
The Special Bulletin

June / July 2011

Budget 2011

Budget 2011 – Building New Zealand’s Future

Budget 2011 was delivered by Finance Minister, the Hon Bill English, on the afternoon of 19 May 2011. As expected, changes were announced to the KiwiSaver scheme, Working for Families and the student loan scheme. The changes are intended to put a halt to the escalating cost of running and funding these schemes and, at the same time, deliver some savings to the Government, which, in the 2010-11 year, incurred a deficit of \$16.7 billion (or 8.4% of GDP). The changes are summarised below.

Other changes, including tax changes, were also announced by Mr English (see summaries below). The tax changes will be given effect by the Taxation (Annual Rates and Budget Measures) Bill 2011 [<http://taxpolicy.ird.govt.nz/sites/default/files/2011-bill-arbm.pdf>], which was tabled in Parliament after the Budget.

To help rebuild Christchurch, the Government is establishing the Canterbury Earthquake Recovery Fund.

The Fund will initially have \$5.5 billion to meet all of the Government’s earthquake-related costs. Once the final bill has been paid off, the Fund will be wound up (see further details below).

To direct further funds into the Canterbury Earthquake Recovery Fund, the Government is launching a four-year maturity Earthquake Bond. Proceeds from the Bond will go to the Canterbury Earthquake Recovery Fund (see summary below).

In his speech, Mr English says that Budget 2011 is about building New Zealand’s future. The initiatives announced are intended to put the Government’s finances and the economy on a sounder footing, sooner. The Government expects to have a significant operating surplus from 2014-15, a year earlier than forecast. Contributions to the New Zealand Superannuation Fund are projected to resume from 2016-17.

Tax announcements

Budget 2011 includes the following tax announcements:

- Thin capitalisation rules for foreign-owned banks to be amended. The amendment will see the minimum prescribed percentage of equity for tax purposes raised from 4% to 6% on 1 April 2012. The raise will further limit foreign-owned banks’ interest deductions against the New Zealand tax base. The Government expects to raise about \$8 million of additional tax revenue in the 2012 fiscal year and \$31 million of additional tax revenue in each subsequent fiscal year.
- Employee benefits to be examined. The examination will consider: (a) whether the definition of income for Working for Families tax credit purposes should be further widened to include more fringe benefits provided to employees; and (b) whether salary that can be traded off for non-taxed, non-cash benefits should be subject to tax.
- Tax treatment of mixed-use assets (assets used for both private and business purposes) to be reviewed. The review will consider, for example, inflated tax deductions that result in either less taxable rental income or tax losses that are then used to offset other income.
- Livestock valuation election rules to be reviewed. The review will consider whether farmers can switch back and forth between the herd scheme and the national standard cost scheme methods, to allow them to receive untaxed increases in market valuations and tax deductions when valuations decrease.

KiwiSaver

Changes to the KiwiSaver scheme were foreshadowed before the Budget. Details of the changes were finally announced during the Budget. The changes include:

- From 1 April 2012, employer contributions will be taxed at the employee's marginal tax rate. Currently, higher income earners who have a higher marginal income tax rate get a larger tax break from the tax-free status of employer contributions.
- For the year to 30 June 2012 and beyond, the Member Tax Credit rate will be halved from \$1 to 50 cents for every \$1 contributed by members, up to \$521 a year (half the current maximum).

- From 1 April 2013, the minimum employee contribution rate will rise from 2% to 3%.
- From 1 April 2013, compulsory employer contributions will rise from 2% to 3%.

The changes are intended to reduce the share of government contributions – currently, close to 50% and over \$1 billion a year – to the KiwiSaver scheme and government borrowings from foreigners. The changes are expected to save \$2.6 billion over four years.

The Government will discuss with employers the recommendation of the Savings Working Group of a one-off enrolment exercise.

Student Loans

Changes to the student loan scheme were also foreshadowed before the Budget. The changes announced during the Budget include:

- Restricting student loan eligibility for those with an overdue student loan repayment obligation of \$500 or more who are in default for more than one year.
- Restricting borrowing for people aged 55 and over to tuition fees only.
- Removing the entitlement for part-time, full-year students to borrow for course-related costs.

- Suspending inflation adjustments to the student loan repayment threshold until 1 April 2015.
- Shortening the repayment holiday for overseas-based borrowers from three years to one year. Borrowers will be required to apply for the repayment holiday and nominate a New Zealand-based contact person before they leave the country.

The changes are intended to direct lending to those who most need it. The changes are expected to save \$447 million over four years.

Working for Families (WFF)

Like the changes to the KiwiSaver scheme, changes to Working for Families were also foreshadowed before the Budget. Details of the changes were announced during the Budget. The changes, to be implemented in four steps from 1 April 2012, include:

- Lowering the abatement threshold, from \$36,827 to \$35,000.
- Increasing the abatement rate, from 20 cents in the dollar to 25 cents in the dollar.
- Aligning the Family Tax Credit (FTC) payments for children aged 16 and over, with the FTC payments for

those aged 13 to 15. This involves putting a halt to inflation adjustments to FTC payments for children aged 16 and over, until FTC payments for children aged 13 to 15 catch up.

The changes are intended to ensure that Working for Families stays sustainable. The changes are expected save \$448 million over the next four years.

For families at the higher end of the Working for Families scale, the changes will see them receiving less than they do now or no longer qualifying for Working for Families.

Outside the Budget: Taxation (Annual Rates and Budget Measures) Bill 2011

The Taxation (Annual Rates and Budget Measures) Bill 2011 [<http://taxpolicy.ird.govt.nz/sites/default/files/2011-bill-arbm.pdf>] was tabled in Parliament after the Budget. The Bill amends the Income Tax Act 2007 to give effect to changes announced in the Budget to the KiwiSaver scheme and Working for Families. The changes are highlighted

above, under the headings “KiwiSaver” and “Working for Families”.

The Bill also sets the annual rates of income tax for the 2011-12 tax year.

Agriculture

Lifting investment in irrigation

The Government announced it will expand the Irrigation Acceleration Fund by \$35 million over five years to support the development of new water harvesting, storage and distribution infrastructure. This measure will support the development of irrigation infrastructure proposals to the “investment-ready” prospectus stage.

The expanded fund is the first stage of the process; for the second stage, the Government will consider in a future Budget investing up to \$400 million of equity in the construction of regional-scale schemes to encourage third-party capital investment.

Funding of this Crown investment vehicle is yet to be finalised, but it is expected to be available from 2013/14. The Crown will be a minority partner, investing on commercial terms, to give confidence to capital markets to invest in large scale irrigation schemes.

The Irrigation Acceleration Fund and equity investment is part of a package of measures to address the strategic value of water. The other measures are the Fresh Start for Fresh Water Fund for historical environmental damage to waterways and the National Policy Statement on fresh water management.

Employment and Social Development

Helping young people into jobs

The Government has announced it is investing \$55.2 million over four years to get young people into jobs. It will see more young people employed with working and training subsidies and through Limited Service Volunteers. The government has designed a package to subsidise employers who agree to train a young person and give them a permanent job.

The Youth Employment Package, has three components:

- 1 Skills for Growth;
- 2 Job Ops with Training; and
- 3 the Limited Service Volunteer programme.

Skills for Growth

Skills for Growth provides a subsidy for employers to employ and train young people in high demand industries (eg aged care, horticulture and agriculture).

Around 1,000 youths a year will benefit from a good job and industry-specific qualifications through Skills for Growth, costing \$17.2 million over four years.

Employers get a \$5,000 subsidy for training and in-work support to help the young person achieve a recognised industry qualification to NZQF Level Two.

The subsidy is paid in stages:

- \$1,000 when the employer provides Work and Income with a training plan and confirmed job offer.
- \$3,000 after the young person has been in employment and training for three months.
- \$1,000 after a year – if the young person has achieved a qualification, been in the job for a year or is still in training.

Job Ops with Training

Job Ops with Training is a refocused version of Job Ops, which incorporates training in the subsidy for employers, costing \$13 million in 2011/12.

Since its introduction in 2009/10, Job Ops has helped more than 10,000 young people get work.

Research shows 90 per cent of young people who completed a Job Ops placement are not on a benefit.

Job Ops with Training will:

- Provide a flexible subsidy of \$5,000 to employers that can be used for both wages and training.
- Require the employer to develop a training plan that results in skill development for the young person.

“Job Ops has been successful for both young people and employers. We believe this takes it a step further by providing training on top of a job.”

Limited Service Volunteers (LSV)

An extra \$25 million over four years will give 1,500 young people a year the LSV experience.

LSV is targeted to young people who’ve been on benefit for longer than six months and lack the confidence to find work.

The six week residential confidence building programme for 18-24 year olds is run by the NZ Defence Force at Burnham, Trentham and Hobsonville.

Employment Assistance Programmes

Social Development Minister, Paula Bennett, has announced that employment assistance programmes will be given a \$15 million boost.

The new funding will go into initiatives including Industry Partnerships, Straight to Work and the skill investment subsidies.

Community social services get \$25 million boost

Social Development Minister, Paula Bennett states that Community Social Services will get a \$25 million boost from the Government's Community Response Fund.

The Minister states that "there will be three funding rounds throughout the 2011/12 year, with about \$8 million available for each round".

Canterbury Earthquake Initiatives

\$10 million Budget support for Canterbury families

Social Development Minister, Paula Bennett stated that an extra \$10 million to support Cantabrians rebuilding their lives and communities after the earthquake will be provided.

The cash injection will support counselling services, assist non-government organisations' case management, co-ordinate services for families and support additional community-based services for those affected by the earthquakes.

The \$10 million will be drawn from funding set aside for the Community Response Contingency.

Canterbury trades training boost

The Government announced that it will provide up to \$42 million for trades training for the Canterbury region. Funding is being set aside for up to 1500 additional training places as part of a comprehensive cross-agency response to meet additional demand for labour for the reconstruction programme called "Skills for Canterbury".

The Skills for Canterbury package includes:

- Up to 3000 more construction-related training places in Polytechnics in Canterbury and around the country (from existing funding).
- \$42 million for additional funded places at polytechnics, private providers and Industry Training Organisations (ITOs), if required.
- Accelerated training programmes at Christchurch Polytechnic Institute of Technology (CPIT) and other polytechnics to complete training more quickly and to allow transition to work during training.
- Additional skills brokers at relevant ITOs to work with employers and Ministry of Social Development (MSD) to place people in training.
- \$1.5 million from Work and Income to subsidise 650 people into training and work by the end of June.
- An extra \$5 million in Budget 2011 for MSD to purchase further Industry Partnership placements to help unemployed people take up job opportunities from the rebuild.

- Additional support for Maori Trainees, with Te Puni Kōkiri (Ministry of Māori Development) appointing a dedicated agent to work with ITOs and employers to support at least 200 Maori into the construction sector.
- A special immigration skill shortage list from the Department of Labour to allow employers to import high-skilled workers that can't be trained in time.
- Considering contractors' commitment to training and trainees as a factor when assessing future government reconstruction contracts.

Budget funds new earthquake recovery authority

Earthquake Recovery Minister Gerry Brownlee states that the new Canterbury Earthquake Recovery Authority (CERA) will receive \$25.5 million of funding over two years.

CERA has been provided \$25 million in new funding, while \$500,000 is reprioritised funding from Vote Economic Development to reflect the transfer of functions from the Ministry of Economic Development to CERA. This amount does not include central Government funding for the rebuild of Christchurch.

Mr Brownlee said that "this funding is purely to set up the new authority. The Government will also spend about \$8.8 billion over the next few years to help Canterbury rebuild through the Earthquake Commission, ACC, meeting costs of residential property damage, rebuilding infrastructure such as roads and essential water systems, and welfare support".

\$5.5 billion for Canterbury Recovery Fund

The Government will provide \$5.5 billion over six years for the Government's new Canterbury Earthquake Recovery Fund, Earthquake Recovery. About \$4.8 billion of this will be provided through new funding, while another \$740 million will be absorbed or reprioritised from other areas. This is in addition to the Earthquake Commission's expected \$3 billion share of repairing residential property and land damage, as well as other costs such as ACC.

Mr Brownlee says that “the Government has created a new fund for the Canterbury earthquake to ensure transparency of the money we spend in rebuilding greater Christchurch.”

This money, combined with the direct cost to the Earthquake Commission of meeting residential property damage, and ACC costs, makes up the Government’s \$8.8 billion estimated total investment in rebuilding Canterbury.

The Canterbury Earthquake Recovery Fund will cover:

- The Government's share of repairing essential local infrastructure - mainly water and roading infrastructure.
- Repairing state owned assets such as state highways, schools and hospitals.
- Welfare support through job loss cover and wage subsidies, as well as costs relating to the immediate response to the emergency.
- The Government’s financial support package for AMI Insurance.

The Recovery Fund also includes about \$3.2 billion that is yet to be allocated. This will be used for any additional costs from areas outlined above, as well as for policy decisions that are yet to be made, such as temporary housing and any remediation of land damaged in the February earthquake.

Earthquake Kiwi Bond to help fund recovery

Finance Minister, Bill English states there will be a new Earthquake Kiwi Bond to help fund the recovery in Christchurch and provide investors with a new savings option. The new four-year bond is similar to a term deposit and is available to New Zealand residents from 19 May 2011.

The new bond will be issued by the New Zealand Debt Management Office (www.nzdmo.govt.nz) as part of its debt issuance programme. The bonds will pay interest based on wholesale government bond rates, with the initial interest rate set at four per cent.

Commerce

New market regulations

Commerce Minister Simon Power says that his priority “has been to put in place a regulatory framework that attracts investors back to our capital markets.” The Minister says that “The Government has committed extra resources to ensure investors have access to the information they need to make informed decisions about their investments”. This includes extra funding of \$6.8 million to cover the first period of the new Financial Markets Authority’s operating and litigation costs, and new capital investment of \$5 million in 2011/12, to cover the cost of office facilities for increased staff numbers and new IT infrastructure and applications.

The Minister says that since 2008 reform of the financial sector has included:

- Requirements for all financial service providers, including financial advisers, to be registered and belong to a dispute resolution scheme.
- Implementation of the financial adviser regime to encourage public confidence in the industry. This comes fully into force on 1 July.
- Prudential regulation of non-bank deposit takers.
- Licensing of auditors by a professional accounting body.
- A licensing regime for trustees to strengthen the quality of the supervision provided by trustees.
- Changes to securities legislation and regulations, in response to recommendations from the Capital Market Development Taskforce.

- Requiring debt issuers, including finance companies dealing with moratoria, to give investors tailored disclosure documents.
- Improving the governance of KiwiSaver schemes by requiring that KiwiSaver schemes have a designated manager, and providing a regulation-making power for the Government to impose periodic reporting requirements on KiwiSaver issuers.

The Minister says that these changes are all important but the most important is the establishment of the Financial Markets Authority (FMA) which is equipped with extra functions, duties, and powers to keep New Zealand’s financial markets working for mum and dad investors, including:

- The power to exercise another person’s right of action against a financial market participant.
- Tools for actively monitoring and enforcing securities law.
- Enhanced warning powers, and a regulation-making power to better regulate unsolicited ‘low-ball’ offers.
- A new oversight regime for registered exchanges, including the ability to undertake real-time surveillance of market activity.
- Enabling regulations to help ensure that financial instruments cannot be structured to avoid securities legislation.

The Minister also advised that the Government is also working on modernising Securities laws and will release an

exposure draft of the new legislation later this year.

Customs

SmartGate funding

Budget 2011 includes an extra \$3.5 million in operational funding for SmartGate. The Budget also provides \$3.4 million in capital spending for 2011-12.

The SmartGate system, which uses face recognition biometric technology from the information stored in a microchip inside ePassports, has recently just clocked its one millionth passenger. Demand is being driven by the increase in New Zealand and Australian passengers with ePassports who are eligible to use it. Tourism volumes are also expected to increase over the next few years.

SmartGate is currently available at Auckland, Wellington and Christchurch airports. The funding will see six more gates and 13 kiosks installed between Auckland, Wellington and Christchurch Airports and will move trans-Tasman travel a step closer to the “near domestic” experience sought by both the New Zealand and Australian Governments.

Customs Minister Maurice Williamson says that the additional SmartGate capacity will greatly assist in the management of major events such as the Rugby World Cup 2011.

Education

Schools - Extra \$1.4 billion for schools over four years

Education Minister Anne Tolley has announced an extra \$1.3 billion in operating funding and \$109 million in capital for education out to 2014/15 in Budget 2011.

The funding includes:

- A 2.92 per cent - or \$118.1 million – increase in new operational funding for schools over four years to allow for rises in costs.
- \$550.3 million over four years for early childhood education (ECE).
- \$66.5 million over four years to increase the number of Trades Academies and Service Academies, to keep more 16 and 17 year olds engaged in education and training as part of the wider Youth Guarantee.
- \$59.7 million in new operating and capital funding over four years for school property, and \$60 million over four years will be reprioritised to build new kura, and upgrade existing buildings.
- \$51.5 million for the school network upgrade project.
- \$12 million over four years of new funding with a specific focus on lifting Māori achievement, and \$17 million of reprioritised funding to extend the Te Kotahitanga programme to an additional twenty schools.

Early childhood education

As noted above, the Government will invest an extra \$550.3 million in ECE over the next four years. Budget 2011 provides an 11.5 per cent increase in ECE spending

from Budget 2010 (an additional \$147 million in 2011-12), bringing the total annual investment to \$1.4 billion.

The Government’s priority is to increase participation for those groups that will benefit the most from early childhood education, including Māori, Pasifika and children from lower socio-economic backgrounds, while also controlling Government expenditure.

Specific measures for ECE include:

- \$416.7 million over four years to meet the increased demand from population growth, and more children staying in ECE for longer periods of time.
- \$61 million over four years to increase funding rates for ECE services to allow for rises in costs.
- \$21.5 million over four years to extend and strengthen the early childhood equity fund, which provides additional resources to services with high enrolments of children from priority groups. Services will receive additional funding to set up in priority communities.
- \$12.8 million operating and \$18 million capital expenditure over four years for an early learning information system to improve information about participation and system performance.
- \$20.3 million over four years to fund early childhood education for children in care and to extend the Home Interaction Programme for Parents and Youngsters (HIPPY).

Māori education

Associate Education Minister Pita Sharples says the Budget will provide significant capital and operational funding to strengthen delivery of school and community-based Māori language initiatives and it will also help teachers to engage

better with Māori students, improve literacy teaching, and support Kura Kaupapa Māori.

New funding for Māori education is as follows:

- \$9 million over four years to support iwi to develop school and community-based language initiatives.
- \$3 million over three years to support Te Runanganui o nga Kura Kaupapa Māori to develop a curriculum and associated resources based on the philosophy of Te Aho Matua.
- \$8 million over four years to realign Kura transport assistance - which has been capped since 1995 - with mainstream schools.

Funding will be reprioritised to the following areas:

- \$60 million over four years to build new kura kaupapa Māori and upgrade existing school buildings.
- \$6.5 million to expand family-based literacy programmes to all decile one, two and three schools, building on the current Reading Together programme.
- 17 million over four years to allow an additional 20 schools to participate in the Te Kotahitanga teacher training programme.

Tertiary education

Specific Key tertiary sector initiatives announced as part of Budget 2011 include:

- Up to 750 additional funded places in new and high performing private training establishments.

- Specific funding of \$17.5 million over four years for English as a second language courses for refugees and migrants.
- Improving the value for money of pilot training, by setting a limit on the fees providers can charge students and excluding solo flight hours from the student loan scheme.
- A two per cent increase in the funding rate for all degree and post-graduate courses.
- Equalising the funding rate for post-graduate courses across universities polytechnics and wānanga.
- Increased funding of \$40 million over four years to raise the profile of New Zealand education overseas.
- 40 additional medical places from 2012.
- \$42 million for increased trades training, in order to ensure that people can be trained when and where they are needed. This measure is in recognition of the fact that there will be some costs associated with the rebuild of Christchurch.

Tertiary Education Minister Stephen Joyce says that the increase in funding for places in private training establishments will be available only to those providers who perform well, and can show they are meeting the tertiary priorities. The Government says that it is continuing to move funding from areas of low demand currently, such as industry training, and looking to improve investment in pilot training.

Environment

New fresh water clean-up package

The Government announced a fresh water policy package on 9 May, which consists of a number of measures aimed at improving water management. It is needed to grow the economy while better caring for our rivers, lakes and aquifers.

The package comprises:

- A National Policy Statement on fresh water management to set a consistent, nationwide regulatory framework for setting water quantity and quality limits to govern the allocation and use of freshwater.
- An Irrigation Acceleration Fund of \$35 million over five years to support the development of irrigation infrastructure proposals to the 'investment-ready' prospectus stage, aimed at unlocking the economic growth potential of primary sectors through the development of more efficient and effective water infrastructure, such as storage and distribution.
- A new contestable fund to help councils and communities clean-up nationally significant water bodies polluted by poor historic management. The

"Fresh Start for Fresh Water Clean-up Fund" initiative will bring together a number of existing one-off clean-ups in Waikato, Rotorua and Taupo into the Fresh Start for Fresh Water Programme as well as reprioritised funding in the Budget for the new contestable clean-up fund of \$7.5 million per year for 2011/12 and 2012/13. The total investment, incorporating existing commitments, is \$26.2 million in 2011/12, \$23.7 million in 2012/13, and including out years will involve \$264.8 million.

- The Government will also consider in a future Budget investing up to \$400 million of equity in water infrastructure schemes.

According to the Government, the water package demonstrates the Government's commitment to maximising the economic growth opportunities of water, while protecting the environment.

The Government will be inviting applications for the new Fresh Start for Fresh Water Clean-up Fund in June 2011 with an expectation of new projects being approved by August 2011.

Health

Public health services

Budget 2011 contains an extra \$2.2 billion for public health services over the next four years, including an additional \$585 million in initiatives in 2011-12.

In the next financial year, the Government will provide \$585 million for health initiatives, consisting of \$420 million of new money, plus around \$165 million from savings to be put back into healthcare.

District Health Boards will receive around \$400 million, made up of \$350 million in population-based funding, plus over \$50 million for service contracts from the Ministry of Health.

The \$2.2 billion extra over four years will fund new initiatives including:

- \$18 million for 40 extra medical training places – part of the Government's promise to boost the number of medical training places by 200 over five years.
- A further \$54.5 million for maternity initiatives to improve safety and quality, and extra WellChild visits, with a particular focus on first time mothers (see below).
- \$80 million for widened access to medicines. It is expected around 32,000 patients in the first year will benefit from this extra funding.
- \$68 million for more elective surgery, continuing the record increase of 4,000 extra operations a year, and reducing waiting times.
- An additional \$40 million for dementia care, which is expected to provide almost 200 extra beds over the next two years and extra respite care.
- \$40 million for mental health, including \$4 million for dementia-related respite care.
- An extra \$130 million for disability support services to meet rising needs and costs.
- \$80 million extra from DHBs for GP visit subsidies and \$14 million for more people qualifying in programmes, such as very low cost access and free under-sixes.

Maternity services

The Government announced in Budget 2011 several new initiatives for maternity services and to help new mothers and their babies. The Government will provide an extra \$33.2 million for maternity services over four years to improve safety and quality and a further amount of \$21.3 million to boost extra WellChild services, with a particular focus on first time mothers.

The extra \$33.2 million for maternity service includes:

- \$18.4 million to improve the safety and quality of services for mothers and babies, by bringing all local maternity professionals together for regular clinical reviews of all births. This funding will also increase the number of midwives in hospitals, together with medical specialists on-site and on-call.
- \$6 million to revamp new parent information services.
- \$6.8 million to help vulnerable mothers access a fuller range of health and social services. It will also assist midwives to make appropriate and timely referrals to other practitioners.
- One-off funding of \$2 million to ensure all DHB maternity data is collected nationally.

In addition to the \$54.5 million in initiatives, \$13 million over four years will be provided to fund the needs arising from the rising birth rate.

Elective surgery operations

Budget 2011 will deliver a further \$68 million over four years to increase funding for elective surgery.

The extra money is in addition to funding provided to District Health Boards through population and price adjustments, in order to provide more operations for New Zealanders who need them.

Disability

The Government will invest \$4 million over the next four years in 'Be. Accessible', Disability Issues.

Be. Accessible has been developed in partnership with Auckland District Health Board, Auckland Council and AUT University, and others in the public, private and disability sectors. It builds on the work already done in preparation for the Rugby World Cup 2011 and will assess key locations in the 12 host cities in the lead up to the Rugby World Cup 2011.

Be. Accessible is intended to be "a social change campaign aimed at influencing the attitudes and behaviours of New Zealanders in creating an accessible New Zealand" and "to inspire and enable businesses, individuals and organisations to step up to the economic and social opportunity to improve accessibility for people with disabilities".

Be. Accessible also delivers on a key initiative of the Ministerial Committee on Disability Issues, to promote mobility and access for disabled people.

Pharmaceuticals

Budget 2011 contains an increase to the pharmaceuticals budget by \$180 million over three years. This \$20 million increase is included in the funding increase District Health Boards are receiving.

The schedule of medicines subsidised by the Government will be expanded, and the Government estimates that at least 32,000 additional patients will benefit from better access to subsidised medicines as a result.

Some of the new medicines that have not been subsidised previously include new cancer treatments, the first Alzheimer's disease drug, and diabetes medicines. Health Minister Tony Ryall also states that the medicines which more people will be able to obtain include several for depression, auto-immune diseases, Crohn's disease, cardiac and respiratory problems.

\$12m to reduce rheumatic fever

Associate Health Minister, Tariana Turia announced, as part of Budget 2011, a \$12 million programme to reduce the rates of rheumatic fever in more vulnerable communities.

The Associate Minister said rates of rheumatic fever are now 14 times higher in New Zealand than in any other OECD country. She says that rheumatic fever and rheumatic heart disease are increasing health issues for New Zealand, both in terms of cost and equity. Of particular concern is the large disparity between ethnic groups, which appears to have worsened over the past 20 years. The mean incidence rates for Māori and Pasifika children aged between five and 14 are now between 20 and 40 times higher than for other New Zealand children of the same age.

The new programme, which will be funded over four years, will support a number of initiatives such as increasing front line community staff, school-based sore throat clinics and a range of research and training programmes for health professionals and community workers.

The Associate Minister says that Budget 2011 will help coordinate initiatives introduced around the country (such as the Whangaroa Project, which involved a clinical network, schools and iwi working together to support a sore throat clinic, or the Sore Throats Matter campaign run by Waikato DHB). The initiative will also place priority on interventions that show the potential to eradicate rheumatic fever.

\$44m extra for dementia care

Budget 2011 delivers an extra \$44 million over four years to look after people living with dementia.

This funding increase includes \$40 million for residential dementia services, and is expected to lead to the provision of almost 200 extra dementia beds over the next two years.

Another \$4 million of new money is for additional respite care for full-time carers of people with dementia. This will include in-home respite.

In addition, District Health Boards will provide an extra \$60 million over four years - an increase of 1.7 per cent for all aged residential care services.

The Health Minister says that individual DHBs are also expanding and improving their local services for older people, including those with dementia, as part of their plans for 2011-12.

Housing

Budget 2011 sets aside a contingency fund of up to \$45 million for 2011-12 so that the Government can respond to recommendations of the Housing Shareholders' Advisory Group. This will be partly offset by an increase in the dividend to the Crown from Housing New Zealand Corporation of \$21 million for 2009-10.

Housing Minister Phil Heatley says that the extra funding will improve the ability of third sector providers to significantly increase the amount of housing available to those on lower incomes or with specialised needs.

Current financial restraints mean that the Government is likely to focus the resources previously invested in the Housing Innovation Fund on supporting smaller niche

providers, while creating a new, larger pool of funding for housing providers which want to grow significantly, according to Mr Heatley.

In addition, a new Rural Community Regeneration Programme is being considered as a replacement for the Rural Housing Programme. The community housing sector, including rural and urban iwi, will have access to this funding. Ministers will make final and detailed decisions about the allocation of the contingency fund before 1 July.

Mr Heatley says that the Government will look to use other assets, including housing stock and land, to support the growth of social and affordable housing wherever it is appropriate.

Infrastructure

Rail

Budget 2011 commits more than \$338 million to improving commuter rail services and supporting KiwiRail to become more commercially viable.

Transport Minister Steven Joyce says that a funding package of \$88.4 million over eight years for Wellington commuter rail will help transform Wellington's rail services. This funding will go towards upgrading and renewing the remainder of the signalling and electric power equipment on the Wellington network.

The Government anticipates that the Crown commitment, coupled with co-investment from the Greater Wellington Regional Council and previous investment from both parties, will transform the service into a modern reliable commuter option for Wellington.

Budget 2011 also contains measures aimed at helping KiwiRail become a commercially viable rail freight business over 10 years.

KiwiRail receives the second \$250 million tranche of the Government's \$750 million commitment to its Turnaround Plan over three years. The majority of the \$4.6 billion Turnaround Plan will be funded by KiwiRail itself from customer revenue during the 10 year plan. The money will be used to continue a range of projects, including new locomotives and wagons, and improvements to the network - particularly on the main trunk route and in the 'golden triangle' of Auckland, Hamilton and Tauranga. The Turnaround Plan is intended to assist KiwiRail to become a more viable nationwide freight participant.

Broadband

Budget 2011 provides nearly \$1 billion to advance the Government's flagship Ultra-Fast Broadband (UFB) and rural broadband initiatives.

- Capital funding of \$942 million will be provided to Crown Fibre Holdings to invest alongside private sector partners in deploying fibre-to-the-premises networks that offer ultra-fast speeds.

This funding, in addition to previous appropriations, means Crown Fibre Holdings now has access to the full \$1.4 billion allocated to the UFB initiative.

The funding allows Crown Fibre Holdings to enter further contracts alongside those already made with Northpower and WEL Networks. It is intended that those contracts will progressively achieve the Government's goal of 75 per cent of New Zealanders having access to ultra-fast broadband by 2019.

- Budget 2011 also provides \$28.2 million to allow state and state-integrated schools to connect to new government-funded fibre networks by funding the connection from the school boundary into the school.

This is intended to ensure that schools can access new networks and quickly deliver the benefits of ultra-fast broadband to students. Under the Government's broadband initiatives, the intention is that more than 97 per cent of schools will be connected to fibre.

Local government

As previously announced by the Government, a new local government funding agency will begin operation in 2011. The New Zealand Local Government Funding Agency – an idea from the Jobs Summit two years ago - will operate as a large scale borrower that will then re-lend to councils.

The new large-scale lender to local authorities is aimed at helping the development of New Zealand's capital markets. This authority will be a collective debt vehicle, issuing securities backed jointly by most large local authorities. The Government says that this will provide cheaper funding for local projects, as well as more liquid, better diversified assets for investors.

The New Zealand Debt Management Office will be contracted by the new agency to manage the borrowing programme.

It is expected that the agency will lower the overall cost of borrowing for all councils by allowing a co-operative approach to raising finance, and is estimated to potentially save local authorities collectively around \$25 million a year.

Councils will not have to go through the agency to borrow money - they can choose to participate or continue raising money independently.

The Government announced in Budget 2010 that it would provide \$5 million towards establishing the agency. Another \$20 million will come from councils.

Transport and electricity

In addition to the above Budget initiatives, the Government is investing \$12.2 billion over the next 10 years in New Zealand's State Highway network; and \$3.8 billion through Transpower until mid 2015 to upgrade the national grid.

Justice

Serious Fraud Office

The Minister Responsible for the Serious Fraud Office (SFO), Judith Collins, announced as part of Budget 2011 that Government has allocated more than \$8 million in funding for the SFO over two years.

A total of \$8.3 million across 2010-11 and 2011-12 will enable the SFO to undertake an increased number of investigations and prosecutions of serious fraud.

In 2010, the SFO opened 27 investigations, including a number of investigations into finance companies. Those cases investigated during that time had involved losses of more than \$1.5 billion, affecting about 115,000 victims – many of whom were investors.

Ms Collins states that the SFO has laid more than 800 charges against 26 people in the last 12 months and that during the past year, the SFO has cleared a backlog of cases, including investigations lasting up to seven years. The average length of a case is now six months.

Community law centre funding

Justice Minister Simon Power announced that Budget 2011 will provide an extra \$4 million in 2011-12 for community law centres.

Mr Power stated that the Government recognises that the centres' main source of funding from interest earned on money held in solicitors' trust accounts on behalf of clients has been dramatically reduced in recent years, as a result of the slow housing market and lower interest rates. The Budget funding is intended to give community law centres certainty about their future, while their traditional funding source recovers. Mr Power also said that centres also need to work on securing additional funding from outside Government, such as brokering pro bono arrangements with law firms.

Legal Aid

Budget 2011 includes \$103.5 million of new spending for legal aid over the next two years, while the Government addresses longer-term sustainability issues facing the system. The new spending is split into \$34.1 million for 2010-11 and \$69.4 million for 2011-12.

The Justice Minister stated that this extra funding will ensure legal aid services continue to be funded at current levels in the short-term, while the Government addresses how to close the \$402 million gap between forecast

demand for legal aid and baseline funding over the next five years.

The Government announced a series of policy changes in April 2011, to save \$138 million over the four years to 2014-15, but says that even with these changes and the additional budget funding, there is still a gap that needs to be addressed.

The Minister will report to Cabinet in September with further options to address the remaining funding gap after officials provide him with advice on a closer review of the purpose of legal aid and associated costs, predominantly in the Family Court.

Safer communities

The justice sector will receive \$157 million in new funding over the next two years in Budget 2011, with the aim of ensuring access to justice and increase public safety.

The Justice Minister states that administration of justice is not immune from cost pressures, which is partly why Justice sector Ministers are overseeing significant changes to improve performance and reduce volumes and costs. Reforms underway include ensuring legal aid quality and sustainability, criminal procedure modernisation, and changes to improve Police, Courts, and Corrections services.

In Budget 2011, the Justice sector receives \$150.1 million operating funding and \$6.9 million capital funding over two years for policy priorities and essential services. The major areas of new spending include:

- \$34.1 million in 2010-11 and \$69.4 million in 2011-12 to address funding shortfalls in legal aid while the Government progresses proposals to address sustainability of the legal aid system.
- \$4 million in 2011-12 to address a funding shortfall for Community Law Centres.
- \$22.5 million over two years and a capital injection of \$3.2 million to meet the increased demand and associated costs for the supervision and conduct of Crown prosecutions.
- \$8.3 million over two years for increased capacity and capability for investigating and prosecuting complex or serious crime; and
- \$1 million in 2011-12 for the constitutional review, which is part of the confidence and supply agreement with the Māori Party.

Māori Affairs

Whanau Ora to expand with nationwide coverage

Associate Health Minister, Tariana Turia states that the Government will invest an additional \$30 million in Whanau Ora over the next four years, including \$11.25 million in the coming year. The funding includes \$25 million allocated in the Budget and, subject to final Cabinet approval, another \$5 million of reprioritised Māori Potential funding from within Vote Māori Affairs.

The funding will have Whanau Ora supported in at least eight new provider collectives in a range of new locations.

Budget maintains momentum for Māori Affairs

The Māori Affairs Minister says that Budget 2011 will ensure the Government maintains momentum with its Māori Affairs programmes, which are delivering encouraging results. The Minister says “within existing baselines, we have found \$2 million to support Māori engagement with the constitutional review and \$2 million to continue community-driven language revitalisation projects.”

According to the Minister “The constitutional review is potentially the most important advance for Māori in a generation, because the role of the Treaty of Waitangi is a key part of the national discussion.” Further the Minister says that, “Once we are agreed on the basis of our partnership, we can address issues with mutual respect, instead of feeling challenged. The constitutional review aims to help our nation unite around a very positive self-image.”

“Our reallocation of funding to community-driven language projects was foreshadowed in the recent report ‘Te Reo Mauriora’, in which an independent panel of experts recommended redirecting resources to encourage families to speak Māori at home,” Dr Sharples says.

“In addition to Whanau Ora, new funding in the Māori Affairs budget of \$250,000 will help settle a long-standing injustice over perpetually-leased lands around Taumarunui. This compensates the Karanga Te Kere landowners for not being included in earlier settlements of this difficult issue, which arose from 19th Century legislation that denied Māori owners control over their lands in perpetuity,” Dr Sharples says.

Public Sector

Public sector savings

The Government announced as part of Budget 2011 that it expects the wider state service to find \$980 million in savings over three years to go towards improving frontline public services and reducing debt.

Agencies will be required to find the savings from 1 July 2012. The savings will comprise two main parts:

- \$650 million from ending the central funding of over 100 state sector agencies’ employer contributions to KiwiSaver, the State Sector Retirement Savings Scheme and the Teacher’ Retirement Savings Scheme. In most cases agencies will have to meet these costs from their existing funding.
- \$330 million in core government administration from 31 core government agencies.

Finance Minister Bill English also states that the Government is requiring state service agencies to fund their own employer contributions to workplace savings schemes – i.e. putting them on the same footing as other employers and improving the incentives for them to fully assess the cost of employment decisions.

The wider state sector will receive over \$100 billion in Government funding over the three years in question to deliver public services to New Zealanders. The Government believes that this level of funding provides sufficient room for agencies to find savings, while improving critical frontline public services.

Mr English says that data collected for 33 government agencies, including many in the core public service, showed they spend about \$1.8 billion a year on administrative and support functions. The report concluded that the government agencies taking part could eventually save between \$230 million and \$425 million a year through greater sharing, standardisation and automation of back office processes and systems.

Core public service agencies are being given time to identify savings of \$330 million over three years and it is expected that most of these savings will come from “back office efficiencies”.

Targets will be finalised after the Budget, based on an agency's size and costs. There will be a number of safeguards to protect the quality of frontline services. Agencies will be able to appeal their target and have it reduced if they can show it would have an unacceptable

impact on frontline services, or it could be better used to fund projects necessary to deliver future savings.

Agencies that have already undergone a specific review, such as the Defence Force and Statistics New Zealand, will be excluded.

Other agencies may be excluded where Cabinet is satisfied they are already achieving internal efficiencies. Organisations whose budgets are set by Parliament rather than the Government are also excluded.

Improved online government services

Budget 2011 provides funding of \$27.6 million over the next two years for igovt services, which is intended to help deliver better public services more efficiently.

Internal Affairs Minister Nathan Guy says that the igovt services provide an easy and secure way of accessing government services online and proving identity. Using one log-on means people no longer have to remember multiple details for different sites, and being able to verify identity online saves the hassle of having to show multiple forms of ID to agencies.

Mr Guy says that without this investment, most government agencies would be forced to develop their own authentication and verification systems. This duplication would be expensive and complicated, and many smaller agencies simply wouldn't be able to provide online services. The Government believes that this is another important step by the Internal Affairs Department to coordinate the use of information and communications technology across government.

Many government agencies, including the Labour Department, New Zealand Transport Agency, the Police, Internal Affairs Department, and the Auckland and Wellington City Councils, are already using igovt log-ons for various online services. The Minister says that an increasing number of agencies are looking to adopt it this year for services such as applying for a new passport or changing electoral roll details. The Internal Affairs Department has entered into negotiations with New Zealand Post to expand the use of igovt services.

A full list of participating agencies and services is available at: www2.i.govt.nz/cls/static/participatingagencies

Research, Science and Technology

Budget 2011 provides for the reprioritising of \$36 million over four years for business research and development, commercialisation and earthquake research.

This includes:

- \$24 million over four years for business R&D and commercialisation.
- \$12 million over four years for earthquake research to help rebuild Christchurch.

An additional \$2 million has already been committed from the 2010-11 financial year as an immediate response to the earthquake.

The funding for business will go into priority areas such as high-value manufacturing products and services, and will be aimed at connecting research with business innovation.

The funding for earthquake research will focus on science that can provide practical support to Canterbury's recovery. According to Science and Innovation Minister Wayne Mapp, the research will look at questions such as why some stairs inside buildings collapsed, as well as important longer-term issues such as better understanding earthquake risks in Canterbury. It is expected that this will assist with the revision of building codes.

The extra funding for business and earthquakes has been reprioritised from within Vote Science and Innovation. The funding has been moved mainly from the areas of biological and social research.

Statistics

The Statistics Minister, Maurice Williamson announced that Statistics New Zealand will receive \$58 million in new operating funding over the next four years from Budget 2011, to ensure the ongoing supply of important economic and social data.

The funding will go towards the programme 'Statistics 2020: Achieving the Statistical System of the Future', which aims to update the department's IT systems.

In addition, Statistics New Zealand will receive an extra \$3.8 million in capital funding over the next four years, totalling \$12.7 million over 10 years. The Government's intention is to enable the organisation to transform the way it produces statistics, increase productivity and reduce the longer-term cost of statistics production.

Mr Williamson says that the funding will benefit individuals, communities, and local and central government agencies which base their decisions on robust information.

State-Owned Enterprises

Government to pursue mixed ownership model

The Government has announced that it believes there is significant merit in extending the mixed ownership model to four state-owned energy companies and reducing the Crown's majority shareholding in Air New Zealand.

Treasury will now undertake preliminary work to prepare for extending the mixed ownership model to Mighty River Power, Meridian, Genesis and Solid Energy and reducing the Government's majority stake in Air New Zealand.

This would happen in a three to five year programme starting in 2012, should the Government be re-elected in November - and subject to market conditions and results of detailed scoping studies.

According to the Minister of Finance, Bill English, "the Treasury estimates that extending the mixed ownership model to the four energy SOEs and reducing the Government's majority shareholding in Air New Zealand are likely to free up between \$5 billion and \$7 billion of capital - depending on the final structure of the programme." The Minister also stated that "the Government will be a substantial net acquirer of assets in the five years to 2015. Its total assets are expected to rise by \$34.3 billion to \$257.7 billion in 2015. About \$21 billion of this increase is funded directly from within core Crown finances. Rather than simply borrow this amount, the Government will use proceeds from the mixed ownership model to recycle existing capital towards high priority future investment in assets like schools, hospitals and broadband. The proceeds will fund about a third of the Government's new investment in core social infrastructure."

The Minister for state-owned enterprises, Tony Ryall, also stated that the Treasury has confirmed that proceeding with the mixed ownership model can meet the five prerequisite tests set by the Government which the Minister says "includes the Government maintaining majority control in the companies, New Zealand investors being at the front of the queue for shareholdings, and having confidence in New Zealanders securing widespread and substantial ownership in the SOEs."

The Minister also stated "that Ministers agree with Treasury advice that extending the mixed ownership model offers significant opportunities for New Zealanders – either directly or through their KiwiSaver accounts and other managed funds – to invest more in quality New Zealand companies. In addition, it will bring sharper commercial disciplines, more transparency and greater external oversight for the companies involved. And finally, it will provide opportunities for the companies to obtain capital to

grow without depending entirely on cashed-strapped governments to support them."

The Government states that initial public offerings are the preferred method for extending the mixed ownership model, given the Government's requirement to achieve widespread and substantial New Zealand ownership across the five companies. No decisions have been taken on precisely how much of each company will be sold or when – other than the Government will retain a majority shareholding.

The Government has stated that "it will remain a strong net investor in the next few years – it will accumulate an extra \$34.3 billion of assets over the next five years alone," the Ministers say. "But we can't continue to fund these assets by building up more debt indefinitely."

Mixed ownership model – fact file

Why New Zealand needs to lift national savings

The Government has said that it is concerned that New Zealand has run balance of payments deficits every year since 1974 and net external liabilities. The debt indicator most closely watched by credit ratings agencies – have jumped to more than 80 per cent of GDP. According to the Savings Working Group, "New Zealanders collectively have been spending too much and saving too little, using large amounts borrowed offshore to fund new investment".

The Government needs to play its part

The Government has stated that National savings include all parts of the economy – households, businesses and the Government. Households and businesses have lifted their savings rates sharply since the 2008 recession, but the Government has deliberately done the opposite to partly absorb the downturn on its own books. This was appropriate at the time, but it's not appropriate now the economy is growing again.

Growth in the Government's assets

The Government states that it runs a large investment programme, but until now it has had little visibility. The Government, on behalf of taxpayers, owned more than \$220 billion of assets at the end of the last financial year. This is expected to grow by \$34.3 billion by 2015, reflecting ongoing investment in schools, hospitals, broadband, electricity, roads, rail and a range of other assets. Under current arrangements, much of this money would have to be borrowed from foreign lenders.

Better managing commercial assets

The combined net value of all SOEs (excluding KiwiRail) and the Crown's holdings in Air New Zealand was about \$15 billion in 2010 – they make up around eight per cent of the Government's total balance sheet. Changing the mix of these assets – through extending the mixed ownership model – would help to fund future priority investments and ensure public debt levels remain prudent and sustainable.

Extending the mixed ownership model

The Government states that earlier this year it asked Treasury for advice on the merits and viability of extending the mixed ownership model currently used for Air New Zealand – where the Government retains a controlling shareholding, but offers a minority stake to outside investors. Specifically, it asked for advice on extending this model to Mighty River Power, Meridian, Genesis and Solid Energy. It has also sought advice on the merits of reducing the Crown's shareholding in Air New Zealand, while still maintaining a majority stake. No other SOEs are being considered for this model.

Advantages of the mixed ownership model

The Government has listed the advantages as follows:

- (i) It frees up capital for the Government to invest in higher priority areas such as schools, hospitals and broadband, while reducing its need for extra borrowing.
- (ii) Air New Zealand has operated successfully under this model, since it was introduced.
- (iii) It improves the pool of investments available to New Zealand investors and deepens the capital markets.
- (iv) It allows companies to access capital and grow without depending entirely on the Government.
- (v) External oversight places sharper discipline and more transparency on a company's performance. It is doubtful that Air New Zealand would have performed as well as it has outside this model.

The Government's five tests for proceeding

The Government states it decided to pursue extending the mixed ownership model after being assured the following five tests can be met:

- (i) The Government will maintain a majority shareholding stake by owning more than 51 per cent of each company.
- (ii) New Zealand investors will be at the front of the queue for shareholdings, and the Government is confident of widespread and substantial New Zealand share ownership.
- (iii) The companies involved will provide good opportunities for investors.

- (iv) The capital freed up will be used on behalf of taxpayers to fund new public assets and thereby reducing the pressure on the Government to borrow.
- (v) The Government is satisfied that industry-specific regulations will adequately protect New Zealand consumers.

What is the Treasury's advice to the Government?

The Treasury advised the Government that it is confident that all five of the Government's tests (see above) can be met. It has advised that extending the mixed ownership model:

- (i) Has significant merit because of the potential to reinforce efficiency, fiscal and capital market policy goals, and provide moderate economic gains.
- (ii) Is viable over a three to five year programme, but is a complex undertaking by international standards.
- (iii) Will require a high degree of flexibility.

New Zealanders will get priority in buying shares

New Zealand investors will be given first priority to buy shares in the companies. The Government states that experience from previous government initial public offerings (including Contact Energy and Auckland International Airport) suggests we can achieve widespread and substantial New Zealand ownership across the five companies. There is substantial capacity between KiwiSaver funds, other managed funds and retail investors, the Government's own investment arms and iwi. Detailed decisions to achieve this are yet to be made.

Preferred option for selling minority shareholdings

Initial public offerings (IPOs) are the preferred method of extending the mixed ownership model, given the Government's requirement to achieve widespread and substantial New Zealand ownership across the five companies.

How much will the Government retain in each company?

No decisions have been taken on precisely how much of each company will be retained by the Crown – other than the Government will retain a majority shareholding.

Implications for other state owned enterprises

No other SOEs are being considered as candidates for the mixed ownership model.

The Government's decision and next steps

The Government will take the policy into the election in November 2011. The Treasury will now prepare a

mixed ownership model work programme for 2012 – although this will not commit the Government to proceeding before it receives a mandate at the election later this year. Iwi will also be consulted before the mixed ownership model programme is finalised.

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