC will develop information-sharing agreements and arrangements with employers, other agencies, and service providers in line with the information sharing powers established in enabling legislation |
| 39. ACC will collect information and commission research needed to monitor whether the Scheme is meeting objectives and whether interventions are effective, to support public transparency |
| **Funding income insurance** |
| **Costs of the Scheme to be shared between employers and workers** |

| NZII: Summary of final proposed design |
|---|
| 40. Costs met through a compulsory levy paid in equal proportion by employers and employees. The levy would be adjusted when necessary to meet the Scheme's costs, similar to the current AC levy |
| 41. *Flat rate levy structure,* split between employers and employees |
| 42. Would operate two funds – one for displacement and one for health conditions and disability. Fully funded to meet annual liabilities. A small reserve fund would help improve the Scheme's sustainability in case wore-than-expected economic outcomes |
| 43. Crown would act as funder and/or lender of last resort when required |
| 44. The legislation would enable Ministers to direct ACC to use NZII's administrative capabilities to support responses to economic crises. This could include ACC using its payments engine and data sharing arrangements with other agencies to deliver response payments. Any payments outside the usual eligibility conditions would be a cost to the Crown |
| 45. Levy pays for insurance payments, case management and administration of the Scheme. |

## Annex B: Levy rates across the range and Government's options to address under- or over-collection

Illustrative Intermediate Options

| If the initial total levy rate is…. | …and the actual Scheme cost turn out to be… | …by | The maximum difference to correct levy pathway is… | …Government has the following choices: | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | **Pace of Levy adjustments*** (Assuming maximum 0.25 percentage point increments per year) | | | **Provide a $1 billion grant* in year 3** | **Provide a $2 billion grant* in year 3** |
| | | | | Up to Year 3* | Over-/Under-Recovery | Long-Term | | |
| **1.7%** | **Higher**<br><br>1.7% is towards the lower end of the feasible range for levy setting.<br><br>Claims experience is unlikely to be significantly lower than this mark, with 1.4% being the equivalent of Jobseeker for ED and HCD. | +0.5 percentage points | **-$1.7 b** | 1.7% | 2.45%<br>(+0.25% for 4 years) | 2.2% | Set a levy of 2.25% and carry this for a longer period | Removes the need for any levy premium over 2.2% |
| | | +1.0 percentage point | **-$6.0 b** | 1.7% | 3.2%<br>(+0.5% for 7 years) | 2.7% | Reduces the time the levy is above 2.7% by 1 year | Reduces the time the levy is above 2.7% by 3 years |
| | | +1.5 percentage points | **-$12.5 b** | 1.7% | 4.2%<br>(+1.0% for 6 years) | 3.2% | Reduces the time the levy is above 3.2% by 1 year | Reduces the time the levy is above 3.2% by 2 years |
| **2.0%** | **Lower** | -0.5 Percentage points | **+$1.9 b** | 2.0% | 1.25%<br>(-0.25% for 4 years) | 1.5% | No dividend from the Scheme is permitted. See note for rate 3.0% in the row below. | |
| | **Higher** | +1.0 percentage point | **-$5.9 b** | 2.0% | 3.5%<br>(+0.5% for 7 years) | 3.0% | Reduces the time the levy is above 3.0% by 2 years | Reduces the time the levy is above 3.0% by 3 years |
| **2.5%** | **Lower** | -1.0 percentage point | **+$5.7 b** | 2.5% | 1.0%<br>(-0.5% for 6 years) | 1.5% | No dividend from the Scheme is permitted. See note for rate 3.0% in the row below. | |
| | **Higher** | +0.5 Percentage points | **-$1.9 b** | 2.5% | 3.25%<br>(+0.25% for 5 years) | 3.0% | Reduces the time the levy is above 3.0% by 3 years | Removes the need for any levy premium over 3.0% |
| **3.0%** | **Lower**<br><br>3.0% is towards the upper end of the feasible range for levy setting.<br><br>This is equivalent to the publicly consulted rate but with modelling adjustments.<br><br>Claims experience could be up to 4.05% but there are limited benefits to setting levies above 3.0% due to the impact on individuals and businesses should there be lower claims costs. | -0.5 percentage points | **+$2.0 b** | 3.0% | 2.25%<br>(-0.25% for 4 years) | 2.5% | No dividend from the Scheme is permitted. There is likely to be more appetite for faster levy reductions than increases.<br><br>Where the surplus is:<br>• Modest: a smaller reduction of levies could allow for a lower net levy for a longer period.<br>• Significant: a one-off levy reduction/levy holiday could be adopted to return over-funding more quickly. | |
| | | -1.0 percentage point | **+$5.5 b** | 3.0% | 1.5%<br>(-0.5% for 7 years) | 2.0% | | |
| | | -1.5 percentage points | **+$12.5 b** | 3.0% | 0.75%<br>(-0.75% for 7 years) | 1.5% | | |

***NOTE:**

- **Pace of levy adjustments:** Ministers can choose to increase levies sooner than year three (or hold levy rates steady for longer). A shorter period with an incorrectly set levy will reduce the impacts presented in this table (and vice versa).
- **Size of levy adjustments**: Ministers can choose to make larger increases (to cost recover quicker) or make smaller increases (to smooth increases over a longer horizon) to levies. Larger levy increases in response to an incorrectly set levy will reduce the impacts presented in this table (and vice versa).
- **Use of grants**: There are alternative ways in which funding support can be provided other than grants, for example low-interest loans. However, any cost to the Crown would impact operating allowances and net debt.
- Modelling is gradually incorporating known policy decisions: excluding levy paying temporary migrants (residency requirements), ensuring a six-month contribution period, and refining any population overlaps between Economic Displacement and Health Condition & Disability claims. These changes are likely to put downward pressure on levy rates
- All scenarios have been calculated as if the NZII Scheme is implemented at the start of the growth period within an economic cycle. A correctly set levy would see early surpluses that are drawn down in economic downturns. Risk of modest upward pressure on levy rates.

## Annex C: Levy rates with the introduction of a levy free threshold

The Cabinet paper notes a range of feasible levy rates of 1.7, 2, 2.5, and 3 percent. These would be split evenly between employers and employees.

A $14,000 levy-free threshold (LFT) aligns with the existing income tax thresholds which brings administrative efficiency gains. If a LFT were introduced, employee levy rates above that threshold would have to be increased to the following to raise the same level of revenue:

| Employee levy flat rate | Employee levy rate above $14,000 (with LFT) |
|---|---|
| 1.39% (the rate included in the discussion document) | 1.86% |
| 0.85% (for the 1.7% total levy rate) | 1.14% |
| 1% (for the 2.0% total levy rate) | 1.34% |
| 1.25% (for the 2.5% total levy rate) | 1.68% |
| 1.5% (for the 3.0% total levy rate) | 2.01% |

The table below shows the weekly levy paid at various income levels with a **levy-free threshold** applied to the range of levy rates.

| PRE-DISPLACEMENT (ANNUAL) GROSS INCOME | LFT + 1.86% | LFT + 1.14% | LFT + 1.34% | LFT + 1.68% | LFT + 2.01% |
|---|---|---|---|---|---|
| **$20,000** | $2.14 | $1.32 | $1.55 | $1.94 | $2.32 |
| **$40,000** | $9.29 | $5.71 | $6.71 | $8.39 | $10.07 |
| **$44,096** | $10.75 | $6.60 | $7.77 | $9.71 | $11.65 |
| **$80,000** | $23.58 | $14.48 | $17.03 | $21.29 | $25.55 |
| **$120,000** | $37.87 | $23.26 | $27.36 | $34.19 | $41.03 |
| **$136,544** | $43.79 | $26.89 | $31.63 | $39.52 | $47.44 |

By way of comparison, the below table shows the weekly levy paid at various income levels for the **flat-rate** employee levy options.

| Pre-displacement (annual) gross income | 1.39% | 0.85% | 1% | 1.25% | 1.50% |
|---|---|---|---|---|---|
| **$20,000** | $5.33 | $3.27 | $3.85 | $4.81 | $5.77 |
| **$40,000** | $10.65 | $6.54 | $7.69 | $9.62 | $11.54 |
| **$44,096** | $11.74 | $7.21 | $8.48 | $10.60 | $12.72 |
| **$80,000** | $21.31 | $13.08 | $15.38 | $19.23 | $23.08 |
| **$120,000** | $31.96 | $19.62 | $23.08 | $28.85 | $34.62 |
| **$136,544** | $36.37 | $22.32 | $26.26 | $32.82 | $39.39 |

As expected, compared to a flat rate levy, a levy-free threshold reduces the levy burden on low-income workers and increases the burden on higher-income workers. A similar pattern is seen at the household level; greater relief is provided to low-income households, and less to higher-income households.