

In Confidence

Office of the Minister of Revenue

Chair, Cabinet Business Committee

## **Ex gratia payments to KiwiSaver members**

### **Proposal**

1 I propose that the Cabinet Business Committee approve Inland Revenue providing ex gratia payments of up to \$10 million to a number of KiwiSaver members. The ex gratia payments would compensate members impacted by delays in passing on contributions to scheme providers since 17 April 2020. The majority of contributions held were employer contributions. While Inland Revenue resolved the majority of these instances by 31 May 2020, a number of contributions were further delayed while issues were resolved. Using a generic formula, Inland Revenue proposes to compensate this group of KiwiSaver customers for the delay in transferring contributions to their investment provider by making ex gratia payments from within its existing appropriations. Cabinet approval is required for ex gratia payments of more than \$75,000.

### **Background**

2 On 17 April 2020, KiwiSaver moved to new systems and processes as part of the implementation of Release 4 of Inland Revenue's business transformation programme.

3 As a result, processing times for KiwiSaver are now much faster. For example, in October 2020, Inland Revenue passed on approximately 92% of contributions within two working days. Prior to KiwiSaver moving to Inland Revenue's new system, START<sup>1</sup>, it could take up to three months to transfer contributions to scheme providers as Inland Revenue had to wait until employers had sent the funds. Processing of the annual government contribution is also much faster. In the first 9 working days of July 2020, more than \$840 million had been transferred compared with \$285 million at the same time in 2019.

4 KiwiSaver members have better information about their contributions and can do more online for themselves. Anomalies, such as deductions not being received from an employer, can now be identified more easily.

5 Inland Revenue's primary focus following Release 4 go-live was on ensuring that the correct KiwiSaver contribution amounts continued to flow through to members' accounts with their scheme providers. Since 17 April, the vast majority of employer and member contributions, representing a total value of approximately \$3.4 billion, have been passed on quickly to scheme providers.

6 There are a number of cases where there have been significant delays in passing on contributions to scheme providers resulting from transitional issues.

7 During cut over for Release 4, when Inland Revenue was moving data between its old and new systems, some issues with the data in the legacy systems were encountered. Detailed analysis identified that these issues were not related to individual scheme members' accounts. Inland Revenue made the call to move forward with the release and quarantined these issues for follow

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<sup>1</sup> START stands for simplified tax and revenue technology and is the name Inland Revenue has chosen for the GenTax software provided by FAST Enterprises LLC.

up after go-live. Transactions that related to these quarantined items were subsequently held up while the issues were resolved. There were a number of complexities involved in moving KiwiSaver to START.

- 7.1 KiwiSaver was previously managed in two separate systems and data had to be moved out of both these old systems into START.
  - 7.2 Prior to 1 April 2020, Inland Revenue had to wait until funds had been received from employers before employer contributions could be passed on to scheme providers. From 1 April 2020, Cabinet agreed to allow Inland Revenue to pass on employer contributions as soon as an employer advises the amount, i.e. before the funds are received (CAB-19-MIN-0109 refers). This has led to some transitional issues as employer contributions have to be treated differently depending on what period they relate to.
- 8 Officials advise me that contributions held for review after Release 4 go-live in April and passed to scheme providers up until 31 May 2020 should be considered as having been sent in a reasonable time. Approximately 85% of the held contributions were passed on by 31 May 2020. Inland Revenue has now released the majority of the remaining 15% of contributions to scheme providers. There are still a small number of contributions Inland Revenue is working through. Many of the things that have caused delays are transitional and Inland Revenue expects to continue to improve the average speed with which contributions are passed on.
- 9 Members do receive interest on contributions Inland Revenue holds at a rate set by legislation. The interest rate payable since 8 May 2020 has been 0%. I believe it is appropriate that Inland Revenue compensates the KiwiSaver members that have had contributions held by the department for a significant period of time by making ex gratia payments to them. The investment market has performed well during the period these contributions have been held by the department.
- 10 Inland Revenue estimates the total amount of compensation to be paid to affected members is up to \$10 million. Although up to 750,000 members are estimated to be affected, the majority of compensation amounts would be relatively small. Current estimates indicate that 95% of the affected members would receive compensation of less than \$50.

### **Calculation of payments**

- 11 Compensation would apply to the contributions held for review after go-live of new systems and processes for KiwiSaver on 17 April 2020 and sent to scheme providers after 31 May 2020.
- 12 Inland Revenue would use a generic formula to calculate ex gratia payments to individual members, rather than considering each individual members' circumstances. Given the number of members involved, a case-by-case approach would be complex and involve considerable work not only for Inland Revenue but also for scheme providers.
- 13 The formula assumes KiwiSaver members have invested in a growth fund. This would result in members, on average, being slightly overcompensated but it would vary from member to member. Inland Revenue has averaged the percentage change in unit price figures for growth funds from the default KiwiSaver scheme providers.<sup>2</sup> The unit prices used to calculate the compensation to be paid to members are for the last working days of the months between May to October 2020 and for 12 November 2020, when the majority of the held contributions were passed on.

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<sup>2</sup> Eight out of nine default KiwiSaver scheme providers use unit pricing to calculate investment returns. One does not use unit pricing as its base methodology for calculating investment returns.

- 14 In my view, this is a pragmatic and fair approach. It means that Inland Revenue would make ex gratia payments of up to \$10 million to affected KiwiSaver members from its existing appropriations. These payments would be made as soon as possible following Cabinet's approval and would be made on a pro rata basis to reflect the date members' contributions were passed on.
- 15 I do not see any ongoing fiscal risk, as Inland Revenue's new systems and processes will ensure members' future KiwiSaver contributions are passed on to scheme providers in a timely manner.
- 16 Cabinet Office Circular CO 18 (2) requires ex gratia payments of more than \$75,000 to be approved by Cabinet.
- 17 Inland Revenue would fund the payments from the existing appropriation for business transformation. There would be no impact on the delivery of the transformation programme.

### **Consultation**

- 18 Inland Revenue has consulted with the Treasury on this proposal. Treasury has advised that a new appropriation is required to make these payments as they are out of scope of existing Vote Revenue appropriations.

### **Financial Implications**

- 19 The proposals in this paper have no financial implications.

### **Human Rights**

- 20 The proposals in this paper have no human rights implications.

### **Legislative Implications**

- 21 The proposals in this paper do not require any changes to legislation.

### **Regulatory Impact Analysis**

- 22 The proposals in this paper do not require a Regulatory Impact Statement.

### **Gender Implications**

- 23 The proposals in this paper have no gender implications.

### **Disability Perspective**

- 24 The proposals in this paper have no implications for people with disabilities.

### **Proactive Release**

- 25 I propose to proactively release this Cabinet paper, and associated minutes, within 30 working days of Cabinet making final decisions.

### **Recommendations**

I recommend that the Committee:

- 1 note that some KiwiSaver contributions have been held by Inland Revenue since 17 April 2020;

- 2 note that the delays in passing on contributions have been caused by transitional issues resulting from the move of KiwiSaver to new systems and processes on 17 April 2020;
- 3 note that departmental Chief Executives require authority from Cabinet to incur expenditure on ex gratia payments that are in excess of \$75,000 (Cabinet Office Circular CO (18) 2 refers);
- 4 authorise the Commissioner of Inland Revenue to make ex gratia payments of up to \$10 million to compensate those affected KiwiSaver members whose contributions were passed on to scheme providers after 31 May 2020;
- 5 note that Inland Revenue will use a generic formula for estimating lost investment returns for contributions passed on after 31 May 2020;
- 6 note Treasury advice that the proposed ex gratia payments are out of scope of existing Vote Revenue appropriations and that a new appropriation needs to be set up for this purpose;
- 7 agree to establish the following new appropriation:

Vote	Appropriation Minister	Title	Type	Scope
Revenue	Minister of Revenue	KiwiSaver ex gratia payments	Non-departmental other expenses	This appropriation is limited to ex gratia payments made to customers arising from delays in transferring KiwiSaver contributions held by Inland Revenue to scheme providers.

- 8 note that Inland Revenue is proposing to fund the ex-gratia payments from operating efficiencies in the 'Transformation Multi-Year Appropriation' and that the proposed fiscally neutral funding transfer to the 'KiwiSaver ex-gratia payments appropriation' will not impact on the delivery of the business transformation programme;
- 9 approve the following fiscally neutral adjustments to appropriations:

Vote Revenue Minister of Revenue	\$m – increase/(decrease)				
	2020/21	2021/22	2022/23	2023/24	2024/25 & Outyears
Departmental other expenses: Transformation MYA	(10.000)	-	-	-	-
Non-departmental other expenses: KiwiSaver ex-gratia payments	10.000	-	-	-	-

- 10 agree that the proposed change to appropriations for 2020/21 above be included in the 2020/21 Supplementary Estimates and that, in the interim, the changes be met from Imprest Supply;
- 11 note that the amount transferred to the 'KiwiSaver ex gratia payments' appropriation established in recommendation 9 above is an estimate and that Inland Revenue would seek approval from the Ministers of Finance and Revenue to return any unused funds to the 'Transformation Multi-Year Appropriation' once affected KiwiSaver members have been compensated.

Authorised for lodgement

Hon David Parker  
Minister of Revenue