MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

BRIEFING

New Zealand Income Insurance – remaining policy choices

Date:	2 June 2022	**Priority:**	High
Security classification:	In Confidence	**Tracking number:**	2122-4092

Information for Ministers	**Deadline**
Rt Hon Jacinda Ardern **Prime Minister**	7 June 2022
Hon Grant Robertson **Minister of Finance**	
Hon Chris Hipkins **Minister of Education**	
Hon Carmel Sepuloni **Minister for Social Development and Employment**	
Hon David Parker **Minister of Revenue**	
Hon Stuart Nash **Minister for Economic and Regional Development**	
Hon Michael Wood **Minister for Workplace Relations and Safety**	

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**		**1st contact**
Francis van der Krogt	Acting Manager, Income Insurance Policy	-	Privacy of natural	✓
		-		

The following departments/agencies have been consulted
ACC, DPMC, IRD, MSD, The Treasury

Minister's office to complete:

- ☐ Approved
- ☐ Declined
- ☐ Noted
- ☐ Needs change
- ☐ Seen
- ☐ Overtaken by Events
- ☐ See Minister's Notes
- ☐ Withdrawn

Comment

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Purpose

This briefing provides officials' advice on the New Zealand Income Insurance Scheme (NZII) to Ministers for the 7 June Ministerial meeting, ahead of the 13 June meeting of the Social Unemployment Insurance Governance Group (SUIGG).

Executive Summary

This briefing complements the attached SUIGG paper on the remaining policy choices for NZII. The SUIGG paper explores the range of options to address each remaining issue.

Decisions are needed on remaining policy issues to inform Cabinet decisions on NZII in late June. Any delays to the June Cabinet date will reduce the chances of being able to pass a NZII bill into law by 2023, and impact delivery dates.

The Ministerial meeting on 7 June provides an opportunity for Ministers to discuss their preferred positions on these remaining choices ahead of the SUIGG meeting on 13 June.

This briefing also provides further advice on the overall impact of NZII from a macro-economic perspective and outlines the tax treatment of NZII as agreed to by the Ministers of Finance and Revenue.

Social partners and officials have reached consensus on most of the remaining policy choices but there are some choices where views diverge. This briefing also provides officials' advice on:

- coverage for health conditions and disability (HCD)
- coverage for self-employed
- extension of NZII entitlement for approved training and vocational rehabilitation
- setting and using the levy
- levy relief
- governance.

In addition to the above issues, the Treasury suggests reviewing the NZII replacements rate. The proposed replacement rate of 80% is generous when compared to international schemes.

A number of policy options in the attached SUIGG paper involve the use of delegated legislation (by establishing a regulation-making power in the primary legislation) to bring elements of the scheme into effect, if and when desired, and to specify any legislative requirements that will apply. MBIE generally does not support the creation of regulation-making powers as part of the June Cabinet decision but does support continuing policy work in these areas (extendibility for approved training and vocational rehabilitation, setting and using the levy, levy relief, and coverage of self-employment).

ACC has also provided an update on NZII implementation in this briefing. The most pressing need for implementation is to release funding from the tagged contingency for the establishment of a new income insurance scheme. Agreement from Cabinet in June will be sought for agreement to release the funding.

Officials have substantially drafted two Cabinet papers covering the case for change and detailed scheme design. These papers will be circulated for Ministerial consultation following the meeting on 7 June and updated following the SUIGG meeting on 13 June. The Cabinet papers will need to be lodged on 23 June for consideration by the Cabinet Economic Development Committee on 29 June.

Recommended action

The Ministry of Business, Innovation and Employment recommends that you:

1. **Note** that the Ministerial meeting on 7 June provides an opportunity for Ministers to discuss their preferred positions on outstanding NZII policy choices ahead of the SUIGG meeting on 13 June 2022

   Noted

2. **Note** that the Cabinet Economic Development Committee will consider the NZII proposal on June 29, 2022

   Noted

3. **Note** that this briefing complements the attached SUIGG paper and provides officials' advice on the remaining policy issues

   Noted

4. **Note** that in addition to the remaining policy issues, the Treasury also suggest further consideration be given to reducing the generosity of replacement rate

   Noted

Overall impact of NZII

5. **Note** that the Treasury estimates that NZII will have a significant beneficial impact on supporting aggregate demand during an economic downturn but not remove the need for other stabilisation mechanisms such as discretionary fiscal policy

   Noted

6. **Note** that the Treasury estimates that the adoption of NZII as currently proposed would move New Zealand from having automatic stabilisers of average responsiveness to one of the stronger responses in the OECD

   Noted

7. **Note** that the Ministers of Finance and Revenue have agreed to the tax treatment of NZII, as recommended by Inland Revenue

Noted

General approach to regulation making powers

8. **Note** that Ministers could choose to preserve scheme flexibility through creating regulation making powers in a number of policy areas

Noted

9. **Note** that regulation making powers can raise expectations of how NZII will operate, create uncertainty about scheme settings, and reduce parliamentary scrutiny over policy decisions

Noted

10. **Note** that MBIE generally does not support the creation of regulation making powers as an option now

Noted

11. **Note** that as an alternative to creating regulation making powers now, MBIE considers further work on these issues with more time to explore the range of options would also preserve optionality and flexibility

Noted

Coverage for health and disability

12. **Note** that MBIE and MSD prefer to cover health and disability from day one of implementation

Noted

13. **Note** that BusinessNZ does not support coverage for health and disability

Noted

14. **Note** that ACC considers that phasing the scheme by deferring health and disability will de-risk delivery, and this view is supported by the Treasury

Noted

15. **Note** that the NZCTU supports the inclusion of health and disability and does not support the deferral of health and disability

Noted

Coverage for self-employed

16. **Note** that officials' preferred option is not to cover self-employed through NZII but recommend further work on how coverage could be extended to some specific contractors/self-employed groups

Noted

17. **Note** that a regulation making power could be created that allows Ministers to extend coverage to groups of workers who have characteristics that are comparable with scheme coverage where this is feasible, but this option is complex and will be challenging to design

Noted

18. **Note** that the NZCTU preference for coverage of self-employed is to compulsorily include all contractors who depend on a small number of clients, but may be comfortable with the 'call-in' option

Noted

Extended NZII entitlement for training and vocational rehabilitation

19. **Note** that officials' preferred option is not to allow for extension of NZII entitlements for the purposes of training or vocational rehabilitation, although this could be introduced through subsequent legislation if desired

Noted

20. **Note** that NZCTU and BusinessNZ prefer to enable extension of NZII entitlement for the purposes of training and vocational rehabilitation through legislation

Noted

Raising and use of the levy

21. **Note** that Ministers have agreed that the levy will be raised and used to administer NZII, and to fund NZII financial payments and case management, and not cover additional services

Noted

22. **Note** that MBIE's preferred option is to limit the raising and use of the levy to administration of NZII, the NZII financial payment and case management, and not to raise levies for providing additional services

Noted

23. **Note** that ACC and social partners' preference is to maintain flexibility to raise and use the levy for purchasing services

Noted

Levy relief for low-income earners

24. **Note** that officials have explored direct and indirect levy relief options to mitigate impacts of the levy for low-income earners and each option brings additional complexity and/or is poorly targeted

Noted

25. **Provide** direction on the preferred approach to mitigate the impacts of low-income earners

Noted

Levy setting process

26. **Note** that the preferred option is for a Minister-led levy-setting process (as opposed to an ACC Board-led process)

Noted

27. **Note** that ACC supports a Minister-led process with assurances that there are clear accountabilities between ACC, MBIE and Ministers, that the process is transparent to the public, and that ACC can provide robust advice to Ministers alongside the technical rates

Noted

Governance

28. **Note** that the NZCTU seeks a continued role for social partners in direction and oversight of the scheme through a representative seat on the Board

Noted

29. **Note** that the Pou Tangata Skills and Employment Iwi Leaders Group has noted a preference for Māori/iwi to nominate representatives to the board

Noted

30. **Note** that to provide for social partner and Māori/iwi participation in governance, officials favour widening of the Board's skill matrix to include worker and employer expertise and obliging the responsible Minister to give consideration to the nominations

Noted

Implementation

31. **Note** that officials will report back to Cabinet by November 2022, with a Better Business Case on implementing NZII, and to support Confidential advice to Government

Noted

32. **Note** that progressing implementation work on NZII requires the release of funding from the tagged contingency established through Budget 2022 for the establishment work of a new income insurance scheme

Noted

33. **Note** that officials will recommend seeking release of the funding in the June Cabinet paper

Noted

Next steps

34. **Discuss** the advice in this paper with officials on 7 June, ahead of the SUIGG meeting on 13 June provides an opportunity to approve access to this contingency

Agree / Disagree

Francis van der Krogt
Acting Manager, Income Insurance Policy
Labour, Science and Enterprise, MBIE

Rt Hon Jacinda Ardern
Prime Minister
..... / ...... / ......

Hon Grant Robertson
Minister of Finance
..... / ...... / ......

Hon Chris Hipkins
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Minister for Workplace Relations and Safety
..... / ...... / ......

Background

1. While the NZII proposal is largely complete, there are still some remaining policy issues that require decisions. These decisions are needed to inform final Cabinet decisions on NZII this month needed to inform legislative drafting should it be decided that NZII goes ahead.

2. The purpose of this meeting on 7 June is for Ministers to discuss their preferred positions on these remaining choices ahead of the SUIGG meeting on 13 June.

3. There is only a brief window to agree the remaining settings to inform legislative drafting. We expect that the NZII Cabinet paper will be lodged on 23 June for consideration by the Cabinet Economic Development Committee on 29 June. To meet this timing the Cabinet papers will be circulated for Ministerial consultation, following the meeting on 7 June, and updated following the SUIGG meeting on 13 June.

4. Any delay in reaching decisions means Cabinet this will reduce the chances of introducing a NZII bill by the end of year, which will in turn reduce the chances of passing the bill into law by the middle of 2023, and delay implementation of NZII.

5. This note provides officials' views on the remaining policy issues and complements the more substantive SUIGG paper.

Overall impact of NZII

Macro-economic impact

6. The macroeconomic literature on social income insurance is rapidly growing and mostly suggests that social unemployment insurance can create an increase in the unemployment rate, which comes from both increasing employment to unemployment flows and decreasing unemployment to employment flows, and an increase in the average wage rate. However, there are potentially some offsetting factors that suggest the impact on unemployment might be small. Displacement and health and disability (HCD) contribute to a relatively small proportion of unemployment flows, and reductions in unemployment to employment flows can be offset to some extent by substitution to new entrants to the labour market.

7. While there is significant uncertainty around the potential role of NZII as an automatic stabiliser, the Treasury's estimate is that it will have a significant beneficial impact on supporting aggregate demand during an economic downturn. This would not, however, remove the need for other stabilisation mechanisms such as discretionary fiscal policy.

8. Under current settings, automatic stabilisers in New Zealand are estimated to change the budget balance by approximately 0.5% of GDP for every 1% of GDP change in the output gap. In other words, when GDP falls, increased government expenditure and reduced taxation change by roughly half that amount – helping to support the economy. The Treasury estimate that the adoption of NZII as currently proposed would increase the change in the budget balance by approximately 0.1% of GDP. As a result,

New Zealand would move from having automatic stabilisers of average responsiveness to one of the stronger responses in the OECD.

The Ministers of Finance and Revenue have agreed to the tax treatment of NZII, recommended by IR officials [IR2022/225 refers]

9. NZII levies and payments will be subject to New Zealand's existing tax framework set out in the Income Tax Act 2007 (ITA). As such there will be tax implications of NZII and consequential amendments will be needed to the Revenue Acts to ensure NZII is referenced correctly.

10. Maintaining consistency with the treatment of the Accident Compensation scheme and the overall framework of the tax system was a key factor when considering the tax treatment of NZII.

11. The following tax implications require no legislative change:

- all employer and employee levies will be subject to GST
- employers registered for GST can claim a deduction on the GST component of the lives paid but employees cannot
- NZII payments will be subject to income tax
- employers will be able to claim a deduction for the cost of employer levies and bridging payment, and if included, the self-employed will also be permitted GST and income tax deductions for levies paid
- ACC levies, KiwiSaver employee contributions, Student Loan repayments and child support deductions will apply to NZII payments
- KiwiSaver employer contributions will not be made on NZII payments

12. Legislative change is required to:

- define NZII payments as salary and wages under the ITA so these payments are subject to PAYE, and NZII claimants are not left with a large tax bill at the end of the year:
    - o a consequence of this is that employees are not permitted an income tax deduction for levies. Allowing this deduction would incur a significant fiscal cost.
- not apply NZII levies to the NZII payment.

General approach on using regulation power to preserve options

13. A number of policy options in the attached SUIGG paper involve the use of delegated legislation (by establishing a regulation-making power in the primary legislation) to bring elements of the scheme into effect, if and when desired, and to specify any legislative requirements that will apply. These include options for extendibility for approved training and vocational rehabilitation, setting and using the levy, levy relief, and coverage of self-employment.

14. Establishing regulation making powers to bring these scheme elements into effect preserves optionality and flexibility for the executive to take more detailed decisions and tailored responses to a particular issue. It also signals the potential for these scheme elements to be established, and in some cases could signal the conditions that must be met before a scheme element would be established.

15. However, providing for scheme elements to come into effect through regulations is also likely to create uncertainty about the scope of NZII, and the use of levy-funding. Further, while delegated legislation provides for significant optionality in these scheme elements, there may be good reasons not to exercise that optionality. Use of delegated legislation also risks allowing the executive to over-ride or establish requirements that are properly made only through the established parliamentary process by elected Members of Parliament. MBIE generally does not support the creation of regulation-making powers as part of the June Cabinet decision.

16. Cabinet could instead take conservative decisions (not creating regulation-making powers now) while further policy work continues on these issues, including the appropriateness of regulation making powers in the Bill later or amendments to the Act in the future.

There are some remaining policy issues to resolve

17. Some policy issues remain to resolve because:

    a. the discussion document provided more than one option for public feedback on some key design features and decisions are now needed on the preferred approach

    b. more detail than provided in the discussion document is needed to inform legislative drafting

    c. further analysis revealed we needed to reconsider some previous choices regarding some key design features

    d. we need to respond to feedback from the public engagement.

18. The full list of issues discussed in the SUIGG paper is:

- *Coverage choices*
    - health conditions and disabilities

- self-employment
- temporary visa holders
- contributions history requirements.

- *Entitlements*
  - notice and bridging payments for casual and fixed-term employees
  - bridging payments for health condition and disability claimants
  - extensions.

- *Levies*
  - levy setting mechanism, and use of levies
  - levy relief for low-income employees.

- *Delivery*
  - NZII governance.

19. The Treasury also suggests reviewing the generosity of NZII's replacement rate. Further advice is provided below, though not discussed in the SUIGG paper.

Generosity of NZII

20. Officials note the proposed replacement rate of 80% is generous, particularly when compared to international schemes while the proposed duration is comparatively less generous.

21. The Treasury suggests that further consideration should be given to the option of the 80% replacement rate progressively being stepped down during entitlement. This would differ from the 80% flat rate as ACC provides but still broadly deliver on the objectives of the scheme (such as enabling longer job search periods and providing economic stimulus) and mitigates the incentive for individuals (especially those on higher incomes) to remain on the scheme for longer than is necessary. There is robust microeconomic literature linking an increase in scheme generosity with an increase in unemployment spells.

22. A flat 80% replacement rate has the benefit of administrative efficiency, but this benefit should be considered alongside the cost of the scheme and risks of moral hazard.

23. There are examples of overseas schemes that step down replacement rates over time. We also note that the median initial replacement rate (prior to any step downs) offered by schemes in advanced countries is approximately 60%.

The attached SUIGG paper identifies where there is consensus on the remaining policy issues between social partners and officials

Coverage for Health and Disability

24. BusinessNZ does not support the inclusion of HCD. They have concerns that the inclusion of HCD creates additional costs, and roles and responsibilities for employers.

25. ACC notes that while the systems and processes for NZII are similar in lots of ways between economic displacement and HCD, additional complexity exists to assess

eligibility to the scheme, assess medical certificates and work capacity, and triage support for return to work for HCD. Additional workforce and infrastructure will also be required. Phasing in elements of the scheme will de-risk delivery and enable a cleaner focus on ensuring timely and accurate payments, before introducing a more vulnerable cohort of claimants, and this view is supported by the Treasury.

26. The NZCTU supports the inclusion of HCD and does not support deferring the implementation of HCD.

27. MBIE and MSD preferred option is for HCD coverage to be from day one of the scheme and that people are covered for a reduced work capacity of at least 50% that is expected to last at least four weeks (as proposed in the discussion document).

28. Officials do not consider the additional roles and responsibilities for employers are overly extensive or burdensome. Most of the obligations and expectations set out in the proposal exist already for employers, such as, reasonable accommodations and employers' obligations to work with ACC to support a person's return to work.

29. It is not uncommon for workers to experience a health condition or disability at some point and the causes are multifaceted. Employers do have and can play an important role in workers' health and supporting them to retain or return to work.

30. Delaying coverage for HCD could attract criticism or perception that it will not be implemented, particularly from the disability community. It may also create risks that complete costs and dimensions of the scheme are not completed at the same time.

31. Health practitioners and people with lived experience did express a willingness to work with ACC to design a workable assessment which will help address concerns about the complexity. ACC note that if HCD was implemented from day one, a high trust approach would be taken to accepting work capacity certification.

Coverage for self-employment

32. The SUIGG did not reach a preferred option for covering (or not) self-employed working arrangements. Several alternative approaches for covering the self-employed were presented in the discussion document for public consultation. The feedback we had acknowledged the complexity of coverage for self-employed and was mixed on whether to cover it or not.

33. Each option considered for covering self-employment comes with challenges, including for implementation but excluding self-employed also brings challenges.

34. Officials' preferred option is to exclude self-employed but recommend further work on how coverage could be extended to some specific contractors/self-employed groups.

35. We consider this option recognises the complexity of including self-employed, while preserving the option of offering some income insurance to some workers who have characteristics similar to employees. A bespoke income insurance function would allow solutions tailored to the nature of the particular risks of specific categories of contractors/self-employed.

36. The risk of employees being misclassified as contractors to avoid employment obligations is being considered as part of another policy process looking at Better Protections for Contractors. A decision to create a mechanism to extend NZII to specific contractors/self-employed in advance of the completion of that work risks the creation of similar but different definitions which could create confusion.

37. We understand that BusinessNZ supports the bespoke income insurance option for specific groups of contractors/self-employed detailed above. The NZCTU have some concerns that a failure to extend coverage to some self-employed groups creates a risk that workers are misclassified. But the NZCTU would be comfortable proceeding with this option if there were procedural safeguards in place and consultation with social partners.

Extensions for training or vocational rehabilitation

38. The discussion document sought views on whether NZII entitlement should be extended for approved training or vocational rehabilitation.

39. While extensions could be a useful tool for NZII to have, not enough is yet known about the uptake of and targeting of extensions to those who would benefit from it. This uncertainty presents moral hazard risks, increased costs to the scheme, and potential for poor labour market outcomes.

40. The NZCTU still strongly supports a provision in legislation to extend coverage for 12 months in certain circumstances where people would benefit from training or vocational rehabilitation. BusinessNZ also support extensions for the purpose of training.

41. Officials consider the risks created by the uncertainty at this time outweigh the benefits of providing for an extension provision.

42. Officials' preference is to not allow for extensions with legislation specifying the maximum entitlement period of six months plus bridging payment. We consider this entitlement is sufficient time for a claimant to look for and return to work and mitigates against risks of reduced job search efforts, diminishing work incentives and further detachment from the labour market. An extensions provision would also be very complex for ACC to deliver and not practical if the right training and vocational rehabilitation services are not available.

43. As noted above, optionality to proceed with extensions in the future could be preserved through a regulation making power. But this could create expectations that the extendibility would be provided. Alternatively, extension to NZII entitlement could be introduced through subsequent legislation if desired.

Raising and use of the levy

44. As proposed, the levy will be raised and used to administer NZII, to fund the NZII financial payments, and to pay for case management. This reflects a clear choice by Ministers considering the role of NZII and other forms of support, including previous Cabinet decisions that Active Labour Market Programmes (ALMPs) sit outside NZII

and would be developed in parallel by government. As such ALMPs have not been costed into the levy and cost benefit analysis.

45. Further the NZCTU advised they would not want ACC to have unilateral responsibilities of additional levies raised for services. Further work would be needed to identify responsibilities for purchasing and how this would work.

46. Access to effective case management, Active Labour Market Programmes (ALMPs), and vocational rehabilitation would support NZII's goal of returning claimants to good work.

47. There are choices about how services to support NZII claimants are funded:

- Government funds agencies to provide services
- use the levy to fund ALMPs
- a mix of government funding and NZII levy.

48. There are several ways to use levies to provide services. For example, "surplus" funds could be allocated to purchase services, or the levy could be used to include the cost of services. Further Ministers could preserve flexibility through regulation making powers that allow for using the levy for services in the future if desired.

49. Currently we do not know enough about what types of services and level of service will be needed by NZII claimants. Other government work programmes such as the review of ALMPs are assessing the case for further investment in these programmes and the potential demand from NZII claimants and will go some way to address what is needed.

50. Following consideration by the Cabinet Economic Development Committee on 29 June, on 30 June, EET Ministers will consider advice on how to address gaps in ALMPS, including for economically displaced workers (those who will also access NZII). This will include advice on early intervention, careers support and active case management for displaced workers. This will set out options to increase the supports available (or extend existing supports) to people to return them to work. The ALMP review will take into account decisions made by SUIGG on 13 June.

51. There are significant policy choices with enabling ACC to purchase additional services (for example, it could create two approaches to the provision of education and training; rehabilitation; and employment support services). Until such work is done, providing for optionality is likely to raise expectations that ACC funds the purchase of additional services.

52. ACC's preference is to allow for discretion and flexibility to raise and use the levy for purchasing services to support good work outcomes. Social partners would also prefer to preserve this optionality. We note also that the current services provided by the Crown will most likely not meet the demand surfaced by NZII. This is likely to mean that there is a significant shortage of supports available to people to return them to work.

53. Establishing a regulation-making power to enable ACC to deliver or purchase spend-to-save initiatives once NZII beds in could address issues for the scheme that other agencies/portfolios are insufficiently incentivised to address. Free and frank opinions [redacted]

54. MBIE does not recommend establishing a regulation-making power now. It prefers that the levy is raised for and its use limited to administration of NZII, NZII payments, and case management.

Levy relief

55. Low-income workers may struggle to meet the cost of the proposed new levy. To minimise this cost, the tripartite working group considered adopting a progressive levy, but set this aside given the very large increase in the levy rate that would impose on middle and higher earning workers. The Forum's discussion document therefore proposed a flat rate levy on salary and wages below $130,911 p.a.

56. Public consultation has further highlighted concerns regarding the affordability of the employee levy for low-income earners. Following the release of the discussion document, officials provided further advice to Ministers on options to mitigate the impact of the levy [MBIE report: 2122-4101 refers]. This advice discussed a range of direct and indirect relief options to levy relief for low-income earners, noting challenges and complexities with each.

57. Consideration of levy relief options has included reconsidering the pros and cons a progressive levy. Progressivity can be introduced through a levy-free threshold, whereby income earnt below a threshold is not subject to the levy, but income earnt above the threshold is. A levy-free threshold will decrease the levy liability for low-income earners.

58. However, lost levy revenue will have to be accounted for by charging a much higher levy rate on income above the threshold. Rough estimates from Inland Revenue suggest that a levy-free threshold of $23,000 p.a. would increase the levy rate charged by 70-80%. This will place a greater levy burden on middle-income households. An alternative to this is make a government contribution to offset the shortfall in levies. This would involve a large fiscal cost and depart from the agreement to fund the scheme through levies.

59. Another, more complex, progressive levy structure is one with a variety of thresholds where the marginal levy rate rises with income, similar to how personal income tax is collected. Like the levy-free threshold, this option means that those further up on the income scale will have to pay a higher effective levy rate. In Austria, social security

contributions are levied progressively as a means of redistributing income from high-income earners to low-income earners[1].

60. Progressive levy structures also involve other challenges. Any progressive levy structure will create operational complexity for payroll providers, employers who manage their own payroll systems, and Inland Revenue:

   a. The more complex the levy structure being applied, the more costly it will be for businesses at a systems level, and the greater chance of genuine error in the levies withheld by employers.

   b. As employers do not collect data on whether their employee has multiple jobs, and real-time tracking of individual incomes is not practical, it is likely that individuals will pay an incorrect levy during the year. This issue also exists for individuals who start work during a tax year. This will reduce the cash on hand for households, and involves an administrative process called a ‘square-up’. This is where Inland Revenue calculates everyone’s actual liability and sends them a bill (or refund) at the end of the tax year which could create debt issues for some levy-payers.

61. A progressive levy structure is complex and will require an in-depth policy and operational design process. On top of this, payroll providers and Inland Revenue need an 18-month lead in time (at a minimum) to build this levy structure into their systems

62. Officials maintain that a flat rate levy is the preferred levy structure. Introducing progressivity into the levy structure creates operational complexities and increases cost pressures on the levy that outweigh the benefit of reducing the levy liability for low-income individuals. The NZCTU has developed a preferred progressive levy structure option, however officials consider the operational implications of this proposal highly impractical.

63. Officials have explored other ways to mitigate the levy burden for low-income individuals through the tax and transfer system. Inland Revenue and MSD officials consider indirect levy relief through existing tax credits is not a viable option for two reasons. Firstly, increasing support through existing tax credits would be poorly targeted as not all of the affected group receive tax credits. More importantly, it would risk compromising the ongoing Working for Families review.

64. Alternatively, new forms of support could be established to compensate levy-payers, such as a refund mechanism, or a special tax code to offset the levy cost. Again, this creates additional complexity for the tax and transfer system, and a higher levy rate will need to be charged to account for this compensation. Inland Revenue and MSD do

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[1] Austria levies a social security tax of up to 18.12%. Within this tax there is an employee contribution to unemployment insurance which increases with monthly earnings: income up to EUR1,342 per month – 0%, between EUR1,342 and EUR1,464 – 1%, between EUR1,464 and EUR1,648 – 2%, greater than EUR1,648 – 3%. Under the German levy structure, someone earning under EUR 450 does not pay a levy. However, once an individual earns over EUR 450 per month, all of their income becomes subject to the full 2.5% levy.

not recommend using the tax and transfer system to mitigate the levy burden on low-income earners.

65. With Cabinet due to take decisions on NZII in June, it is highly desirable to confirm whether to maintain a flat-rate structure, or to adopt a progressive structure. An early decision on this question will provide a clear signal to levy-payers, employers, payroll administrators, and the agencies delivering NZII – Inland Revenue and the ACC. Ideally, this decision would be made in June, along with other scheme design choices.

66. Ministers' meeting on 7 June is an opportunity for Ministers to indicate whether any of the options for levy relief should be discounted at this stage.

Levy setting process

67. The discussion document provides limited detail on managing or changing levy funding once operational.

68. Officials' preference is for a Minister-led process (as opposed to the ACC Board-led process) that is bound by legislated principles and a Minister-directed funding policy, and with recourse to a Crown lending facility.

69. The rationale for the slightly greater level of Ministerial control over the funding approach compared to the AC scheme is that NZII will be reliant to a greater extent on Crown funding for periodic liquidity (debt) to manage its cashflow given the short duration nature of the scheme. ACC will remain closely involved in levy-setting, especially to ensure application of its actuarial expertise.

70. ACC is comfortable with a Ministerial-led process with assurances that:

- accountabilities are very clear between ACC, MBIE and Ministers
- the process is made transparent to the public, including publication of technical rates alongside a clear set of decision-making criteria
- ACC can provide robust advice to Ministers alongside the technical rates, which looks to the future while also considering immediate implications.

Governance

71. The Forum has called for employee, employer and Māori participation in NZII governance. The key choice is whether to provide for direct representation on the ACC Board.

72. Decisions on the approach to governance at the board level are needed for legislative drafting.

73. The NZCTU proposes establishing representative seats on the board for social partners. The Pou Tangata Skills and Employment Iwi Leaders Group has noted a preference for Māori/iwi to nominate representatives to the board.

74. A representative seat on the board would give the most direct voice for employee, employer and Māori/iwi representation but would create a complex operating model for the board.

75. Officials and BusinessNZ favour widening of the ACC board's skill matrix to include worker and employer expertise, with appropriate safeguards to ensure that decisions makers are seeking and giving due consideration to how social partners and Māori/iwi nominate Board representatives. However, this is unlikely to meet the expectations Māori/iwi and NZCTU in terms of providing confidence that Māori/iwi and employees' voices and concerns are heard and reflected in decision-making at the board level.

76. Decisions on governance arrangements below the board level are not needed now as it is preferable to maintain flexibility for these arrangements ahead of organisational design.

Update on implementation

77. We propose to report back by November 2022 with a Better Business Case on implementing the scheme for Cabinet approval.

78. ACC and MBIE, with involvement from MSD and Inland Revenue, are currently developing a Better Business Case to guide implementation of NZII. Confidential advice to Government [redacted]

79. The design and implementation preparation funding allocated in Budget 2022 will provide ACC, with the support of Inland Revenue and MSD on critical components of NZII, to complete high-level scoping, cost estimation, delivery planning and complete some early commercial planning.

There are some risks to implementation

80. A key risk is that necessary expertise will not be available to implement the operational design and development according to the implementation timeline and objectives. The timing of a number of large reorganisation projects are expected to overlap, drawing on the same pool of expertise (e.g., IT, Māori cultural capability), in a tight labour market.

81. This will be somewhat mitigated by the extension to the implementation timeframe. Agencies are also implementing mitigations through a joint resourcing strategy for workforce (ACC, Inland Revenue, MSD, MBIE) which includes strategies for attracting high-priority talent, flexible location arrangements to utilise workers outside Wellington.

82. The proposed delivery timeframes and scheme launch date are dependent on the successful mitigation of several risks, including resourcing, multi-year funding for the full implementation being approved as early as possible for the implementation phase to allow for resource and vendor commitments to be made, and the management of scope largely through the approval of the detailed policy settings.

If the Government wishes to progress implementation work on NZII the immediate need is to release funding from contingency

83. At Budget 2022 the Minister of Finance and Minister of Social Development and Employment jointly agreed, as authorised by Cabinet [refer CAB-22-MIN-0129 - Initiative 13624 refers], to establish a tagged contingency for the establishment of a new income insurance scheme, for MBIE and ACC to draw down over the scheme's implementation period.

84. Cabinet also agreed that funding would be released with joint Ministerial approval subject to:

- Cabinet deciding to proceed with the proposed NZII and
- further advice from ACC on preparatory and implementation work required for implementing NZII.

85. A recommendation seeking release of the funding will be included in the Cabinet paper for consideration by Cabinet Economic Development Committee in June.

Next steps

86. Ministers are meeting on 7 June to discuss the Government's preferred position on the remaining scheme design choices. The 13 June SUIGG meeting is an opportunity for a discussion with the social partners.

87. The Minister of Finance and Minister for Social Development and Employment offices are also arranging a meeting with the National Iwi Chair Forum, Co-Chairs to discuss the NZII proposal.

88. Officials have substantially drafted Cabinet papers, and are/have consulted these with agencies, and will update the papers following the ministerial pre-meeting on 7 June, and the SUIGG on 13 June.

89. Cabinet DEV Committee could take these papers on 29 June, for confirmation by Cabinet on 4 July. With the July parliamentary recess, Cabinet committees will not begin to meet again until August.

90. Subject to a Cabinet decision to proceed, PCO will draft a bill to establish NZII. Officials will work closely with the PCO to ensure the legislation meets the policy intent.

91. We propose that Cabinet delegates authority to small group of ministers to approve detailed design choices over the course of legislative drafting from July through to November 2022.

Attachment

Briefing to the SUIGG: New Zealand Income Insurance – remaining policy choices

To: Social Unemployment Insurance Governance Group

From: Social Unemployment Insurance Working Group

Date: 2 June 2022

Briefing: New Zealand Income Insurance – remaining policy choices

Purpose

1. To confirm the final design settings for New Zealand Income Insurance ahead of Cabinet decisions later this month.

Executive summary

2. Public consultation has closed on the Future of Work Forum's proposal to introduce a New Zealand Income Insurance scheme. Along with public submissions, targeted engagement was undertaken with Māori/iwi and key stakeholders across a range of sectors.
3. The Working Group received 255 submissions and around 1,819 survey responses. The number of responses received is low for a proposal of this significance. Around two-thirds of respondents and submitters opposed the proposal and around one-third support the proposal.
4. Many of the issues raised in consultation were considered by Ministers and social partners in the development of the discussion document. Where no new considerations have been raised in submissions, the Working Group proposes that the settings outlined in the discussion document be confirmed.
5. There is a small set of issues, which were either unresolved in the discussion document or where new information has been raised, which warrants further consideration. This includes:
    a. Coverage: of health conditions and disabilities, the self-employed, temporary visa holders, and the eligibility requirement for a contributions history
    b. Entitlements: extensions of duration of cover
    c. Employer obligations: notice periods and bridging payments for casual and fixed-term workers, and bridging payments for medical dismissals
    d. Levies: rules for their use, levy-setting process, and mitigating the levy impact on low-income workers
    e. Delivery: governance arrangements.
6. The Social Unemployment Insurance Governance Group is meeting on 13 June to discuss these issues and to confirm SUIGG's comfort with the existing design settings proposed for the remaining dimensions of the scheme.

7. Ideally, Cabinet would take decisions on whether to proceed and on scheme design, by early July 2022. This timing would allow sufficient for time for drafting of the Bill and passage through the House by mid-2023.

8. Decisions on funding and timing to operationalise New Zealand Income Insurance are subject to further advice.

Recommendations

We recommend that you:

1. **note** that the discussion document proposed a near-complete set of design parameters for the New Zealand Income Insurance (NZII) scheme (summarised in Annex Two)

2. **note** that the consultation process did not highlight significant new considerations in respect of a number of these proposed design parameters

3. **note** that this paper is focused on presenting options for the remaining design choices for NZII, for the SUIGG to provide direction ahead of Cabinet Economic Development Committee considering the policy proposals for the scheme at the end of June

4. **note** the timetable for decisions is compressed if Cabinet is to make decisions to enable the Bill to be drafted and introduced by the end of 2022

5. **discuss** the options presented in this paper at your 13 June meeting (Annex One outlines preferred options and a summary of key considerations).

Privacy of natural persons

Francis van der Krogt
Acting Manager, Income Insurance Policy

02 / 06 / 2022

Background

9. The Social Unemployment Insurance Governance Group is meeting on 13 June 2022 to consider a range of remaining policy choices for the design of the proposed New Zealand Income Insurance scheme.

10. Over 12 weeks in February, March and April, the public's feedback was sought on the proposal of the Government, Business New Zealand (BusinessNZ) and the New Zealand Council of Trade Unions (NZCTU) to establish a New Zealand Income Insurance scheme. A discussion document set out proposed settings for coverage, entitlements, employer and employee obligations, scheme delivery and funding arrangements, including a levy rate.

11. Public consultation closed on 26 April. Officials have been analysing submissions and feedback from targeted engagement and considering implications for scheme design. Further detail on the public consultation is provided in the next section. We have also supported the passage of legislation to enable ACC to undertake work to prepare for scheme implementation.

12. With the formal consultation completed, decisions are now required to confirm:
    a. whether to proceed with the proposed scheme, and
    b. the detailed design of the scheme, focussing on those design aspects left unresolved in the discussion document (assuming a decision to proceed).

13. It is desirable for Cabinet to take decisions on these matters by early July 2022, since this will allow sufficient time to draft legislation by December 2022 to enable passage by mid 2023.

14. Decisions on funding and timing to operationalise New Zealand Income Insurance are subject to further advice.

15. This paper focuses on outstanding design choices.

Consultation

16. The public submissions and online survey closed on 26 April 2022. In addition, officials have worked with the Pou Tangata Skills and Employment Iwi Leaders Group on the approach to engaging with Māori/iwi and undertook targeted engagement with key stakeholders (see Annex Six for more detail).

17. The project received 255 submissions and 1,819 survey responses, and held around 50 targeted engagements. The number of submissions received is relatively low given the significance of the New Zealand Income Insurance proposal.

18. About two-thirds of submitters and respondents opposed the scheme. Common concerns submitters and respondents identified include:
    - the levy will have a material impact for low-income workers
    - the levy and bridging payments are unaffordable for small business
    - the scheme helps mid- and high-wage earners at the expense of more vulnerable workers

- a preference for alternative options, such as implementing the recommendations of the Welfare Expert Advisory Group, expanding ACC cover to sickness and disability, introducing statutory redundancy, and making KiwiSaver more accessible in cases of job loss.

19. Around one third of submitters and respondents expressed support for the scheme. Common reasons given in support by submitters and respondent include:
    - the lack of statutory redundancy in New Zealand
    - relatively low and closely targeted welfare support
    - the current disparity between support for those unable to work due to an accident and those who fall ill

Remaining policy choices

20. Many of the issues raised in consultation were considered by Ministers and social partners in the development of the discussion document. Where no new considerations have been raised in submissions, the Working Group proposes that the design settings in the discussion document be confirmed (see Annex Two for an outline of the scheme settings proposed in the discussion document).
21. There are also some substantive design matters requiring further attention, either because a preference had not been determined, further detail was required for legislative drafting, or feedback and further analysis has identified a need to reconsider choices.
22. Annex One summarises options for SUIGG's consideration for each of the outstanding policy issues. More detailed discussion of the options, including relevant feedback from consultation, is set out below. This advice has been developed by the Working Group of cross-agency officials, BusinessNZ and NZCTU.
23. Officials and social partners have considered the potential options to address each outstanding issue in light of:
    a. policy objectives – favouring options that promote a return to good employment for people being displaced from work, or losing work capacity due to a health condition or disability
    b. operational viability – favouring options that are readily implemented, and that minimise compliance costs for employers and working people
    c. potential impacts on the levy – seeking to avoid options that could increase the cost of the scheme, and hence the levy rate.

A. There are choices in how to include health conditions and disabilities in New Zealand Income Insurance

The Forum's proposal

24. Coverage of loss of work due to health conditions and disabilities (HCD) is a fundamental component of the New Zealand Income Insurance proposal presented in the Forum's discussion document.

25. Health conditions and disabilities are a significant cause of loss of work and earnings. Providing coverage through New Zealand Income Insurance would provide working people with better protection against these risks. Similarly to coverage for displacement, coverage for HCD would help address both the immediate loss of income and promote a return to good work.

26. Coverage through New Zealand Income Insurance would also be a step towards parity with the accident compensation scheme, which only compensates for losses due to injury.

27. While there is a limited private market for income loss due to HCD, but costs are high, common health conditions and disabilities (and pre-existing conditions) can be excluded, and lengthy stand-down periods can apply.

28. The Forum proposed coverage for any health condition or disability that results in a reduction of capacity to work of at least 50 percent and that is expected to last for no less than four working weeks.

29. Compared to international schemes the proposed 50 percent reduction in work capacity is towards the less generous end of the scale but is not an outlier. The combination of a capacity threshold and incapacity duration for eligibility is somewhat unusual compared with international schemes. Most schemes set a capacity threshold and have a short waiting period, and employers are usually required to fund a period of sick leave before the scheme pays. The incapacity duration is an alternative to a waiting period to ensure people who have used all their sick leave can access the scheme immediately after job loss.

Further considerations and additional choices

30. Public engagement identified concern that the work capacity assessment may be too complex, particularly for fluctuating or deteriorating conditions and for determining a level of loss. The health and disability sector also raised concerns about health practitioners' capacity and capability to undertake assessments.

31. Other stakeholders supported coverage for HCD, viewing it as a good step towards reducing inequities, with some considering there was more value in covering HCD than displacement.

32. BusinessNZ has proposed reconsidering coverage of HCD by New Zealand Income Insurance, noting in particular the effect on the scheme's cost and questioning whether it is fair to allocate these costs to employers, given they may have little influence over employee health. NZCTU strongly supports the inclusion of HCD as part of the initial roll-out of the programme.

33. ACC has noted that commencing coverage for HCD and displacement simultaneously introduces risks to implementation of the scheme. Partly this is due to the more

complex eligibility assessment required for each claimant, based on the work capacity assessment and information from the employer (in contrast to displacement, where ACC will simply receive notification of a planned redundancy). In general, simultaneous commencement of both types of cover will require a bigger workforce from Day 1 and more complex infrastructure.

34. The range of options for the SUIGG's consideration therefore are:
    a. commence cover for HCD from Day 1 of New Zealand Income Insurance, as proposed in the discussion document, or
    b. defer commencement of HCD cover to simplify roll-out of the scheme, or
    c. do not provide coverage for loss of work capacity due to health conditions and disabilities.

Comment

35. International evidence suggests that income insurance coverage for loss of work capacity due to a health condition or disability can result in improved labour market productivity and better employment outcomes. These outcomes result from increased work participation and productivity, reduced sickness absence, and earlier reported health benefits. In New Zealand, it would also improve equity for older workers, who are more likely to lose work capacity due to a health condition or disability, and Māori workers, who have disproportionately worse health outcomes than other population groups.

36. Businesses have some influence over worker health and wellbeing, through workplace practices. There is strong evidence that these can positively or negatively impact mental and physical health. Good workplace practices focused on supporting worker health and wellbeing will help to manage the extent of claims. The government and social partners all have roles to play in supporting uptake of good workplace practices.

37. Deferring the commencement of HCD cover by the scheme is unlikely to address the concerns raised by some businesses about cost and fairness, but it may simplify the roll-out of New Zealand Income Insurance. A deferral would provide the opportunity to test the scheme's systems and processes for ED before introducing a more complex and vulnerable cohort of claimants. NZCTU would not support a deferral.

38. International experience indicates there is no perfect work capacity assessment method, but assessment by GPs is the most cost-effective. To address concerns about the complexity of the work capacity assessment, the assessment process and information to be collected can should be designed in collaboration with clinicians/health practitioners and representatives of people with lived experience. It will also be important to involve employers and business. This will help ensure that the systems that are established are best suited to the needs of the various parties in the assessment.

B. The scheme requires rules governing the use of levies

The Forum's proposal

40. The discussion document highlights the importance of employment and rehabilitation services to support people back into good work, and notes that some services are currently already provided by the Crown (although noting that the availability of services currently would not meet the likely scale and nature of demand for such services under NZII).

41. The discussion document proposed that case managers would connect claimants with employment services and products provided by the Ministry of Social Development (MSD) if suitable and available[1]. It also noted that, over time, it may be desirable for ACC to purchase a wider range of services from various providers. While this would cost more, effective employment services could reduce the time people spend receiving insurance, reducing overall costs.

42. The Forum, however, proposed that the levy would fund the costs of entitlements, administration, and case management. Case management is the process of a case worker or manager engaging one-on-one (whether in person or over the phone or online) with a claimant to identify their aspirations for their return to work and potential barriers to that, and then providing related support or referring the claimant to existing support provided elsewhere. The levy would not fund additional supports that claimants may need, eg health or employment services.

43. The initial levy estimates have therefore not allowed for the costs of purchasing such services as vocational rehabilitation and other employment support, or training courses.

44. This reflects a strategic choice. The Crown currently funds public health and employment services, and vocational education and training (some co-funded by users, eg students). The crux of the choice is whether to focus on developing the Crown-funded services provided by partners such as MSD that may be required by New Zealand Income Insurance claimants, or to enable the ACC to purchase those services through the levy. Implementation of the services/purchasing could occur at a future point, once more information was known about claimants' need.

45. The availability of training courses, vocational rehabilitation, or employment support could be an important part of supporting New Zealand Income Insurance claimants to return to good jobs. There are gaps in these services (in that they are absent, have limited capacity, or only accessible to specific groups or in certain locations), and the introduction of New Zealand Income Insurance is likely to increase demand further.

46. The Government has reforms and review underway to enhance the availability of publicly funded services. These include the review of active labour market programmes, which is assessing the case for further investment in services to meet existing demand and potential future demand from introducing New Zealand Income Insurance (see Annex Five for further information). The reform of vocational education

[1] Eligibility criteria are in place for many of these supports. MSD provides employment services to help people at risk of poor labour market outcomes prepare for, find, and retain suitable employment that improves their long-term wellbeing. Access is prioritised to people at risk of long-term benefit receipt.

and health and disability sector reforms are addressing issues such as the accessibility of services which will also benefit Income Insurance claimants.

Further considerations and additional choices

47. Public consultation identified a high level of interest in employment services being available alongside income insurance payments. Return to work will be straightforward for many, but some may need additional help, which will vary from person to person.

48. While there is no immediate suggestion of increasing the New Zealand Income Insurance levy to provide funding to purchase services, the SUIGG may wish to retain this option. Provision of services, including prevention initiatives, could potentially reduce scheme costs overall and improve employment outcomes. However, there will be significant uncertainty about what service gaps may exist until the scheme is operational.

49. To this end, the New Zealand Income Insurance scheme legislation could establish a regulation-making power to establish or purchase services where they can demonstrably improve labour market outcomes for New Zealand Income Insurance claimants and provide value for money.

50. Alternatively, the levy use could be limited in legislation to insurance payments, case management (including by third parties) and administration of the scheme, with no regulation-making power permitting the Government to expand this.

Comment

51. Establishing such a regulation-making power would make it more straightforward for the Government to expand the scheme's service offering (and increase levies if necessary).

52. The regulation-making power could incorporate requirements for return on investment (ROI) to constrain establishment and obligate cessation of poor performing initiatives. The ROI requirement could be narrower or broader. For example, investment could be limited to levy-neutral 'spend-to-save initiatives'. Such initiatives could seek to reduce the scheme's overall costs through preventing redundancies, or job separations due to HCD, or reducing the duration of time that people spend receiving insurance entitlements. Or investments could seek to improve employment outcomes (such as long-term wage growth) even if this does not reduce the scheme's costs.

53. In any case, investment would require a sound programme logic, and be subject to rigorous evaluation to test for value for money, and to enable reprioritisation where appropriate.

54. The benefit of the alternative option, to not provide for such a regulation-making power, is that this provides transparency and clarity about the scheme's services and the purpose of the levy. A further benefit is that, by Ministers retaining purchasing choices for active labour market programmes, the Government can determine which services to prioritise and for whom. This avoids the risk of initiatives bypassing appropriate scrutiny. The option prevents potential upwards pressure on either the levy or on the costs of the services due to added competition.

55. Under this option, the scheme's success will rely on complementary active labour market programmes being provided through Crown funding with sufficient capacity to serve those claimants who may need extra help.

C. The Forum has consulted on options for self-employment, but not yet chosen a preferred approach

The Forum's proposal

56. Income insurance schemes struggle with self-employment. Coverage for displacement is especially complex.

57. Covering the genuinely self-employed creates risks of abuse by those who can arrange their affairs to access insurance payments. Covering self-employment also distorts business decisions by shifting business risks from the self-employed to others.

58. However, there are concerns about the number of self-employed in New Zealand who are misclassified as contractors, when they should be employees. Excluding self-employment from scheme coverage is likely to increase the relative cost of employee labour and therefore increase employers' incentives to misclassify employees as contractors to avoid scheme-related costs such as the levy and bridging payment.

59. Excluding the self-employed therefore risks more workers being shifted into a contracting/self-employment model, where they miss out on the rights and protections of employees, and of the scheme. It would be perverse if a scheme intended to protect the vulnerable had this effect.

60. These decisions will impact a large number of people. There are 343,000 self-employed without employees, and a further 182,000 self-employed with employees.

61. Reflecting the trade-offs involved in either covering or excluding the self-employed from income insurance, the Forum's discussion document presented approaches for public feedback. These range from full exclusion to full inclusion, with intermediate options. However, the cost estimates for New Zealand Income Insurance assume the self-employed are excluded from any coverage in the scheme.

    a. Exclude all self-employed workers, or

    b. Compulsorily include all self-employed workers only for HCD, or

    c. Compulsorily include all self-employed workers for both economic displacement and HCD, or

    d. Compulsorily include contractors who depend on a small number of clients (because they have similar characteristics to employees) for both economic displacement and HCD, or

    e. Offer an opt-in scheme for all self-employed workers (potentially with those self-employed who resemble employees compulsorily included) for both economic displacement and HCD.

62. Each of these options has strengths and weaknesses. Option (a) risks excluding misclassified employees and exacerbating misclassification. Option (c) would ensure coverage of misclassified employees, but also cover the genuinely self-employed.

63. Option (b) – covering the self-employed for HCD only is more feasible than for displacement, but the self-employed would need to pay both the employer and employee levy. This would be especially burdensome for vulnerable misclassified workers.

64. Option (d) would cover those self-employed dependent on a small number of clients, as a proxy for employment. This may be infeasible to deliver as the necessary information is not collected, easy to game, and may not target well those self-employed who most resemble employees.

65. Option (e) risks the adverse selection problem, whereby those at high risk of needing insurance opt-in to coverage, while others opt out.

Further considerations and additional choices

66. Feedback from public consultation acknowledged the complexity of including self-employed in the scheme, and views were mixed about whether to cover self-employed or not.

67. Since the discussion document was released, work has also continued on the Better Protections for Contractors (BP4C) project. A tripartite group has recommended changes that would seek to clarify the boundary between employees and contractors. The aim is to reduce misclassification of employees as contractors, by making the decision about how to classify a worker more straightforward and providing more encouragement for employers to get it right up front. The contractors affected (those who most resemble employees) are also those likely to benefit most from New Zealand Income Insurance cover, and whose work (other than their contractor status) is most compatible with that covered by the scheme.

68. These recommendations should improve protections for contractors. This means that the risk of exacerbating misclassification through introducing income insurance without covering the self-employed is somewhat reduced, making this option more attractive than previously.

69. The NZCTU is concerned that any removal of the self-employed in the scheme would create a risk of incentivising further casualisation of workers.

70. To mitigate the risk further, a regulation-making power could be established to define coverage and eligibility for specific groups of self-employed workers who have some of the characteristics of employees, where administration is feasible (including ways to identify all the affected workers).

71. While this adds complexity (such a regulation would need to define the trigger for entry into the scheme for the designated group(s) and how their levies will be collected), it is an option that can be enabled in legislation, changed through regulation, and modified over time as the scheme matures and working arrangements evolve. Workers could be called into scheme coverage for HCD, or displacement, or both.

Comment

72. On balance, the best option appears to be to exclude the self-employed from New Zealand Income Insurance. Officials will do further work on how to include specific groups of self-employed with characteristics compatible with scheme coverage. The SUIGG could also consider establishing a regulation-making power in the legislation to include such groups of self-employed once the policy work has been done. However, it could be complex to design and administer such regulations.

73. This approach avoids the risks of covering the genuinely self-employed, while continuing to do work to identify how to cover those with characteristics compatible with the scheme coverage.

D. The Forum has consulted on an option to extend cover to 12 months for approved training or vocational rehabilitation but not reached a view

The Forum's proposal

74. A claimant's period of entitlements is proposed to be six months (plus a bridging payment, where applicable) and the levy rate has been estimated on that basis. The discussion document sought feedback on whether there should also be an extension provision within the scheme.

75. The discussion document suggested that, if such a provision were to be included in the scheme, it could be a discretionary entitlement to a maximum of 12 months' cover for approved training or vocational rehabilitation[2]. Eligibility criteria would be designed to ensure extensions were well targeted and effective. Suggested criteria included:

- the appropriate services and/or programmes are available and in place (as these are not funded by the scheme)
- there is early identification of training or vocational rehabilitation needs
- for training – there is a clear link between training and labour market demand
- for vocational rehabilitation – the programmes or services support recovery and a return to work
- only courses/services offered by approved providers would be considered
- claimants must report on their progress.

76. A decision is required whether the scheme could allow for extensions of a claimant's cover. This relates to scheme flexibility and effectiveness (on the one hand) and cost (on the other). This decision is required now, as it is a core aspect of the scheme design to include in primary legislation. Details about eligibility for extensions can be determined later and established in regulations made following enactment.

77. A decision will also be required prior to finalising the levy rate about whether to implement the extension provision from commencement of the scheme's operation or to wait.

Further considerations and policy choices

78. Overall, feedback from consultation was mixed. 48% of survey respondents disagreed with extension up to 12 months; 38% agreed. Targeted engagement was more supportive of extensions for vocational rehabilitation than for training to upskill (strongly supported by health and disability sector stakeholders, who noted that with some illnesses people will take longer than six months to recover).

79. Training programmes can cause a lock-in effect, which in general means that starting programmes early in unemployment spells makes it more likely that participants will forego good employment chances. Workers with low skill levels or obsolete skills benefit from training if they obtain skills in demand, which can outweigh the lock-in effect given a low likelihood of employment with their current skills. Further, there is

[2] Vocational rehabilitation means a service (health treatment, case management, employment support) that helps someone with a health problem to stay at, return to and remain in work. See the Waddell Review, 2008 (UK).

evidence that longer courses (between several months and one year) provide greater benefits than short-term courses (up to three months). Longer training linked to a Just Transition programme or Industry Transformation Plan could support Future of Work objectives.

80. Macroeconomic conditions are also a factor: in a recession, the lock-in effect is more likely to be outweighed by the benefits from training.

81. In the case of claimants who have lost work capacity due to a health condition or disability, it is likely that some people will take longer than six months to recover and regain work capacity. Workwise, a not-for-profit organisation that provides integrated mental health and employment services for people with severe mental health conditions, provided figures to illustrate this. Over the three years 1 July 2017 to 30 June 2020, 2,401 of the clients it worked with gained employment. The proportions of people gaining employment over the different timeframes were roughly consistent each year, averaging as follows:

- 52% gained employment within three months
- 25% gained employment within six months
- 24% gained employment within 12 months.

82. Extension provisions do, however, present moral hazard risks and have the potential for poor labour market outcomes. Evidence from international jurisdictions suggests that linking training to duration can create incentives to cycle between periods of (compensated) unemployment and programme participations, leading to longer periods of non-employment.

83. It is also not clear how extended periods of income support will interface with our current ecosystem for student support, or what effects such support would have on demand for vocational education and training.

84. Extensions of cover would also increase the direct cost of the scheme, but these impacts are highly uncertain as officials have been unable to model the likely uptake of extensions based on the settings outlined in the discussion document.

85. The options for SUIGG's consideration are:

    a. provide for possible extensions in future by establishing a regulation-making power that allows the Government to determine the conditions and eligibility criteria under which extensions may be permitted, or

    b. do not provide for extensions.

86. Secondary choices relate to how narrow or wide the conditions and eligibility criteria might be, how to cover costs to the scheme, and the timeframe for implementation.

Comment

87. Establishing a regulation-making power in the legislation would provide for a future increase in entitlements, targeted at claimants who would obtain better labour market outcomes than without an extension. The regulation-making power would allow the Government to determine eligibility criteria. It would also be prudent for the legislation to set out general parameters for the regulation-making power to ensure that return-

on-investment and equity are factored into design of the regulations. NZCTU strongly supports the idea of retaining flexibility to deliver extensions at this stage.

88. At the time a decision is made to ‘switch on’ extensions by making regulations, the levy funds could be assessed and if necessary, the levy rate increased to cover the cost of extensions. In addition, ACC could start using extensions very narrowly, and could trial extensions with different cohorts to learn which claimants benefit.

89. The second option is to not provide for extensions within the scheme. This option increases certainty about scheme costs but means the Government will not have the future flexibility to tailor and target duration of cover, for example in the event of a recession, except by amending the primary legislation.

E. Some levy payers will struggle to meet the cost of the levy and to meet basic costs of living

90. Creating a levy-funded income insurance scheme will enhance support for workers who experience job loss. However, the cost of the levy may also increase the pressure some workers face to meet their essential costs.

The Forum's proposal

91. New Zealand Income Insurance will be funded through a compulsory flat-rate levy of 2.77%, with employers and employees each paying 1.39%, up to an income cap of $130,911. For example:

- a full-time minimum wage worker ($21.20) would earn $848 per week and pay an $11.79 levy per week, and
- a full-time worker on median hourly earnings ($27.76) would earn $1,110.40 per week and pay a $15.43 levy per week.

92. In developing the New Zealand Income Insurance proposal, the Forum considered adopting a progressive levy to reduce the impact of the levy on low-income workers. Introducing levy progressivity – for example through a levy-free threshold – creates a revenue shortfall for the scheme.

93. If this shortfall is to be met by other levy-payers, then the levy rate they face must rise accordingly. The discussion document considered an option for a levy-free threshold of $23,000, roughly estimated to increase the levy rate on income above the threshold by 70-80%. Because the likely increase in the levy rate was so large and entailed significant administrative complexity, the Forum set aside this option.

94. The current proposal does not include any measures to offset the cost of the levy on low-income workers.

Further considerations and additional choices

95. The perceived high cost of the levy has been a major theme from the public consultation on the proposals, particularly through engagement with Māori. Submitters highlighted that the levy would be particularly hard to adjust to in the current inflationary environment, and there was feedback that low-income families should pay no or a low levy. There were also concerns that the employer levy – and bridging payment – would be challenging to meet for employers and may lead to some business closures.

96. Since releasing the discussion document, we have provided initial advice to Ministers about options for levy-relief (2122-4101 refers). Ideally, such relief would:

- be well-targeted (provide timely support to people in need, while excluding others)
- involve minimal compliance costs, and
- avoid further complicating the tax and transfer system.

97. Achieving all these objectives is difficult. Each of the approaches we have explored involve significant trade-offs. Levy relief will also create substantial costs for the Government, or other levy-payers, or both.

98. Earlier analysis suggested that a 'fiscal offset' arising from introducing New Zealand Income Insurance could help to meet (or offset) the cost of providing levy relief. It now looks likely that any fiscal offset will be very modest, and the scheme will be a net fiscal cost taking into account the cost of Crown employer levies payable.

99. We have explored two main approaches to levy-relief:

- introducing a progressive levy so that low-income workers face little or no levy cost. This could be achieved through a levy-free threshold, or varying levy rates based on income, or both. The NZCTU proposed variations of a progressive levy, including a levy-free threshold, variable levy rates,[3] or halving the levy rate below a set threshold.
- compensating low-income workers for the cost of the levy, through increasing tax credits, establishing a new tax credit or a refund mechanism, or creating a special tax code.

100. A progressive levy would be poorly targeted and increase administrative and compliance costs:

    a. Any progressive levy structure will create operational complexity for payroll providers, employers who manage their own payroll systems, and Inland Revenue. The more complex the levy structure, the more costly it will be for businesses at a systems level, and the greater chance of genuine error in the levies withheld by employers.

    b. Employers do not collect data on whether their employee has multiple jobs and real-time tracking of individual incomes is not practical, which means it is likely individuals will pay an incorrect levy during the year. This issue also exists for individuals who start work during a tax year. This will reduce the cash on hand for households, and involves an administrative process called a 'square-up'. This is where Inland Revenue calculates everyone's actual liability and sends them a bill (or refund) at the end of the tax year which could create debt issues for some levy-payers.

101. Developing a progressive levy will require an in-depth policy and operational design process. On top of this, payroll providers and Inland Revenue need an 18-month lead in time (at a minimum) to build this levy structure into their systems.

102. Increasing support through existing tax credits would also be poorly targeted as not all of the affected group receive tax credits. This would not further complicate the tax and transfer system – though these tax credits are complex for families and agencies to administer.

103. New forms of support to offset the levy cost – such as a refund mechanism, or a special tax code – could be designed that are well targeted but would be administratively burdensome and add significant complexity to existing arrangements. A higher levy rate will need to be charged to account for this compensation.

[3] An issue with a levy-free threshold is that all levy-payers benefit from it. To use the above example, if a person earns $50,000, the first $23,000 would be subject to a levy-free threshold. To address this, the NZCTU proposed a variable levy rate, so that higher income earners would not benefit from the levy-free threshold.

104. Several work programmes across government are currently analysing the impact of proposals on incomes for low-income families, and whether additional support may be required through the tax and/or transfer systems. Providing additional support via the tax and transfer system may therefore set a precedent for other work programmes.

105. NZCTU would support a progressive levy being enabled through the legislation.

Comment

106. As currently designed, New Zealand Income Insurance will impose additional costs on low-income workers. Introducing the scheme requires either accepting these impacts or adopting one (or a combination) of the levy-relief approaches described above.

107. An early decision on this question would provide a clear signal to levy-payers, payroll administrators, and the agencies delivering New Zealand Income Insurance.

108. In announcing the introduction of New Zealand Income Insurance, Ministers may wish to indicate their preferred approach to levy relief.

F. The Forum has committed to tripartite and Māori representation in governance, but not settled on specific governance arrangements

The Forum's proposal

109. Governance comprises the arrangements and practices that allow an organisation to set its direction and manage its operations to achieve its outcomes and fulfil its accountability obligations.[4] Effective and efficient governance will be important to the New Zealand Income Insurance scheme's success.

110. While boards of directors are a central element of governance, a governance system is much wider than just the composition and make-up of the board. Governance as a system includes:

- the roles and expectations of ministers
- the board as a collective
- monitoring arrangements, and
- empowering legislation.

111. The Forum has called for social partner and Māori representation in governance. Māori participation contributes to meeting the Crown's obligations under Te Tiriti o Waitangi. Social partner participation ensures that New Zealand Income Insurance continues to benefit from employer and employee perspectives.

112. There are also other groups with a legitimate interest in contributing to the scheme's governance, such as representatives of the health and disability community.

113. The discussion document identified a range of opportunities for participation in governance by social partners and Māori, including membership of the board, and advisory roles to the board.

114. Since ACC is a Crown entity, the starting point for governance of New Zealand Income Insurance is the framework set by the Crown Entities Act 2004. This includes a requirement that board members are appointed based on the skills required to govern a Crown entity. Subject matter expertise relevant to the organisation is also important; in the case of ACC that includes investment, insurance, and customer experience expertise. The skills required for each Crown entity are described in a 'skills matrix' that reflects its business.

115. Because the discussion document provides only a general description of governance choices, the SUIGG needs to consider this matter further.

Further considerations and additional choices

116. There has been limited public feedback on governance. Many submitters and survey respondents have questioned whether the scheme design and governance has been adequately co-designed with Māori. Iwi Leaders have been clear that they wish to see a strong role for iwi through co-governance of the scheme.

117. This view is reinforced in analysis of the proposals commissioned by the Pou Tangata Skills and Employment Iwi Leaders Group:

[4] https://oag.parliament.nz/good-practice/governance/the-basics

"Rather than a 'tick-box' consulting exercise, co-governance in this instance would mean representation and participation across all levels of decision-making. This would further ensure that the scheme is designed from within a Māori ecosystem, embedded in a Kaupapa Māori worldview, supported by a critical understanding of labour market issues for Māori."

118. That analysis also highlights the importance of accountability to Māori, a kaupapa Māori approach to design and delivery of the scheme, and a recognition of Māori data governance.

119. NZCTU has been clear that it sees a continued role for social partners in direction and oversight of the scheme. Ideally, this would include a representative seat on the board for the scheme. NZCTU is concerned that a non-representative option, ie where a person is appointed on the recommendation of a social partner but whose obligations are to the board and ACC, does not sufficiently protect or reflect the interests of the various groups. NZCTU would like to see a board with oversight of the part of ACC that is responsible for New Zealand Income Insurance, separate to that of the main ACC board.

120. BusinessNZ want to ensure that employers' perspectives are represented in decision-making.

121. Through discussions between officials, the social partners and iwi leaders we have identified two options for participation in governance:

   a. provide for representatives of social partners and Māori to be appointed to the board in a representative capacity, or

   b. a package consistent with the Crown Entities Act 2004:

      i. broadening the skills matrix for the ACC board to include employer and employee skills and experience, and knowledge of te ao Māori. Create a mechanism for representative bodies (of Māori, employers, and employees) to nominate candidates for board positions, for consideration by the Minister in making board appointments, and

      ii. require ACC to identify opportunities for Māori, representatives of employers, employees, and the HCD community to participate in aspects of governance below the board level (such as advisory boards, and board sub-committees), and

      iii. consider how to monitor the functioning of the wider 'return-to-work' ecosystem and create roles for iwi/Māori, employers, and employees in that monitoring function.

Comment

122. The two approaches described above present very different choices.

123. The first option would provide the most direct voice for those partners in the governance of the scheme. However, it potentially creates complexities for the operation of the board as the representatives will have twin accountabilities – to their

appointing or electing organisation or body[5], and to the ACC and prudential operation of the scheme and its outcomes. NZCTU has advocated for establishing a separate board for the part of ACC responsible for delivering the scheme. However, a separate board would create complexity and ambiguity in determining which board is accountable for which dimension of entity performance.

124. The second option provides an opportunity for participation at different levels of the scheme's governance – board operations, advice to the board, and performance monitoring.

125. Crown entity boards comprise directors appointed for their skills in delivering the entity's outcomes, rather than directly representing other groups. Procedural obligations could be established for the responsible Minister to seek nominations from the social partners and Māori and to widen the skills matrix to ensure the ACC board includes people with relevant social partner and te ao Māori skills and experience. However, this approach may not protect the interests of the partners to the same extent as appointments in a representative capacity.

126. Decisions on sub-board level governance arrangements are not required now. It will be useful for these decisions to be informed by the wider organisational changes the ACC will make to establish New Zealand Income Insurance, and the development of the wider 'return-to-work' ecosystem of which New Zealand Income Insurance will be a part.

127. The concept of an ecosystem recognises that a number of partners contribute to supporting workers return to good jobs, and that it is useful to assess performance at a system level and not just at the level of individual agencies.

[5] An appointment or electoral process and structure would need to be defined in legislation for each of the partners to be represented.

G. Excluding temporary visa holders from coverage is widely regarded as inequitable

The Forum's proposal

128. The Forum has proposed levying those migrants with a temporary right to work in New Zealand, while excluding them from New Zealand Income Insurance coverage.

129. How New Zealand Income Insurance treats migrants with temporary work rights is a significant issue since they comprise a large group of the workforce.

130. In June 2019 there were 268,883 temporary migrants with work rights. The number is expected to rise this year with border restrictions easing.

131. The Forum's discussion document proposed that migrants on resident visas would pay the same contributions and receive the same benefits as New Zealand citizens. Working holiday makers, international students and other temporary work visa holders would not be eligible for coverage by the income insurance scheme.

132. To ensure this approach does not disadvantage New Zealand job seekers through reducing the cost of temporary migrant labour relative to residents and citizens, the Forum proposed that working holiday makers, international students and other temporary work visa holders – and their employers – would still contribute to the scheme's costs.

133. The discussion document acknowledged, however, that charging levies without providing coverage is inequitable. The cost estimates for New Zealand Income Insurance assume all temporary visa holders pay levies and receive insurance entitlements. This approach to the costing was necessary because it was not possible to identify and isolate temporary visa holders from residents and citizens.[6]

Further considerations and additional choices

134. Public engagement revealed concern that the exclusion of temporary migrants from coverage, while requiring them to pay the levy is widely considered inequitable. The NZCTU has also called for reconsidering temporary workers' access to New Zealand Income Insurance.

135. The SUIGG may wish to consider an alternative option to provide coverage for temporary migrants in circumstances where they have a greater connection to New Zealand. Of several identified options, the preferred alternative is to levy all holders of temporary work visas and allow those with two years' residence in New Zealand to access the scheme[7]. This would be consistent with access to entitlements under the Social Security Act.

[6] The effect of this assumption is to overstate the scheme's operating costs, and hence the levies required to pay claims. The current approach of levying temporary workers, but not entitling them to receive income insurance, serves to subsidise residents and citizens.

[7] Note that two years' residence as the holder of temporary visa is not the same as holding a residence visa.

Comment

136. The alternative option strikes a balance between the inequity of levying temporary workers but not covering them, and the labour market risks of either granting them access to income insurance or excluding them from coverage and levies.

137. This option requires the temporary migrants to demonstrate a connection to New Zealand, ensuring that those migrants who are well-established here would receive support to find good jobs if displaced or if they lost work capacity through a health condition or disability.

H. Requiring a contributions history could be inequitable, and do little to address abuse

The Forum's proposal

138. Social income insurance schemes usually require claimants to satisfy minimum contribution or employment requirements before they can access support.

139. The discussion document proposed a contribution history of six months over an 18-month period preceding the claim for eligibility. The contributions may be across multiple employers and may include statutory parental leave (both paid parental leave and unpaid leave). The proposed contribution history requirement is low by OECD standards.

140. The contributions history requirement has three purposes. Firstly, the contributions period was intended to help mitigate gaming risks. A contributions history means claimants would need to show a strong connection to the labour market before qualifying for income insurance payments.

141. Secondly, the contributions period was intended to foster a sense of reciprocity, whereby a person must contribute to the scheme before claiming support. The requirement for six months employment in the previous 18 months matches the entitlement to up to six months' insurance cover over 18 months. Such a reciprocal contributions history could promote the scheme's social licence.

142. Thirdly, the contributions history was expected to help contain costs, by reducing the number of insurance claims.

Further considerations and additional choices

143. Public consultation revealed support for the idea of requiring a minimum level of contribution prior to eligibility, in the spirit of reciprocity, though only a narrow majority of survey respondents (52%) agreed with the proposal.

144. The consultation also revealed concern that some would struggle to meet the minimum requirement, especially those already facing disadvantage. Others noted that neither private insurance schemes, nor the accident compensation scheme require minimum contributions periods.[8]

145. The Pou Tangata Skills and Employment Iwi Leaders Group has expressed particular concern about the disproportionate impact of the contribution requirements on Māori and recommended revisiting the policy.

146. Household Labour Force Survey data provides a broad indication of the percentage of people made ineligible by the contribution history requirement, showing some disproportionate impacts, including a modest disproportionate effect on Māori and a significant disproportionate effect on young people:

[8] These schemes can avoid contributions requirements in part because other levy/premium payers contribute to scheme costs, and because a person who claims after only a brief 'membership' of a scheme may subsequently contribute for an extended period before they claim again, if ever.

	% of people made redundant, laid off, or business closed who don't meet contribution history	% of people who lose work due to sickness, illness or injury who don't meet contribution history
Overall population	12%	14%
Māori	17%	15%
Pacific peoples	13%	17%
Women	13%	15%
15 – 17-year-olds	41%	28%

147. Further consideration also suggests that requiring a minimum contributions history is unlikely to mitigate gaming risks significantly. A lengthy contributions period does not affect a worker's or employer's incentives to lodge a spurious claim for income insurance. Critically, claims for insurance require the cooperation of employers and employees. The principal role of the bridging payment is to discourage collusion between employers and employees to lodge such spurious claims. The bridging payment is expected to be a more effective brake on abuse than prior contributions.

148. In the case of HCD claims, requirements for medical certificates by health practitioners will be the key check on spurious claims, rather than contributions.

149. The full range of options for SUIGG's consideration are:

    a. maintain the contribution history requirement, or

    b. reduce the contribution history requirement, or

    c. remove the contribution history requirement for eligibility.

Comment

150. While the contributions history requirement is unlikely to reduce gaming risks and does disadvantage those with a limited labour market attachment, reducing or removing it would increase the cost of the levy significantly and this would especially affect low-income earners.

151. For example, reducing the contribution history to three months over an 18-month period would increase scheme costs by an estimated additional 6-10% for the economic displacement side of the scheme and around 16-18% for HCD. Complete removal of the requirement will increase costs further.

152. For this reason, maintaining the existing, relatively low, contributions history requirement is preferred. It may be possible to reduce the contributions history requirement after the scheme has operated for some time, if it proves to be a significant barrier to accessing the scheme and when the true cost of operating the scheme is clearer. It would be more challenging to introduce (or extend) a contributions history requirement than to do the reverse.

I. The Forum has not yet agreed to a process for setting levies

The Forum's proposal

153. The discussion document sought feedback on high-level levy settings, for instance whether the scheme should be funded by compulsory levies, how levies should be shared between employees and employers, whether levies for HCD and redundancy should be set separately, and whether levies should be subject to an income cap (indexed).

154. Public feedback was mixed on a number of the questions, but no principled arguments were put forward that alter the preferences expressed in the Forum's proposals.

Further considerations and additional choices

155. In addition to these settings, a number of additional procedural parameters that need to be legislated also need SUIGG consideration. These are:

    a. levy setting process and frequency, and

    b. funding principles.

Levy-setting process and frequency

156. An initial levy has been calculated based on the scheme specification in the discussion document. Over time the levy will need to increase or decrease over time as more data becomes available and scheme experience changes.

157. Establishing a clear and robust levy setting process will support scheme transparency and financial sustainability and will help to maintain public confidence.

158. It is proposed that key requirements be set in legislation, in support of a broader legislated and operational levy-setting process (see Annex Three), namely requirements for:

    a. the Minister to establish a funding policy, to give practical effect to legislated funding principles (discussed below)

    b. ACC to publicise an annual statement of the financial condition and outlook for the scheme

    c. the ACC/IIS Board to recommend to the Minister the need for a levy review if this is required earlier than the default interval (based on the scheme's financial condition)

    d. periodic review of, and consultation on, levy rates at intervals not longer than three years (ie sooner, if recommended by the ACC/IIS Board).

159. The scheme will differ in two key respects from the accident compensation scheme. Its funding model will be:

    - simpler than the accident compensation scheme's fully funded model, and
    - reliant on Crown lending, entailing a more prescient risk for the Crown.

160. Therefore, it is appropriate to consider whether a slightly simpler, Minister-led levy process could be warranted for the new scheme. This would involve the Minister leading consultation on levy changes and making final decisions on adjustments to the levy (through an appropriate regulation-making power).

161. The key advantage of the Minister-led option is that it more clearly separates responsibilities for levy-setting from the scheme's operation, which could strengthen public confidence in the scheme's funding process. This option would also simplify the process slightly and ensure trade-offs between scheme and Crown risk (scheme debt-funding) were considered in equal measure. However, this latter consideration could also be managed in an explicit way via specific parameters set in funding policy. It would be important in this option to ensure that Minister was required to seek ACC's expert advice on the actuarial and other relevant considerations before consulting on any levy options.

Overarching funding principles

162. It is proposed that the legislation establish:

- overarching funding principles, and
- provision for more a more detailed, prescriptive funding policy (that has regard to the overarching funding principles), to be established according to ministerial directive.

163. Establishing overarching funding principles will ensure levy-setting and stewardship of funding is guided by clear and consistent objectives over time. Given it would be set in legislation, the principles would need to provide sufficient detail to be meaningful, but also latitude for specific scheme funding parameters to be adapted to differing contexts over time in the funding policy.

164. The following overarching funding principles are proposed, having been developed with reference to accident compensation scheme funding principles (s 166A) and Treasury principles for setting charges in the public sector (see Annex Four for more detail)[9]:

a. Sustainability, resilience: a key principle for the long-term credibility of the scheme

b. Levy stability: levies should be set to look through fluctuations in cost and revenue impacts as far as practicable.

c. Economic efficiency: levy rates should avoid either over- or under-collection as far as practicable, recognising each state entails cost.

165. Additionally, it is proposed that the following general principles underpin the levy framework:

d. Transparency and accountability: in terms of the levy, the approach to levy-setting, scheme financial condition, and scheme equity.

e. Clearly defined use of funds: levy funds should only be used for scheme purposes (which is subject to scope choice, described in section H above) and be used effectively and efficiently.

Comment

166. The Working Group broadly agrees with the proposed levy process and funding principles.

[9] The Treasury (2017). Guidelines for Setting Charges in the Public Sector.

J. Bridging payments for medical dismissals could be unnecessary, and discourage hiring of people with health conditions and disabilities

The Forum's proposal

167. The Forum has proposed that employers pay a four-week bridging payment when making an employee redundant or dismissing an employee on medical grounds. Bridging payments seek to prevent avoidable job losses.

168. In the case of medical dismissals, the bridging payment aims to incentivise employers to make best efforts to support HCD claimants to return to work rather than choose to dismiss them on medical grounds. The discussion document noted that bridging payments were less relevant for HCD claimants but proposed that a bridging payment would be paid by employers to all workers who are medically dismissed while on New Zealand Income Insurance.

Further considerations and additional choices

169. The case for proceeding with the HCD bridging payment is not as strong as for displacement and may even harm employee interests.

170. Employers are likely to have already made efforts to support HCD claimants ahead of decisions to end the employment relationship. Existing obligations require employers to ensure deliberation is fair and actions reasonable, including considerations such as the likelihood and capacity of an employee to return to work.

171. It is understood that medical dismissals are relatively rare, and the New Zealand Labour Law Society noted that, in their experience, most medical dismissals are for terminal illness. A number of submitters to the public consultation considered that imposing additional costs on employers for health and disability matters outside of their control would be unfair.

172. The medical dismissal process is relatively onerous and can take weeks or even months. This is likely to provide a sufficient "grit" in the system to make employers carefully consider medical dismissals. As such, the introduction of a bridging payment requirement may not influence medical dismissals in the same way as it would redundancies.

173. Further, requiring a bridging payment for medical dismissals could just as likely create a further disincentive to employers hiring disabled people or people with health conditions and will create an inconsistency between how medical dismissals for health reasons are treated in comparison to medical dismissals for injuries.

Comment

174. For the reasons discussed above, the SUIGG may wish to consider removing the proposal that employers be required to make a bridging payment to claimants dismissed on medical grounds.

175. Since only a small number of HCD claimants would likely qualify for a bridging payment, removing the entitlement is not likely to disadvantage many people. It will also not significantly alter the existing difference between the maximum base coverage for displacement claims (a four-week bridging payment plus six months' income insurance payments) and HCD claims (six months' income insurance payments, with a small possibility of a bridging payment).

K. Standard bridging payments and notice periods may be impractical for fixed-term and casual employees

The Forum's proposal

176. The Forum proposes a four-week notice period and four-week bridging payment paid by the employer to workers who are made redundant. The notice period provides early warning to workers (and the ACC) of the displacement, and the bridging payment seeks to mitigate the risks of unnecessary and spurious redundancies by imposing a cost on employers who make employees redundant.

177. However, there are difficulties with designing appropriate employer obligations for fixed-term and casual employees:

    - A standard four-week notice and four-week bridging payment may be disproportionately generous for very short-term and uncertain work and impose undue costs on employers.
    - For casual employees, there are no guaranteed hours of work, and their hours can be reduced close to zero in order to avoid any notice and bridging payment obligation by the employer.

178. The discussion document therefore proposed that the bridging payment would be paid to fixed term employees, including seasonal workers, but pro-rated if job loss occurs in the four weeks immediately prior to the contracted end date (so that an employee could be paid till the contracted end date, and not beyond it).

Further considerations and additional choices

179. The public consultation revealed support for providing meaningful coverage for people engaged in casual, seasonal, and fixed-term employment while also noting the difficulties in verifying when these groups experience a no-fault loss of employment.

180. The choices for a providing fixed-term and casual employees with an entitlement that recognises a right to a notice period and bridging payment for either a pro-rated approach (one method of pro-rating was included in the discussion document) or a wage-loading approach (where workers receive an additional payment on top of their wages instead of being entitled, as other workers are, to a notice period and bridging payment in case of job loss.

181. Both options require choices about how to calculate the amount paid, or the length of notice provided, to workers. Any calculation should ensure there is enough notice and income replacement so that workers can find good work, but not so much that employers are required to pay employees beyond the period they agreed the contract would end, or for a period disproportionate to the length of time worked for that employer

Pro-rating approach

182. We have identified a pro-rating approach based on length of employment already completed (with no bridging payment extending beyond the contracted end date). This approach allows for fixed-term and casual employees to be treated similarly. This approach could also incentivise the use of short fixed-term contracts. Under employment law, fixed-term arrangements are only permissible where there is a genuine reason for the fixed-term nature.

183. A simple and easily understood formula is included in the table below, and applied to the notice and bridging payments for casual and fixed term employees:

	Pro-rated notice period	Pro-rated bridging payment
Casual employees		
Length of time in that employment:	Employer required to offer at least 80% of average hours worked over preceding 3 months	
> 6 months	4 weeks	4 weeks
> 3 months	2 weeks	2 weeks
< 3 months	1 week	1 week
Fixed-term employees		
Total length of rolled-over fixed contracts from current employer:		Whichever is sooner of the contracted end-date or end of pro-rated bridging period:
> 6 months	4 weeks	4 weeks
> 3 months	2 weeks	2 weeks
< 3 months	1 week	1 week

184. An alternative would be to provide for a 'loading.' The loading approach would require employers to pay an additional loading on the wages of people engaged in casual and fixed-term work instead of carrying the obligation for notice and bridging payment. It would operate similarly to Pay-As-You-Go (PAYG)[10] where payment of at least 8% on top of wages can be made in lieu of the employee's annual entitlement.

Comment

185. Discussions between officials and social partners have concluded that the scaling approach is preferable. It is the lowest risk and is administratively simpler. It is strongly preferred by the NZCTU. A key benefit is that the formula can be designed to be simple to apply, easy to understand, and reasonably fair. It reduces the incentive to engage workers on a casual and fixed-term basis, because the employer still holds the obligation for payment if a worker loses their job, although there is some incentive effect likely since the obligation is scaled. This option is not without risk and complexity. Since it can be harder to verify the loss of work, there is a greater risk that

[10] PAYG can apply to workers for whom annual leave calculations are not practical: for instance, when a worker cannot request and be granted annual leave to take tomorrow, if there is no certainty that they would have been asked to, or be offered, work tomorrow.

casual and fixed-term employees do not receive notice, bridging, or income insurance payments.[11]

Next steps

186. Officials will draft Cabinet papers setting out the case for change and proposed design features of the scheme to seek policy decisions that will enable drafting instructions to be issued.

187. In addition, officials will continue to:

- develop regulatory impact statements on the case for change and the scheme's detailed design
- develop an implementation business case to inform a Confidential advice to Government
- support development of options for providing additional return-to-work support for New Zealand Income Insurance claimants via the review of active labour market programmes, and
- engage with the SE ILG to bring a Māori/iwi lens to this work.

Annexes

Annex One: Remaining policy choices – preferred approaches or options, and summary of key considerations

Annex Two: Summary of all proposed scheme settings (and remaining choices)

Annex Three: Proposed levy-setting process

Annex Four: Proposed scheme funding principles

Annex Five: Review of active labour market programmes and links with New Zealand Income Insurance

Annex Six: Consultation – further detail on initial findings

[11] This is because employers can terminate casual and fixed-term workers without following the restructuring / redundancy process required for other workers. This makes it difficult to define and verify a no-fault job loss and therefore makes it difficult to provide meaningful cover for this group.

Annex One: Remaining policy choices – preferred approaches, or options, and summary of key considerations

Policy choice	Preferred approaches, or options	Key considerations
A. Coverage of health conditions and disabilities	*Options* 1. Commence coverage for health conditions and disabilities at the same time as coverage for displacement, or 2. Defer commencement of coverage for health conditions and disabilities, or 3. Do not provide coverage for health conditions and disabilities	• Some concern has been raised that: o covering the loss of work capacity due to a health condition or disability (HCD) increases the scheme's cost and consequently the costs on employers, and o commencing coverage for HCD and economic displacement simultaneously introduces risks to implementation of the scheme (as HCD claims introduce more complex eligibility assessment) • Deferring the commencement of HCD cover is unlikely to address the costs concerns, but it may simplify the roll-out of the scheme.
B. Levy use	*Options* 1. Allow levies to be collected and used for the purchase of additional services (through a regulation-making power), or 2. Do not allow levies to be collected and used for purchase of additional services	• Employment and rehabilitation services are important to support people back into good work; some services are currently already provided by the Crown but are likely to be insufficient to meet demand from NZII claimants • NZII cost estimates and levy calculation allow only for insurance payments, provision of targeted and tailored case management, and scheme administration, and do not allow for the purchase or provision of additional services, such as employment services, vocational rehabilitation, or training • Government has several reforms and reviews underway to enhance the availability of publicly funded services that may be beneficial for NZII claimants, including the review of active labour market programmes, the health and disability sector reforms, and the reform of vocational education. • Levy purpose could be broadened to enable ACC to collect and use levies for purchasing employment-related services to close gaps • Funding services from levies is likely to increase the levy rate (unless provision of services reduces insurance liabilities, or the initial levy rate is such that sufficient surpluses are generated) and will have uncertain impacts on the wider government ecosystem of employment supports
C. Coverage for the self-employed	*Options* Exclude the self-employed from coverage (both for displacement and health conditions and disabilities), and: 1. Either: do further policy work on how to include specific groups of self-employed with characteristics compatible with scheme coverage 2. Or: establish a regulation-making power to include specific groups of self-employed with characteristics compatible with scheme coverage	• Self-employed is large portion of the labour force (343k self-employed without employees, 182k with employees) • Coverage of self-employed not costed in initial NZII levy • Exclusion from coverage worsens misclassification risks, but inclusion creates moral hazard risks ('self-redundancy') • Difficult to design an option that effectively covers misclassified employees while excluding the true self-employed • 'Better Protections for Contractors' project aims to reduce misclassification • Providing for regulations to be made in future would enable us to consider specific characteristics that would be compatible with coverage, but will create expectations that these will be part of the scheme

Policy choice	Preferred approaches, or options	Key considerations
D. Extensions for approved training or vocational rehabilitation	*Options* 1. Provide for possible extensions in future by establishing a regulation-making power that allows the Government to determine the conditions and eligibility criteria under which extensions may be permitted, or 2. Do not provide for extensions.	• Discussion document sought views on the option of allowing ACC to extend the duration of claimants' entitlements up to 12 months for approved training or vocational rehabilitation • Creating a regulation-making power would not commit the Government to enabling extensions, but will create expectations that these will be part of the scheme • Unclear how extended periods of income support will interface with current ecosystem for student support, or effects on demand for vocational education and training • Extensions of cover would also increase the direct cost of the scheme, but impacts are highly uncertain

E. Levy relief	*Options*
	1. Provide only for a flat levy rate in the scheme and continue work on alternatives for levy relief, or
	2. Include a regulation-making power to enable a progressive levy to be set and commence work to design the levy structure
		• Some working families will struggle to meet the cost of the flat-rate levy for the scheme
		• Options for levy relief have significant drawbacks and would require significant further work before implementation:
		  ○ develop progressive levy rates: this would significantly increase levies for mid- and higher-income workers, would be poorly targeted, and would add administrative cost
		  ○ provide some form of Crown compensation for low-income households: this would be difficult to target, likely involve significant fiscal trade-offs and be administratively complex
		• If a progressive levy is to be developed, the legislation will need to provide for this within the levy-making power; this may create an expectation of a progressive levy being set when it may not be a feasible option
		• Challenging to move to a progressive levy if the scheme begins with a flat levy rate
		• Equally, making provision for compensation through the tax and transfer system is likely to be challenging
		• Desirable to confirm approach to levy structure to provide certainty for levy-payers, payroll administrators, and implementation agencies

F. Governance	*Options*
	1. Provide for representatives of social partners and Māori to be appointed to the board in a representative capacity, or
	2. A combination of measures to embed the perspectives of social partners and Māori:
	  a. Widen the ACC board skills matrix to enable it to make decisions that incorporate the perspectives of workers, employers and te ao Māori, and
	  b. Establish obligations for the Minister to seek board nominations from the social partners and Māori and to give those nominations due consideration, and
	  c. Require ACC to identify opportunities in sub-board level aspects of scheme governance for representatives of social partners, Māori, and disabled people (board sub-committees, advisory boards), and
	  d. Consider roles for social partners and Māori in monitoring the wider return-to-work ecosystem
		• Future of Work Forum called for governance of the scheme to include tripartite and Māori representation
		• Crown entity boards comprise directors appointed for the skills they contribute to the board's overall skillset to deliver the entity's outcomes, rather than directly representing a second entity or organisation
		• Appointing representatives of social partners and Māori to the board, to act in a representative capacity, would:
		  ○ provide the most direct voice for those partners in the governance of the scheme, but
		  ○ entail twin accountabilities for those representatives – to their own nominating organisations and to ACC – leading to a complex governance model

Policy choice	Preferred approaches, or options	Key considerations
G. Temporary visa holders	*Preferred approach* Levy all holders of temporary work visas and allow those with two years' residence in New Zealand access to New Zealand Income Insurance, consistent with access to entitlements under the Social Security Act 2018	• Discussion document proposed to levy temporary work visa holders, but to exclude from coverage because this preserves employment opportunities for New Zealand citizens and residents • Public feedback has indicated significant concern that levying but not covering holders of temporary work visas is inequitable • Exempting from levy payment would lower cost of migrant labour relative to residents/citizens
H. Contributions history requirement	*Preferred approach* Maintain the proposed contributions history requirement for eligibility of six months' contributions over the previous 18 months	• The contributions history requirement proposed in the discussion document creates access barriers for some groups of workers – particularly young people, and to a lesser extent Māori • Removing the contributions requirement is likely to raise levy costs substantially which would exacerbate the affordability concerns for low-income workers in particular
I. Levy-setting process	*Preferred approach* A process led by minister(s) with clear accountabilities for ministers, MBIE and ACC, which would provide expert technical input and robust advice	• ACC's expert advice on the scheme's performance will be required to develop cost estimates when NZII levy rate needs to be set • Levy-setting and associated public consultation could be led by the ACC (as for accident compensation levies currently) • A minister-led process could give ministers more choices in the range of levy options consulted upon, given that Ministers are responsible for the final choices of levy rate

J. Bridging payment for a medical dismissal due to a health condition or disability	*Preferred approach*
	Do not require a bridging payment for medical dismissals due to a health condition or disability
		• Discussion document proposed requiring employers to make a bridging payment when dismissing employees due to their health condition or disability
		• Requiring a bridging payment in this situation:
		  o could reduce employment opportunities for people with existing health conditions and disabilities
		  o would not introduce any additional disincentive for employers to not dismiss a worker on medical grounds
		  o could create boundary issues in determining distinctions in dismissals for health reasons as opposed to those based on injury

K. Bridging payments and notice periods for fixed-term and casual employees	*Preferred approach*
	Pro-rate notice periods and bridging payments for fixed-term and casual employees:
	a. 1-week notice period and 1-week bridging payment where length of current employment is under 3 months, and
	b. 2-week notice period and 2-week bridging payment where length of current employment is between 3 and 6 months, and
	c. 4-week notice period and 4-week bridging payment where length of current employment is more than 6 months, and
	d. For fixed-term employees, in all cases the maximum length of a bridging payment will not extend beyond the contracted end date to the employment
		• A 4-week notice period and 4-week bridging payment may not be appropriate for fixed-term and casual workers who are displaced:
		  o Could encourage employers to avoid obligations through a gradual wind-down of casual hours
		  o Durations of employment may be short, meaning employers could face disproportionately high costs for short-term and uncertain contracts
		• Discussion document identified pro-rating as a potential approach

Annex Two: Summary of all proposed scheme settings (and remaining choices)

Proposed setting in discussion document	Remaining policy choices
Coverage for displacement	
• Would cover displacement (loss of work, due to the disestablishment of a job)	
• Would not cover job loss due to poor employee performance, gross misconduct, or resignation	
• 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 working arrangements	
• Would cover most working arrangements	
• Full- and part-time permanent employees (casual and fixed-term employees whose pattern of work resembles permanent employment, and who have an expectation of future income, would also be treated as permanent)	
• Fixed-term and casual employees (where displacement prevents completion of time-limited employment agreements, with entitlements covering the remainder of the employment agreement)	
• Seek to cover those self-employed people who most resemble employees	Should the scheme cover self-employed and if so how
Coverage dependent on minimum contributions, with limits for subsequent claims	
• Workers would need to have contributed to the scheme for six months or more over the 18 months preceding the claim	Should eligibility be contingent on a contribution history and if so what level of contributions is required
• Statutory parental leave (paid and unpaid) would be included in the qualifying period	
• A limit would apply so workers could only claim up to a total of six months of entitlements every 18 months	

Proposed setting in discussion document	Remaining policy choices
Coverage provided for New Zealand citizens and residents	
• Insurance payments would be made available to New Zealand citizens and residents only	Should temporary visa holders be eligible for cover
Entitlements for displaced workers	
• Provide income replacement rate of 80% of prior income (up to a cap of $130,911, adjusted annually) for a maximum of six months (see 'employer support' and 'help to return to work' for bridging payment)	
• 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	
• 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	
• Feedback sought on option of enabling extensions to a maximum of 12 months' cover for the purpose of approved training or vocational rehabilitation	Should entitlements be able to be extended
Entitlements generally treated as income for social security payments	
• MSD and IR would generally treat insurance payments as income, for welfare and tax purposes	
Employers to support the scheme's operation	
• 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	What should the bridging payment and notice period be for fixed-term and casual employees

Proposed setting in discussion document	Remaining policy choices
Coverage and entitlements for loss of work capacity due to a health condition or disability	Should the scheme cover loss of work capacity due to a health condition or disability If yes, should commencement for HCD coverage be deferred
Similar provisions for displacement and loss of work capacity due to a health condition or disability	
• 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 health condition or disability that leads to a significant reduction in work capacity, and coverage for all working arrangements	
• Would cover any health condition or disability 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	
• Would cover all working arrangements (with all forms of self-employment fully covered)	Should self-employed be covered for loss of work capacity due to a health condition or disability
Health practitioners and employer to certify the effect of the health condition or disability on work capacity	
• 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.	
• 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.	

Proposed setting in discussion document	Remaining policy choices
Employers to help workers return to work and keep jobs open	
• Employers would take reasonable steps to support an employee to continue working (including workplace changes or redeployment where possible) before the employee stops work.	
• Employers would make reasonable efforts to protect the job where a reasonable prognosis is made of a return to work within six months	
• If an employer decided that an employee had to be dismissed because of their health condition or disability the same notice and bridging payment would apply as for displacement	Should there be a bridging payment for workers dismissed due to a health condition or disability
Insurance claimants' obligations	
Claimants to search for work, with payments suspended in cases of serious non-compliance	
• Expected to be based in NZ, to search for suitable employment or to prepare for employment (with deferrals for those in certain circumstances, eg approved training, participating in an ALMP, recuperating from acute phase of health condition),	
• 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	
• Expected to provide subsequent work capacity medical certificates (similar to those used by ACC or MSD) if required	
• Expected to engage in return-to-work activities where relevant and required	
• Work obligations could be deferred on guidance by health practitioner	
Delivering Income Insurance	
Scheme to be administered by ACC	

Proposed setting in discussion document	Remaining policy choices
• Employers or workers could lodge claims with ACC, which would administer the scheme	
• Governance of the scheme would include tripartite and Māori representation	What is the preferred approach to social partner and Māori/iwi representation in governance
• Could begin operating in 2023 at the earliest	
Scheme would help people return to good jobs	
• Would operate a case management system and connect people with support to find or prepare for work	
• Partner agencies could provide support to claimants to search or prepare for work, where appropriate	
• 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	
• Would operate an efficient and independent dispute resolution process, with multiple escalation steps where needed	
Scheme would take enforcement action where necessary	
• Would take appropriate action to collect levy payments, and to deter and respond to misrepresentation	
ACC would require high quality and timely information to deliver the scheme effectively and efficiently	
• ACC will develop information-sharing agreements and arrangements with employers, other agencies, and service providers	
• 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	

Proposed setting in discussion document	Remaining policy choices
Funding income insurance	
Costs of the scheme to be shared between employers and workers	
• 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.	What is the process to adjust the levy to meet the scheme's future costs
• Proposed initial levy of 2.77% of salary and wages, split between employers and employees (1.39%). Includes GST and administration costs.	
• 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.	
• Crown would act as funder and/or lender of last resort when required. Could be through repaid levies. Scheme's legislation would provide the flexibility to vary entitlements and eligibility in times of economic crisis. This could include extending maximum entitlement periods or using the scheme to administer a wage subsidy. This could require Crown funding.	
• Levy pays for insurance payments, case management and administration of the scheme	What can the levy be used to purchase

Annex Three: Proposed levy-setting process

The levy process proposed is outlined below.

What	Description and rationale	Who/how
Overarching funding principles – legislated	To provide certainly over time on what the funding objectives are for the scheme, similar to the accident compensation scheme's principles of financial responsibility (s.166A). Legislative certainty is required to provide confidence in the scheme's sustainability. Given it would be set in legislation, the principles would need to provide sufficient detail so as to be meaningful, but latitude for the scheme to flex in different contexts.	Parliament/Legislation
Funding policy – process legislated for, but substantively created by Ministerial directive	The funding policy would give practical effect to legislated funding principles. Given it could be periodically updated as context required, it could be detailed (eg establishing limits on levy increases, debt repayment timeframes, etc).	Minister, as a Ministerial directive (likely Cabinet agreed)
Scheme financial condition statement - requirement legislated for, but substantively operational	For ACC to annually publicise a statement of the financial condition and outlook for the scheme. This could include a forecast of out-year levy requirements for instance (determined according to the funding policy). This could be a separate document or delivered as part of annual reporting.	ACC, given technical expertise
An ability to recommend to the Minister the need for a levy review – legislated process	Shorter review periods are mainly envisaged to be required in exceptional circumstances where the scheme's funding state had deteriorated so as to require a change in levy or debt repayment terms. It could also however be invoked if the scheme established an unduly large surplus (a potential scenario through establishment).	ACC/IIS Board

What	Description and rationale	Who/how
Review and consult on levy rates – legislated process	Review and consultation would be at intervals not more than three-yearly (or sooner if recommended by the ACC/IIS Board). This is to ensure that scheme funding requirements are regularly socialised, and the scheme is properly funded.	Option 1: ACC/IIS Board (ACC) consults on levy rates (subject to Cabinet agreement) Option 2: Minister (MBIE) consults on levy rates (subject to Cabinet agreement)
Agree levy rates, and amend levy regulations – per normal regulatory process	As per normal regulatory process: • the Minister would recommend any changes to Cabinet • MBIE/PCO would draft regulations, which the Minister would seek agreement to from Cabinet	MBIE/PCO Minister Cabinet

Annex Four: Proposed scheme funding principles

The proposed funding principles for legislation are outlined below.

What	Description
Funding principles	
Sustainability, resilience	A key principle for the long-term credibility of the scheme is that the scheme should be self-sustaining over time. Claims costs and scheme administration should be funded from the levy and be Budget-neutral post set-up. Resilience refers to the ability to manage cashflow mismatches or liquidity events likely to require Crown balance sheet support. The design should aim to ensure Budget neutrality with no impact on operating balances.
Levy stability	ACC and other scheme research suggests levy-payers value levy stability (eg for managing cashflow). Levies should be set to look through fluctuations in cost and revenue impacts as far as practicable.
Economic efficiency	It is important to avoid either over- or under-collection of levies far as practicable. On the one hand this entails an opportunity cost within the economy and on the other entails potential for unmanageable deficits.
General governing principles	
Transparency and accountability	The levy, the approach to levy-setting and scheme financial condition should be accessible and understandable to aid public understanding about when and why levies are required to change. There should also be transparency on scheme equity, in terms of how the costs of the scheme are distributed across population groups and across time.
Clearly defined use of funds	Levy funds should only be used for scheme purposes (which is subject to scope choice, described above) and be used effectively and efficiently.

Annex Five: Review of active labour market programmes and links with New Zealand Income Insurance

Summary

There is a broad consensus that the Government's capacity to help people into good work can be enhanced. The proposed introduction of New Zealand Income Insurance is likely to increase demand for ALMPs.

To enhance employment services, there is a range of policy, funding, and operational questions to address. These include questions about what additional ALMPs may be needed and by whom; how they will be funded; and which agency will provide them.

Agencies are working together to address these questions through:

- a review of ALMPs
- development of a case management approach for New Zealand Income Insurance claimants
- the Ministry of Social Development's (MSD) future employment services model.

Together, these closely related projects will provide Ministers with comprehensive advice on the options for enhancing employment services. This includes how to meet the increased demand arising from New Zealand Income Insurance, how New Zealand Income Insurance case management will operate, and how it could connect insurance claimants with any services available from partners.

The ALMP review will provide advice to Employment, Education and Training Ministers in late June 2022. Confidential advice to Government

Decisions on the ALMP review and development of the case management approach for New Zealand Income Insurance are not required for finalising the policy proposals for the scheme, but work will need to track in parallel to ensure successful implementation.

Background

ALMPs are government-funded or government-provided interventions that:

a. actively assist people into employment (including removing barriers to their ability to get or retain a job, or to move between jobs)

b. increase earning capacity, and

c. improve the functioning of the labour market.[12]

[12] As defined for the current review commissioned by Employment, Education and Training Ministers Group. There is a range of ways ALMPs may be defined.

This definition excludes includes vocational rehabilitation services, being whatever helps someone with a health problem stay at, return to, and remain in work.[13] Other types of ALMPs can also provide employment support to people with a health condition or disability.

The core education system is excluded from the definition because it does not actively assist people into employment in the short term. However, vocational education can complement ALMPs. The national careers system, however, does provide ALMPs, such as the Direct Career Service and careers.govt.nz.

There is a broad consensus that the Government's capacity to help people into good work through ALMPs can be enhanced. This was a key finding of the Welfare Expert Advisory Group report, and other expert advice including from the OECD and the New Zealand Productivity Commission. The proposed introduction of New Zealand Income Insurance is likely to increase demand for ALMPs.

To fully explore the options to enhance the provision of ALMPs, a number of questions need to be addressed, including what additional services might be needed and by whom, how these should be funded, and which agencies should provide them.

Further detail is provided below on how agencies are working together to address these questions through:

a. the cross-agency ALMP review (joint MBIE-MSD work)

b. development of the case management approach for New Zealand Income Insurance claimants (ACC-led)

c. MSD's future employment services model (MSD-led).

NZ Income Insurance will increase demand for employment services

The proposed introduction of New Zealand Income Insurance is likely to increase demand for ALMPs, although the quantum of that demand is unclear. Providing ALMPs for New Zealand Income Insurance claimants who require them will be important to achieve the scheme's aim of a return to good work.

New Zealand Income Insurance will provide income replacement, claims management, and case management. Most claimants will be able to return to work using their own resources. For claimants unable to self-manage their return to good work, the case management service will connect claimants to ALMPs provided by partners – if services are available and any eligibility criteria are met. The types of ALMPs claimants might be referred to will depend on need. The New Zealand Income Insurance scheme costs and proposed levy rate do not make provision for funding ALMPs (or health services), beyond case management.

Officials estimate that approximately 135,300 will access New Zealand Income Insurance following either displacement or the loss of work due to a health condition or disability. Further information about estimates is provided below.

[13] Waddell, Burton, and Kendall (2008) state "vocational rehabilitation is whatever helps someone with a health problem stay at, return to and remain in work". It usually involves professional groups or services (including health professionals) working together with the person to support them to return to work.

Estimates of economic displacement

The estimates of the number of economically displaced workers vary greatly: between 39,686 and 125,000 workers annually. The wide variance in the estimates reflects the limitations to the data, which comes from the Household Labour Force Survey (HLFS) that was matched with other Statistics New Zealand data to create displaced worker profiles. The HLFS is survey-based and therefore subject to sampling error, and in some cases, matching was not possible. The data is useful to observe trends and relativities, rather than definitively quantify demand.

HLFS data also helps to shed some light on the characteristics of workers who are displaced due to a health condition, injury, or disability (HCID). The number of people displaced for these reasons is less affected by the economic cycle than workers displaced for economic reasons.

Estimates of displacement due to a health condition, injury, or disability

An estimated 20,000 people are displaced from work each year due to a health condition, injury, or disability. This is an underestimate because it only includes those leaving their jobs permanently and does not include those who still employed but reduce their hours or take extended leave.

ALMP review aims to address gaps in employment supports

A large number of New Zealand Income Insurance claimants are likely to need only self-help online support. However, it is probable that the introduction of New Zealand Income Insurance will increase demand for ALMPs for a number of reasons, including the availability of the scheme and increased awareness that support is available and greater visibility of people who may need support. Some claimants may share characteristics with people currently receiving MSD's employment services and could be in scope for targeted ALMPs.[14] However, some claimants who need support may not be captured in this targeting or meet current eligibility criteria.

The ALMP review, commissioned by the Employment, Education and Training (EET) Ministers Group in 2021, aims to address questions about the sufficiency of support for people including future New Zealand Income Insurance claimants, as well as addressing recommendations from the Welfare Expert Advisory Group.

A gaps analysis completed in December 2021 as part of the review found:

a. A gap in initiatives specifically responding to economic displacement, including early intervention (ie, supports provided before a person's employment ends).

b. Insufficient interventions for disabled people and people with health conditions who have multiple barriers to employment.

[14] MSD's employment services are focused on people at risk of long-term benefit receipt. This includes people not currently on a main benefit. MSD case managers consider a range of factors to determine whether someone is at risk of long-term benefit receipt and therefore prioritised for access to ALMPs. These factors include age and location, employment history and educational attainment, specific barriers to employment (eg medical conditions, caring responsibilities), and benefit status and history.

c. Gaps in early response interventions for people experiencing mental health deterioration and in integrated health and employment supports for people with mental health conditions.

d. A gap in support for women, Māori, Pacific people, and youth to move into training and work opportunities that will lead to higher-skilled roles and industries.

e. The potential for ALMPs to work better alongside the education system to increase opportunities and occupations for earning while learning.

ACC is developing a case management approach for New Zealand Income Insurance claimants

International experience shows that effective case management is a core form of support for income insurance claimants, supporting a timely return to good work.

Many claimants may need no or only limited assistance to return to work, while others will need more. Displaced workers, by definition, have general work skills and specific occupational skills, and an overall high level of work-readiness. However, others will need more intensive support to return to work. One-on-one case management is an expensive intervention. To be effective and cost-efficient, the type and intensity of case management support should be targeted and tailored to need. Promptly identifying the group that needs more support is challenging.

There will be choices to make about the types of one-on-one employment supports New Zealand Income Insurance case managers could provide, ie funded by the levy, and those which are more specialist or intensive and should be provided to claimants who need them through a Crown-funded ALMP. This is a key question for both the ALMP review and designing the case management service for New Zealand Income Insurance.

Similarly, there will be choices about where ACC sources case management services for the scheme. While it is proposed that ACC will have overall responsibility for delivering the scheme, the proposal contemplates ACC and MSD potentially agreeing to each provide particular case management services for different cohorts of claimant. ACC also envisages contracting community-based providers who offer a holistic one-stop-shop approach, especially iwi/Māori providers.

It could similarly contract providers who integrate mental health and employment case management support.

This model could capitalise on the existing expertise of the respective agencies and build on the MSD's future employment services model (further information is provided below). It will also incorporate the New Zealand Income Insurance scheme's guiding principle of letting workers search for work that suits their skills and experience and engage in programmes that help in that search or in retraining.

ACC and MSD are working to develop the case management model. This work is in the early stages. Initial thinking is to triage people based on their transferable skills and their self-efficacy, but more work is needed to develop a streamlined and efficient way to do this using available data. The framework may also include a mechanism to adjust the level of support if a claimant's needs change over time. No decisions have been made about who will deliver employment case management or employment services. SUIGG is considering whether the levy could also be used to fund employment services.

MSD's employment services are refocusing on people with the highest needs

Both the ALMP review and the ACC case management approach are closely linked to supporting displaced workers and people losing work capacity due to a health condition or disability. In addition, MSD has undertaken a broader review of its employment services prioritisation approach.

Cabinet agreed to a future employment services model for MSD on 23 May 2022. Cabinet confirmed that the core objective for MSD's employment services is to help people at risk of poor labour market outcomes prepare for, find and retain suitable employment.

To operationalise this objective, MSD will prioritise providing its employment services, within existing appropriations and eligibility settings, to people who most need employment support to achieve the best outcomes, by:

a. refocusing support on people with a high risk of long-term benefit receipt and other key priority cohorts who interact with the benefit system,[15] whether they are currently on a main benefit or not

b. continuing to support other people on benefit who have fewer barriers to employment, with a level of service proportionate to their needs

c. identifying specific opportunities to support people who are not on benefit and may be at risk of, or experiencing, poor labour market outcomes other than long-term benefit receipt, to be determined by future policy, legislative and funding decisions.

This will be implemented through changes to MSD's investment and prioritisation approach and continued enhancements to its operating model. For instance, MSD's Employment and Social Outcomes Investment Strategy 2022-2025 informs national and regional decisions about how MSD invests in employment services, aiming to achieve sustainable employment outcomes and improve equity, through prioritising four investment changes:

a. increasing the cost-effectiveness of its job placement investment

b. increasing the overall share of investment in cost-effective programmes with work readiness components, particularly training – including for investment targeting young people, Māori, and Pacific peoples

c. increasing the share of investment targeted towards women, older workers, and those over 45 on Jobseeker Support – Health Condition and Disability (JS-HCD), particularly through investment in cost-effective programmes with work readiness components

d. increasing the share of investment in evidence-based interventions to support disabled people, including those with health conditions, into employment.

Cabinet's agreement to the future employment services model sets the intended direction of travel for MSD. It also informs Ministers' consideration of what role MSD will play in providing employment support to NZII claimants. As noted, we do not have clear information on the expected demand for ALMPs from potential NZII claimants, however they will have a range of needs.

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[15] Key priority cohorts include people on benefit who may be further from the labour market and seek additional support to address needs and/or barriers to employment, eg medical conditions, caring responsibilities.

Officials will provide further advice on whether there are any gaps in the prioritisation model that need to be addressed to meet the needs of future New Zealand Income Insurance claimants, including whether any additional ALMPs are needed. This advice will need to consider trade-offs in funding (Confidential advice to Government and ensuring equitable access to employment services for people who most need support, including those on benefit who may be furthest from the labour market.

Next steps

The three programmes of work discussed above together aim to provide advice on a more comprehensive ALMP system both for future New Zealand Income Insurance claimants, and for other people who need support to find and retain good jobs.

Officials are developing advice for EET Ministers for their meeting on 30 June 2022 Confidential advice to Government The ALMP review will take into account decisions made by SUIGG on 13 June.

Decisions on the ALMP review and development of the case management approach for New Zealand Income Insurance are not required for finalising the policy proposals on design of the New Zealand Income Insurance scheme and drafting of the enabling legislation. However, these work programmes will need to track along in parallel to ensure successful implementation of the scheme.

Annex Six: Consultation – further detail on initial findings

Public feedback on the discussion document comprises 1,819 survey responses and 255 submissions to MBIE, and the project team held around 50 targeted engagements with iwi/Māori and stakeholders representing business and employers, the health and disability sector (including health practitioners), disabled people, private insurers, academics and economists, and social and employment service providers. This was a relatively small number of submissions given the scale of the proposal.

Around two-thirds of respondents and submitters opposed the scheme

Overall, around two-thirds of both survey respondents and submitters opposed the introduction of the scheme.

Opposition was divided fairly evenly between those who argued the scheme was:

- an unaffordable and unnecessary cost that will add inflationary pressures to the New Zealand economy at a time many firms are struggling, or
- highly regressive, helping out middle class wage-earners at the expense of more vulnerable workers.

Many submitters opposed to the scheme expressed uncertainty about the case for the scheme – citing limitations in the discussion document on the extent of the wage scarring in problem in New Zealand and of supporting evidence that an income insurance scheme lasting six months would be an effective fix for wage scarring.

Several submitters also criticised the proposal for insufficient consideration of alternative options, such as implementing the recommendations of the Welfare Expert Advisory Group, expanding ACC cover to sickness and disability, introducing a statutory redundancy scheme, or changing KiwiSaver to be more accessible in cases of job loss.

Around one-third of respondents and submitters supported the scheme

Around one-third of respondents and submitters expressed support for the scheme in general, for reasons including the lack of a statutory redundancy provision in Aotearoa New Zealand and the current disparity between support for those unable to work due to an accident and those who fall ill.

However, even supporters expressed reservations about the value of the scheme relative to wider welfare reform, or only favoured coverage for either health conditions and disabilities, or redundancy – but not both.

Mixed views on scheme duration

44% of survey respondents consider the scheme duration is too long or far too long. They note it could increase disconnection from the workforce, which would be the opposite of the scheme's intent.

At the same time, a small portion of respondents (12%) consider that six months is too short or far too short, with feedback that six months is not long enough to retrain or rehabilitate. Alternative suggestions include having a scheme duration of a minimum of 12 months or to allow for extensions.

Māori respondents noted effort to honour Te Tiriti, but some questioned whether the proposals went far enough

Māori organisations and individuals noted the recognition of Te Tiriti o Waitangi in the discussion document and welcomed efforts in the design of the scheme to cover vulnerable working arrangements where Māori are over-represented.

However, some submitters felt the scheme did not demonstrate a kaupapa designed by Māori which was necessary to fully honour Te Tiriti. In that vein, some suggested the scheme should also reflect *wairua* as a dimension of wellbeing. Feedback also underscored the importance of the scheme offering Māori-led services to support tangata whenua.

Mixed views on coverage

As noted above, there were mixed views on what events the scheme should just cover, even among supporters of the scheme. These mixed views also extend to the types of work arrangements that should be covered.

There was widespread support for the scheme covering full-time workers but less support for coverage of part-time workers.

A small minority of survey respondents (52% to 39%) preferred to exclude non-standard workers such as casual or seasonal workers and the self-employed. Many submitters noted the practical challenges of covering these working arrangements, such as determining an “established pattern of work”.

In most targeted engagements officials held, there was acknowledgement that covering non-standard work arrangements, including self-employment, for redundancy is challenging. Feedback on the inclusion of non-standard work is mixed, and suggestions have been made to enable an opt-in to NZIIS or bespoke options similar to ACC’s CoverPlus Extra product.

Those who supported coverage of non-standard workers noted that this group includes many more vulnerable and less well-off workers such as women, people with disabilities and Māori or Pacific peoples. However, some submitters were concerned at the lack of coverage for those who stop working to care for others, or who leave work due to bullying or harassment – noting these were also not the fault of the worker.

Concern about levying temporary migrant workers without providing coverage

Although there was widespread support for excluding temporary migrant workers from scheme coverage, a strong theme in submitter feedback was concern over the unfairness of requiring them to pay levies without being entitled to coverage. This was seen by come to contradict the philosophy of insurance coverage. Alternative suggestions included not levying migrant workers or allowing some form of levy rebate when leaving New Zealand.

There are concerns around the contribution history

There were strong views that the requirement to have contributed to the scheme for 6 months over the preceding 18 months would disadvantage particular groups or more vulnerable workers, eg Māori, Pacific people and women. Therefore, suggestions were made to remove this requirement.

Respondents do not agree that employers will benefit

Respondents generally considered the scheme represented poor value for money for employers. Survey results show a large difference of opinion on whether it is fair to charge employers and employees equally. 35% of respondents thought that employees should pay “a lot more” of the levy.

Respondents did not support bridging payments

There is little support for the proposed bridging payment of 80% of wages for four weeks, particularly from business and employers. Views include that it is too complex and unaffordable, that it could impact existing redundancy packages in the future, and that it should not be required in the case of medical dismissal since this is outside the control of the employer.

There is also concern about businesses “ducking” their obligations or not being able to pay bridging payments in the case of a closure. Equally, there are still concerns about the moral hazard risk of sham redundancies, which the bridging payment seeks to address.

Respondents also noted that the bridging payment could be difficult to apply to non-standard work and could discourage employers offering casual work. Some stakeholders suggest a ‘casual loading’ as an alternative to a bridging payment.

Services to support return to work are important

Many stakeholders note the importance of having other effective and available services alongside case management to support people to return to good work. Stakeholders identify that in the absence of these services, claimants’ return to work and broader labour market outcomes could be compromised. Some express concern that MSD’s employment services will be spread more thinly and beneficiaries may miss out.

The governance model should improve outcomes for Māori

Governance is of particular interest for iwi/Māori. People see an opportunity for the governance model to better reflect and support aspirations and improve outcomes for Māori. Some submitters suggest that Māori need to be represented at every level of the scheme with decision-making rights, and that Māori involvement needs to be more than a single seat on the board and should also include co-design and delivery of services for Māori.

Feedback from the disability community includes that disability representation in governance is essential and that current processes impacting disabled people should not be replicated.

Choice of ACC to administer the scheme

Submitters express concern that ACC is not the right agency to deliver the scheme as it lacks the skills and capability to help people back to work. Concerns include ACC’s track record in relation to outcomes for Māori.

Other submitters recognise that ACC is well placed to run an insurance scheme, given it has operated a successful accident compensation scheme over the past 50 years.