25OIA2095

21 May 2025

[redacted]

Dear [redacted]

Thank you for your request made under the Official Information Act 1982 (OIA), received on 30 March 2025. You requested the following:

> *Any and all briefings provided to Ministers on options to amend tax credit settings to:*
>
> - *enable greater financial security AND/OR*
> - *reduce the Effective Marginal Tax Rate of low income individuals*
>
> *Any and all briefings to Ministers provided in the last 5 years on the impacts on high effective marginal tax rates.*

On 2 April 2025 you clarified your request to confirm that the tax credit settings refer to Working for Families Tax Credits.

Information being released

I have decided to release 14 documents in scope of your request, attached as **Appendix A**. My decisions on release are outlined in **Table 1** below. Where information is withheld, the relevant withholding ground is applied. Some information has been withheld under section 9(2)(a) of the OIA, to project the privacy of natural persons.

Table 1: Documents released

Item	Date	Document	Decision
1.	21/01/2021	Confirmation of decisions for the Budget 2021 proposal to increase main benefit rates	Released in full
2.	29/03/2021	The interaction between the MFTC and WFF abatement thresholds	Partially released
3.	08/04/2021	Working for Families Tax Credits introductory briefing	Partially released
4.	08/04/2021	Welfare Overhaul Working for Families Review	Partially released
5.	16/04/2021	Working for Families Review: revised recommendations	Partially released
6.	18/04/2021	Data on the prospective extended BSTC option	Released in full

Item	Date	Document	Decision
7.	17/09/2021	Working for Families Review update and options for Budget 2022	Partially released
8.	22/09/2021	Speaking notes for Income Support Ministers meeting on the Working for Families Review	Released in full
9.	04/11/2021	Initial Working for Families changes to support low-income families	Partially released
10.	21/07/2022	Working for Families Review – Public Engagement	Partially released
11.	27/09/2022	Update on Working for Families – October Income	Partially released
12.	27/04/2023	Future direction of the Working for Families Review	Partially released
13.	02/08/2023	Further information on The Working for Families Review options – DRAFT*	Partially released
14.	18/06/2024	Response to the impending overlap of the Working for Families abatement threshold and Minimum Family Tax Credit threshold	Partially released

The attached Cabinet paper is in draft form, and was not considered by Cabinet.

Information withheld/refused

I have identified 13 additional documents in scope of your request and have decided to withhold these documents, as well as their titles, in full under section 9(2)(f)(iv) of the OIA, to maintain the constitutional conventions for the time being which protect confidentiality of advice tendered by Ministers of the Crown and officials.

There are 7 documents that are not able to be found. I have decided to refuse these documents in full under section 18(e) of the OIA, as the documents alleged to contain the information requested do not exist or, despite reasonable efforts to locate them, cannot be found. The documents are as follows:

Table 2: Documents not located

Item	Document
1.	Welfare Overhaul: Working for Families Review
2.	Budget Sensitive Briefing Note - Proposed benefit increases and their impact on MFTC/WFF
3.	Proactive release: CPI indexation of Family Tax Credit/Best Start Tax Credit and adjustment of Minimum Family Tax Credit
4.	Increase in Working for Families Tax Credit Rates

Item	Document
5.	Working for Families review – administrative options and remedial amendments
6.	Working for Families Review: Administrative and remedial options
7.	Working for Families tax credits penalties and interest on overpayment debt: future direction

As required by section 9(1) of the OIA, I have considered whether the grounds for withholding the information requested is outweighed by the public interest. In this instance, I do not consider that to be the case.

Information publicly available

Table 3 outlines 20 documents in scope of your request that are or will soon be publicly available on Inland Revenue's Tax Policy website (taxpolicy.ird.govt.nz) or at the following links:

- Information release: Working for Families Tax Credit December 2022: https://www.taxpolicy.ird.govt.nz/-/media/project/ir/tp/publications/2022/2022-ir-cab-swc-22-sub-0190/2022-ir-cab-swc-22-sub-0190-pdf.pdf?modified=20221212033006&modified=20221212033006
- Budget 2024 Information Release: www.taxpolicy.ird.govt.nz/publications/2024/ir-budget-2024
- OIA Request: https://www.ird.govt.nz/-/media/project/ir/home/documents/oia-responses/september-2024/2024-09-18-data-about-the-minimum-family-tax-credit-for-past-two-years.pdf?modified=20250117003732&modified=20250117003732

Table 3: Documents publicly available or soon to be publicly available

Item	Date	Document
1.	21/07/2022	Working for Families Review: Evidence and Options
2.	27/09/2022	Working for Families Review: CPI indexation of Family Tax Credit/Best Start Tax Credit and adjustment of Minimum Family Tax Credit threshold
3.	20/10/2022	CPI indexation of Family Tax Credit/Best Start Tax Credit and adjustment of Minimum Family Tax Credit Cabinet documents
4.	15/11/2022	Working for Families Review: Further advice on options to progress for Budget 2023 and beyond
5.	14/03/2023	Working for Families: Improving support for working families and Budget 2023
6.	20/07/2023	Working for Families Review Preferred approach for December Cabinet report back

Item	Date	Document
7.	23/02/2024	Working for Families changes for Budget 2024
8.	07/03/2024	Interaction between the Independent Earner Tax Credit and Working for Families tax credit
9.	19/03/2024	Implementing Budget 2024 Personal Income Tax Proposals
10.	27/03/2024	Consequential impacts of Personal Income Tax Changes
11.	04/04/2024	Consequential amendments to the Minimum Family Tax Credit following Budget decisions
12.	04/04/2024	Personal Income Tax - Implications of a 31 July application date
13.	10/04/2024	Relationship between the Minimum Family Tax Credit threshold decisions and Working for Families abatement threshold
14.	11/04/2024	Cover note for MFTC report [IR2024/119 refers]
15.	12/04/2024	Further information – changes to the Minimum Family Tax Credit threshold in line with Budget 2024 package
16.	18/04/2024	Sharing information to enable implementation of the Personal Income Tax Changes
17.	21/05/2024	Update on Public Sector Organisations' PIT change readiness
18.	21/05/2024	Part- Year transfer recipients - worked example
19.	23/05/2024	Budget Sensitive - Australia and New Zealand Personal Income tax thresholds and rates
20.	02/09/2024	Independent Earner Tax Credit and Working for Families interaction

I am therefore refusing these documents under section 18(d) of the OIA, as they are or will soon be publicly available. Item 20 will soon be publicly available as part of the second proactive release of the Taxation (Annual rates for 2024-25, Emergency Response, and Remedial Measures) Bill on Inland Revenue’s Tax Policy website (taxpolicy.ird.govt.nz).

Right of review

If you disagree with my decision on your OIA request, you have the right to ask the Ombudsman to investigate and review my decision under section 28(3) of the OIA. You can contact the office of the Ombudsman by email at: info@ombudsman.parliament.nz.

Publishing of OIA response

We intend to publish our response to your request on Inland Revenue’s website (ird.govt.nz) as this information may be of interest to other members of the public. This letter, with your personal details removed, may be published in its entirety. Publishing responses increases the availability of information to the public and is consistent with the OIA's purpose of enabling more effective participation in the making and administration of laws and policies and promoting the accountability of officials.

Thank you again for your request.

Yours sincerely

Samantha Aldridge
Policy Lead – Families and Individuals

Appendix A

Item 1

MINISTRY OF SOCIAL DEVELOPMENT
TE MANATŪ WHAKAHIATO ORA

DEPARTMENT OF THE PRIME MINISTER AND CABINET
TE TARI O TE PIRIMIA ME TE KOMITI MATUA

Inland Revenue
Te Tari Taake

TE TAI ŌHANGA
THE TREASURY

Report

Date: 21 January 2021

To: Rt Hon Jacinda Ardern, Prime Minister, Minister for Child Poverty Reduction
Hon Grant Robertson, Minister of Finance
Hon Carmel Sepuloni, Minister for Social Development and Employment
Hon David Parker, Minister of Revenue

Confirmation of decisions for the Budget 2021 proposal to increase main benefit rates

Purpose of the report

1. This report provides further advice on the Minister for Social Development and Employment's Budget 2021 bid to increase rates of main benefits. It:
   - provides updated modelling using the Half Year Economic and Fiscal Update 2020 (HYEFU);
   - seeks confirmation of key parameters for that bid; and
   - responds to a request for additional information on the youth rates of main benefits.

Executive Summary

2. Joint Ministers met on 1 December 2020 to discuss a possible income support package for Budget 2021. As a result of this meeting, the Minister for Social Development and Employment has been invited to submit a Budget 2021 bid to increase main benefit rates by $25 per week per adult from 1 July 2021 and progress complementary and minor income support changes to reduce the need for Transitional Assistance Payments (TAPs). Together, these changes will:
   - cost $2.2 billion over the forecast period (or $530 million per year in outyears);
   - reduce the number of children living in poverty by 9,000 on the before-housing-costs primary measure (BHC50) and 14,000 on the after-housing-costs primary measure (AHC50), with a margin of error of ±5,000[1]; and

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[1] The poverty modelling is from the TAWA model, which uses Stats NZ's Household Economic Survey. The margin of error is a statistic expressing the amount of unavoidable random sampling error in a survey. The larger the margin of error, the less confidence one should have that the survey-based estimate accurately represents the entire population.

- benefit 436,000 individuals and families, with an average gain of $23 per week when factoring in flow-ons to other assistance (such as the Accommodation Supplement (AS) and Temporary Additional Support (TAS)).

3. This report also seeks your agreement to include a partial increase to the Minimum Family Tax Credit (MFTC) as part of the Budget bid to increase main benefits. A partial increase to the MFTC threshold ensures that sole-parent families (working at least 20 hours per week) continue to be guaranteed to be financially better off receiving the MFTC rather than remaining on benefit. While a partial increase means some two-parent families (working at least 30 hours) may be better off remaining on a benefit, it balances delicate trade-offs associated with fiscal costs, financial incentives to work full-time and the impact of any changes on the upcoming review of Working for Families (WFF).

4. Officials also understand that Ministers do not want to consider consequential increases to rates of student support or financial assistance for caregivers as part of the Budget 2021 bid to increase rates of main benefits. Funding for increases in these areas are therefore being sought independently through separate Budget bids led by the relevant Ministers, either through Budget 2021 or a future Budget.

5. Joint Ministers have also requested further information on the youth rates of main benefits as these rates[2] are between $38 and $173 per week lower than adult rates. Historically, it was considered that younger people generally have lower living costs and required stronger financial incentives to work. Officials' view is that while there are strong grounds for further increases to the youth rates, there are broader considerations, including:
   - fiscal costs;
   - wider trade-offs with other welfare priorities; and
   - risks of creating perverse financial incentives if youth rates of benefit are increased in isolation of increases to Student Allowances.

6. Given these additional considerations, you may wish to consider delaying decisions on youth rates until a future Budget.

Recommended actions

It is recommended that you:

Updated modelling

1. **note** that the Budget bid to increase main benefits (including the complementary changes and the increase to the Minimum Family Tax Credit) will cost $2.2 billion over the forecast period ($530 million per year in outyears) and reduce the number of children living in poverty by 9,000 on the before-housing-costs primary measure and 14,000 on the after-housing-costs primary measure with a margin of error of ±5,000

Summary of key parameters included in the bid

2. **note** that the Budget bid as invited by the Minister of Finance also includes:
   - changes to the Temporary Additional Support (TAS) formula so that the TAS disability exception better reflects disability costs and reduces the number of people financially disadvantaged from future income support changes;
   - changes to the definition of income for Childcare Assistance to exclude other supplementary payments as income; and
   - a Transitional Assistance Payment (TAP) for those financially disadvantaged by the changes

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[2] Youth rates apply to those receiving a main benefit aged between 16 and 24 years old.

3. **note** that the proposed main benefit rate increase has implications for the Minimum Family Tax Credit (MFTC) and was also included in the budget invitation letter

4. **note** that since 2006 the MFTC threshold has been fully aligned with benefit settings to ensure all eligible low-income families are financially better off working at least 20 hours (sole parents) or 30 hours (two-parent families) and receiving the MFTC rather than remaining on an abated main benefit [CAB-MIN-04-13/4]

5. **note** as a departure from the policy, Cabinet recently decided to only partially increase the MFTC in 2021/22 in response to increases in the benefit abatement thresholds [CAB-20-MIN-0512]

6. **agree** that the Budget bid to increase main benefits also include a partial increase to the MFTC threshold to ensure sole-parent families working at least 20 hours per week (but not necessarily two-parent families) will be financially better off receiving the MFTC rather than remaining on the benefit

Yes/No	**Yes/No**	**Yes/No**	**Yes/No**
Minister for Child Poverty Reduction	Minister of Finance	Minister for Social Development and Employment	Minister of Revenue

7. **note** that joint Ministers have previously indicated they do not wish to flow the proposed main benefit increase through to student support or financial assistance for caregivers, and instead any funding for increases in these areas are being sought through separate Budget bids led by the relevant Ministers (either through Budget 2021 or a future Budget)

Youth rates

8. **note** that while changes to youth rates of main benefits could also be included in the Budget Bid, officials recommend deferring consideration of the youth rates of main benefits until Budget 2022

9. **indicate** if you would like to receive further detailed advice on increases to the youth rates of main benefits, including possible complementary changes for the student support system

EITHER

9.1 for Budget 2021

Yes/No	**Yes/No**	**Yes/No**	**Yes/No**
Minister for Child Poverty Reduction	Minister of Finance	Minister for Social Development and Employment	Minister of Revenue

OR

9.2 for Budget 2022

Yes/No	**Yes/No**	**Yes/No**	**Yes/No**
Minister for Child Poverty Reduction	Minister of Finance	Minister for Social Development and Employment	Minister of Revenue

OR

9.3 no further advice in the short to medium-term

Yes/No	Yes/No	Yes/No	Yes/No
Minister for Child Poverty Reduction	Minister of Finance	Minister for Social Development and Employment	Minister of Revenue

10. **note** that if further advice is requested, joint agencies (including the Ministry of Education) will provide updated modelling and advice to joint Ministers (including the Minister for Education)

11. **forward** this report to the Ministers for Children and Education for their information.

Yes/No

Minister for Child Poverty Reduction

Kristie Carter	Keiran Kennedy	Polly Vowles	Eina Wong
Director Child Poverty Unit Department of the Prime Minister and Cabinet	Manager The Treasury	Policy Manager Ministry of Social Development	Principal Policy Advisor Inland Revenue

Rt Hon Jacinda Ardern	Hon Grant Robertson	Hon Carmel Sepuloni	Hon David Parker
Prime Minister and Minister for Child Poverty Reduction	Minister of Finance	Minister for Social Development and Employment	Minister of Revenue

Increasing main benefits through Budget 2021

7. The Minister for Social Development and Employment has been invited to submit a Budget 2021 bid to increase main benefit rates by $25 per week per adult[3] from 1 July 2021. The invitation also included:

    - complementary and minor income support changes that reduce the need for TAPs in the future; and
    - the flow-on cost of a partial increase to the MFTC threshold to ensure sole parent families working at least 20 hours (but not necessarily two-parent families) will be financially better off receiving the MFTC than remaining on a main benefit.

8. The fiscal and distributional impacts of the proposed Budget bid have been costed in line with HYEFU forecasts. Compared to PREFU, HYEFU shows lower forecasted benefit numbers and therefore fiscal costs over the forecast period. A full breakdown of these impacts is attached as Appendix One.

9. The total cost of the main benefit increase is **$2.2 billion** over the forecast period (or $530 million per year in outyears). The expected reduction of this policy change on children living in poverty in 2021/22 is:

    - 9,000 on the before-housing-costs primary measure (BHC50), with a margin of error of 5,000; and
    - 14,000 on the fixed line after-housing-costs (AHC) measure, with a margin of error of 5,000.

10. Approximately 436,000 individuals and families are expected to benefit from the policy, with an average gain of $23 per week when factoring in flow-ons to other assistance (such as TAS and AS). Ministers have previously expressed concerns about main benefit increases being eroded by offsets in TAS; however, TAS recipients would gain by $24 per week on average – with the gains depending on individual circumstances [REP/20/11/1081 provides more information on these interactions].

11. Like other major reforms, such as Budget 2019 changes, there is a group of non-beneficiaries receiving AS who will be disadvantaged due to the flow-on impacts of increasing main benefits[4]. Around 23,000 people would receive a reduction of their AS of around $5 per week. Similar to previous reforms such as the recent $25 per week increase on 1 April 2020, officials do not recommend extending a TAP to cover this group as this flow-on impact is intended, and reflects that this group is likely to experience wage increases throughout the year (e.g. due to the minimum wage increase occurring on 1 April 2021).

Outlining key policy parameters of the Budget 2021 bid

12. The modelling outlined in this paper has been undertaken on the basis of the following policy parameters discussed by joint Ministers. Should the bid be successful, changes to regulations to give effect to these changes as well as an amendment to primary legislation to give effect to the MFTC change will be required.

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[3] "Per adult" includes those under 18 and receiving a main benefit e.g. the Youth Payment.

[4] Increases to main benefits increase the entry threshold for AS meaning that non-beneficiaries are required to use more of their income to cover their accommodation costs.

Amending the Temporary Additional Support formula

13. Currently, TAS recipients with high disability costs can receive additional support above the TAS upper limit through an additional top-up called the disability exception amount[5].

14. Due to a technical anomaly in the TAS formula, a small number of people receiving the disability exception can receive more support for disability costs than the level of disability costs claimed (e.g. receive more TAS than the deficiency in income). Clients with high disability costs can therefore face a significant reduction in their income because of small changes to income support settings, or changes in circumstances, resulting in the complete loss of the disability exception. Further information on the TAS disability exception is outlined in Appendix Three.

15. The Budget bid proposes amending the TAS formula to ensure people receiving the disability exception can no longer receive more in TAS than the deficiency in income. This will result in a short-term reduction in support for some clients. The change in the formula will also make the exception more generous for those with very high disability costs to offset any negative impacts. This will prevent any future instances of financial disadvantage if people have a change in circumstance and/or have an increase in income as a result of the Annual General Adjustment or other income support changes. As a result, TAP's will no longer be required for people with high disability costs in future years.

16. With this proposed change, it is estimated this change in the formula would still financially disadvantage around 120 people (around 60 people more than the number of people disadvantaged if a main benefit increase was progressed on its own). In order to avoid this group being financially disadvantaged, officials recommend also introducing a TAP for the benefit increase on 1 July 2021.

17. While changes to the disability exception are primarily intended to prevent people from being disadvantaged going forward, they are also expected to benefit around 1,600 people with high disability costs by an average of $24 per week (in addition to any gains from the main benefit increase itself). The policy change is estimated to cost around $2.6m per year and $9.2m over the five-year forecast period.

18. This change is consistent with the intent of a number of the recommendations made by the Welfare Expert Advisory Group, including recommendations related to reforming supplementary and hardship assistance to improve income adequacy and improving the health and wellbeing of people with health conditions and disabilities.

Changing the definition of income for Childcare Assistance

19. Currently, Childcare Assistance is the only supplementary assistance which considers other supplementary assistance as income. This means that increases in benefit rates and the flow-on effects to supplementary assistance can reduce eligibility for Childcare Assistance. This could reduce the financial incentive for people to work. For example, two low-income families with the same level of childcare costs and income can receive very different levels of support for childcare depending on whether or not they receive AS.

20. Amending the definition of income for Childcare Assistance would exclude other supplementary payments as income, to reduce the impact of income support increases on eligibility for Childcare Assistance. This change will prevent around 260 people from being financially disadvantaged from the main benefit increase and all future increases. The change will also provide additional support to around 2,200 families with childcare costs (by an average of $24 per week) most of which are non-beneficiaries.

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[5] The disability exception amount is calculated as 30 percent of the client's excess disability costs (total disability costs minus their Disability Allowance).

21. If the main benefit bid does not progress through Budget 2021, officials recommend that this change is instead progressed through the Minister for Social Development and Employment's Budget 2021 bid 'Improving Childcare Assistance'. This is because this change is a key element for improving access to Childcare Assistance for low- and middle-income families. This change was also one of the detailed recommendations in the Welfare Expert Advisory Group's report in 2019.

Partial increase to the Minimum Family Tax Credit - to ensure all sole parents working at least 20 hours per week are financially better off receiving the MFTC than they would be remaining on the benefit.

22. The policy intent behind the MFTC is to provide a financial incentive for low-income families to move off the benefit and into "full time" work. For MFTC purposes, "full-time" is defined as 20 hours or more per week for sole-parent families, and 30 hours or more per week for two-parent families.

23. Since 2006, Cabinet policy has been to fully align the MFTC threshold with benefit settings to ensure all low-income families, regardless of whether they are sole parent or two-parent families, are financially better off working and receiving MFTC rather than on benefit [CAB Min (04) 13/4].

24. However, as part of its December 2020 decision to increase to the benefit abatement thresholds, Cabinet departed from this policy, agreeing to only partially increase the MFTC threshold for the 2021/22 tax year [CAB-20-MIN-0512].

25. This partial increase ensured sole parent families working at least 20 hours per week (approximately 90 percent of MFTC recipients) would still be financially better off receiving the MFTC rather than remaining on benefit. However, two-parent families working at least 30 hours per week (approximately 310 MFTC recipients) could potentially be better off remaining on benefit than receiving the MFTC.

We are seeking agreement to continue with the partial increase approach to the MFTC alignment if main benefit rates are increased

26. A partial increase to the MFTC threshold would still ensure that sole-parent families working at least 20 hours per week are guaranteed to be financially better off receiving the MFTC than they would be remaining on benefit. The MFTC threshold would be increased to $32,396 (after tax per year) from 1 July 2021 to 31 March 2022. This partial increase would have a fiscal cost of $32m over the forecast period (1 July 2021 to 30 June 2025). The fiscal cost may increase if any two-parent families move back onto an abated main benefit.

27. By comparison, under a full increase of the MFTC threshold, all eligible MFTC recipients (both sole parent and two-parent families) would be financially better off receiving the MFTC than they would be remaining on benefit. The MFTC threshold would be increased to $35,672 (after tax per year) for the same period. A full increase would cost $56m over the forecast period, with a small proportion of this cost offset by savings resulting from any two-parent families not going back onto the benefit.

28. As was the case in December 2020 when the benefit abatement thresholds were increased, the trade-offs between full and partial increases of the MFTC threshold are:

- the fiscal cost of full alignment, and the impact full alignment would have on the upcoming review of the WFF; versus
- the removal of the work incentives the MFTC provides to two-parent families.

29. In the present situation an additional issue arises under the full alignment approach. The size of the proposed benefit increase ($25 per adult) would mean that from 1 April 2023, a fully aligned MFTC threshold would (on a grossed-up basis) exceed the WFF abatement threshold ($42,700). This would not occur under the partial increase approach, at least not for the forecast period.

30. If the MFTC threshold were to exceed the WFF abatement threshold, MFTC recipients would see a reduction in their Family Tax Credit and In-Work Tax Credit entitlements they previously might have received. Therefore, officials consider the full increase approach is not an appropriate option at this time. The relationship between the MFTC threshold and the WFF abatement threshold will be considered as part of the review of WFF which will be in 2021 [REP/20/11/1047 refers].

The bid to increase main benefits will not include consequential increases to student support…

31. Officials understand that Ministers do not want to consider consequential increases to rates of student support as part of the Budget 2021 bid to increase rates of main benefits. This is on the basis that while the $25 weekly increase to main benefits earlier this year improved relativities between the two sets of rates, the base rates of main benefits generally remain around $25 per week lower than student support because of the $50 weekly increase to student allowance and student loan living cost rates in 2018.

32. The Minister of Education has been invited to submit a Budget 2021 bid to index Student Allowances rates and the maximum Student Loan living cost entitlement to wage growth to align with main benefit adjustments.

… or financial assistance for caregivers

33. Officials understand that Ministers do not wish for increases to main benefit rates to flow through to the Orphan's Benefit (OB), Unsupported Child's Benefit (UCB), or Foster Care Allowance (FCA)[6].

34. Following the $25 increase to main benefits as part of the COVID-19 response, rates of OB/UCB/FCA were independently increased by $25 per week. Increases to OB/UCB/FCA are generally progressed separately or alongside FTC increases because these payments are considered more analogous to FTC than main benefits given they are designed to meet the cost of children.

35. Oranga Tamariki have advised that the Minister for Children has been invited to submit a Budget 2021 bid to increase financial assistance for caregivers. This bid has three components:

    - removing the remaining disparities in standardised payments for caregivers receiving the OB, UCB, and FCA, by increasing the base rate of the OB and UCB by $30 for children aged 0-4 years, and $10 for children aged 5 years and over[7]
    - a small increase to the nappy payment for OB, UCB and FCA caregivers, to more accurately reflect the cost of nappies
    - Further increasing the base rate of the OB, UCB and FCA by $10 per week.

Additional advice on youth rates of main benefits

36. At the joint Ministerial meeting on 1 December 2020, further information was requested on the youth rates of main benefits. Youth rates of main benefits[8] are currently between $38 and $173 per week lower than adult rates depending on age and living circumstances. The following table shows the current rates by age and benefit.

[6] OB/UCB provide financial assistance to caregivers who care for children outside of the state care system. FCA provides financial assistance to caregivers of children in the state care system.

[7] This base rate increase accounts for the standard and nappy payments which are currently received by FCA caregivers but not OB/UCB caregivers.

[8] Youth rates apply to those receiving a main benefit aged between 16 and 24 years old.

<table>
<tr><th>Age</th><th>Jobseeker Support
(without children)</th><th>Sole Parent Support</th><th>Supported Living Payment
(single without children)</th></tr>
<tr><td>16 to 17</td><td>$213 for those who can't live with their parents or guardian and aren't supported by them or anyone else (Youth Payment) – 2,000 recipients</td><td>$202 for those who either are living with or supported by parents who earn less than FTC income threshold (Youth Parent Payment) – 1,000 recipients

$375 for those not living at home or being supported by their parents</td><td>$253 – 1,000 recipients</td></tr>
<tr><td>18 to 19</td><td>$213 living away from home – 5,000 recipients

$175 living at home – 8,000 recipients</td><td rowspan="3">$375</td><td rowspan="3">$307</td></tr>
<tr><td>20 to 24</td><td>$213 – 36,000 recipients</td></tr>
<tr><td>25+</td><td>$251</td></tr>
</table>

37. There are several historical reasons why youth rates are set lower than adult rates.

- **Stronger financial incentives to work -** it was considered important that young people were encouraged to work. People under 25 normally earn less so the lower rate was intended to keep benefit payments in proportion with what they earn.
- **Likely to have lower living costs -** it was generally assumed that young people have more flexible, less expensive living arrangements and fewer financial responsibilities. People over the age of 25 were considered more likely to have other financial commitments than those under that age.

38. However, the lower rates of main benefits for young people may no longer be entirely justified on these grounds. Paying lower rates of financial assistance based on age can therefore have human rights implications. The Ministry of Social Development has received a number of human rights complaints on the basis of age seeking justification for the difference in rate and has one active human rights complaint about this issue.

- Over time, the gap between benefits and work has increased significantly for people without children, therefore there are strong financial incentives to work even if young people were paid at the higher adult rate.
- Young people living independently may not have lower living costs than those aged 25 and over. Currently, someone aged 24 living away from home will receive around $40 per week less in benefit assistance, even though they may face the same costs as someone aged 25 and over. Moreover, supplementary payments such as the AS and TAS already account for different levels of housing costs.
- Lower youth rates can exacerbate existing income adequacy issues faced by single people in the benefit system, particularly those who face the same costs as those receiving the higher adult rate of benefit. These adequacy issues may cause young adults to take the first job available to them, rather than being able to find a job that matches their skills, experience or interest.

39. In the table below, officials have modelled two options to better align youth rates with adult rates of main benefits. It is important to note that while making changes to youth rates will improve income adequacy and alleviate poverty and hardship for young people

without children, there are no/minimal child poverty implications because beneficiaries with children generally already receive the adult rate of benefit[9].

Option	Description	Additional fiscal cost	Child Poverty impacts
Align youth rates of main benefits with adult rates (increases of $40 to $175 per week)	This approach would pay young people the same as other adults, but for those receiving Jobseeker Support aged 18-19 living at home, the rate would become equivalent to what someone in a relationship (i.e. half the couple rate of benefit) would receive.	**$394m over forecast period** **($90m p.a.)**	No additional impact
$50pw increase to youth rates	This approach would increase youth rates by a further $25 per week, in addition to the $25 per week increase applied to all rates.	**$269m over forecast period** **($61m p.a.)**	No additional impact

40. The options in the table above still retain the 'living at home' rates of benefit. Removing the living at home rates entirely would add an extra $21m per year to the fiscal costs (or $93m over the forecast period). Officials do not recommend considering this option further when trading-off fiscal costs, child poverty impacts and interactions with the student support system (outlined further below).

Any decisions around youth rates of main benefits should consider interactions with the student support system

41. While there may be strong grounds for making changes to youth rates, officials recommend deferring decisions on these rates until Budget 2022. This is to ensure the proposal can be considered alongside wider priorities, both within welfare and wider government priorities (such as health and education). This is particularly important given the wider interactions with the student support system (e.g. financial incentives to study) that need to be worked through, as a large number of student allowance recipients also receive the youth rates of student allowances. Historically, student support rates have generally been set at the same level, or higher, than main benefit rates to ensure that study is not discouraged.

42. Increasing main benefit rates by $25 per week alongside the removal of the youth rates would mean main benefit rates would be higher than student allowances for young people (e.g. almost $40 per week higher for those living away from home) which may disincentivise young people from studying. This is before considering the Winter Energy Payment and the differing rates of accommodation support across the two systems. The following table outlines several key differences between the student and benefit systems and Appendix Two compares rates of support between benefits and students.

	Student Allowance	Jobseeker Support (Main benefits)
Age	Qualify for adult rate at 24. Entitled to support at 16 in some circumstances.	Qualify for adult rate at 25. Entitled to support at 16 in some circumstances.
Relationship status	Relationship is recognised where the student and their partner are both at least 24, and/or they have a child. Otherwise considered single.	Relationship is recognised regardless of age.

[9] A small group of 16/17 teen parents receive the youth rate of YPP. In addition, there may be child poverty impacts if young people live in multi-family households where there are children living in the wider household.

	Student Allowance	Jobseeker Support (Main benefits)
Parental income	Parental income is taken into account in most cases up until age 24.	No impact (other than for Young Parent Payment).
Impact of living at home	Rates are lower if living with parents or guardians, regardless of age.	Rates are lower if living with parents or guardians, only when aged 18-19.
Housing support	Accommodation Benefit of up to $60 per week for those living away from home (sole parents receive Accommodation Supplement rates).	Accommodation Supplement
Winter Energy Payment	Not eligible	Eligible
Approach to indexation	CPI – *note the Minister of Education is progressing a bid through Budget 21 to index Student Allowances and the maximum Student Loan living cost entitlement to wage growth*	Wage growth

Next steps

43. Subject to your agreement to the parameters of the bid to increase main benefits by $25 per week per adult, the Minister for Social Development and Employment will submit this bid for consideration as part of Budget 2021 next week.

44. Should you wish to consider options to increase the youth rates of main benefits through Budget 2021, officials can provide joint Ministers and the Minister of Education with further detailed advice, including options for complementary changes in the student support system to avoid any potential implications these decisions may have for young people's decisions on their education and employment.

Appendix One

Table 1: Financial implications

	2020/21	2021/22	2022/23	2023/24	2024/25	5-year total
Main benefit increases		$534.7m	$530.5m	$523.0m	$513.8m	$2,102.0m
Changes to TAS disability exception		$2.1m	$2.2m	$2.4m	$2.6m	$9.2m
Change to CCA income definition		$3.8m	$4.2m	$4.6m	$5.2m	$17.8m
MFTC		$8.0m	$8.0m	$8.0m	$8.0m	$32.0m
Project costs		$2.3m	-	-	-	-
Cost of package		**$550.9m**	**$544.9m**	**$538.0m**	**$529.6m**	**$2,161.3m**

45. Note that the costs and distributional analysis include interactions with the already agreed benefit abatement changes but do not include the direct impacts of this policy in these figures. Officials can provide further modelling on the combined impact of these changes as part of any communications material.

Table 2: Child Poverty impacts

Options	Child Poverty BHC50 (primary measure)	Child Poverty AHC50 (primary measure)
Main benefit increases	9,000 (±5,000)	14,000 (±5,000)
Youth rates	No impact	No impact

Table 3: Distributional impacts

	Average gains		Financially disadvantaged	
	Numbers who gain	Average gain	Numbers worse off	Average loss
Main benefit increases	436,000	$23	23,000	$6
Changes to TAS disability exception	1,600	$24	120	$15
Change to CCA income definition	2,200	$24	0	$0
Total package	437,000	$23	23,000	$6

Appendix two – comparing levels of benefit and student support with the proposed $25 increase and with the removal of youth rates for benefit

The below table shows the anticipated levels of Jobseeker Support from 1 July 2021 (should the Budget 21 bid to increase main benefits be successful) in comparison with current levels of student support (noting this will increase on 1 April 2021 with the Annual General Adjustment). The table is based off the single rate of Jobseeker Support with no children. The table does not include the Winter Energy Payment (WEP) which would increase the level of support for those receiving a main benefit during the winter months.

Age	**Benefit (Jobseeker Support)** * *net (after tax code M) with $25 increase and AGA, without WEP*	**Student Allowance** * *net (after tax code M), not including AGA*
16-17	**$242.47** (Youth Payment for those not living with, or supported by their parents)	Away from home: up to **$237.90**
16-17 – with youth rates of benefit removed	**$280.88** (Youth Payment for those not living with, or supported by their parents)	Away from home: up to **$237.90** *$42.98 less than benefit*
18-19	At home: **$204.08** Away from home: **$242.47**	At home: up to **$200.79** Away from home: up to **$237.90**
18-19 - with youth rates of benefit removed	At home: **$229.71** Away from home: **$280.88**	At home: up to **$200.79** *$28.92 less than benefit* Away from home: up to **$237.90** *$42.98 less than benefit*
20-24 (20-23 for students)	**$242.47**	At home: up to **$200.79** Away from home: up to **$237.90**
20-24 (20-23 for students) **– with youth rates of benefit removed**	**$280.88**	At home: up to **$200.79** *$80.09 less than benefit* Away from home: up to **$237.90** *$42.98 less than benefit*
25+ (24+ for students)	**$280.88**	At home: **$230.47** Away from home: **$275.02**
25+ (24+ for students) **– with youth rates of benefit removed**	**$280.88**	At home: **$230.47** *$50.41 less than benefit* Away from home: **$275.02** *$5.86 less than benefit*

Appendix Three: Further information on the TAS disability exception

Issue

1. The amount of TAS that can be paid is determined by a formula which assesses whether a client's costs are greater than their income. The amount of TAS available is generally equal to their income deficiency, up to a limit of 30 percent of their main benefit rate (the upper limit). The disability exception amount allows clients who are receiving the upper limit of TAS to receive additional support if their disability-related costs are greater than the available Disability Allowance.
2. The disability exception amount was intended to ensure that clients were not financially disadvantaged when TAS replaced the Special Benefit in 2006. The disability exception, and its design, was only meant to be a temporary arrangement until a long-term solution could be found.
3. Due to a technical anomaly in the TAS formula, a small number of people receiving the disability exception can receive more support for disability costs than both the level of disability costs claimed and the deficiency in income. Clients with high disability costs can therefore face a significant reduction in their income because of small changes to income support settings, or changes in circumstances, resulting in the complete loss of the disability exception.
4. Early last year, MSD estimated that around 70 people with high disability costs would lose an average of $13 from the Annual General Adjustment every year. This number increases when you include any income support policy changes or changes in circumstances from clients.

Example

5. The example below shows how a TAS recipient can have an income deficiency of $82.60 per week, yet receive a TAS payment of $112.32 per week due to qualifying for the disability exception. If this person has an income increase of 50 cents or more it can mean they lose the entire $30.21 disability exception as they no longer qualify for the TAS upper limit and therefore the disability exception.

	Hypothetical rates
<u>Costs</u>	
Accommodation Costs (minus accommodation loading)	$134
Disability	$165
Standard Costs (70% of Main Benefit)	$191.59
Total Costs (A)	**$490.59**
<u>Income</u>	
Supported Living Payment	$273.70
AS	$70
DA	$64.29
Total Income (B)	**$407.99**
Total Income Less Total Costs (deficiency) (=A-B)	-$82.60
Upper Limit for TAS (30% of Main Benefit) (C)	$82.11
Disability exception (D)	$30.21 (= ($165-$64.29) x 30%)
Total TAS (= C+ D)	**$112.32** ($82.11 upper limit plus $30.21 disability exception amount)
Total Financial Assistance	**$520.31**

Solution

6. To address this issue requires a change to the underlying TAS formula to ensure people are no longer entitled to a payment amount that is greater than the deficiency in their income. Because some people can currently receive more than their income deficiency, it means some people will be financially disadvantaged. In effect, this change increases the number

of people worse off in the short term but prevents any people from being worse off over the medium to long term. Those worse off in the short term will be compensated by a one-off TAP as described in the body of the report.

7. At the same time, it is proposed that the disability exception amount would be changed so that it meets the first $100 of excess disability costs in full (rather than a partial subsidy). The remaining costs would continue to be subsidised at the current co-payment rate of 30 percent. This helps mitigate the negative impacts from fixing the anomaly in the TAS formula and means 1,600 people benefit by $24 per week.

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Briefing note

Reference:	BN2021/140
Date:	29 March 2021
To:	Revenue Advisor, Minister of Revenue – Thomas Allen Private Secretary, Minister of Revenue – Nikki Chamberlain
cc:	Naomi Ferguson, Commissioner David Carrigan, Deputy Commissioner Emma Grigg, Policy Director Kerryn McIntosh-Watt, Policy Director Phil Whittington, Chief Economist Joanne Petrie, Executive Support Advisor to the Commissioner Jill Compton, PA to Deputy Commissioner Josh Green, Manager, Government & Executive Services
From:	Philip Marshall, Senior Policy Advisor
Subject:	**The interaction between the MFTC and WFF abatement thresholds**

Purpose of this note

1. You have asked us to provide additional information on the issues that relate to the closing gap between the minimum family tax credit (MFTC) threshold and the Working for Families (WFF) abatement threshold. This includes the mechanics of how the MFTC threshold and the WFF abatement threshold interact, and whether a cross-over of these two thresholds would result in a shift of customers back to the benefit system.

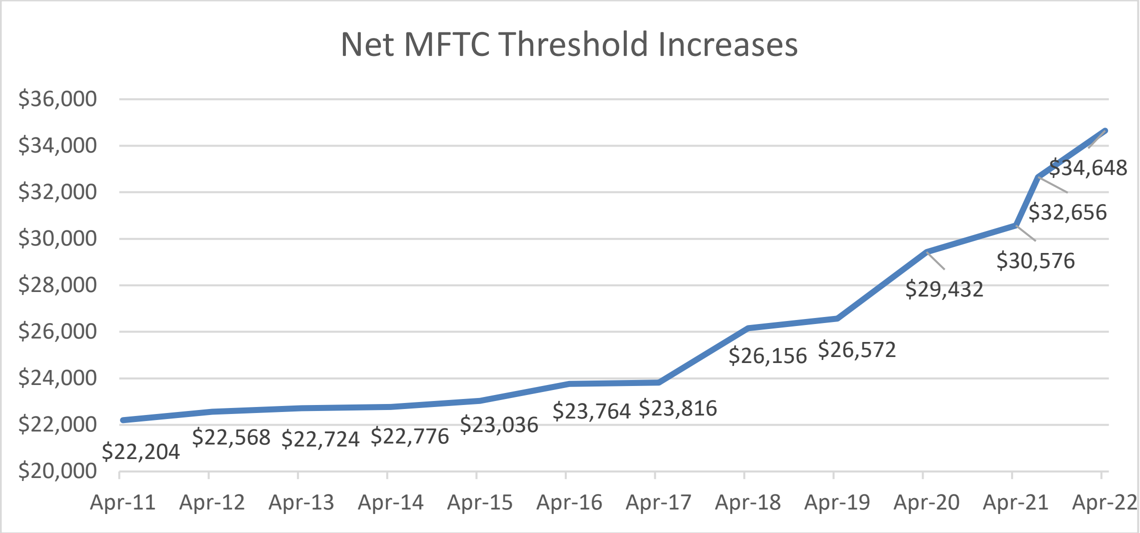
Context

2. The MFTC provides a financial incentive to low-income families to move off the benefit and into "full-time" work. For the tax credit system to work as intended, the MFTC must be increased whenever main benefits go up. The current MFTC threshold is $29,432 (after tax). This will increase to $30,576 ($35,874 before tax) from 1 April 2021.

3. The WFF abatement threshold is the point at which Family Tax Credit (FTC) and In-Work Tax Credit (IWTC) entitlements start to reduce at 25%. The WFF abatement threshold is currently set at $42,700 (before tax). The WFF abatement threshold is not indexed to annual wage growth. The last time the WFF abatement threshold increased was on 1 July 2018 when it increased from $36,350 to the current threshold as part of the Families Package.

Revenue impacts of the proposed benefit changes

4. Recent increases to benefit settings (and the increases currently proposed for Budget 21) have been significant. As a consequence, significant increases have been made to the MFTC threshold, as illustrated below[1].



5. The increases to the MFTC threshold from 1 April 2021 onwards are on a "partial alignment"[2] basis whereas prior increases were made on a "full alignment"[3] basis.

Interaction between the MFTC and WFF abatement thresholds

6. The following table shows the projected MFTC thresholds for the current forecast period, if both $25 benefit increases are introduced as part of Budget 21. The MFTC thresholds are then converted into "before tax" amounts to allow comparison with the WFF abatement threshold amount. Based on the projected increases it is anticipated that the MFTC threshold (before tax) would exceed the current WFF abatement threshold of $42,700 from 1 April 2026. These projections assume no further policy changes are made to benefit settings, and Average Weekly Earnings wage growth.

	1/7/2021	1/4/2022	1/4/2023	1/4/2024	1/4/2025
Net MFTC amount per year ($)	32,656	34,684	35,048	35,464	35,984
Gross MFTC amount per year ($)	38,395	40,853	41,295	41,799	42,429

7. By contrast, under a full alignment approach, the gross MFTC threshold would have exceeded the WFF abatement threshold from 1 April 2022.

8. If both $25 benefit increases are introduced and the MFTC thresholds are increased accordingly, any further benefit increases (other than minor adjustments) would be limited as these would further accelerate the point at which the MFTC threshold would exceed the WFF abatement threshold.

[1] The last two data points are the anticipated "partial alignment" increases to the MFTC threshold that would result if the proposed two-stage benefit increase of $25 and $25 are implemented as part of Budget 21.
[2] "Partial alignment" calculates the MFTC threshold based on the sole parent rate of the benefit.
[3] "Full alignment" calculates the MFTC threshold based on the couple rate of the benefit.

Issues arising if the MFTC threshold exceeded the WFF abatement threshold

9. If the MFTC threshold were to exceed the WFF abatement threshold, inconsistencies in the policy intents would arise.

10. The MFTC threshold represents a guaranteed minimum level of income for families with children.

11. If the MFTC threshold exceeds the WFF abatement threshold, some families would have incomes that are treated as sufficiently low to warrant them receiving an MFTC top-up payment. However, at the same time, their incomes would be considered too high for full WFF payments, and they would therefore receive abated FTC and IWTC payments. This reduction of income support at an income level *lower* than the deemed minimum income is incongruous.

12. For example, if the MFTC threshold (before tax) is $43,000 and the WFF abatement threshold remains at $42,700, a family working full time and earning $42,900 per year, would be entitled to an annual MFTC top-up of $100, and yet would receive abated FTC and IWTC payments.

13. The greater the amount that the MFTC threshold exceeds the WFF abatement threshold, the greater the number of families who would be affected by this anomaly.

14. From an administrative standpoint, such inconsistencies would be difficult to explain to customers, resulting in greater confusion around how entitlements are calculated. Based on customer feedback, the more complex the WFF system becomes, the more likely customers are to opt to receive the WFF entitlements as a lump sum at the end of the year, or at the extreme, to shift back onto benefit.

15. It is difficult to estimate what effect an MFTC threshold higher than the WFF abatement threshold would have on customers' work decisions. The evidence on financial incentives to work indicates that financial incentives are only one of many factors that influence people's decisions on whether to work and how much to work.

16. The above issues relating to the MFTC and the potential inconsistencies with the WFF abatement threshold will be considered as part of the wider review of WFF settings being undertaken this year.

Philip Marshall
Senior Policy Advisor
s 9(2)(a)

Item 3

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Briefing note

Reference:	BN2021/160
Date:	8 April 2021
To:	Revenue Advisor to Parliamentary Under Secretary for Revenue – Ruairi Cahill-Fleury
cc:	Naomi Ferguson, Commissioner David Carrigan, Deputy Commissioner Emma Grigg, Policy Director Kerryn McIntosh-Watt, Policy Director Phil Whittington, Chief Economist Joanne Petrie, Executive Support Advisor to the Commissioner Jill Compton, PA to Deputy Commissioner Government & Executive Services (Ministerial Services)
From:	Kathleen Littlejohn
Subject:	**Working for Families Tax Credits introductory briefing**

Working for Families Tax Credits introductory briefing

1. Officials will be providing an introductory briefing on Working for Families Tax Credits to Dr Russell on Wednesday 14 April.

2. Please find attached two documents which we have prepared to support this discussion.

Kathleen Littlejohn
Policy Advisor
s 9(2)(a)

Saskia and Carl

Saskia and Carl have two children, Ben (aged 10) and Josh (aged 12) in their full-time care.

Both Saskia and Carl work full time. Carl's hours can fluctuate so they decide to receive their WfF in a lump sum for the period 1 April 2020 to 31 March 2021.

After the end of the tax year, both Saskia and Carl receive automatic income tax assessments. Saskia's salary for the year was $50,000 and Carl's wages totalled $42,500.

With a total family income of $92,500, two children in their full-time care and having earned income each week, they receive $1,943 in WfF (IWTC only as FTC fully abated at an income of $85,192).

On 6 April 2021, the couple's 3rd child, Brianna, is born.

Saskia has applied for Paid Parental leave (PPL) and asks for this to start from the date of Brianna's birth.

The couple decides to switch to weekly WfF payments to help with the costs for the new baby, so they need to estimate their income.

Saskia anticipates she will not return to work before the end of the tax year on 31 March 2022 after her PPL has finished. Saskia updates her myIR requesting weekly payments and adds her income as $16,000 (rounding up her PPL entitlement) and Carl's $42,500 in expected wages.

With an anticipated family income of $58,500 ($965 in the hand per week (Saskia $272 + Carl $693)) and 3 children, this couple will receive $289 each week ($217 FTC + $72 IWTC). This provides the family with $1,254 in the hand each week.

After Saskia's 26 weeks of PPL finish, they will receive an additional $60 per week in Best Start Tax Credit for a total of $349 in WfF per week.

Moana and Will

Moana and Will have 3 children – Ana (age 4), Maia (age 6) and Rawiri (age 10). Moana works full time for wages and Will is self-employed.

They receive their WfF payments weekly, with Moana being the primary caregiver in IR's system.

In February 2021, Moana estimates she'll earn $45,800 for the period 1 April 2021 to 31 March 2022. Will estimates his self-employed income for the same period to be $52,600.

On this combined income with 3 children, working each week, IR pays the family $94 each week (FTC $22, IWTC $72).

Moana and Will separate in June. They discuss custody and agree to a 'week about' care arrangement. Will submits a WfF registration and advises he has the children in his care 7 days out of each fortnight. Will states he will continue to work some hours each week, although reduced due to his level of care.

Moana reduces her hours at the café to 20 hours per week. She estimates her new income at $25,000 ($415 in the hand each week). Because her income is low, but she continues to meet the 20 hours per week requirement for a single-parent family, she qualifies for Minimum family tax credit. Her weekly WfF entitlement is $306 per week ($148 FTC, $72 IWTC, $86 MFTC).

These customers will receive their end of year square up after Moana's automatic income tax assessment is processed and Will's individual income tax return is filed. This will determine the correct family scheme income for the period they were together during the tax year.

INTRODUCTION TO WORKING FOR FAMILIES TAX CREDITS– 8 APRIL 2021

Summary

Working for Families (WfF) Tax Credits provides targeted financial assistance to low- and middle-income families with dependent children aged 18 and under. WfF is a refundable tax credit. That is, it effectively operates as a cash transfer to families with children.

This note summarises:

- Objectives of WfF
- The types of WfF tax credits
- Eligibility
- The definition of income (family scheme income)
- Shared care
- Payment frequency, changes and square ups
- Current issues with WfF experienced by customers
- Review of WfF

Appendix also includes:

- Recent changes
- Historical components
- Cross-agency co-operation

Objectives of WfF

WfF was introduced on 1 April 2005 to assist low- and middle-income families with children by expanding existing tax credits along with creating new tax credits. The package also included other measures such as the accommodation supplement. The goals of WfF were to:

- Make work pay,
- Ensure income adequacy, and address issues of poverty,
- Achieve a social assistance system that supports people into work, is less complex, and delivers timely and correct entitlements.

Types of tax credit

WfF comprises four components with different criteria. Families will qualify for different tax credits depending on their income, whether they are in work and the number of hours they work.

WfF is received by 57% of all NZ families with children, at an annual expenditure of nearly $3 billion.

- **Family tax credit (FTC)**: the ‘base unit’ of the abating WfF tax credit.
    - This payment is available to families with dependent children and is not conditional on work obligations or whether they are receiving a benefit. The amount received depends on the number of dependent children they have and any shared care arrangements.

  - The maximum rate is $5,878 for one child and $4,745 for each subsequent child per year. The abatement rate is 25 cents for each dollar over $42,700
  - A person cannot receive FTC for a child for whom they are receiving a foster care allowance, unsupported child's benefit, orphan's benefit, or board payment.
  - During the 2019 tax year, FTC was paid to the families of 577,500 children[1] at a cost of $1.989 billion.

- **Best Start tax credit (BSTC)**:
  - BSTC is a payment of $60 per week for families supporting a new-born baby and is universal for all families for the first year. It was introduced in 2018 as part of the Families Package, replacing the Parental Tax Credit (see Appendix for more detail).
  - The BSTC abates at 21 cents for each dollar over $79,000 for the 2nd and 3rd years of the child's life.
  - A person cannot receive Paid Parental Leave (PPL) payments and Best Start payments at the same time for the same child.
  - During the 2019 tax year, BSTC was paid to the families of 53,100 children[2] at a cost of $23 million[3]. The forecast expenditure for the 2020 fiscal year is $188 million.

MSD pays FTC and BSTC to their clients. This can result in transition issues as clients move on or off benefit and must interact with both MSD and IR (discussed below).

- **In work tax credit (IWTC)**:
  - This is a payment available for families who have some income from paid work each week. Like FTC, this payment depends on how much someone earns, and the abatement rate is the same as the FTC.
  - The maximum rate is $3,770 for up to three children, with the maximum rate for each subsequent child being $780 per year.
  - The IWTC is one of two financial incentives to work payments in the welfare system, the other being the MFTC discussed next. It is available for families who have some income from paid work each week and are off benefit. The abatement settings are the same as the FTC.
  - If someone is in receipt of an income-tested benefit or a student allowance, they are not eligible to receive the IWTC.
  - From 1 April 2021, a person will keep receiving IWTC payments for up to two weeks during an unpaid break from work, for example: changing jobs, leaving employment, or unpaid time such as school holidays.
  - A person who is receiving a foster care allowance, unsupported child's benefit, orphan's benefit, or board payment for a child in their care remains eligible to IWTC providing they meet the other requirements.
  - During the 2019 tax year, the IWTC was paid to the families of 203,200 children[4] at a cost of $606 million. These families represent 35% of all NZ families with children.

- **Minimum family tax credit (MFTC)**:

[1] Families with unknown number of children are assumed to have one child
[2] Families with unknown number of children are assumed to have one child
[3] It should be noted this represents a partial tax year as Best Start tax credit began from 1 July 2018
[4] Families with unknown number of children are assumed to have one child

- MFTC 'tops up' a family's income to a minimum level. It is paid dollar for dollar up to the threshold. This is effectively a guaranteed minimum income of $30,576 net of tax.
- To be eligible, a single parent must work at least 20 hours a week, and in a two-parent family one or both parents between them must work at least 30 hours a week.
- MFTC is paid for families who work for salary/wages (PAYE income).
- If a family is in receipt of an income-tested benefit they cannot claim the MFTC.
- During the 2019 tax year, the MFTC was paid to the families of 5,660 children[5] at a cost of $13 million. For the 2018 tax year, 90% of MFTC recipients were sole parents.

*Alongside the WfF components sits the **Independent Earner Tax Credit (IETC)**. This credit is for tax residents earning between $24,000 and $48,000 in a year who do not receive any of the following:*

- *An income tested benefit*
- *New Zealand Superannuation*
- *A veteran's pension*
- *Working for Families Tax Credits*
- *An overseas equivalent of any of the above.*

Recipients can access the IETC by using a specific tax code to reduce their PAYE during the year, wait for a calculation as part of their automatic income tax assessment, or make a claim by filing their IR3 income tax return at the end of the tax year. The maximum amount claimable is $520. Previous research has indicated that a significant number of recipients are from high-income households.

Eligibility

The are some common criteria for WfF tax credits. For a person to qualify they must:

- Be 16 years or older;
- Be the principal caregiver for 1 or more dependent child(ren);
- Meet the residence requirements or their child(ren) must meet the residence requirements; and
- Not receive a parent's allowance or a children's pension under the Veteran's Support Act 2014 (VS Act).

A principal caregiver has the primary responsibility for the day-to-day care of the child, on a non-temporary basis. A dependent child must:

- Be in the primary care of the principal caregiver;
- Be included as a member of the principal caregiver's family;
- Be financially dependent on the principal caregiver[i];
- Not be a child for whom a foster care allowance, unsupported child's benefit, orphan's benefit or board payment is made (all credits except IWTC).

In terms of residency requirements, the principal caregiver or their partner must not be a transitional resident, and either:

- The principal caregiver has been both an NZ resident and present in NZ for a continuous period of 12 months at any time and is tax resident in NZ for the period they are applying for the WfF tax credits; or
- The dependent child is both an NZ resident and present in NZ.

[5] Families with unknown number of children are assumed to have one child

The Ministry of Social Development (MSD) can grant an emergency benefit in some circumstances when the residency requirements under the Social Security Act 2018 are not met. From 1 April 2020, customers who have dependent children while on an emergency benefit may qualify for WfF while on a temporary visa. This is usually paid by MSD.

Family scheme income

To maintain the integrity of WfF as social assistance and to ensure fairness in its outcomes, WfF uses 'family scheme income' rather than taxable income as the basis for calculating entitlements. Adjustments are made to the annual net income of the person and their partner, which are designed to ensure the income used to calculate WfF is a true reflection of a family's income situation. The following are some of the forms of income which contribute to family scheme income:

- Salary or wages;
- ACC compensation payments;
- Paid parental leave;
- Child support paid or received;
- Investment income;
- Self-employed income;
- Other business income;
- Passive income of children;
- Non-resident partner income;
- Other payments to help meet day to day living expenses (such as financial help from another person) totalling over $5,000 a year.

Shared care

When the care of a child is shared, the WfF entitlement for that child is generally apportioned according to the child's care proportions. For a child to be considered in shared care they must be in the care of a person, on average, for at least one third of the year and the shared care arrangement must be intended to be in place for four months or more. Over a year this equals 122 days, or 5 days every fortnight. Customers will generally need to provide the days they would normally have the child or children in their care including the pick-up and drop off times, the arrangement over the school term holidays and Christmas holidays, and the date the arrangement started.

Generally, if there is a shared care arrangement, IR (rather than MSD) must pay WfF to ensure the entitlement is apportioned correctly. However, MSD can pay when shared care is under a formal agreement and the family's income is under $3,558 per month.

Shared care is apportioned differently for different components:

- For FTC and BSTC, the payment is apportioned based on the amount of care each parent or caregiver has.
- IWTC is not apportioned according to care: each qualifying principal caregiver who meets the IWTC requirements can receive up to the maximum IWTC rate. This is consistent with the policy's intent as a financial work incentive.
- For MFTC, only one person can receive the MFTC. Generally, a decision will need to be made as to who the principal caregiver is, and MFTC will be paid to that person only. The exception to this is complete alternate weeks in each parent's care, as this means the customer is the principal care giver during the week in which they have care.

Payment frequency, changes and square ups

WfF is an annual entitlement that can be received weekly or fortnightly during the year or as a lump sum after the end of a tax year. To receive weekly or fortnightly payments, a family must provide their estimated family scheme income and their family circumstances as they are receiving their annual entitlement 'in advance'. If a family chooses to receive a lump sum payment, they will not need to estimate their income, but will need to provide their family circumstances for the year.

Customers are expected to update Inland Revenue with relevant changes in their family's circumstances during the tax year. Customers receiving weekly or fortnightly payments are encouraged to advise Inland Revenue of these changes promptly so that their ongoing payments can be adjusted as soon as possible, reducing the risk of overpayment and assisting with costs if income has reduced or if they have an additional dependent.

At the end of the tax year families who have estimated their income will have their final WfF entitlement calculated based on their family scheme income and circumstances in the 'end of year square up'. Customers are advised of any further entitlement or any amount they are required to repay. Customers who solely receive their WfF from MSD are not required to have an end of year square up.

Issues within WfF

Complexity

- The Welfare Expert Advisory Group's 2019 report made reference to the complexity of the WfF scheme, stating "Agreement is near universal that the benefit and tax credit systems are unmanageably complex."[6] For WfF, customers are often unaware of the different criteria for each components and may fail to inform Inland Revenue when they do not qualify for a specific component as they do not distinguish between the parts of the one payment they receive in hand.
- Interactions with other types of welfare assistance can also be a source of confusion, with customers unsure what they are entitled to from Inland Revenue and/or MSD.
- The concept of family scheme income: customers can be unsure what income to declare for income tax versus WfF versus what to declare to MSD.
- Estimating income can be difficult. Many families struggle to accurately predict their income across a full tax year. Relationship periods for WfF mean that when eligibility starts or stops, or someone starts or stops living with a partner, the family scheme income for that period must be estimated as if it were for a full year. Much of this is not intuitive for customers.
- MFTC especially requires customers to estimate their income accurately to avoid overpayment. Because these customers are on low incomes, they are likely to pick up extra shifts or overtime at work, receive help from family and friends, seasonal work and so on. The likelihood of overpayment therefore increases.

Customer experience

[6] Whakamana Tangata: Restoring Dignity to Social Security in New Zealand, 2019

- Customers whose personal and financial situations remain largely stable are likely to have the best experience with WfF as they are not required to report as many changes to IR. These customers are most likely to receive a similar and steady amount of WfF.
- Changes in circumstances mean fluctuations to WfF entitlements for those receiving weekly or fortnightly payments. Customers with less stability in their lives – for example, those who have casual, seasonal, weather-dependent or otherwise unreliable employment situations, whose hours of work change frequently, who have changes to the number of children in their care or the amount of care they provide, or who begin or end relationships – will find it more difficult to accurately predict their circumstances and keep IR up to date with changes. Customers may also have to wait for a situation (such as a care dispute) to stabilise before they are confidently able to advise IR of the outcome.
- Through the Early Intervention process, a series of criteria are run over accounts check if customers are receiving correct entitlements. For example, we check estimates based on payday filing information, or for financially independent children. In this way, Inland Revenue helps prevent overpayment of WfF where possible. It should be noted that Inland Revenue is unable to run these checks for customers whose income is not from PAYE sources, such as self-employed customers.
- WfF also has a significant positive impact. Customers rely on payments and they make a tangible difference in families' lives. IR's Business Transformation has also helped improve our ability to respond rapidly, e.g. IR can now refund missed payments within two hours if needed.

Overpayments

- As at June 2020, WfF overpayments totalled $167 million from 44,939 individuals. Overpayment tends to occur due to underestimate of income or a delay in notification of a change in circumstances. Overpayment (debt) can be difficult for customers to manage. IR offers instalment arrangements and other hardship assistance, including consideration of full or partial write offs if relevant criteria are met.
- An example is the interaction between Paid parental leave and BSTC has resulted in some overpayments due to the timing of applications and IR's system. Families may not receive these concurrently. If they apply for PPL later, this can result in families having to repay some of their BSTC, which can be confusing because it is a "universal" payment.
- WfF is also assessed annually, so families who have changes in circumstances they could not have predicted during a tax year (such as a redundancy) may find themselves in significant debt or subject to accumulative adjustment (having reduced or nil payments for the remainder of a tax year). A family could attempt to avoid overpayment by switching to the annual payment option; however, this may impact their ability to meet their costs during the year.

Split administration between MSD and IR

- Both IR and MSD administer WfF payments. A customer in receipt of an income-tested benefit will usually receive their WfF payment along with their weekly benefit payment (although they can choose to have their payments made through IR). A customer will only receive payments from one agency at any given time depending on their personal circumstances.
- Customers moving between work and benefit may be referred between departments to provide information for one agency to take over WfF payments from the other. IR may need to request confirmation from MSD that they have stopped payments, although generally this information is provided via an automatic exchange of information between departments. If the information is not complete or accurate, this can impact on the WfF payments, resulting in under or overpayments.

- MSD customers do not need to have IRD numbers for the children in their care in order to have MSD pay their WfF, while IR do (excluding the eight-week grace period). This can lead to fraudulent payments and 'double dipping' where departments are unable to recognise they are both paying a caregiver WfF for the same child as there is no unique identifier in MSD's system.
- MSD and IR customers also have different paydays for WfF because MSD customers are paid their WfF in with their benefit. This tends to generate feedback on public holidays as IR's customers generally receive their WfF as normal, but MSD customers are paid early.
- As part of the WfF review (discussed below), consideration will be given to IR taking on payments to MSD clients.

Operational pain points

- Complexity also has impacts on staff. A high level of knowledge is required to administer WfF accurately and consistently across all customers.
- Co-administration with MSD can provide more room for human error, as the referral system is not always accurate or the same information can be requested multiple times.
- Where IR's system is unable to perform a WfF calculation, a complex manual spreadsheet is required to correct the calculation and give the customer the correct result.

WfF Review underway

After the Welfare Expert Advisory Group released its final report *Whakamana Tangata: Restoring Dignity to Social Security in New Zealand* in February 2019, work has begun on an overhaul of the welfare system in New Zealand. As part of this, officials from IR, jointly with MSD, Treasury and the Child Poverty Unit, are undertaking a review of Working for Families tax credits. The review will likely consider substantial reform of the in-work supports of WfF, less reformative policy changes, and operational changes to improve the delivery of WfF to our customers.

Initial work has begun that will help to inform the review process, including:

- A 'stocktake' of the WfF components (and the Independent Earner tax credit)
- Work on broader issues that impact the policy and administration of WfF as a whole, for example, WfF debt, the definition of relationships, definition of income, and the Kaupapa Maori values framework, and potential engagement with stakeholders.

There is a joint Ministers meeting on 13 April to discuss the scope and parameters of the review, including timeframes. Advice will be provided to prompt discussion of what the objectives of the review should be. Depending on what Ministers would like to achieve, the review could take several years including legislation and implementation.

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[i] Financial independence for WfF tax credit purposes is defined in Section YA 1 Income Act 2007

APPENDIX

Recent changes

From 1 July 2020, the hours worked requirement for IWTC was removed. The principal caregiver and/or their partner must be in paid work and derive income in a week to qualify for IWTC. Previously, a single parent would have needed to work 20+ hours per week to qualify, and a two-parent family would need to work 30+ hours between the two parents to qualify. The hours worked requirement is still in place for MFTC.

From 1 April 2021, there will be a 'grace period' introduced for the IWTC. A family will continue to remain eligible for the IWTC for up to two weeks after ending paid work.

In December 2020, the MFTC threshold for the tax year ending 31 March 2021 was increased from $27,768 to $29,432. From 1 April 2021, the threshold increased again to $35,873.

Historical components

There are some historical components of WfF. While no longer available, some customers have retained eligibility or may be eligible if they apply for back-dated entitlements.

- Child Tax Credit (CTC) – uses the same abatement formula as the FTC and IWTC and is paid at the rate of $780 per child. From 1 April 2006, this component was replaced with the In-Work Tax Credit for eligible families. A small number families retain their historic CTC entitlement. A family must retain continuous entitlement to CTC to carry on receiving it.
- Parental Tax Credit (PTC) – a payment intended to help qualifying families with the cost of a new-born for the first ten weeks of the child's life and replaced by BSTC from 1 July 2018. The PTC rate is $2,200 for each child. Prior to 1 April 2015, PTC was paid for eight weeks and the prescribed amount was $1,200 per child.

Additionally, up until 30 June 2018, the age of the child determined the maximum entitlement of FTC. From 1 July 2018, the rates are based on one rate for the eldest child, and a lower rate for each subsequent child, of any age.

Cross-agency co-operation

Ministry of Business, Innovation and Employment (MBIE)
Inland Revenue makes Paid parental leave payments on behalf of the Ministry of Business, Innovation and Employment (MBIE). A customer is not entitled to receive Paid parental leave payments and BSTC payments simultaneously for the same child.

Department of Internal Affairs (DIA)
SmartStart is a website run by the Department of Internal Affairs. SmartStart allows a customer to register their child's birth, apply for BSTC and apply for an IRD number for their child. Inland Revenue

can pay up to eight weeks of WfF for a child with no IRD number, after which time the payments will stop until the IRD number application is complete. Less customers are impacted by the end of grace period payment reduction due to SmartStart.

The Ministry of Social Development and Employment (MSD)
The Ministry of Social Development (MSD) and Inland Revenue both make payments of WfF tax credits. MSD does not require a customer to have an IRD number for the child in order to make payments beyond eight weeks.

Working for Families Tax Credits

An overview

April 2021

Policy and Regulatory Stewardship
Kaupapa me te Tiaki i ngā Ture
taxpolicy.ird.govt.nz

Purpose of Working for Families

- Refundable tax credits for low and middle income families with children
- Introduced 1 April 2005
- Objectives:
  - Make work pay
  - Ensure income adequacy
  - Support people into work, less complex, correct entitlements on time

Type of tax credits

- Family Tax Credit (FTC)
- Best Start Tax Credit (BSTC)
- In Work Tax Credit (IWTC)
- Minimum Family Tax Credit (MFTC)

+ Independent Earner Tax Credit (IETC)

Eligibility for applicant

- 16 years+
- Principal caregiver for dependent child
- Caregiver or child must be NZ resident

Dependent child

- Must be in day to day care of principal caregiver
- Family member of principal caregiver
- Financially dependent on principal caregiver

Abatement

- Most WfF credits abate after certain thresholds are reached
- Gradual abatement means that people are generally better off overall (they don’t lose their whole payment if they have an increase in income)
- However, gradual abatement means that people’s payments need to change with even very small changes in income – this increases the chance of over and under payment
- Gradual abatement also results in high effective marginal tax rates for particular income groups

Family scheme income

- Annual net income of applicant and their partner, with adjustments = “family scheme income”

- Adjustments include income that is available to meet day to day costs

- Ensure integrity and fair outcomes

Family scheme income includes:

- Child support paid or received;
- Some income where the person is a major shareholder of a close company or settlor of a trust
- Passive income of children;
- Non-resident partner income;
- Other payments to help meet day to day living expenses (such as financial help from another person) totalling over $5,000

Shared care

- 122 days per year / 5 days per fortnight
- IR’s system can apportion payments more easily than MSD’s system
- Different tax credits apportioned differently
- Different legislation to child support recognised care

Payments and changes

- Weekly / fortnightly / annual (lump sum)
- Weekly / fortnightly ‘upfront’: estimate required
- Annual option: no estimate needed, but must provide family details e.g. children in care
- Customers need to update IR as soon as possible
- Delays affect rate of payment or cause overpayments

End of year square up

- After end of tax year – when automatic income tax calculations or IR3s are complete
- Customers who receive annual payment are paid
- Customers who receive weekly/fortnightly are squared up – over or under payments quantified
- MSD-only customers not subject to square up

Complexities

- Complexity of WfF as part of wider complex welfare system
- Family scheme income: difficult concept
- Estimating income for a year
  Especially for MFTC customers

Overpayments

- June 2017: $167 million debt, 44,939 customers
- Causes include: underestimation, delay in changes in circumstances
- Some system issues e.g. PPL and BSTC interactions

Operational issues – co-administration

- Both IR and MSD administer WfF payments.
- Beneficiaries generally receive WfF with benefit although not compulsory
- Customer will receive WfF from one agency at a time
- Automatic information exchange helps manage transfer of payment

Working for Families Review

- Welfare Expert Advisory Group report – overhaul of welfare system

- Inland Revenue – Review of WFF
  - Stocktake of components
  - Broader issues

- Long term focus for the review

Item 4

Inland Revenue
Te Tari Taake

TE TAI ŌHANGA
THE TREASURY

DEPARTMENT OF THE PRIME MINISTER AND CABINET
TE TARI O TE PIRIMIA ME TE KOMITI MATUA

MINISTRY OF SOCIAL DEVELOPMENT
TE MANATŪ WHAKAHIATO ORA

Joint Report: Welfare Overhaul: Working for Families Review

Date:	8 April 2021	**Report No:**	DPMC-2020/21-771; T2021/632; REP/21/4/356; IR2021/156
		File Number:	SH-3-6

Action sought

	Action sought	Deadline
Rt Hon Jacinda Ardern **Prime Minister / Minister for Child Poverty Reduction**	**Agree** to recommendations and **discuss** at meeting	Ministers' meeting on 13 April 2021 at 8am
Hon Grant Robertson **Minister of Finance**	**Agree** to recommendations and **discuss** at meeting	Ministers' meeting on 13 April 2021 at 8am
Hon Carmel Sepuloni **Minister for Social Development and Employment**	**Agree** to recommendations and **discuss** at meeting	Ministers' meeting on 13 April 2021 at 8am
Hon David Parker **Minister of Revenue**	**Agree** to recommendations and **discuss** at meeting	Ministers' meeting on 13 April 2021 at 8am

Contact for telephone discussion (if required)

Name	Position	Telephone		1st Contact
Murray Shadbolt	Principal Advisor, Welfare and Oranga Tamariki Team, The Treasury	s 9(2)(a)	s 9(2)(a)	
Deborah Tucker	Senior Analyst, Child Poverty Unit, Department of the Prime Minister and Cabinet	s 9(2)(a)	s 9(2)(a)	
Daniel Frischknecht	Principal Analyst, Income Support, Ministry of Social Development	s 9(2)(a)	s 9(2)(a)	
Eina Wong	Principal Policy Advisor, Policy and Regulatory Stewardship, Inland Revenue	s 9(2)(a)	s 9(2)(a)	

Minister's Office actions (if required)

Return the signed report to Treasury.

Enclosure: No

Joint Report: Welfare Overhaul: Working for Families Review

Executive Summary

1. Working for Families (WFF) was implemented between 2004 and 2007 to support income adequacy and reduce child poverty; and to improve financial incentives for low-income earners to participate in the labour market.

2. Since then, there have been important changes in the labour market and the welfare environment that impact on these objectives and the landscape that WFF is operating in. There have been sustained increases in the minimum wage, and general wage growth in the labour market, although the buoyancy experienced in 2004 has been dampened by economic factors over time, such as the Global Financial Crisis and now the impact of COVID-19. While the labour market is still predominantly made up of permanent stable employment, there are a significant proportion of low-income jobs that are precarious and have variable hours and earnings that impact particularly on women, Māori and Pacific workers.

3. The welfare context has also changed considerably since 2004, with significant increases in income support through the Families Package, recent and planned changes to benefit rates, introduction of elements of universalism through Best Start, and greater support for working beneficiaries through increases to abatement thresholds, and employment and training programmes.

4. The Government has set ambitious ten-year child poverty targets, which aim to halve rates of child poverty by 2027/28. In order for the targets to be achieved, further significant income support packages will be required.

5. While WFF has achieved its key objectives for some groups, like any transfer system that is designed to target particular groups of the population, it has a number of issues. It can be fiscally costly when altered, results in a poor interface between benefit and work, does not respond well to changing work and family circumstances, and results in high effective marginal tax rates for many families.

6. A review of WFF is on the medium-term Welfare Overhaul work programme [CAB-19-MIN-0578 refers] and, in light of the changing context and ongoing issues with the current scheme, we propose bringing this review forward. Fundamental and structural change will likely be required, rather than minor changes to existing settings.

7. We are seeking your feedback regarding the direction for the review, including the relative balance between the objectives. There are overlaps and trade-offs across key design choices – and officials can provide further advice on options once we have received Ministers feedback on the key trade-offs and objectives. We are seeking feedback on the relative emphasis on:

   - <u>increasing payments to low-income working households to support the 'working poor' versus payments to beneficiary households</u>, particularly given recent and proposed increases to beneficiaries

     - Officials' view is that WFF remains an important lever for improving income adequacy, but in light of recent and proposed income increases for beneficiaries there are questions for Ministers of whether any further increased payments should be focused on working households only, or both beneficiary and working households

- targeting versus universalism – should WFF be more targeted to low-income families to improve child poverty objectives more cost-effectively, or should settings be more universal to improve adequacy for both low-income families and a larger number of relatively higher-income families?
    - Officials' view is that targeting for WFF remains desirable, but there are also questions for Ministers on whether tax credits should be more or less targeted relative to current settings
- whether in-work assistance strongly incentivises a movement off-benefit at a particular amount of work versus incentivising working more in the benefit system – should in-work assistance encourage movement off benefit at particular levels of hours worked and/or earned income or should the assistance phase in and merge with the benefit system and be available to working beneficiaries?
    - Officials' view is that there remains a need to provide a payment to low-income working families in recognition of the costs of working and people should expect to see a return from working an additional hour, but there are questions on the design of in-work assistance.

8. The original WFF reform also intended to achieve a social assistance system that supports people into work, by making sure they get the assistance they are entitled to in a timely manner, and with delivery that supports them into, and to remain in, employment. This continues to be an important consideration and, regardless of the direction and scale of reform, there is a need to modernise and simplify the system to better respond to changing work and care arrangements, improve the client experience, and improve the interface between benefit and work.

9. There are also choices to consider on the scope of the review and whether WFF should be broadened to include in-work assistance for those without children and/or disabled people; and whether the Childcare Assistance review should be part of the WFF review. Officials' view is that work on childcare assistance and disability supports should remain separate to the WFF review to manage the scope, with each policy project keeping each other informed as work develops.

10. We are seeking your feedback regarding the timing of any changes. Decisions in Budget 2022 with a shortened legislative process would allow for changes to be made from 1 April 2023 at the earliest. This would allow about 10 months for policy development and consultation, and for Ministers to consider potential options. Implementation of changes could also be phased over a number of years.

11. Officials will prepare detailed timeframes for policy development, engagement, legislation and implementation, and a detailed workplan alongside further development of options, based on decisions in this paper.

Recommended Action

We recommend that you:

Context and rationale for a review of Working for Families

a **note** that Working for Families combines dual objectives of income adequacy and work incentives, and has achieved its key objectives for some groups, but has resulted in mixed effectiveness for others b **note** that the original Working for Families reform also included a third delivery objective to achieve a system that supports people into, and to remain in, work by making sure they get the assistance they are entitled to in a timely manner, and that this continues to be important regardless of the scale and direction of reform

c **note** that the Welfare Expert Advisory Group recommended significant changes to Working for Families tax credits, including making the Family Tax Credit more generous and more universal, replacing in-work payments with a new Earned Income Tax Credit, and making Best Start universal for all children under three, as part of a wider welfare package

d **note** that the Government has set ambitious ten-year child poverty targets, which will require further significant income support packages to make progress

e **note** that, since the last significant changes to New Zealand's system of tax credits for families in 2004, there have been important contextual changes, including:

- changes to labour market settings, including sustained increases in the level of the minimum wage
- significant increases in income support through the Families Package, indexation changes, and recent and planned main benefit increases
- introduction of elements of universalism through Best Start
- changes to the In-Work Tax Credit to increase its flexibility
- greater support for working beneficiaries through increases to abatement thresholds and employment programmes

f **note** that, while Working for Families tax credits are achieving their key objectives for some groups, current settings are complex, cause significant problems for those with changing work and family arrangements, result in a poor transition between benefit and work, and can result in high effective marginal tax rates for some families that discourage working more hours

g **note** that reform could be small-scale within the existing framework, or significant in that it could look to replace some or all of the existing tax credits with new payments, and that officials recommend a more fundamental reform given the current issues with Working for Families

h **agree**, in light of the changing context and the Government's commitment to ambitious targets for the reduction of child poverty, to bring forward the review of the Working for Families tax credits currently on the medium-term Welfare Overhaul work programme

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

Objectives and direction for the review

i **indicate** whether you are comfortable with the following high-level objectives for the system of tax credits for families, and provide any feedback on the relative balance between these objectives:

- supporting income adequacy and reducing child poverty
- improving financial incentives for low income earners to participate in the labour market

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

j **provide** feedback to officials regarding the direction for the review, including the relative balance between:

- **income adequacy for beneficiaries versus working families** – should payments to low-income working households to support the 'working poor' be increased versus payments to beneficiary households, particularly given recent and proposed income increases to beneficiaries

- **targeting versus universalism** – should WFF be more targeted to low-income families to improve child poverty objectives more cost-effectively, or should settings be more universal to improve adequacy for both low-income families and a larger number of relatively higher-income families?

- **incentivising movement off-benefit at a particular amount of work versus incentivising working more in the benefit system** – should in-work assistance encourage movement off benefit at particular levels of hours worked and/or earned income or should the assistance phase in and merge with the benefit system and be available to working beneficiaries?

k **note** that there are choices for Ministers on whether the following should also be in scope:

- whether new or reformed tax credits should be extended to families without children (as recommended by the WEAG with the Earned Income Tax Credit)
- whether a tax credit to support disabled people should be considered
- whether the Childcare Assistance review should be part of the WFF review

l **agree** that a disability tax credit and childcare assistance be separate, but related, items considered as part of the existing welfare overhaul work programme in order to ensure that the WFF review has a feasible scope

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

m Indicate whether you would like further advice on whether new or reformed tax credits should be extended to families without children

Agree/Disagree **Prime Minister**	*Agree/Disagree* **Minister of Finance**	*Agree/Disagree* **Minister for Social Development and Employment**	*Agree/Disagree* **Minister of Revenue**

Timing and implementation for changes arising from the review

n **note** that on current reporting methods, in order to have a full impact on child poverty reporting for the next three-year target period:

- changes to transfer payments would need to be implemented by July 2022
- if changes were implemented in April/July 2023, the impact on child poverty reporting would be spread across the next two target periods
- if implemented in April/July 2024, the impact would be seen in the next target period covering the 24/25, 25/26 and 26/27 years

o **note** that decisions in Budget 2022 with a shortened legislative process would allow for significant WFF changes to be made from 1 April 2023 at the earliest

p **note** that a longer implementation timeframe (such as 2024) would allow more time for engagement with stakeholders and more fundamental reform to be considered

q **indicate** the timeframe in which Ministers are seeking reform

r **indicate** if you wish to have a nominated lead Minister for the duration of the review, who would be responsible for responding to parliamentary questions, Official Information Act requests, and other requests from the media and public

s **refer** this report to the Minister for Children for their information

Refer / Not referred
Prime Minister Ardern

Next steps

t **discuss** the content of this report at your meeting on 13 April at 8am.

s 9(2)(a) [redacted]

Kristie Carter
Director, Child Poverty Unit,
Department of Prime Minister and Cabinet

s 9(2)(a) [redacted]

Keiran Kennedy
Manager, Welfare and Oranga Tamariki, The Treasury

s 9(2)(a) [redacted]

Polly Vowles
Manager, Income Support Policy,
Ministry of Social Development

s 9(2)(a) [redacted]

Carolyn Elliott
Acting Manager, Policy and Regulatory Stewardship,
Inland Revenue

Rt Hon Jacinda Ardern
Prime Minister / Minister for Child Poverty Reduction

Hon Grant Robertson
Minister of Finance

Hon Carmel Sepuloni
Minister for Social Development and Employment

Hon David Parker
Minister of Revenue

Joint Report: Welfare Overhaul: Working for Families Review

Purpose of Report

1. This paper provides advice on a review of Working for Families tax credits (WFF) – it seeks Ministers' preferences on the relative emphasis of the objectives and key design questions to guide the direction of the review and the potential options for reform. It provides initial advice on the high-level considerations and trade-offs, and seeks Ministers' direction on the scope, scale and timing of the review.

Context

2. The WFF package was implemented between 2004 and 2007 to increase support primarily for low to middle-income families. The package included introducing the WFF tax credits among other changes. The objectives at the time were to:
    a. support income adequacy and reduce child poverty
    b. improve financial incentives for low-income earners to participate in the labour market
    c. achieve a social assistance system with delivery that supports people into work, and to remain in work, by making sure they get the assistance they are entitled to in a timely manner.

3. The introduction of WFF increased income adequacy and reduced child poverty in working households, though not in 'non-working' households. However, subsequent increases to the Family Tax Credit (FTC) in the Families Package in 2018 are estimated to have significantly reduced poverty across working *and* 'non-working' households with children.

4. The WFF tax credits and key statistics are summarised as follows:

WFF key statistics …

Approximately 57% of all families with children (around 310,000 households in New Zealand) receive WFF, and 35% receive IWTC (using administrative and TAWA outputs). WFF is made up of the following tax credits:

- Family Tax Credit: main income adequacy payment received by both beneficiary and working families, which pays $113pw for the eldest child and $91pw for each subsequent child. It is paid to 290,000 families who are mainly lower-income families, with some higher-income larger families (e.g. families with three children earning $100,000 would still be receiving around $85 pw in WFF payments) – around 58% are sole parent families, and 42% are couples.
- In-Work Tax Credit: main in-work payment which pays $72.50pw for families with 1-3 children (with an extra $15pw for fourth and subsequent children). It is paid to 203,000 families in work – 40% are sole parents, and 60% couples.
- Minimum Family Tax Credit: payment to 4,000 non-beneficiary households – 90% are sole parents and 10% couples. MFTC tops up the wages of low-income working families with children to a guaranteed minimum of $30,576 after tax (2021-22 tax year).
- Best Start Tax Credit: provides payments of $60pw to all families for the child's first year, and for the subsequent two years if they earn $79,000 or less. 27,000 families received Best Start (IR's recipients only).

Total 2019 tax year spend for WFF $2.8 billion across all credits:

- Family Tax Credit - $2 billion
- In-Work Tax Credit - $600 million
- Minimum Family Tax Credit - $13 million
- Best Start Tax Credit - $23 million

5. The Welfare Expert Advisory Group's report *Whakamana Tāngata: Restoring Dignity to Social Security in New Zealand* recommended fundamental changes to the design and targeting of WFF, and significant increases to main benefits and the FTC. The key WFF changes proposed included:

   a. replacing the In-Work Tax Credit (IWTC), the Minimum Family Tax Credit (MFTC), and the Independent Earner Tax Credit (IETC)[1], with a new tax credit similar to the Earned Income Tax Credit (EITC), which provides work incentives targeted to people lower down the income scale (including for those without children)

   b. making the FTC more universal, through higher payment rates and a two-tier abatement rate that is low for most families and high for families earning over $160,000

   c. making the Best Start Tax Credit universal for all children under three.

6. The review of WFF is part of the medium-term Welfare Overhaul work programme [CAB-19-MIN-0578 refers]. In light of the changing context and the Government's commitment to ambitious targets for the reduction of child poverty, we recommend bringing forward the review of the WFF currently on the medium-term Welfare Overhaul work programme.

7. In addition, the Welfare Overhaul will consider wider changes to income support settings, including childcare assistance and financial assistance available for people with a health condition and disability. Officials will consider any interactions of this review with other work already underway as part of the Welfare Overhaul.

Links to child poverty targets

8. The Government has set ten-year child poverty targets, which require baseline rates to be halved by 2027/28. The targets on all three measures are ambitious, but the target on the before-housing-cost measure is likely to prove particularly challenging. To achieve it, the income of low-income households with children must rise considerably faster than the median-income, whereas the general trend in the economy is for middle incomes to grow faster than those at the bottom. Further significant income support packages will likely be required to achieve the targets, particularly on the before-housing-cost measure.

9. The extent to which any reforms are expected to result in substantial reductions in measured poverty is essentially dependent on the extent to which any changes are expected to substantially improve the adequacy of incomes for low-income families. Adequacy improvements could be directed towards the incomes of beneficiaries, the 'working poor', or both.

Labour market and welfare context has changed since WFF was introduced

New Zealand has experienced sustained wage growth since WFF, though a significant portion of lower end workers continue to experience poor labour market outcomes

10. WFF was phased in during a buoyant labour market (between 2004 and 2007). Demand for labour was relatively high and unemployment low. Since 2004, there have been sustained increases in the minimum wage and general wage growth. Evidence suggests, however, that wage growth has been significantly higher for higher paid employees, with the wage rates of lower decile employees (other than those on the minimum wage), rising at a much slower rate[2].

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[1] IETC is paid to workers earning between $24,000 and $48,000 p/a at a rate of up to $10 p/w. It is paid to 550,000 individuals with a total spend of $240 million (based on 2019 tax year figures).

[2] Rosenberg, Dr Bill. Shrinking portions to low and middle-income earners: Inequality in Wages & Self-Employment 1998-2015, NZCTU, August 2017.

11. The IWTC and MFTC have played a relatively modest role over time in encouraging people into work and to stay in work. There is some evidence that the introduction of the tax credits increased the labour force participation of predominantly low-income sole parents and reduced participation of relatively higher-income secondary earners in couples.

12. While New Zealand continues to be made up of predominantly standard employment relationships, it is widely accepted that technology will continue to drive diversified and more flexible work arrangements, and transitions between jobs will be more likely and more frequent. Pressure on firms to be adaptive is likely to increase the number of temporary workers and contractors.

13. New Zealand has relatively high rates of part-time workers (30% of women work part-time and women make up 70% of the part-time workforce) and high rates of underemployment by OECD standards. While part-time (and some full-time) working arrangements may be classed as permanent many of these roles can be precarious. There are significant numbers of low-paid employees in the retail, food and accommodation sectors on contracts with low guaranteed hours that vary week to week. Around one in ten permanent workers also have multiple jobs.

14. The data points to a greater likelihood that workers in these lower-end jobs are women, Māori and Pacific workers. Māori and Pacific women in particular are over-represented in low-wage employment, and casual, temporary and other forms of insecure employment. COVID-19 has only exacerbated the situation for these groups, who are also more likely to be in industries impacted by COVID-19 restrictions. Women with caring responsibilities, and especially sole parents, are also exposed to the adverse effects of economic recessions that can lock in long-term unemployment, poverty (including in-work poverty), and lead to increased rates of child poverty.

Options for reform will need to respond to these realities and prepare for future labour market challenges

15. The OECD Jobs Strategy, prior to COVID-19, argued that countries needed to step up their efforts to adapt policy to the challenges of the changing world of work, focusing on helping those at risk of being left behind, ensuring everyone has access to social protection, and a tax and benefits system that makes work pay and protects workers.

16. The need for a more flexible system that encourages and facilitates people to remain in, re-enter or enter the labour market, in an environment of uncertainty, could be heightened in the future. This points to a need to further improve the transition between work and benefits, and the complex interface between wages, welfare and WFF entitlements. It also suggests that achieving the objectives of WFF is potentially more challenging if labour demand remains low and/or variable, and unemployment high and persistent for some groups and in some regions.

17. As part of the COVID-19 response, there has been a focus on employment, education and training supports to increase work opportunities and to encourage people into industries with higher labour demand. Flexiwage has been expanded and there is a manifesto commitment to extend the Training Incentive Allowance. The Government is also exploring Social Unemployment Insurance with social partners, which would have an impact on the labour market, the returns from work, and would have a significant overlap with WFF entitlements.

There have been significant increases in income support through the Families Package, and recent and planned changes to benefit rates and abatement thresholds

18. Over previous decades, in-work incomes have increased by significantly more than benefit incomes due to wage growth exceeding the rate of income support over an extended period. This has had the impact of:

a. increasing the financial incentives to work for low to middle-income families considerably compared to the early 2000's (with wages doing more of the 'heavy lifting' in providing adequate incomes compared to in-work payments)

b. reducing the value of the tax credits available for working families as the payment rates and abatement threshold have eroded relative to wages, particularly the IWTC.

19. To address some of these issues, there have been recent increases in income support for both beneficiaries and low to middle-income working families. In 2018, the Government introduced the Families Package, which boosted the incomes of low- and middle-income families with children by increasing the FTC payment rates and raising the abatement threshold and rate; introduced a Best Start payment and a Winter Energy Payment; and reinstated the Independent Earner Tax Credit (which was due to be removed in 2018).

20. As well as helping to improve income adequacy for both beneficiaries and working families, these changes also extended the number of families eligible for WFF tax credits, partly offsetting the reduction in families eligible for WFF in prior years.

21. In response to stakeholders views on the inflexibility of the IWTC, the hours test has now been removed and a 'grace period' introduced to allow a family to continue receiving the payment for up to two weeks when they are not in work.

22. There have also been targeted income increases for beneficiaries through increases to the benefit abatement thresholds, the $25 per week increases to main benefits on 1 April 2020 and the indexation of main benefits to wages. The Government is also considering options for increasing mains benefits further, including $20 per week increases on 1 July 2021 and additional increases on 1 April 2022.

23. Together these income support changes will provide significant income increases for beneficiaries. In light of these changes, there are now choices for Ministers on whether to continue to address income adequacy concerns for beneficiaries and/or whether to progress complementary changes that target further income increases to low-income working households.

There are problems with the current WFF framework

24. Working for Families has achieved its key objectives for some groups and has improved income adequacy and reduced poverty for both working and (subsequent to the Families Package), non-working households also. Like any transfer system that is designed to target particular groups of the population, it has a number of issues, including that it can be fiscally costly when altered, is complex, results in a poor interface between benefit and work, and high effective marginal tax rates (EMTRs) for many families.

25. The following summarises some of the ongoing issues with WFF, and more recent problems highlighted by clients and beneficiary non-governmental organisations:

a. *WFF changes are not particularly cost-effective as a lever for child poverty reduction* because the FTC and IWTC payments go to both low income and middle income families with children, so relatively small increases carry a high fiscal cost and have less of an impact on child poverty reduction in comparison to increasing main benefits for families with children. However, WFF has greater coverage than main benefits because it includes the working poor (i.e. broadly half of all children in poverty are in working households).

b. *'Making work pay'* – despite increases in the minimum wage and wage growth generally, there continue to be concerns that work 'does not pay', mainly for sole parents, particularly once childcare costs are taken into account. Low and middle-income families face high EMTRs (particularly sole parents) – the MFTC withdraws on a dollar-for-dollar basis, and at certain income levels both WFF and Accommodation Supplement payments withdraw simultaneously.

c. *Interface between benefit and work and structure/design of in-work assistance* – needing to be 'off-benefit' to qualify for MFTC/IWTC creates problems for people whose circumstances change frequently, and the settings can discourage working more hours. There has also been confusion for clients with the recent changes to the IWTC, suggesting that improvements to the settings have not necessarily made the system simpler.

d. *Client experience and operational settings between IR and MSD* – the current system of payments is complex, involves multiple payments, and primarily relies on families 'seeking out' their entitlements rather than proactive engagement. Weekly payments within an annual entitlement create complexity for clients; and entitlements and levels change depending on amount of work undertaken, and changes in relationships and care of children (especially shared care).

26. Interviews by NGO groups have highlighted the high compliance costs some people face because systems do not cater well for change[3]. The same groups that have more precarious work[4] and are more prevalent in poverty statistics are also more prevalent in statistics for child support and shared care arrangements. They are therefore more likely to experience changes in circumstances and require more interactions with government agencies to update and correct entitlements, and are also more at risk of incurring unnecessary debt to government.

Scale of reform

27. WFF now operates in a different labour market and welfare landscape compared to when it was introduced. There have been periodic reviews and improvements of some components of WFF, and various options have been explored through Budget processes, but no fundamental review has taken place since its inception.

28. Fundamental reform would involve replacing some/all of the existing payments with new tax credits that are significantly different in design. Options here include introducing an EITC-type payment, phasing in the IWTC so working people on benefit also qualify and/or the complete removal of a work-incentive or work-focused payment with a new series of income adequacy tax credits targeting different costs.

29. Alternatively, there are changes that could be made to parameters within the existing framework, while keeping the broad structure and existing suite of payments. This includes options to make changes to payments rates, income thresholds, extending eligibility and/or improving client experience.

30. In order to address the issues with the current scheme, fundamental and structural change will likely be required, rather than minor changes to existing settings. Achievement of the Government's child poverty targets will also require further significant income support packages. Together, this suggests a review and significant reform is warranted.

[3] For example, the Family 100 Project and discussion with Benefit Advocate groups.

[4] Women, Māori and Pacific, disabled persons, and low-skilled casual workers.

31. While WFF has continued to play an important role in improving income adequacy (and reducing child poverty), and improving the returns from work, there is an argument to re-examine the balance and relative emphasis between the two objectives, particularly given the different settings and landscape that WFF is now operating in.

32. In terms of child poverty reduction, how much can be achieved through the benefit and tax systems, and how much can be achieved by supporting work effort is a common issue that OECD countries continue to grapple with. In virtually all OECD countries, non-employed families are the most economically disadvantaged; and it is generally agreed that good quality, sustainable employment is a primary route through which parents can move their children out of poverty. In saying that, broadly half of all children in poverty in New Zealand are in working households.

33. Policy choices in this area should not be seen as choosing between either work or benefits, but require a balanced approach that supports income adequacy for those on benefit, encourages increased employment among parents where appropriate, and also increases the rewards of paid work at the same time. A starting point might be to determine what policies are needed to help ensure that families are not poor when they are in paid work[5]. In New Zealand, the majority of children in poverty living in beneficiary households are in sole parent families, whereas the vast majority of those in working households are in couple-led families.

34. Recent and proposed increases to benefit levels and the benefit abatement threshold changes will make a significant contribution to income adequacy for beneficiaries and to child poverty reduction.

35. Minimum wage increases and the recent FTC increases as part of the Families Package are also further supporting low-income workers, but there is an argument to consider increases to in-work assistance to address income adequacy and child poverty for working households also, and to ensure that work pays.

36. Some key design considerations/questions include:

- **Income adequacy for beneficiaries versus working families.** Given the recent and proposed increases in incomes for beneficiary households:
  - should there be a complementary focus on income adequacy and making work pay for low-income working households?
  - should any increases in support through the tax credit system go to all low-income households (both working and beneficiary), or specifically to low-income 'working' households?
- **Targeted versus universal.** Should settings be more targeted to low-income families to improve income adequacy/child poverty objectives more cost-effectively, or should settings be more universal to improve adequacy for both low-income families and a larger number of relatively higher-income families?
- **Incentivising movement off-benefit at a particular amount of work versus incentivising working more in the benefit system.** Does the emphasis on getting people off benefit and into work remain a key issue (i.e. current eligibility for in-work assistance relies on a minimum number of hours worked and/or being off benefit), or is there a willingness to accept greater numbers of 'beneficiaries' who

[5] Whiteford, P, Adema, W (2007), 'What Works Best in Reducing Child Poverty: A Benefit or Work Strategy'?, OECD Social, Employment And Migration Working Papers No. 51.

are working more (i.e. workers could be on an abated benefit with in-work assistance phasing in with benefit abatement).

45 When considering any changes to income support settings, there are inevitable trade-offs between increasing incomes, improving incentives to work and managing fiscal costs. This is often referred to as the 'iron triangle' and highlights the choices and trade-offs between raising the living standards of those on low incomes or in poverty, encouraging work, and ensuring fiscal costs to governments are affordable and sustainable.

46 The following discusses these key considerations and design questions, some of the trade-offs, and potential options for changes to help inform the focus of the review. The key design choices and options will have some overlaps and there will be trade-offs across them. Officials can provide further advice on options once we have received Ministers feedback on the key trade-offs and objectives.

Income adequacy for beneficiaries versus working families

47 Recent and proposed increases to benefit rates will improve benefit incomes considerably and reduce child poverty. However, there are also a significant number of working families in poverty. Around half of those aged under 65 in low-income households or in material hardship are from households with at least one full-time worker or with self-employment as the main source of income: the other half are from workless households or households with only a part-time worker or workers.

48 The recent minimum wage increases will have ensured many of those in full time work have experienced income increases and maintained the gap between benefit and full-time work for some groups, however, the value of in-work supports have eroded relative to wage growth.

49 The gap is relatively smaller for some groups, particularly secondary earners and sole parents who have higher income support levels and may face childcare costs from working while on a single income. Ministers may wish to see WFF (or replacement tax credits) do more of the 'heavy lifting' and ensure that work pays for these groups, particularly because wages received in work do not reflect the additional needs/costs associated with having children.

50 The Minimum Family Tax Credit (MFTC) guarantees that work pays when working part-time (at 20 hours for sole parents), combined with the In-Work Tax Credit (IWTC) , but the gain diminishes as hours increase due to a combination of abatement and childcare costs. This pattern is similar for a secondary earner in two-parent families (where the threshold is 30 hours).

51 Officials are seeking Ministers' direction on whether to put more emphasis on payments to low-income working households to support the 'working poor' or whether any increases in support should go to low-income beneficiaries, or both working and beneficiary households.

Potential options

52 Options to <u>improve in-work supports</u> could include:

- increasing the IWTC payment rate, or a similar in-work payment
- replacing the MFTC with a new in-work payment, or introducing a lower abatement within the existing structure.

53 Options that <u>improve adequacy for all families (beneficiary and working)</u> include:

- increasing the FTC or a similar family payment that goes to both workers and beneficiaries.

54 Options to <u>improve beneficiary incomes</u> further include:

- rolling part of the current IWTC payment into the FTC, increasing the payment for beneficiaries and leaving a reduced in-work payment
- rolling all of the current IWTC payment into the FTC, making it available to all low-income households irrespective of work status, and leaving no specific in-work payment.

55 Officials' view is that given the recent and proposed income support transfers targeted towards beneficiary households, there is an argument to complement this with transfers in the form of in-work assistance to low-income working households. The review could therefore look at ways to increase payments more towards the 'make work pay' objective, while still maintaining a focus on child poverty.

Targeted versus universal

56 As noted earlier, WFF is now more targeted than when it was introduced due to indexation settings and wage growth, but recent changes made to FTC/IWTC as part of the Families Package extended eligibility to some higher income families. Best Start Tax Credit was also introduced – which is universal for all children younger than 1.

57 The FTC payment is the primary 'lever' within WFF to reduce child poverty, but even relatively small increases carry a high fiscal cost because it covers around 310,000 families and goes a fair way up the income distribution. For example, a working family with three children earning $100,000 would still be receiving an abated WFF payment of around $85pw (with cut-out at around $120,000). If WFF (or a similar family payment) is more tightly targeted then it would enable greater increases to incomes of lower-income families within the same fiscal envelope.

58 If there were to be changes to WFF towards a more universal approach, it would improve income adequacy for more families, reduce hardship and absolute poverty and recognise the costs of raising children is universal. However, it would increase fiscal costs significantly, and make measured child poverty worse on the before-housing-cost moving-line measure, because middle incomes would increase along with lower incomes. In order for poverty to reduce on this measure, the income of low-income households with children must rise faster than those around the median.

59 This fiscal cost and poverty reduction trade-off is particularly important for the ten-year child poverty targets, which are to halve the 2017/18 rates. Reaching the targets is likely to require regular and significant increases in income support for low-income families over time and the BHC measure is likely to be the most challenging of the targets.

60 We are seeking Ministers' direction on whether WFF should be more targeted to low-income families to improve income adequacy/child poverty objectives more cost-effectively, or whether eligibility should be kept at current levels, or extended to provide greater coverage further up the income distribution.

Potential options

61 Options to universalise Best Start include:

- making the payments universal for all children under three years (as recommended by the WEAG).

62 Options to further target Best Start include:

- higher payment rates for lower income families (e.g. for the first six to 12 months), or extending duration of the targeted payment for lower income families (e.g. up to five years of age); and/or changes to lower the abatement threshold and increase the abatement rate.

63 If Ministers wish to target FTC/IWTC (or a similar payment) to families on the lowest incomes, income increases could be targeted at the lowest income families with no/minimal increases for those on relatively higher incomes. The main trade-off with such an approach is that the abatement rate would need to be increased, which can reduce the return from working for those higher up the income scale.

64 Options towards a less targeted approach that would extend eligibility to those higher up the income distribution include:

- changing the abatement settings of WFF so that payments are indexed or increased to adjust for historic wage growth
- lifting payment rates without corresponding changes to abatement settings to allow higher income families to also receive more assistance.

65 Officials' view is that a given level of targeting of FTC, or a similar payment as a result of this review, remains desirable and is the most affordable way to achieve the child poverty targets. However, there are questions for Ministers on whether tax credits should be more or less targeted relative to current settings. If Ministers wish to make parts of WFF universal, then changes to Best Start may be the most cost-effective lever.

Movement off benefit or beneficiaries working more

66 In-work payments can:

- help to incentivise movement into work or work a certain number of hours; and/or
- help meet the additional costs associated with working; and/or
- provide a sufficient gap between benefits and work to ensure incomes reflect the additional efforts and opportunity costs of working (e.g. ensuring fairness/equity across people in different employment circumstances).

67 These objectives are not independent and can overlap significantly but are important considerations as they can influence the design of any in-work payment. The IWTC is likely to reflect a combination of all three objectives above. Ministers have choices on the role that in-work payments play within the WFF scheme as well as the broader tax and transfer system.

68 Currently, the MFTC provides a strong financial incentive to move off benefit and work a certain number of hours, however it discourages greater working hours, given it withdraws on a dollar for dollar basis. The on/off benefit rule is also difficult for people to navigate, complicates the benefit/work interface and can result in gaps in support – all of which can act as a barrier to work.

69 As part of considering the role of a work-focused payment, it is important to understand the labour supply effects of financial incentives associated with welfare support settings. If work incentives are dampened by policy changes that increase support to

those out of work, then poverty reduction goals will likely be costly to achieve, given risks of reduced employment and increased rates of welfare receipt.

70 As noted above, evidence on the effects of the introduction of the WFF tax credits on improving financial incentives to work found relatively modest impacts – there was some evidence of increased labour force participation of low-income sole parents, and reduced participation of relatively higher-income secondary earners in couples, which was anticipated.

71 Much of the research on the role of work-focused payments is based on evaluations of the US's EITC. There have been similar concerns with the EITC that it may improve incentives for sole parents to participate in the labour market, but worsen incentives for second earners because of the family income test.

72 The EITC is conditional on earned income, whereas WFF has some components that are conditional on employment and being off-benefit (IWTC and MFTC). The MFTC requires a minimum number of hours worked (a cliff-face entry) and the IWTC has a work requirement (without hours since the recent changes), whereas the EITC has a phase-in region at low earnings that encourages more earnings – they both have a plateau and phase-out region.

Potential options

73 Officials will explore how to design an in-work payment to best achieve the objectives and will seek further direction on relative trade-offs as the work progresses. In this report we are seeking Ministers' decisions on whether in-work payments should remain tied to being off-benefit and a minimum number of hours worked, or whether there should be a phase-in system, as with the EITC, and a focus on the level of earnings from hours worked and the ability to earn more as more hours are worked. The latter would extend in-work support to working beneficiaries and potentially increase the number of beneficiaries.

74 Options that maintain a <u>focus on moving off-benefit</u> include:

- retaining a work incentive payment and the off-benefit rule to incentivise working a particular number of hours or level of earned income.

75 Alternatively, if there is a level of comfort with more <u>'beneficiaries' working</u> and increasing their hours of work beyond the benefit abatement threshold, options could include:

- extending in-work payments to beneficiaries by removing off-benefit rule, either by phasing in-work payment with more generous abatement (e.g. EITC-type payment); or blending with existing IWTC payment
- A new bespoke in-work cost alleviation payment to recognise in-work costs, that could be phased in similarly as above.

76 Officials' view is that there remains a need to provide a payment to low-income working families in recognition of the costs of working and people should expect to see a return from working an additional hour. This applies to all workers including those receiving a main benefit. MFTC in its current form does not meet this criterion and, on that basis, officials would recommend settings that no longer required a MFTC payment. The payment provides a high return from working a set number of hours, with no reward for increasing the number of hours worked. This can also create tensions between the work/benefit interface, particularly for people working variable hours.

Modernising WFF delivery

77 Irrespective of questions of balance and the scale and nature of the reform of WFF, there is a need to simplify the system to improve client experience, and better respond to people's circumstances and changing work and care arrangements. This is part of the third objective of the original WFF reform – supporting people into work and to remain in work by making sure they get the assistance they are entitled to in a timely manner.

78 Recipients report greatest levels of satisfaction with WFF when they are in a stable environment with no changes in care arrangements, circumstances, or income fluctuations. When personal circumstances change and the recipient is required to interact with government, their satisfaction decreases due to the complexity in dealing with multiple agencies, variations within WFF and Child Support, and the potential for over and underpayments of entitlements. Financial uncertainty or stress as a result of changes is the most reported cause of a poor experience by a recipient, and can result in debt or less timely support.

79 Alongside any changes to the structure of WFF, reform also needs to respond to these problems that clients experience with the interface between benefit and work, the complexity of payments, and navigating the operational arms of both the Ministry of Social Development (MSD) and Inland Revenue (IR). The system needs to ensure certainty of support during changes in circumstances, such as work and/or shared care arrangements, with payments being more neutral in response to family formation and relationships, and clarity around assessment periods, and the payment agency. Options being developed should aim to increase the accuracy of payments, ensuring people receive the right amount at the right time, and reduce the unnecessary creation of debt to government. Some of these issues have been previously raised as part of IR's Business Transformation but have not been fully progressed.

80 Options could include considering:

- whether a single agency should deliver WFF or a similar tax credit system
- the definition of income and the period over which income is assessed, which may also reduce debt to government
- improving the information exchange between agencies.

Scope of review

81 We propose the scope of the review primarily focuses on the current WFF tax credits (Best Start tax credit and Family tax credit, In-Work tax credit and Minimum Family tax credit).

82 Other welfare payments and tax credits (including Child Tax Credit and Independent Earner Tax Credit (IETC)) would not be directly in scope but would be considered as the review progresses to ensure coherency of the wider tax and transfer system. Specific payments with strong connections to WFF are main benefits, the Winter Energy Payment and the Accommodation Supplement, Paid Parental Leave, Child Support payments and childcare subsidies, and the Orphan's benefit and Unsupported Child Benefit. The development of options could also highlight where simplifications of the wider welfare system could be achieved.

83 There are also choices for Ministers as to whether to broaden the scope of the review to include assistance for those currently not covered by WFF, and/or whether to include the childcare assistance review within the WFF review.

Assistance only to families with children or broadening scope to include in-work assistance for those without children and/or disabled people

84 Currently WFF is only available to families with children, with the IETC providing a work incentive to individuals without children. The IETC provides up to $10 per week for low-income working people earning between $24,000 and $48,000. There are choices for Ministers on whether any new or reformed tax credits should be extended to families without children (as recommended by the WEAG with the EITC). Note this is likely to significantly increase the fiscal costs of any reforms but may provide some simplification and better support changes in family circumstances.

85 In some other countries there are also tax credits available to support disabled people. For example, the United Kingdom has a Working Tax Credit which is made up of several components – which includes a disability element. In addition, Canada has a Disability Tax Credit that was introduced in 1988 to offset additional unavoidable disability costs that other taxpayers do not face. The purpose of the Canadian disability tax credit is to provide for greater tax equity by allowing some relief for disability costs that are indirect or difficult to quantify.

86 In New Zealand's context, there is no clear parallel with a Disability Tax Credit. Instead, the government provides a wide range of financial assistance to help meet the additional needs and costs associated with having a disability (e.g. Disability Allowance and Supported Living Payment). Significant further work would be required to determine whether such a tax credit would be appropriate in New Zealand's context, and would be best considered as part of the existing review underway as part of the Welfare Overhaul work programme looking at the financial assistance available for people with a health condition and disability.

Childcare Assistance

87 A broad review of childcare assistance is on the long-term welfare overhaul work programme [CAB-19-MIN-0578 refers]. We understand that in the context of discussions on MSD's Budget 21 bid on improving Childcare Assistance, Ministers have expressed interest in bringing the review forward, with the potential for a public announcement to be made. Officials will be providing advice to Ministers by the end of April 2021 on possible options for the scope, timing and milestones for the review.

88 As there are strong synergies between WFF and childcare assistance, there would be distinct advantages in doing the two reviews alongside each other. However, we do not recommend that the review of childcare assistance form part of the WFF review as it would be likely to cause its scope and management to become too broad and potentially unwieldy.

89 The aims, objectives and delivery mechanisms of WFF and childcare assistance are largely separate and have different agencies as key stakeholders. The WFF review would be of primary interest for the Treasury, IR and MSD, while the review of childcare assistance would be done with major involvement from the Ministry of Education, Ministry for Women and the Ministry of Business Innovation and Employment (MBIE).

90 As MSD will be involved in both reviews, officials will ensure that they progress in parallel and take full advantage of the potential improvements in the interactions between WFF and childcare assistance.

Related work programmes

91 Other priorities on the government's work programme that would have an impact on the WFF review are the Social Unemployment Insurance project, the Debt to Government project, and the Welfare Overhaul.

Timing of review and stakeholder engagement

92 The timeframe for the review will need to take into consideration:

- policy development
- consultation, whether targeted or public
- legislative change and feasible timeframes for implementation (IT changes, staff training, communications)
- other related work programmes and budget changes.

93 A working group of officials from IR, MSD, the Treasury, and the Child Poverty Unit will work on the options for change. MBIE, the Ministry of Education and other agencies will be consulted. Officials consider that a year for policy development and consultation prior to Budget approval would be required for most of the significant policy options, and a year for standard legislative change and implementation.

94 Timing for the review will also be informed by which Budget Ministers wish to make decisions in. Decisions in Budget 2022 with a shortened legislative process would allow for changes to be made from 1 April 2023 at the earliest. However, this would be a shortened timeframe for policy development and consultation with the risk that some aspects are less well developed or informed, which adds risks for implementation and delivery. Implementation of changes could also be phased over a number of years.

95 Decisions in Budget 2023 would provide further time for policy development of more fundamental change and consultation, with changes to be made from 1 April 2024 or later depending on time required for legislation and implementation, reflecting the degree of change to WFF. However, this option would need to take into account the election period in 2023 and how this affects the legislative process.

96 We understand that there is potential for implementing a social unemployment insurance programme in the near term. These changes will involve IR and MSD in policy development and implementation. This group is also working on developing and implementing Budget 2021 income support options. There is a risk that changes in timing or priority of these other projects will impact on the delivery of advice on WFF. Officials working on the related projects will keep each other informed as work develops on the respective projects and will advise Ministers if competing priorities have an impact on delivery.

Stakeholder engagement

97 There is a question whether Ministers want to involve the public and key stakeholders in the policy development stage. Public consultation can provide information on the likely practical impacts of different options but require more time to incorporate in the review. Targeted stakeholder engagement may provide more informed opinions on the effectiveness of the options on the objectives, as key stakeholders generally have a better understanding of the technical nature of the tax and transfer system.

Child poverty targets – interaction with timing

98 The Government is required to set its next round of intermediate child poverty targets by June this year, which will set out the level of reduction it is aiming for over the next three years. Alongside the benefit increase that is intended for Budget 2021, the review of Working for Families is the other major opportunity to achieve direct and immediate reductions through income support changes in the next three years. The Government's intentions for the review have a direct relationship to the size of the child poverty targets that are announced this year.

99 Current methods for child poverty reporting mean that the impact of transfer payments is only partially seen in the year after implementation, with the full impact seen in the year after. The upcoming period covers the 21/22, 22/23 and 23/24 years, which means that on current methods:

- in order to have a full impact in the reporting on the next three-year target period, changes would need to be implemented by July 2022.
- if implemented in April/July 2023, the impact will be spread across the next two target periods (half in 2023/24 with the other half in 2024/25)
- if implemented in April/July 2024, the impact will not be seen until the target period covering the 24/25, 25/26 and 26/27 years.

100 Stats NZ is currently considering how to improve the timeliness of policy impacts being reflected in child poverty statistics, including changes that could potentially address the partial/full issue. If these changes are made, then it is possible that a WFF increase implemented by July 2023 will have its full impact within the coming three-year period.

101 The timing of implementation will also influence when changes impact on child poverty targets. Officials recommend the review seek decisions in Budget 2022 if Ministers would like decisions to be implemented by 1 April 2023 at the earliest, and include targeted engagement with key stakeholders. Officials will provide advice on the scale or extent of the decisions that can be made according to this timeframe.

Lead Minister and announcement of review

102 Officials recommend that decisions on options be considered by this Income Support Ministerial group before being considered by Cabinet. While the review is underway, it would be useful to have a nominated Minister responsible for responding to parliamentary questions, OIA requests and other requests from the media and public.

103 Ministers may also want to more formally announce the timing of the review of WFF. This could be done after this meeting, or alongside other Budget 2021 announcements, or as part of a refresh of the Welfare Overhaul work programme.

Next Steps

104 Officials will prepare more detailed timeframes for policy development, engagement, legislation and implementation and a detailed workplan alongside further development of options, based on decisions in this paper.

Item 5

Inland Revenue
Te Tari Taake

TE TAI ŌHANGA
THE TREASURY

DEPARTMENT OF THE PRIME MINISTER AND CABINET
TE TARI O TE PIRIMIA ME TE KOMITI MATUA

MINISTRY OF SOCIAL DEVELOPMENT
TE MANATŪ WHAKAHIATO ORA

Joint Report: Working for Families Review: revised recommendations

Date:	16 April 2021	**Report No:**	DPMC-2020/21-860; T2021/1007; REP/21/4/383; IR2021/175
		File Number:	SH-3-6

Action sought

	Action sought	Deadline
Rt Hon Jacinda Ardern **Prime Minister / Minister for Child Poverty Reduction**	**Agree** to revised recommendations discussed at meeting	None
Hon Grant Robertson **Minister of Finance**	**Agree** to revised recommendations discussed at meeting	None
Hon Carmel Sepuloni **Minister for Social Development and Employment**	**Agree** to revised recommendations discussed at meeting	None
Hon David Parker **Minister of Revenue**	**Agree** to revised recommendations discussed at meeting	None

Contact for telephone discussion (if required)

Name	Position	Telephone		1st Contact
Murray Shadbolt	Principal Advisor, Welfare and Oranga Tamariki Team, The Treasury	04 917 6979	022 698 6915	
Deborah Tucker	Senior Analyst, Child Poverty Unit, Department of the Prime Minister and Cabinet	04 817 9641	021 195 6592	
Daniel Frischknecht	Principal Analyst, Income Support, Ministry of Social Development	04 918 9583	027 370 8900	
Eina Wong	Principal Policy Advisor, Policy and Regulatory Stewardship, Inland Revenue	04 890 3220	021 0239 7626	

Minister's Office actions (if required)

Return the signed report to Treasury.

Enclosure: No

Joint Report: Working for Families Review: revised recommendations

Purpose

1. Following the Income Support Ministers' meeting on 13 April, at which the Working for Families report (*Joint Report: Welfare Overhaul: Working for Families Review - DPMC-2020/21-771; T2021/632; REP/21/4/356; IR2021/156*) was discussed, Ministers' agreed on a number of recommendations and asked that a revised set be provided to record decisions on the direction for the Review. This note provides the updated recommendations based on the discussion at the meeting, along with the original noting recommendations.

Recommended Action

We recommend that you:

Context and rationale for a Review of Working for Families

a **note** that Working for Families combines dual objectives of income adequacy and work incentives, and has achieved its key objectives for some groups, but has resulted in mixed effectiveness for others

b **note** that the original Working for Families reform also included a third delivery objective to achieve a system that supports people into, and to remain in, work by making sure they get the assistance they are entitled to in a timely manner, and that this continues to be important regardless of the scale and direction of reform

c **note** that the Welfare Expert Advisory Group recommended significant changes to Working for Families tax credits, including making the Family Tax Credit more generous and more universal, replacing in-work payments with a new Earned Income Tax Credit, and making Best Start universal for all children under three, as part of a wider welfare package

d **note** that the Government has set ambitious ten-year child poverty targets, which will require further significant income support packages to make progress

e **note** that, since the last significant changes to New Zealand's system of tax credits for families in 2004, there have been important contextual changes, including:

- changes to labour market settings, including sustained increases in the level of the minimum wage
- significant increases in income support through the Families Package, indexation changes, and recent and planned main benefit increases
- introduction of elements of universalism through Best Start
- changes to the In-Work Tax Credit to increase its flexibility
- greater support for working beneficiaries through increases to abatement thresholds and employment programmes

f **note** that, while Working for Families tax credits are achieving their key objectives for some groups, current settings are complex, cause significant problems for those with changing work and family arrangements, result in a poor transition between benefit and work, and can result in high effective marginal tax rates for some families that discourage working more hours

g **note** that reform could be small-scale within the existing framework, or significant in that it could look to replace some or all of the existing tax credits with new payments, and that officials recommend a more fundamental reform given the current issues with Working for Families

h **agree**, in light of the changing context and the Government's commitment to ambitious targets for the reduction of child poverty, to bring forward the Review of the Working for Families tax credits currently on the medium-term Welfare Overhaul work programme

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

Objectives and direction for the Review

i **agree** with the following high-level objectives for the system of tax credits for families:

- supporting income adequacy and reducing child poverty
- improving financial incentives for low income earners to participate in the labour market

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

j **note** that you discussed at the meeting the direction for the Review, including the relative balance between:

- **income adequacy for beneficiaries versus working families** – should payments to low-income working households to support the 'working poor' be increased versus payments to beneficiary households, particularly given recent and proposed income increases to beneficiaries?

- **targeting versus universalism –** should WFF be more targeted to low-income families to improve child poverty objectives more cost-effectively, or should settings be more universal to improve adequacy for both low-income families and a larger number of relatively higher-income families?

- **incentivising movement off-benefit at a particular amount of work versus incentivising working more in the benefit system** – should in-work assistance encourage movement off benefit at particular levels of hours worked and/or earned income or should the assistance phase in and merge with the benefit system and be available to working beneficiaries?

k **agree** that there is a particular focus in the Review on low-income working families while maintaining support for beneficiary families

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

l **agree** that the Review prioritise options that shift more towards an emphasis on targeting support to low-income families rather than more universal support

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

m **agree** that the Review prioritise the principle of people being better off in work, and assisting with costs for people in work

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

n **agree** to provide advice on extra costs for disabled people in work, and include options on a Disability Tax Credit (including for those without children) as part of the Working for Families Review

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

o **agree** that new or reformed Working for Families tax credits *not* be extended to families without children

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

p agree that childcare assistance be a separate but related item, considered as part of the existing welfare overhaul work programme

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

q **agree** that the Working for Families Review include the Accommodation Supplement

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

Timing and implementation for changes arising from the Review

r **note** that on current reporting methods, in order to have a full impact on child poverty reporting for the next three-year target period:

- changes to transfer payments would need to be implemented by July 2022
- if changes were implemented in April/July 2023, the impact on child poverty reporting would be spread across the next two target periods
- if implemented in April/July 2024, the impact would be seen in the next target period covering the 24/25, 25/26 and 26/27 years

s **note** that decisions in Budget 2022 with a shortened legislative process would allow for significant Working for Families changes to be made from 1 April 2023 at the earliest

t **note** that a longer implementation timeframe (such as 2024) would allow more time for engagement with stakeholders and more fundamental reform to be considered

u **agree** that officials report back on the Review to Ministers in the middle of the year, including advice on initial options, to inform decisions for Budget 2022

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

v **agree** that the fiscal envelope for the Review is broadly the current envelope of spending on Working for Families tax credits and the Accommodation Supplement combined

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

w **agree** that the Minister for Social Development and Employment be the lead Minister for the Review

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

x **agree** that the Ministry of Social Development be the lead agency for the Review, with other key agencies part of the joint working group

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

y **agree** to announce the Review of Working for Families, which is part of the Welfare Overhaul work programme, alongside other announcements in Budget 2021

Agree/Disagree	*Agree/Disagree*	*Agree/Disagree*	*Agree/Disagree*
Prime Minister	**Minister of Finance**	**Minister for Social Development and Employment**	**Minister of Revenue**

z **note** that officials will work with Ministers' offices on the content of the Budget 2021 announcement aa **refer** this report to the Minister for Children for their information.

Refer / Not referred
Prime Minister

s 9(2)(a)

Kristie Carter
Director, Child Poverty Unit,
Department of Prime Minister and Cabinet

s 9(2)(a)

Keiran Kennedy
Manager, Welfare and Oranga
Tamariki, The Treasury

s 9(2)(a)

Polly Vowles
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s 9(2)(a)

Carolyn Elliott
Acting Manager, Policy
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Rt Hon Jacinda Ardern
Prime Minister / Minister for Child
Poverty Reduction

Hon Grant Robertson
Minister of Finance

Hon Carmel Sepuloni
Minister for Social Development
and Employment

Hon David Parker
Minister of Revenue

Item 6

Policy and Regulatory Stewardship
Kaupapa me te Tiaki i ngā Ture
55 Featherston Street
PO Box 2198
Wellington 6140
New Zealand

T. 04 890 1500

Briefing note

Date:	18/08/2021
To:	Jason Raven, PAG, DPMC
cc:	Deborah Tucker, Principal Analyst, Child Poverty Unit, DPMC Laura Browne, Senior Analyst, TSY Polly Vowles, Policy Manager, Welfare System and Income Support, MSD
From:	Mila Maxon, Policy Advisor, IR
Subject:	**Data on the prospective extended BSTC option**

Commissioning

1. DPMC has requested information to inform a policy option on extending the BSTC:

   "BestStart figures – number of recipients receiving this payment, by child age, year, and cost."

   And:

   "Regarding BestStart I'm keen to make sure there's a breakdown of the number of people receiving it and cost separately for the year one universal component and for the year 2/3 component."

2. This information is provided below.

The extended BSTC option

3. The extended BSTC option would see eligibility for the BSTC extended to families with children up to the age of 5, with payment rates set at $40pw for the families with 3- to 4-year-olds.

4. We note that a complication of this option is that babies born in the first year the BSTC became available in 2018 will age out of eligibility before it can be extended, and we are considering the administrative implications.

Option settings

5. The following table uses the (anticipated) status quo BSTC rate of $3306 per year ($63.60 p/w) instead of the current rate of $3120 per year ($60 p/w) in anticipation of a CPI indexation of 5.93% that will apply from 1 April 2022 under existing settings.

Best Start Tax Credit rates (TY23)	Status Quo (weekly/annual)	Extended option (weekly/annual)
Child rate, aged under 1	$63.58 / $3306	$63.58 / $3306
Child rate, aged from 1 to 2	$63.58 / $3306	$63.58 / $3306
Child rate, aged from 3 to 4	–	$40.00 / $2080

Main impacts (tax year 2022/23) – provided by TAWA modelling

6. The extended BSTC option has an estimated fiscal cost of $135m, with 62,000 households each gaining around $41 per week on average. These households are mostly in the lower half of the income distribution.

7. It is estimated that:

   - 7,000 children would be lifted out of poverty using the Fixed-line After-Housing-Cost-50 (AHC50) measure; and

   - 5,000 children would be lifted out of poverty using the Before-Housing-Cost-50 (BHC50) measure.

Annual Fiscal cost[1]	Reduction in # of Children Fixed AHC50[2]	Reduction in # of Adults Fixed AHC50[2]	Reduction in # of Children BHC50[2]	Reduction in # of Adults BHC50[2]	# of gaining households[3]	Average gain p/w for gaining households[4]
$135m	7,000	3,000	5,000	3,000	62,000	$41

8. For more details, refer to *TAR 289: Best Start Tax Credit option change for Working for Families review*.

BSTC population data

9. There are several caveats to the data provided below.

10. This data excludes MSD customers who have no interaction with IR because MSD record data differently. Crown accounting suggests that 78% of BSTC expenditure

[1] Margin of error (MoE) for annual fiscal costs are up to $13m.
[2] MoE for poverty measures are up to 4,000.
[3] MoE for numbers of winners and losers analysis measures are up to 6,000.
[4] MoE for costs of winners and losers analysis measures are up to $2.

is distributed by IR and 22% is distributed by MSD.[5]

11. The data for BSTC is based on payments received during the year, which are influenced by two main factors:
    - The baby's date of birth – Because the first year's entitlement is universal, the non-abated payment will be spread across two tax years for most familes.
    - The lag in the first BSTC payment due to PPL being paid first.[6]

12. Subject to the above caveats, the following table shows BSTC entitlement paid in each tax year since its introduction on 1 July 2018.

Tax year ending March	Number of families with BSTC entitlement (cumulative)	BSTC entitlement	Number of families with non-abated BSTC[7]
2019	27,000	$23m	27,000
2020	75,000	$131m	63,000

13. Data for the 2021 tax year is not available because assessments are not yet finalised.

14. The BSTC cannot easily be separated on a per child basis because, like each WFFTC, it is paid out in a lump sum per family.

15. In tax year 2020, there were around 12,000 families who received an abated BSTC payment. I.e., there were 12,000 families with children aged over 1-year who had an annual family scheme income greater than $79,000. The 63,000 families with a non-abated payment include babies both aged under and over 1-year old.

16. Of the 27,000 families who received a BSTC payment in tax year 2019, some are included in the 63,000 non-abated group in tax year 2020, and some are in the 12,000 abated group.

17. Further modelling is required to understand:

    - Total BSTC recipient information (MSD breakdown of number of children for whom BSTC was paid on an annual basis, and birthdates), and
    - Grouping by age cohort (rather than tax year or fiscal year receipt)

Children aging out of the BSTC

18. From 1 July 2021, the first cohort of eligible babies began to age out of the BSTC scheme. There were 57,000 babies registered with IRD with birth dates between 1 July 2018 and 30 June 2019, all of whom would have received the universal first year payment. By 30 June 2022 this group of children will not receive any more BSTC payments under the status quo settings.

[5] This data relates to the 2019-2020 fiscal year, rather than the tax year.

[6] There is also an interaction between PPL and BSTC entitlement that can result in overpayments of the BSTC, which is not reflected in this note.

[7] Due to data limitations this information is based on best estimates.

Item 7

MINISTRY OF SOCIAL DEVELOPMENT
TE MANATŪ WHAKAHIATO ORA

TE TAI ŌHANGA
THE TREASURY

Inland Revenue
Te Tari Taake

DEPARTMENT OF THE PRIME MINISTER AND CABINET
TE TARI O TE PIRIMIA ME TE KOMITI MATUA

Report

Date: 17 September 2021

To: Rt Hon Jacinda Ardern, Prime Minister / Minister for Child Poverty Reduction

Hon Grant Robertson, Minister of Finance

Hon Kelvin Davis, Minister for Children

Hon Carmel Sepuloni, Minister for Social Development and Employment

Hon David Parker, Minister of Revenue

Working for Families Review: update and options for Budget 2022

Purpose of the report

1 This report:

- provides you with an update on the Working for Families (WFF) review, and how the work programme is being sequenced following recent feedback from Income Support Ministers
- sets out options for a package that redistributes support to low-income families alongside the planned Consumer Price Index (CPI) adjustment of WFF payments in April next year.

2 The paper includes some options that involve introducing a second abatement threshold for the Family Tax Credit (FTC) and In-work Tax Credit (IWTC) in April 2022. If Ministers wish to progress any of these two-tier options, Inland Revenue need to begin implementation by the end of September in order to make the necessary system changes in time. We are therefore seeking a decision now as to whether to proceed with these 'two tier' options, and draft a Cabinet paper seeking agreement to them, or rule out this kind of option for April 2022.

Executive Summary

Phasing of the WFF review work programme

3 Based on your feedback at the last Income Support Ministers' meeting, officials have structured the review of WFF into two phases:

- phase one will consider modest-cost options for Budget 2022 that increase and redistribute support to low-income families alongside the planned 5% CPI adjustment in April 2022
- phase two will consider more fundamental changes to the structure and design of WFF payments, with a particular focus on in-work support, and changes to improve administration, operations and client experience.

4 Ministers have agreed to defer public engagement until May 2022, which aligns with the longer development timeframe for the more substantial options in the WFF review. Alongside this, officials will continue progressing a number of related workstreams, including potential changes to the Accommodation Supplement, the Review of Childcare Assistance, and Child Support Pass on.

Modelling a redistribution package focused on changes to the Family Tax Credit

5 Officials have undertaken further exploratory modelling of different combinations of FTC increases and abatement changes, and identified a range of options. As the table below shows, we have grouped these various options into four categories along a spectrum of cost/impact from lower to higher. Introducing changes to abatement generally reduces the cost of a flat FTC increase of the same size by around $100m.

6 Within each grouping, there are further choices regarding the specific design of the abatement settings. We have primarily focused on 'two tier' abatement options to further target support to low-income families. For around the same cost, similar FTC increases (and child poverty impacts) can also be achieved working within the current single-tier abatement structure by simply increasing the abatement rate, with slightly different distributional impacts.

Table 1: Options identified

Option	FTC increase		Child poverty		Two tier abatement approach			Single tier abatement approach		
	FTC increase above CPI	FTC increase with CPI (eldest & subs. child)	BHC50	AHC50		Second abatement Threshold	Second abatement rate		Abatement threshold	Abatement rate
Lowest cost ($60-90m)	$5	$11.71 and $10.42	5,000	7,000-8,000	A	$60,000	29%	C	$42,700	27%
						$65,000	31%		$45,200	29%
					B	$75,000	33%			
						$75,000	35%			
Lower cost ($130-170m	$7.50	$14.21 and $12.92	7,000-8,000	11,000-13,000	A	$60,000	29%	C	$42,700	27%
						$65,000	31%		$45,200	29%
					B	$75,000	33%			
						$75,000	35%			
Higher cost ($200-240m)	$10	$16.71 and $15.42	11,000-13,000	15,000-16,000	A	$60,000	29%	C	$42,700	27%
						$65,000	31%		$45,200	29%
					B	$75,000	33%			
						$75,000	35%			
High cost ($360-400m)	$15	$21.71 and $20.42	16,000-17,000	22,000-23,000	A	$60,000	29%	C	$42,700	27%
						$65,000	31%		$45,200	29%
					B	$75,000	33%			
						$75,000	35%			

7 Further advice on the impact of the different settings is included in the body of this paper. Different abatement settings all involve trade-offs between different objectives, and the abatement structure you ultimately progress will depend on the specific distributional impact and incentive structure you want to achieve. In summary:

- The single-tier options redistribute funding from a much broader range of middle-higher income families, and a have a more modest impact on EMTRs.
- The two-tier options redistribute funding from a smaller group of comparatively higher income families, and a significant increase in EMTRs is concentrated within this group.

8 Effective marginal tax rates increase under all the options. These options reflect a key trade-off between objectives frequently encountered in income support – more focused targeting of support to families on low-middle incomes at the cost of reducing incentives to work.

9 Some of the impacts on work incentives created by the options in this paper could potentially be mitigated by further changes progressed as part of phase two of the review. However, such options may turn out to be limited if fiscal, operational, or other constraints arise in the intervening period, and some of the more expensive options in this paper may limit your 'headroom' for further WFF reform.

Additional option: a relevant change you could consider for Best Start Tax Credit (Best Start)

10 One relevant change to abatement settings that could be considered is to align Best Start settings with other WFF payments (FTC and IWTC), so that any new higher abatement settings for WFF do not apply alongside the withdrawal of Best Start payments for families with young children.

11 Aligning Best Start abatement settings would involve winners and losers, as well as additional fiscal costs, and further work is required to understand the distributional impact and costs of the change. As with the second threshold, Inland Revenue would need a decision on this kind of structural change by the end of September if it was to be implemented by April next year. For this reason, officials recommend further analysis and advice on whether to proceed with this option as part of phase two.

Smoother indexation arrangements

12 Ministers have also expressed an interest in shifting to smoother indexation changes over time, and we have included information on the costs of these changes in this paper. If you wish to make permanent changes to the way payments are indexed, there is a choice as to whether to use prices or wages:

- **Annual CPI indexation ($58m p.a. for FTC and Best Start)** – this would not substantially change FTC rates over the long term, but would be smoother and mean slightly higher rates in the years between scheduled adjustments – and carry some additional cost as a consequence. If you wish to introduce annual indexation tied to prices, we recommend using the headline CPI, rather than the bespoke 'without tobacco' index introduced in 2010.
- **Annual wage indexation ($85m p.a. for FTC and Best Start)** This would support the Government's child poverty objectives, but is more costly, particularly over the longer term: The impact and the fiscal cost of wage indexation is initially small, but 'snowballs' over time and becomes increasingly substantial. If you wish to ensure the incomes of low-income families keep pace with middle-income families, we recommend wage-adjusting the FTC and Best Start, and indexing the IWTC if you also want to maintain work incentives over time.

13 In both cases, such changes would have additional fiscal costs, which may limit your options for the second phase of the review; you may prefer to consider permanent indexation changes as part of the subsequent phase.

Next steps

14 A summary of the key choices in this paper is outlined in table 2. To assist your decisions, as useful context we have also included information on other options you have been considering for Budget 2022: Best Start and Child Support Pass on. This is attached as Appendix Three.

15 If you wish to introduce a 'two tier' option with a second abatement threshold for FTC and IWTC with an implementation date of 1 April 2022, we will prepare a paper for a Cabinet meeting before the end of September that seeks in-principle agreement to the change. Precise details can be confirmed via a subsequent paper and pre-commitment on Budget 2022 in November, followed by urgent legislation.

16 If you wish to proceed with a 'single tier' option for April, we can confirm policy details via follow-up advice and seek agreement to the final package through a single Cabinet paper in November. If you instead wish to discuss an alternative timeframe for changes in 2022 or later, such as by postponing the planned CPI indexation round, we will provide you with further advice.

Table 2: Summary of choices outlined in this paper

<table>
<tr><td colspan="5">1. Options for cost
The FTC increase largely determines the cost and the child poverty impact.</td></tr>
<tr><td rowspan="2">Option</td><td colspan="2">FTC increase</td><td colspan="2">Child poverty</td></tr>
<tr><td>Increase above CPI</td><td>Increase with CPI (eldest & subs. child)</td><td>BHC50</td><td>AHC50</td></tr>
<tr><td>1. Lowest cost ($60-90m)</td><td>$5</td><td>$11.71 and $10.42</td><td>5,000</td><td>7,000-8,000</td></tr>
<tr><td>2. Lower cost ($130-170m)</td><td>$7.50</td><td>$14.21 and $12.92</td><td>7,000-8,000</td><td>11,000 -13,000</td></tr>
<tr><td>3. Higher cost ($200-240m)</td><td>$10</td><td>$16.71 and $15.42</td><td>11,000-13,000</td><td>15,000-16,000</td></tr>
<tr><td>4. High cost ($360-400m)</td><td>$15</td><td>$21.71 and $20.42</td><td>16,000-17,000</td><td>22,000-23,000</td></tr>
<tr><td colspan="5">2. Approach to abatement
The abatement structure influences distributional impacts and the effective marginal tax rates - primarily how much negative impacts are concentrated on “higher” income families or spread over a broader range</td></tr>
<tr><td>Approach</td><td colspan="2">Losers</td><td colspan="2">EMTRs</td></tr>
<tr><td>A: Modest two-tier structure (lower threshold)

2nd threshold set at 60/65k and an abatement rate at 29%/31%</td><td colspan="2">10-35k households lose $0-10, mostly earning above 100k</td><td colspan="2">Significant impact on work incentives for families above $60-65k - increases EMTRs by 4-6 ppt</td></tr>
<tr><td>B: Sharper two-tier abatement structure (higher threshold)

2nd threshold at $75k and an abatement rate at 33%/35%</td><td colspan="2">10-30k households lose $10-15, mostly earning above 100k</td><td colspan="2">Very significant impact on work incentives for families above $75k - increases EMTRs by 8-10 ppt</td></tr>
<tr><td>C: One tier abatement structure
Increase to the abatement rate, possibly with a small increase to the abatement threshold</td><td colspan="2">Less than 10k households losing less than $5.</td><td colspan="2">Modest to significant impact on work incentives for families for larger number of families above 42-45k - increases EMTRs by 2-4 ppt</td></tr>
</table>

Recommended actions

It is recommended that you:

1 **indicate** if you wish to proceed with a Working for Families redistribution package in April 2022, alongside the planned CPI adjustment for the Family Tax Credit and Best Start Tax Credit that is scheduled to increase the Family Tax Credit first child rate by $6.71 and the subsequent child rate of $5.42

Yes / No

2 **note** that there are two key decisions for the shape of any package: the size of the Family Tax Credit increase (which primarily determines the cost of the package and

the child poverty impact) and the approach to the abatement structure (which influences distributional impacts and the effective marginal tax rates)

3 **indicate** the size of any additional Family Tax Credit rate increase that you wish to base a package around:

3.1 no increase above the planned adjustment in April

Yes / No

3.2 a further $5 per child at around $60-90m

Yes / No

3.1 a further $7.50 per child at around $130-170m

Yes / No

3.2 a further $10 per child at around $200-240m

Yes / No

3.3 a further $15 per child at around $360-400m

Yes / No

4 **indicate** the approach you wish to take to the structure of abatement for the package:

4.1 approach a: a more modest two-tier structure with a 2nd threshold set at 60/65k and an abatement rate at 29%/31%

Yes / No

4.2 approach b: a sharper two-tier structure with a 2nd threshold at $75k and an abatement rate at 33%/35%

Yes / No

4.3 approach c: a one-tier abatement structure that increases the abatement rate, potentially accompanied by a small increase to the abatement threshold

Yes / No

4.4 approach d: no changes to abatement, noting that the cost of any FTC increase would be above those set out in this paper and in recommendation 3 above

Yes / No

5 **note** that, in order to make the necessary system changes by April 2022, a decision to introduce a two-tier structure with a second abatement threshold needs to be made by Cabinet by late September, and a single-tier abatement option needs to be agreed by November this year.

6 **indicate** if you wish to make either of the following permanent changes to indexation as part of any package in April:

6.1 indexing Working for Families tax credits to prices on an *annual* basis

Yes / No

6.2 indexing Working for Families tax credits to wages on an *annual* basis

Yes / No

7 **agree** that, if you wish to index Working for Families payments to prices as per 6.1 above, to use the all groups CPI

Yes / No

8 **indicate**, if you wish to index Working for Families payments to wages as per 6.2 above, which payments you would like to adjust:

8.1 the Family Tax Credit and Best Start Tax Credit

Yes / No

8.2 In-Work Tax Credit

Yes / No

8.3 the abatement thresholds for the In-Work Tax Credit, Family Tax Credit and the Best Start Tax Credit.

Yes / No

s 9(2)(a)

Kristie Carter
Director,
Child Poverty Unit

..... / ...... / ......

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Polly Vowles
Manager, Income Support Policy
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Rt Hon Jacinda Ardern
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Hon Grant Robertson
Minister of Finance

..... / ...... / ......

Hon Kelvin Davis
Minister for Children

..... / ...... / ......

Hon Carmel Sepuloni
Minister for Social Development and Employment

..... / ...... / ......

Hon David Parker
Minister for Revenue

..... / ...... / ......

Update on WFF work programme and how it is being phased

17 The Government has announced a review of Working for Families. Ministers have agreed the review will focus on:

- targeting more support to lower income families, rather than universal support
- increasing support for low-income working families, while maintaining support for beneficiary families
- help make work pay and assist with the costs for people in work.

18 The Government has also set ten-year child poverty targets, which require baseline rates to be halved by 2027/28, and three-year targets covering the 2021/22, 2022/23 and 2023/24 years. Implementation needs to occur by mid-2022 for any changes to have a full impact on the period.

19 On 11 August, Income Support Ministers met to discuss the review, and considered recent advice from officials [refer DPMC-2021/22-100; REP/21/8/830; T2021/1994; IR2021/321]. Ministers indicated that

- the level of redistribution required by the fiscally neutral options had undesirable distributional impacts that meant such options would not be progressed, but that there could still be room for changes to abatement settings at the upper end
- the planned 5% CPI adjustment of WFF payments scheduled for April 2022 provided an opportunity to make some changes which would not result in families being worse off than they were previously
- changes to indexation settings should be considered to 'smooth' future increases
- there may be room in Budget 2022 for a modest-cost package in April 2022 that combined an FTC increase with abatement changes
- there may be the potential for a more substantial package in Budget 2023, which means more fundamental design changes, and improvements to the coherency of the system could be considered over a longer timeframe.

20 Based on your feedback, officials propose that the review of Working for Families be structured into two phases. **Phase one** will consider *options for Budget 2022 that redistribute support to low income families*, and is the focus of the remainder of this paper.

21 **Phase two** will consider more fundamental changes to the structure and design of WFF payments. As part of phase two, the following workstreams have been developed with a focus on Budget 2023 or later

- *Workstream One: improvements to the structure and design of in-work tax credits* – this workstream is focused in particular on the In-Work Tax Credit (IWTC) and the Minimum Family Tax Credit (MFTC).
- *Workstream Two: improvements to assist with the costs of children in the early years, particularly with childcare* – this is focused in particular on Best Start and the IWTC, and how these payments interact with childcare assistance
- *Workstream Three: administrative and operational improvements* – this is focused on changes that would increase accuracy, reduce debt and improve client experience, along with consideration of more fundamental operational changes such as a single agency responsible for delivering WFF payments.

22 Ministers have agreed to defer public engagement until May 2022, which aligns with the longer development timeframe for the more substantial options in the WFF review. Alongside this, officials have been progressing a number of related workstreams, including potential changes to the Accommodation Supplement, the Review of Childcare Assistance, and Child Support Pass on.

Budget 2022 options for implementation in April next year

23 As requested by Ministers, officials have explored modest-cost options that could be implemented alongside the planned 5% CPI adjustment in April 2022, and which combine:

- increases to rates of the FTC
- abatement changes that redistribute money from comparatively higher earners (for example, families earning over 100k).
- "smoother" ongoing indexation arrangements (could be either prices or wages).

The scheduled CPI adjustment provides an opportunity to change abatement settings

24 The scheduled CPI adjustment in April 2022 provides an opportunity to change abatement settings that lessen the extent to which families see payments reduce. On its own, the scheduled adjustment is estimated to increase rates of the FTC and Best Start by 5.9%. For the FTC, this translates to an increase in the first child rate of $6.71 and the subsequent child rate of $5.42, and for Best Start an increase of $3.56 per child per week.[i]

25 The total cost of the April adjustment across all payments is estimated at $53m for the last three months of 2021/22 and $210m for the first full year of 2022/23, with $175m of this for the FTC (with some flow on impacts for the IWTC), and $18m for Best Start. This funding has already been accounted for in forecasts, which means that all costs in this paper are in addition to that.

Officials have undertaken further exploratory modelling of different FTC changes

26 Officials have undertaken further exploratory modelling of different FTC changes, which have combined increases of various sizes to FTC rates (between $5 and $15 per child on top of the planned adjustment), and various increases to abatement settings to reduce the cost. We have explored both:

- 'two tier' options that apply a second abatement threshold at different points (between $60,000 and $85,000) and then introduce higher rates of abatement above that threshold (ranging between 25% and 39%)
- 'single tier' options that introduce a higher rate of abatement above the current threshold which aim to achieve broadly similar objectives. One option also includes a small increase to the abatement threshold, to target more income to, and improve incentives for, low-income families, particularly the 'working poor'.

27 We explicitly ruled out any options that reduced the incomes of households in poverty on the after-housing-cost measure and/or that shifted households below the AHC poverty threshold. We have generally attempted to target any financial disadvantage at higher income families (eg families earning over $100k).

28 We have narrowed this list of options down to a smaller range of potential options for Ministers to consider, set out in the following tables. These are grouped from lower cost, smaller increases in the FTC ($5, $7.50) – which still have a small but meaningful impact on child poverty – through to higher cost options that have a more substantial impact ($10, $15). Within each group, we have also presented choices for the specific design of the abatement settings, grouped into three broad approaches:

- a more modest two-tier abatement structure with a 2nd threshold set at 60/65k and an abatement rate at 29%/31%
- a sharper two-tier abatement rate with a 2nd threshold at $75k and an abatement rate at 33%/35%
- a one-tier abatement structure that increases the abatement rate, potentially accompanied by a small increase to the abatement threshold.

Table three: Two tier abatement options

Option	FTC increase		Child poverty		Abatement approach			Cost	Gains and Losses for Households			
	FTC increase above CPI	FTC increase with CPI included (eldest & subs. child)	BHC50	AHC50		Second abatement threshold	Second abatement rate	($)	Winners	Average gains	Losers	Average losses
Lowest cost ($60-80m)	$5	$11.71 and $10.42	5,000	7,000-8,000	A	$60,000	29%	$68m	313,000	$17	25,000	$4
						$65,000	31%	$56m	303,000	$18	35,000	$9
					B	$75,000	33%	$81m	315,000	$18	23,000	$11
						$75,000	35%	$67m	309,000	$19	29,000	$15
Lower cost ($130-160m)	$7.50	$14.21 and $12.92	8,000	11,000 - 13,000	A	$60,000	29%	$145m	328,000	$21	10,000	$2
						$65,000	31%	$132m	314,000	$21	24,000	$6
					B	$75,000	33%	$156m	323,000	$22	15,000	$10
						$75,000	35%	$141m	314,000	$22	24,000	$12
Higher cost ($210-220m)	$10	$16.71 and $15.42	11,000-12,000	15,000-16,000	A	$60,000	29%	$222m	337,000	$24	*N/A*	
						$65,000	31%	$207m	325,000	$25	13,000	$5
					B	$75,000	33%	$232m	329,000	$26	11,000	$8
						$75,000	35%	$216m	322,000	$26	16,000	$13
High cost ($360-390m)	$15	$21.71 and $20.42	17,000	22,000	A	$60,000	29%	$376m	*Impacts available on request*			
						$65,000	31%	$360m				
					B	$75,000	33%	$386m				
						$75,000	35%	$368m				

Table four: Single tier abatement options

Option	FTC increase		Child poverty		Abatement approach			Cost	Gains and Losses			
	FTC increase above CPI	FTC increase with CPI included (eldest & subs. child)	BHC50	AHC50		First abatement threshold	First abatement rate	($)	Winners	Average gains	Losers	Average losses
Lowest cost ($65-90m)	$5	$11.71 and $10.42	5,000	7,000-8,000	C	$42,700	27%	$68m	330,000	$16	8,000	$1
						$45,200	29%	$86m	315,000	$18	22,000	$4
Lower cost ($140-165m)	$7.50	$14.21 and $12.92	7,000-8,000	11,000-13,000	C	$42,700	27%	$145m	337,000	$20	*N/A*	
						$45,200	29%	$163m	330,000	$22	8,000	$2
Higher cost ($220-240m)	$10	$16.71 and $15.42	11,000-13,000	15,000-16,000	C	$42,700	27%	$223m	339,000	$24	*N/A*	
						$45,200	29%	$240m	338,000	$25		
High cost ($380-395m)	$15	$21.71 and $20.42	16,000-17,000	22,000-23000	C	$42,700	27%	$380m	*Impacts available on request*			
						$45,200	29%	$394m				

The gains and losses are when compared with a pre-indexation status quo ie they show what will happen to a family's income when the changes come into effect. Comparison to a 'post indexation' scenario can be provided if required.
Child poverty reduction estimates are in addition to any currently expected through the CPI adjustment. These are estimates only, and are subject to considerable uncertainty due to sampling error, with 95% margins of error of several thousand depending on the option. These margins of error are not shown in the table above - where the child poverty impacts are expressed as a range here, it is instead because there are small differences between the midpoints for the various options grouped together. If Ministers decide to proceed with a specific option, officials will provide updated figures.

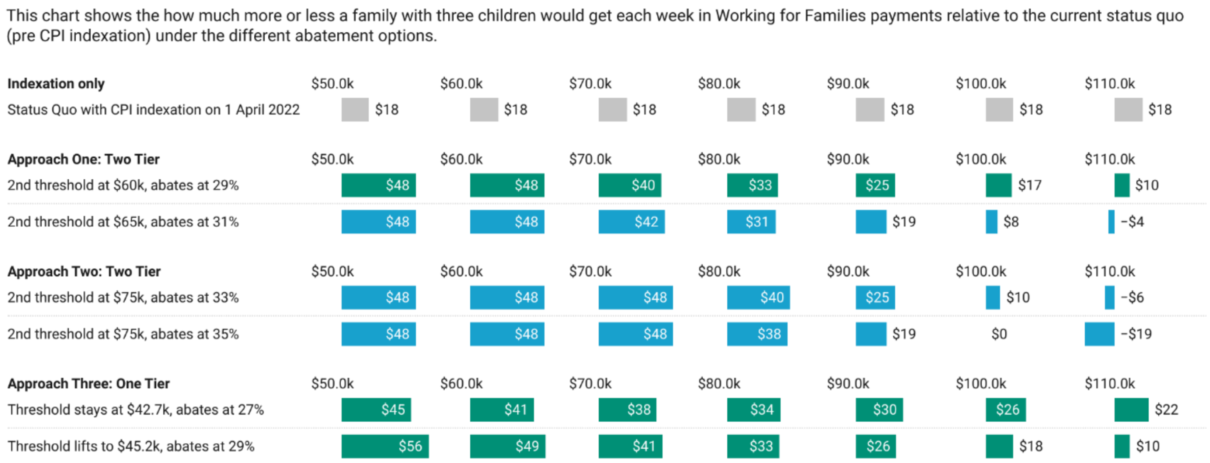
Assessing the impacts of the options

Increasing abatement reduces cost by limiting gains for relatively "higher" income families, which has drawbacks

29 Abatement settings can limit the extent to which Government expenditure goes to families with higher incomes, and targets funding to those who are more likely to need it. The abatement changes in this paper result in some meaningful savings: across the options, they generally reduce the cost of increases to the FTC by around $100m, with little or no change to child poverty impacts.

30 Appendix two shows the families who gain or lose under the various options across the income distribution, and the chart below shows how an increase of $10 above CPI with different settings would impact on the FTC entitlement for a family with three children. As this shows, some families will be disadvantaged by the changes. Some receive less than they would have under the CPI adjustment, and under certain options some families will see their WFF entitlement go down in nominal terms.

Chart one: FTC increase of $10 above CPI: impact of different abatement options for a family with three children



31 While these are generally 'higher income' families earning over 100k, the vast majority (83%) are two-earning parents, and 77% are receiving WFF at these levels due to having three or more children. Families earning over 100k make up 4% (or 12,700) of WFF families, and 6% (around 39,900) of WFF children.[1] As a reference point, previous analysis indicated the median family taxable income for a couple with children was $100,700. Increasing abatement as proposed would impact on the incomes of families who may have higher incomes *relative to other WFF recipients*, but many of these families are in fact also below the median income for families overall

Chart Two: Receipt of Working for Families payments by family income

32 Consistent with this, distributional analysis from TAWA shows that, once households are adjusted for family size/composition, nearly all losing households are below the median, with most in the fourth decile of equivalised household income (see chart at right in Appendix Two).

[1] Based on 2020 tax year administrative data. These figures exclude IR's BSTC-only customers because of universal eligibility which skew the data.

33 To give a broader sense of scale of the prevalence of Working for Families, payments go to around 350,000 families with children, out of 633,000 families with children in New Zealand each year. Half of FTC or IWTC recipients (around 155,800 families) have over $40,000 of taxable income, which is around the point at which the FTC and IWTC begin to abate (at $42,700). There are around 687,000 children in families receiving WFF.

Increasing abatement increases effective marginal tax rates for affected families

34 Another key consideration is the impact on effective marginal tax rates (EMTRs), which currently differ for families in different situations. On current settings, families lose 25c in the dollar through the withdrawal of the FTC and IWTC, on top of what they lose through personal tax (this depends on the family, but likely 30-33c). In combination, this means most families receiving WFF have EMTRs of at least 55-58%, which means they lose at least 55-58c of each additional dollar earned.

35 For some families, EMTRs are higher still, if they are in receipt of the Accommodation Supplement (25c in the dollar), are receiving Best Start and earn over $79,000 (21c in the dollar), have a student loan (12c), and/or receive Childcare Assistance (tiered income thresholds). The options included in this paper would increase EMTRs further, particularly the two-tier options aimed at higher income levels that increase the abatement rate by 10 percentage points. In some cases, EMTRs could exceed 100%, making increased work hours particularly unfavourable.

36 In general, the single-tier options and the options that introduce a second threshold lower down the income distribution have a more modest impact on EMTRs and spread those over a much broader range of middle-higher income families. The two-tier options that place the threshold higher up (eg $75,000) concentrate a more significant increase in EMTRs for a smaller group of higher income families.

37 One group of families who would be particularly impacted are those with a second earner. As a second earner works more, the family is more likely to see their various support payments abated, and this group is typically more responsive to EMTRs when deciding whether to work, or to work more/less than they already do.

An additional abatement change that could be considered

You could align Best Start settings with other WFF abatement settings

38 If you do wish to significantly increase the rate of abatement for WFF payments, you may wish to consider making changes to abatement settings for Best Start. For the second and third years of a child's life, Best Start payments are currently abated at 21% for family income over $79,000 a year. This abatement for Best Start occurs alongside the abatement of WFF tax credits (IWTC and FTC), which means both sets of payments withdraw simultaneously for some families.

39 This creates a much higher effective marginal tax rate for Best Start recipients, who in total across Best Start, FTC/IWTC, and personal tax would likely lose around 76-80c for each additional dollar earned under current settings. This is before any student loan, Accommodation Supplement, or childcare assistance is factored in, which means EMTRs could approach or exceed 100% for some groups, the point at which any increase in earnings would be fully cancelled out or even decrease with the withdrawal of payments. A significant abatement increase could mean EMTRs become very high or even negative for some groups of Best Start recipients earning over $79,000.

40 You could consider using the review to align Best Start's abatement with that of FTC/IWTC, and shift to a system where Best Start abates sequentially as part of a single WFF system. This would involve winners and losers, as well as additional fiscal costs. Further work is required to understand the distributional impact and costs of the change. As with the second threshold, Inland Revenue would need a decision on this kind of structural change now if it was to be implemented in April next year. For

this reason, officials recommend that if you are interested in this option, further analysis be done as part of phase two of the review.

Permanent changes to indexation that could be included

Annual CPI adjustment would mean smoother changes over time, but carries additional cost

41 Under current settings, rates of FTC and Best Start are adjusted once the CPI has a cumulative increase of 5%. The original intent of the 5% policy was to make rates easy to communicate and to reduce the administrative burden of increasing rates every year.

42 Officials do not believe a shift to annual indexation would have a significant impact on administration. Annual CPI indexation would not substantially change FTC rates over the long term, but would be smoother and mean slightly higher rates in the years between scheduled adjustments. If you wish to introduce annual CPI indexation, officials recommend implementing this from April 2023 onwards.

43 Annually indexing rates to prices would carry some additional cost, which falls unevenly across the forecast period – primarily because rates would be slightly higher than they are under current settings in the years between adjustments. There is also some cost associated with a 'compounding' effect under annual adjustment, whereby the previous year's CPI adjustment would also be adjusted by the following year's CPI adjustment. Table 6 below shows the cost of annual CPI indexation.

44 If you wish to switch to annual adjustments, we recommend that you also remove the current provision that means that tobacco is excluded from the CPI's basket of goods used to adjust WFF payment rates. The original policy was designed to prevent increases to tobacco excise tax flowing through to higher incomes, thereby reducing impact of the policy. These excise increases have now ceased, which provides an additional justification for ending the policy and using the standard CPI index.

45 You could consider introducing CPI indexation for the IWTC which, all things being equal, would assist in maintaining work incentives over time. This increases fiscal costs further, and you may prefer to leave the level of IWTC as a deliberate policy decision that takes into account other factors such as benefit/wage relativities. This could be considered within the context of other changes to in-work payments as part of phase two of the review.

Annual wage indexation would also be smoother, with a greater impact & higher fiscal cost

46 Indexing WFF to wages would support your child poverty objectives and also respond to recommendations from key stakeholders. The rationale for wage indexation applies differently to different payments, depending on your objectives, because of the different roles and purposes these payments have:

- If your objective is to ensure that the incomes of low-income families keep pace with other New Zealanders, then the rationale for wage indexing the rates of FTC and Best Start is strongest, as these are payments that are primarily designed to support income adequacy.
- If you also wish to maintain financial incentives to work, then there is a case for also indexing IWTC rates, as this operates as a general income supplement for working families and a payment that is used to address benefit/wage relativities. Wage indexation of all WFF rates would broadly maintain incentives to work as the relative gap between benefit levels and in-work incomes would remain unchanged.

47 Wage indexing WFF income abatement thresholds would ensure the value of payments are not eroded as incomes grow over time, and the incomes of increasing numbers of families shift over the threshold. However, there is a wider set of policy considerations with adjusting thresholds, including alignment with personal tax thresholds, which are not automatically adjusted. Indexing the thresholds also significantly increases the long-term fiscal cost of adjusting payments to wages.

48 Table 4 shows the impact of different indexation arrangements on the first child rate over time. As can be seen, the impact is initially small, but grows. By 2027/28, the first child rate is around $4-5 higher than with CPI adjustment.

Table 5: Impact of different indexation methods on first child rate of Family Tax Credit

		Apr-21	Apr-22	Apr-23	Apr-24	Apr-25
FTC first child rate	Status quo	$113.04	$119.75	$119.75	$119.75	$126.63
	Annual CPI	$113.04	$119.75	$121.81	$124.12	$126.67
	Annual Wages	$113.04	$119.75	$122.54	$125.04	$128.02

49 Table 5 shows the costs of different indexation options over the forecast period. The cost of the current indexation method is already included in forecasts, whereas for the other methods the costs shown are in addition to the status quo and would require funding through Budget 2022.

Table 6: Cost of different indexation methods over the forecast period

	21/22	22/23	23/24	24/25	25/26
Status quo					
Cumulative CPI 5%	*$53m*	*$210m*	*$210m*	*$265m*	*$432m*
Additional cost of annual CPI					
FTC, BS		$17m	$85m	$106m	$23m
FTC, BS, IWTC		$19m	$99m	$132m	$62m
Additional cost of annual wage					
FTC and BS		$23m	$110m	$139m	$69m
FTC, BS, IWTC		$26m	$128m	$171m	$116
FTC/BS/IWTC and thresholds		$36m	$177m	$259m	$238m

50 Table 6 estimates the costs of different indexation options over a longer period. As can be seen, the impact and the fiscal cost of wage indexation is initially small, but 'snowballs' over time and becomes increasingly substantial.

51 The costs use current rates and thresholds and are likely to be higher if indexation is progressed with any of the options in this report. The costings for the indexation of rates also do not factor in any increase to the WFF threshold over the entire period, which suppresses the cost. In practice, Governments may well adjust the threshold to reflect increasing incomes and the long term costs may be closer to the costing that includes threshold indexation.

Table 7: Cost of different indexation methods over the next decade

	22/23	23/24	24/25	25/26	26/27	28/29	30/31	32/33
Additional cost of annual CPI								
FTC, BS	$17m	$85m	$106m	$23m	$106m	$21m	$119m	$85m
FTC, BS, IWTC	$19m	$99m	$132m	$62m	$159m	$99m	$223m	$214m
Additional cost of annual wage								
FTC and BS	$23m	$110m	$139m	$70m	$166m	$87m	$175m	$128m
FTC, BS, IWTC	$26m	$128m	$171m	$116m	$228m	$177m	$290m	$268m
FTC/BS/IWTC and thresholds	$36m	$177m	$259m	$238m	$391m	$411m	$583m	$606m

52 Because these costs become increasingly higher over time, this may limit the available fiscal headroom for other, more reformative options as part of phase two of the WFF review.

Next steps

53 If you still wish to progress a package alongside the CPI adjustment, then the process from here is dependent on the options and timing of implementation. There are a range of choices:

- If you wish to introduce a second threshold for implementation from 1 April 2022, we will prepare a Cabinet paper for the end of September that seeks an in-principle decision to a package of changes with a 'two tier' abatement structure, as well as to introduce urgent legislation in early December. Specific settings for the rate increase and the second abatement threshold/rate could be agreed now and included in the same paper, or confirmed via a subsequent Cabinet paper in November. When the specific parameters are confirmed, Ministers would seek Cabinet's agreement to a pre-commitment on Budget 2022.
- If you wish to proceed with a 'single tier' option for April 2022, a Cabinet paper is not required now, and there is some more time to confirm policy details over the coming weeks. We will prepare follow up advice based on any further feedback or parameters you specify, with the specific changes confirmed via a Cabinet paper in November. The paper would also seek agreement to a pre-commitment on Budget 2022 and to introduce and pass legislation in December.
- A third option would be to delay the CPI indexation change until after Budget day (eg 1 July 2021) and progress changes as part of the Budget process. This would pose several practical challenges. Legislation would have to be passed in November to postpone the change[2], which may be challenging to communicate in advance of budget announcements. It would also create additional operational challenges for Inland Revenue. For instance, an increase to the FTC rate part way through the year may impact on the accuracy in calculating families' entitlements, and may possibly lead to some confusion for families around how their entitlement are calculated, resulting in increased customer contacts around the time of the change. Due to these trade-offs, we do not recommend delaying the CPI increases.

54 Finally, you could explore changes that are not tied to the CPI adjustment – either as part of Budget 2022 or for Budget 2023. This would allow more time to consider the options, but would miss the opportunity to use the CPI adjustment to minimise the impact of financial disadvantage associated with the changes, and would have less alignment with the target periods and reporting timeframes for the child poverty targets.

[2] Under current legislation, FTC and BSTC payment rates must be increased from 1 April 2022 to reflect movements in the CPI since 1 July 2018. The current legislation requires this increase to be made by Order in Council no later than 1 December 2021, with the new rates needing to apply from 1 April 2022. If Ministers wished to postpone the CPI increase of payment rates to a date later than 1 April 2022, this would need to be provided for by way of an amendment to primary legislation prior to 1 December 2021.

Appendix one: work incentives and distributional impacts of selected options			**$11.71 increase to FTC first child rate** $5 per child above CPI	**$14.21 increase to FTC first child rate** $7.50 per child above CPI	**$16.71 increase to FTC first child rate** $10 per child above CPI
	Abatement change	**Impact on work incentives**	**Fiscal cost and distributional impacts of abatement change combined with FTC increase.**		
Two Tier – modest abatement Decision needed by September 2021	2nd threshold at **$60k**, abates at **29%**	**Increases EMTRs by 4%**, will not impact families earning below $60k (approx. 58hrs on minimum wage).	**$68m AHC50: 7k BHC50: 5k** 25k households worse off by $4pw compared with pre-indexation. Average gain is $17pw.	**$145m AHC50: 12k BHC50: 8k** 10k households worse off by $2pw compared with pre-indexation. Average gain is $21pw.	**$222m AHC50: 16k BHC50: 12k** No households worse off compared with pre-indexation. Average gain is $24pw.
	2nd threshold at **$65k**, abates at **31%**	**Increases EMTRs by 6%,** will not impact families earning below $65k (approx. 63hrs on minimum wage).	**$56m AHC50: 7k BHC50: 5k** 35k households worse off by $9pw compared with pre-indexation. Average gain is $18pw.	**$132m AHC50: 11k BHC50: 8k** 24k households worse off by $6pw compared with pre-indexation. Average gain is $21pw.	**$207m AHC50: 15k BHC50: 12k** 13k households worse off by $5pw compared with pre-indexation. Average gain is $25pw.
Two Tier – sharp abatement Decision needed by September 2021	2nd threshold at **$75k**, abates at **33%**	**Increases EMTRs by 8%**, will not impact families earning below $75k (approx. 72hrs on minimum wage).	**$81m AHC50: 8k BHC50: 5k** 23k households worse off by $11pw compared with pre-indexation. Average gain is $18pw.	**$156m AHC50: 12k BHC50: 8k** 15k households worse off by $10pw compared with pre-indexation. Average gain is $22pw.	**$232m AHC50: 16k BHC50: 11k** 11k households worse off by $8pw compared with pre-indexation. Average gain is $26pw.
	2nd threshold at **$75k**, abates at **35%**	**Increases EMTRs by 10%**, will not impact families earning below $75k (approx. 72hrs on minimum wage).	**$67m AHC50: 8k BHC50: 5k** 29k households worse off by $15pw compared with pre-indexation. Average gain is $19pw.	**$141m AHC50: 12k BHC50: 8k** 24k households worse off by $12pw compared with pre-indexation. Average gain is $22pw.	**$216m AHC50: 15k BHC50: 11k** 16k households worse off by $13pw compared with pre-indexation. Average gain is $26pw.
One Tier Decision needed by November 2021	Threshold stays at **$42.7k**, abates at **27%**	**Increases EMTRs by 2%**, will not impact families earning below $42.7k (approx. 41hrs on minimum wage).	**$68m AHC50: 8k BHC50: 5k** 8k households worse off by $1pw compared with pre-indexation. Average gain is $16pw.	**$145m AHC50: 11k BHC50: 7k** No households worse off compared with pre-indexation. Average gain is $20pw.	**$223m AHC50: 15k BHC50: 11k** No households worse off compared with pre-indexation. Average gain is $24pw.
	Threshold lifts to **$45.2k**, abates at **29%**	**Increases EMTRs by 4%,** for all families earning above $45.2k (approx. 43hrs on mw). **Reduces EMTRs by 25%,** for families earning between $42.7 and $45.2k. *Families earning below $60k will gain by up to $12pw from lifting the first threshold.*	**$86m AHC50: 7k BHC50: 5k** 22k households worse off by $4pw compared with pre-indexation. Average gain is $18pw.	**$163m AHC50: 12k BHC50: 8k** 8k households worse off by $2pw compared with pre-indexation. Average gain is $22pw.	**$240m AHC50: 16k BHC50: 13k** No households worse off compared with pre-indexation. Average gain is $25pw.

These TAWA modelling results use data from the IDI, which was provided by Stats NZ under conditions designed to give effect to the security and confidentiality provisions of the Statistics Act 1975. The results are the work of the author, not Stats NZ or individual data suppliers.

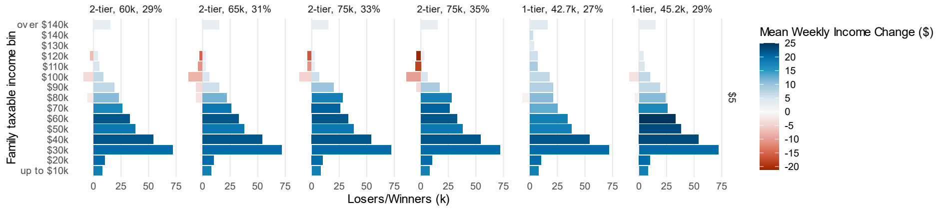
The 95% confidence margins of error due to sampling for these child poverty reduction estimates are in the range 5,000 - 7,000 for AHC50, and 3,000 - 6,000 for BHC50.".

KEY	Number of losers	Average loss
	less than 17k	$1-$5
	less than 26k	$6-$10
	over 26k	$11-$15

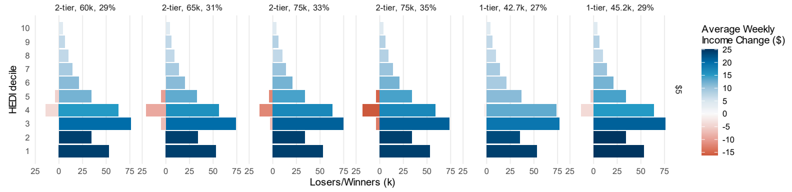
Appendix two: gains and losses by income deciles and bands – for a $5 increase

The chart at left shows the winners and losers for different abatement approaches by family income – as can be seen, the losses largely occur for families earning over 100k. The chart at right shows how the gains and losses when adjusted for family size and composition (equivalised). Once family structure is taken into account, the losses are below the median.

Different abatement approaches: gains / losses by taxable family income



Different abatement approaches: gains / losses by equivalised household income deciles



	APPROACH A: TWO TIER (MORE MODEST IMPACT)				APPROACH B: TWO TIER (SHARPER IMPACT)				APPROACH C: ONE TIER			
	Second threshold: 60k, 29% abatement				Second threshold: 75k, 33% abatement				First threshold: 42k, 27% abatement			
	Winners		Losers		Winners		Losers		Winners		Losers	
	Families	Average gain	Families	Average loss	Families	Average gain	Families	Average loss	Families	Average gain	Families	Average loss
< $10k	8,000	$18			8,000	$18			8,000	$18		
$10-20k	10,000	$20			10,000	$20			10,000	$20		
$20-30k	72,000	$20			72,000	$20			72,000	$20		
$30-40k	54,000	$22			54,000	$22			54,000	$22		
$40-50k	38,000	$19			38,000	$19			38,000	$18		
$50-60k	33,000	$22			33,000	$22			34,000	$18		
$60-70k	26,000	$17			26,000	$21			25,000	$13		
$70-80k	23,000	$11	5,000	-$2	28,000	$18			21,000	$11	7,000	-$1
$80-90k	19,000	$7			20,000	$10			21,000	$8		
$90-100k	9,000	$7	9,000	-$4	7,000	$6	11,000	-$5	18,000	$7		
$100-110k	5,000	$5			3,000	$3	4,000	-$11	7,000	$9		
$110-120k	4,000	$4	3,000	-$7	3,000	$3	4,000	-$16	7,000	$6		
$120-130k									4,000	$4		
$130-140k									3,000	$6		
>=$140k	15,000	$3			15,000	$3			16,000	$4		

The table below shows gains and losses above and below $100k of taxable family income. The tables total differently as numbers below 3,000 are suppressed for privacy reasons

	Winners		Losers		Winners		Losers		Winners		Losers	
< $100k	293,000	$18	17,000	-$3	297,000	$19	14,000	-$5	302,000	$17	8,000	-$1
>=$100k	29,000	$3	8,000	-$7	27,000	$3	10,000	-$19	36,000	$5	S*	S*
All	321,000	$17	25,000	-$4	324,000	$18	24,000	-$11	338,000	$16	9,000	-$1

Appendix three: impacts of Child Support Pass On, Best Start options

Best Start options cost between $100-135m per year

55 Two options were included in the previous paper, both of which could be implemented by 1 July 2022 if decisions were made early in the process for Budget 2022 (e.g. March), and subject to what other changes Ministers also require from Inland Revenue at that time.

- Option A: Extending the targeted component of Best Start for eligible families by $40 per week for children age three to five years
- Option B: Increasing the Best Start rate from $60 per week to $80 per week

56 Note that the gains in the table below are compared to a post-indexation status quo.

Scenario	Annual Fiscal cost*	Reduction in number of Children Fixed AHC50†	Reduction in number of Adults Fixed AHC50†	Reduction in number of Children BHC50†	Reduction in number of Adults BHC50†	Number of gaining households‡	Average gain per week for gaining households§
OptionA	$135m	7,000	3,000	5,000	3,000	62,000	$41
OptionB	$96m	3,000	2,000	2,000	2,000	110,000	$17

* MoE for annual fiscal costs are up to $13m

† MoE for poverty measures are up to 4,000

‡ MoE for numbers of winners and losers analysis measures are up to 6,000

§ MoE for costs of winners and losers analysis measures are up to $2

Previous analysis estimated Child Support Pass On had a cost of $87.4m per year

57 Previous analysis in 2019 estimated that

- CSPO would increase the incomes of 42,500 sole parent beneficiaries by an average of $44 per week, with a median gain of $19 per week.
- It also had the potential to reduce the number of children in poverty by around 5,000 – 10,000, depending on the poverty measure used.

58 MSD has started implementation work to progress CSPO ahead of Budget 2022 decisions. This would mean CSPO could be implemented around July 2023, with the first child support payment passed on around September 2023.

59 If CSPO is implemented around September 2023 it will have a partial impact in the reporting on the second round of three year child poverty targets, with the full impact showing in the reporting on the first year of the subsequent period (covering 24/25, 25/26, 26/27). The estimated contribution to the second round of three-year targets can therefore be seen as roughly half the estimated impact.

60 Since this original analysis, significant changes have been made to income support settings, such as the increases to the main benefit abatement threshold in April 2021, which means this analysis needs to be revisited as it is likely that sole parent beneficiaries would receive a higher increase to their incomes and overall cost would increase due to these changes. In addition, the child poverty impact analysis needs to be updated as previous analysis was based on MSD's administrative data, which was sufficient for providing a broad 'order of magnitude' estimate but not suitable for precise modelling.

Speaking notes for Income Support Ministers meeting on the Working for Families Review
Wednesday 22 September 2021

Welfare Overhaul: Working for Families Review

You are attending an Income Support Ministers'[1] meeting on Wednesday 22 September to discuss the report entitled *Working for Families Review: update and options for Budget 2022*.

Key decisions to be made

The report seeks decisions from Ministers in relation to:

- Officials' proposed sequencing of the WFF review work programme into two parts, Phase One and Phase Two.
- Phase One options for an April 2022 package to redistribute support to low-income families, namely:
    - Increasing FTC and introducing a new two-tier abatement to reduce fiscal cost;
    - Aligning the BSTC abatement threshold with the WFF abatement threshold; and
    - Introducing permanent annual indexation of WFF rates (either using Average Wage Growth or CPI).

[1] The Minister for Child Poverty Reduction, Minister of Finance, Minister for Children, Minister for Social Development and Employment, and Minister of Revenue.

Further comment

Increasing FTC and introducing a two-tier abatement

Inland Revenue officials consider that all of the FTC options that include two-tier abatement are unsatisfactory.

Higher abatement rates would negatively impact work incentives and increase EMTRs. A two-tier abatement scheme would put greater expectations on Phase Two to improve work incentives or reduce EMTRs (which is one of the objectives of the Review).

However, if there are subsequent fiscal limitations or other unforeseen constraints, the scope for addressing these impacts in Phase Two may be limited.

BSTC abatement threshold alignment and permanent indexation options

Inland Revenue officials **do not recommend** changing the BSTC abatement threshold or introducing permanent annual indexation of rates at this stage.

Instead, we consider they would be better dealt with as part of Phase Two.

Compressed timeframes meant there was limited opportunity for officials to prepare thorough analysis on these options in this report. The trade-offs have not been presented to Ministers.

Also, there is a risk that if these options are progressed, options in Phase Two could be constrained either fiscally, or could be expected to rectify unintended outcomes (for example, greater negative impacts on work incentives or reduced income support).

Delaying the upcoming CPI indexation of FTC and BSTC

The current legislation requires FTC and BSTC payment rates to increase by the amount of CPI increases no later than 1 December 2021, with the new rates to apply from 1 April 2022.

The option of delaying these upcoming increases until 1 July 2022 was briefly raised in the report (para 53, bullet point 3).

Inland Revenue officials **do not recommend** such a delay due to the trade-offs involved:

- Managing the communications of delaying the 1 April 2022 CPI increases prior to Budget 2022 decisions and announcements would be challenging.
- an increase to the FTC rate part way through the year may impact on the accuracy in calculating families' entitlements, and may lead to confusion for families around how entitlements are calculated. This could result

in increased customer contacts during a peak period for Inland Revenue.

- the cost of the 1 April 2022 CPI increases are already included in forecasting. Postponing the CPI increases until 1 July 2022 may mean a higher fiscal cost if the CPI increases further before then.

Increasing the FTC rates from 1 July 2022 would also require a corresponding adjustment to the MFTC threshold, which would have increased three months prior on 1 April (to reflect benefit settings).

Postponing the 1 April 2022 CPI increases would require amendments to primary legislation in November 2021.

Budget Sensitive

Office of the Minister for Child Poverty Reduction

Office of the Minister for Social Development and Employment

Cabinet

Initial Working for Families changes to support low-income families

Proposal

1 This paper seeks agreement to:

1.1 increase the Family Tax Credit (FTC) rate and increase the FTC and In-Work Tax Credit (IWTC) abatement rates to support low-income families, on top of the planned Consumer Price Index (CPI) adjustment of Working for Families (WFF) payments in April 2022; and

1.2 pass on the FTC increase to the rates of Orphan's Benefit (OB), Unsupported Child's Benefit (UCB), and Foster Care Allowance (FCA) and related allowances.

2 The paper also seeks agreement to some related minor technical policy changes to be included in the legislation.

Relation to government priorities

3 Reducing child poverty is critical to the Government's priority of improving child wellbeing and laying the foundations for the future. Child poverty is a long-term enduring issue that is affecting New Zealand children now and continues to impact them into the future. We are committed to continuing our bold ambitions to more than halve child poverty within ten years, and to contribute to our goal of making New Zealand the best place in the world for children and young people.

4 The changes proposed in this paper contribute to the welfare overhaul work programme, which lays the foundations to achieve the Government's vision of a welfare system that ensures people have an adequate income and standard of living, are treated with and can live in dignity, and are able to participate meaningfully in their communities. The proposal also plays an important role in supporting our economic recovery – providing further stimulus to the economy at the same time as reducing inequality and enhancing support for Māori and Pacific families who are disproportionately represented in our lowest income families.

5 Improving child wellbeing is an area of cooperation under the Cooperation Agreement between The NZ Labour Party and The Green Party of Aotearoa NZ.

Executive Summary

6 The WFF package was implemented between 2004 and 2007 to support income adequacy and reduce child poverty; and to improve financial incentives for low-income earners to participate in the labour market.

7 In its report in 2019, the Welfare Expert Advisory Group recommended significant changes to WFF as part of a wider suite of changes to income support settings. The Government agreed to review WFF as part of the Welfare Overhaul work programme.

8 We are committed to making fundamental changes to WFF in the coming years. The review will consider changes to the structure and design of WFF payments, with a focus on support for additional in-work costs, particularly childcare costs, and administrative, operational and client experience improvements.

9 We are now prioritising this review as the next critical step towards our commitment to support income adequacy for both beneficiary and low-income working families, and reduce child poverty.

10 The Government has set both three-year child poverty targets, and ten-year targets to more than halve rates of measured child poverty in New Zealand by 2027/28, and a goal to make New Zealand the best place in the world for children and young people. Additional changes to increase incomes for low-income families are key to progressing towards our current three- year child poverty targets, and any changes need to be implemented through Budget 2022 in order to have a full impact on the three-year targets.

11 Under current settings, the indexation of FTC and Best Start Tax Credit (BSTC) is triggered once the CPI has a cumulative increase of 5% since the last adjustment. The increases have now reached 8.57%, meaning both the FTC and BSTC will be increased from 1 April 2022. This provides an opportunity to make further changes alongside this adjustment.

12 We want to take early action now to respond to the increasing financial pressure and hardship that many families have experienced as a result of the COVID-19 restrictions and make progress towards our next three year child poverty targets.

13 That is why, in addition to the CPI increases, we propose to:

13.1 increase the FTC payment by $5 per child per week from 1 April 2022. This will see extra income going to hundreds of thousands of low to medium income families with children.

13.2 make a small increase to the abatement rate for the FTC and IWTC, from 25% to 27%. The payments abate sequentially from a family taxable income of $42,700. This small increase to the abatement rate will help to concentrate the greater gains to households on the lowest incomes.

14 Introducing these changes together ensures the additional investment from the policy changes and CPI indexation are targeted to the families in greatest need, while also still seeing gains higher up the income spectrum, and ensuring no one is worse off than they were before the changes.

15 In total, these changes mean:

15.1 the eldest child rate for FTC will increase by $14.69 per week; and the subsequent child rate will increase by $12.83 per week

15.2 child poverty is forecast to reduce by 5,000 +/- 4,000 children on the before-housing-costs, moving-line measure (BHC50); and by 6,000 +/- 5,000 children on the after-housing-costs, fixed line poverty measure (AHC50).[1]

16 This proposal, in combination with the planned CPI indexation, will provide many lower income working and beneficiary families with a meaningful boost to their weekly income. In total, 346,000 families will be better off by an average of $20 per week.

17 We intend to progress these changes through urgent primary legislation to ensure Inland Revenue has sufficient time to make the required system change. This also provides an opportunity to include several additional, relatively minor items that would otherwise require an alternative legislative vehicle or Orders in Council to be progressed.

18 We propose passing on the FTC increase to the rates of the OB, UCB, and FCA to provide additional support for caregivers. The $5 rate increase for these payments would also apply from 1 April 2022.

19 In addition, we are seeking agreement to make additional relatively minor changes through this Bill to:

19.1 make a remedial amendment to the CPI measure used to make adjustments to FTC and BSTC

19.2 make two changes for 1 April 2022 through primary legislation rather than by Order in Council - the CPI adjustments to FTC and BSTC, and the previously agreed Minimum Family Tax Credit (MFTC) threshold adjustment.

20 There is a flow-on to the Community Services Card (CSC) from increasing the FTC, which may change the eligibility to the card for a small number of families (yet to be determined). Officials will provide these Ministers with a report shortly, once data is available. We are seeking agreement to delegate authority for the Minister of Finance, Minister of Health and Minister for Social Development and Employment to make decisions on any consequential changes to the CSC income thresholds.

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[1] Access to the data used in this study was provided by Statistics NZ under conditions designed to give effect to the security and confidentiality provisions of the Statistics Act 1975. The results presented in this study are the work of the author, not Statistics NZ or individual data suppliers.

Background

21 In 2018 the Government established the Welfare Expert Advisory Group (WEAG) to advise them on the future of New Zealand's social security system, including the WFF scheme. In its report in 2019, "Whakamana Tāngata: Restoring Dignity to Social Security in New Zealand", the WEAG recommended significant changes to the design and targeting of WFF, as part of a wider suite of changes to income support settings. Cabinet subsequently agreed to a review of WFF as part of the medium-term Welfare Overhaul work programme [CAB-19-MIN-0578].

22 On 12 May 2021, the Cabinet Social Wellbeing Committee (SWC) noted that Income Support Ministers had agreed to bring forward the Review and determined its scope [SWC-21-MIN-0068].

23 Income Support Ministers agreed that:

23.1 The original WFF objectives of supporting income adequacy and reducing child poverty, and improving financial incentives for low-income earners to enter the labour market remain important.

23.2 The review focus on:

23.2.1 low-income working families, while maintaining support for beneficiary families

23.2.2 options that target support to lower-income families rather than more universal support

23.2.3 the principle of making work pay and assisting with the costs for people in work.

Summary of Working for Families payments

Around 57% of all families in New Zealand receive WFF, at a cost of $3 billion for the 2021 financial year. WFF is made up of the following tax credits:

- **Family Tax Credit (281,000 families, $2.1 billion)**: the main payment received by both beneficiary and working families and is not dependent on work status. Currently, families receive $113 per week for the eldest child and $91 per week for each subsequent child. This payment begins to abate at $42,700 of annual income at 25%.
- **In-Work Tax Credit (190,000 families, $602m)**: the main in-work payment for families who do not receive a benefit. It pays $72.50 per week for families with 1 to 3 children, with an extra $15 per week for each subsequent child. After the Family Tax Credit is fully abated, it is abated at 25%.
- **Best Start Tax Credit (75,000 families, $276m):** this payment provides $60 per week to all families with a child under one year old, and for lower income families with a child under 3. In the two subsequent years, this payment begins to abate at $79,000 of income at 21%.
- **Minimum Family Tax Credit (4,000 families, $21m):** this payment tops up incomes of working families who go off benefit to a guaranteed minimum income level, so that these families are not worse off when they leave benefit. The minimum income is currently set at $31,096 after tax.

24 Changes have already been made to improve WFF through the Families Package, as well as more recently two key changes to the IWTC:

24.1 removing the hours test – effective from 1 July 2020, the requirement for working families to meet the hours test was removed, meaning that people can now continue to be eligible for IWTC payments even if they work as little as an hour a week (previously a minimum of 20 hours a week for sole parents and 30 hours for couples was required).

24.2 introducing 'grace periods' – as part of the response to COVID-19, the Government announced 'two-week grace periods' that took effect from 1 April this year. This means families can now continue to receive the IWTC payment for up to two weeks while not working. This ensures people who are transitioning between jobs, for example, or who have short periods without work can still receive the IWTC payment.

More fundamental changes to WFF will be considered next

25 The Review of WFF is considering fundamental changes to the structure and design of WFF payments. The following work streams have been developed:

25.1 *Improvements to the structure and design of in-work tax credits* – focused on improving the settings for in-work assistance and the work-benefit interface, with a key objective of making work pay. It could include options such as replacing the IWTC and the Minimum Family Tax Credit (MFTC), introducing a phase-in tax credit, or improving the existing tax credits.

25.2 *Improvements to assist with the costs of children in the early years, particularly additional in-work and childcare costs* – will include a focus on in-work poverty, particularly for single earner households, and sole parents and second earners. Options could include consideration of a second earner tax credit targeted at very low-income households, Best Start options, a new childcare tax credit and/or merging Childcare Assistance into the tax credit system. The work will progress alongside the Childcare Assistance Review.

25.3 *Administrative and operational improvements* – focused on changes that would improve accuracy of payments, reduce debt to government agencies, and improve client experience, along with consideration of more fundamental operational changes such as how WFF payments are delivered.

26 Income Support Ministers will also consider options for fundamental reform of the Accommodation Supplement with a focus on Budget 2023 or later.

27 As these more fundamental changes are explored, there is a strong case for making immediate adequacy-focused changes now, given the additional pressures for many families arising from the impacts of COVID-19, and the need to continue to make progress on the child poverty targets.

Proposal to increase the Family Tax Credit combined with an increased abatement rate

28 There are several reasons why there is a strong case for taking immediate action as part of the WFF review to improve the adequacy of income support for families on our lowest incomes.

28.1 There is an ongoing need to make progress towards our child poverty targets:

28.1.1 Reducing child poverty was an agreed objective of WFF in 2004 [CAB Min (04) 13/4]. Since then we have passed the Child Poverty Reduction Act 2018 with cross-party support, which provides a framework to ensure progress is being made on multiple fronts to reduce child poverty. As part of this legislation, we set ten-year child poverty targets to more than halve rates of measured child poverty in New Zealand by 2027/28, and have recently set our second round of three-year targets, which cover the 2021/22, 2022/23 and 2023/24 years. These are currently estimated to require reductions of around 2-3 percentage points (ppt) or 25-35,000 children on each measure over the three-year period.

28.1.2 As previously advised [SWC-21-MIN-0095], we have an ambitious and comprehensive plan for achieving our targets. The Families Package, the indexation of main benefits to wages, and successive benefit increases in 2020, 2021, and 2022 have provided significant and immediate improvements to the living standards of low-income families in New Zealand. However we know there is more to do. Additional changes to increase incomes for low-income families are key to progressing towards our current three- year child poverty targets, and any changes need to be implemented through Budget 2022 in order to have a full impact on the three-year targets.

28.2 We also know that COVID-19 and the associated alert level restrictions have created additional pressures for many families. Additional support has been provided, for example, through the rollout of the Wage Subsidy to respond to Alert Levels and through extra funding for social services. However permanent changes to further support families will not only help achieve progress towards reducing inequality, it will also provide further support and stimulus to our economy as we recover from the economic impact of COVID-19.

28.3 The planned CPI adjustment of Working for Families also provides us with a window of opportunity to make changes to the targeting of payments. Under current settings, the indexation of FTC and Best Start Tax Credit (BSTC) is triggered once the CPI has a cumulative increase of 5%. The increases have now reached 8.57%, meaning both the FTC and BSTC will be increased from 1 April 2022. This provides an opportunity to make further changes that target assistance to those on lower incomes which do not result in families being worse off than they were previously.

Ministers explored a range of options to target gains to those on the lowest incomes

29 In considering immediate WFF changes, Ministers explored a range of options, which combined increases to FTC rates with various increases to abatement settings to reduce the cost and target the gains to those on the lowest incomes. We explored both:

29.1 ‘two tier’ options that apply a second abatement threshold at different points (between $60,000 and $85,000) and then introduce higher rates of abatement above that threshold (ranging between 25% and 39%)

29.2 ‘single tier’ options that introduce a higher rate of abatement above the current threshold which aim to achieve broadly similar objectives.

30 In general, the single-tier options were less likely to result in families being financially disadvantaged by the changes. They also had a more modest impact on effective marginal tax rates (described further below) and spread those over a much broader range of middle-higher income families.

The proposed change, combined with the scheduled lift in the FTC and the Best Start rate, will mean a meaningful increase in assistance in April next year

31 We propose to:

31.1 increase the FTC rate by $5 per child per week for all eligible families from 1 April 2022, on top of the scheduled CPI indexation

31.2 apply a small increase to the abatement rate for the FTC and IWTC, from 25% to 27%, which will help to concentrate the greater gains to households on the lowest incomes. The payments currently abate at 25% from a family taxable income of $42,700.

32 Under existing settings, the FTC and BSTC payments will increase by 8.57% in April next year, which means FTC rates are currently scheduled to rise by around $10 for the first child, and $8 for each subsequent child. The proposed increase to FTC will occur on top of this, which means the total proposed combined FTC increase on 1 April next year is:

32.1 $14.69 to the first child rate ($127.72 per week/$6,642 per year)

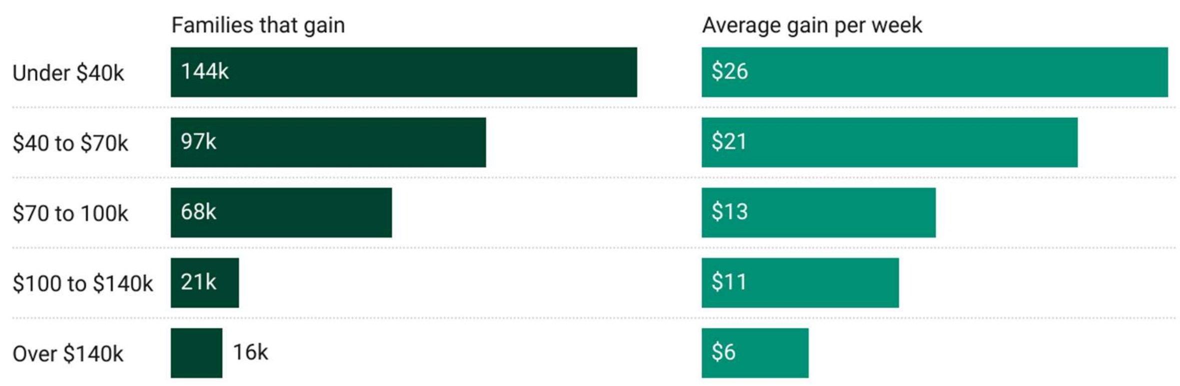
32.2 $12.83 to the subsequent child rate ($104.08 per week/$5,412 per year)

33 The new rates, including the policy change noted above, are shown below:

	TY2021 Pre-CPI	**TY2022 Scheduled rate**	**TY2022 Proposed rate**	**Total increase**
Eldest child rate of FTC	$113.04	122.73	$127.73	+$14.69
Subsequent child rate of FTC	$91.25	$99.08	$104.08	+$12.83
Best Start rate	$60.00	$65.15	$65.15	+$5.15
FTC/IWTC abatement rate	25%	25%	27%	+2ppt
FTC/IWTC abatement threshold	$42,700	$42,700	$42,700	no change

34 In combination, 346,000 families will be better off by an average of $20 per week in total. As shown in the following chart, the gains will be larger for lower income families.

Chart 1: Average gains from policy changes and CPI indexation by family taxable income



Families with taxable income over $140k are likely to be gaining as a result of the indexation of the Best Start Tax Credit which is universal for the first year.

Source: TAWA analysis • Created with Datawrapper

Introducing these changes together ensures additional investment is targeted to the families in greatest need, while still seeing gains higher up the income spectrum.

35 Increasing abatement rates maintains broadly the same child poverty impacts as the FTC increase alone. However, pairing the changes reduces the cost of an FTC increase, which is critical in the current tight fiscal environment, and aligns with our manifesto promise to carefully manage government finances. The policy changes are forecast to reduce child poverty:

35.1 on the before-housing-costs, moving-line measure (BHC50) by 5,000 (± 4,000) children, and

35.2 on the after-housing-costs, fixed line measure (AHC50) by 6,000 (± 5,000) children

36 Approximately two thirds of families currently in receipt of WFF will receive more than they would have done under CPI indexation alone. Most of these families (90%) have a family taxable income below $60,000 per year. Families higher up the income spectrum will receive less than they would have done under CPI indexation alone, however, modelling suggests that no families will be worse off compared to what they currently receive.

Increasing abatement rates increases effective marginal tax rates (EMTRs) for affected families, but the overall impact of this is expected to be small

37 Effective Marginal Tax Rates (EMTRs) are a measure of how an increase in employment earnings translates to an increase in income 'in the hand', after accounting for income tax combined with abatement of targeted payments. Currently, families earning above the $42,700 abatement threshold lose 25c in the dollar through the withdrawal of the FTC and IWTC, on top of personal tax. For some low-income families, the EMTRs are higher, particularly if they are also in receipt of the

Accommodation Supplement, have a student loan, and/or receive Childcare Assistance (tiered income thresholds).

38 An increase in FTC payments and a two-percentage point increase in the abatement rate would mean a small increase in the EMTR for affected families. This could have some small impacts on financial incentives to work for sole parent families, or families with a second earner with incomes above $42,700 p.a.. However, the change would be unlikely to have a measurable impact on work incentives or labour supply decisions in the aggregate. Decisions to work are also influenced by many factors other than financial incentives (e.g. availability/suitability of employment and/or childcare).

Passing on the FTC increase to the rates of the Orphan's Benefit (OB), Unsupported Child's Benefit (UCB), and Foster Care Allowance (FCA)

39 We propose passing on the $5 per week increase to the FTC to the rates of the OB, UCB, and FCA. The $5 rate increase for these payments would also apply from 1 April 2022. There will be flow on impacts to the Birthday Allowance and Holiday Allowance, which are paid at half of the weekly base rate payments.

40 Caregivers who receive the OB, UCB, and FCA do not qualify for FTC for the same child. However, increases to FTC rates have resulted in commensurate increases to the base rates of the OB, UCB, and FCA in 2005, 2007, and 2018. This is because the FTC makes a partial contribution towards the costs of raising children. These caregivers are largely whānau and family members of the child, who have a critical role in preventing the need for tamariki enter the State care system.

41 Passing on the FTC increase to caregiver payments will benefit around 15,000 caregivers currently providing the day-to-day care for around 24,000 tamariki who are unable to be cared for by their parents. Many of these caregivers are under financial pressure[2] and increasing financial support for caregivers helps them to support the tamariki in their care.[3]

Potential flow-on to the Community Services Card from increasing the FTC

42 Officials have identified a flow-on to the Community Services Card (CSC) from increasing the FTC, which may change the eligibility to the CSC for a small number of families because the FTC is considered income for assessing eligibility for the CSC.

43 This flow on occurred in 2018 as a result of the Families Package. Ministers agreed to increase the CSC income thresholds to ensure no families lost eligibility to the CSC as a result [CAB-17-MIN-0516 refers]. The changes were estimated to cause 15,000 families to lose eligibility to the CSC, and the corresponding increase cost $0.13

[2] Many are living in low-income households, with around half of caregivers outside of the State care system earning less than $43,000 per year.

[3] Evidence also indicates that increasing the financial resources of low-income households has benefits for the children in those households, including reduced care and protection involvement and entry to State care. See Oranga Tamariki (2019) Evidence Centre Research Brief: How do welfare and tax settings affect children's involvement with child protective services?, available at https://www.orangatamariki.govt.nz/research/latest-research/welfare-and-tax-settings/

million over the forecast period. These changes to the FTC through the Families Package were far more significant than the changes proposed through this Cabinet paper.

44 Officials are currently working to estimate how many families could be impacted by this policy change, but expect it to be small. We are seeking agreement to delegate authority for the Minister of Finance, Minister of Health and Minister for Social Development and Employment to make decisions on any consequential changes to the CSC income thresholds. Officials will provide these Ministers with a report shortly, once data is available.

Monitoring outcomes

45 The effects of the proposed changes can be monitored using data IR currently collects as part of administering WFF. This data includes the number of WFF recipients, the makeup of those families, the amount and type of payments made, and end of year assessment data on under and overpayments. This administrative data provides descriptive information about WFF recipients, and the actual fiscal cost to the Government of the chosen settings. Inland Revenue and MSD hold data about the WFF payments they make. For MSD this is limited to FTC and BSTC payments made to main benefit recipients.

46 The agencies who are involved in the WFF review are also currently working on advice about how any changes that are progressed as part of the broader WFF review will be evaluated.

Proposal to use the Bill enabling the FTC changes to also give effect to several other relatively minor WFF changes

47 Progressing the FTC changes outlined in this paper will require urgent primary legislation (the Bill) in order to effect the changes by 1 April 2022. This provides an opportunity to include several additional, relatively minor items that would otherwise require an alternative legislative vehicle or Orders in Council to be progressed.

48 Therefore, in addition to the FTC changes outlined above, we are seeking agreement from you to include in the Bill the two following relatively minor changes.

Remedial amendment to change the CPI measure used to adjust FTC and BSTC

49 The Income Tax Act 2007 currently requires FTC and BSTC rates to be increased in line with cumulative increases to the CPI measure referred to as CPI ‘all groups excluding tobacco and cigarette products’ (CPIX).

50 On 21 April 2016, Cabinet agreed that this CPIX measure would be used to calculate welfare payments until the end of 2020 when annual tobacco excise tax increases ceased, and then to revert back to using CPI (all groups) [CAB-16-MIN-0189 refers].

51 This approach included the indexation approach for WFF payments. In 2017 the Income Tax Act 2007 was amended to change the CPI measure from CPI (all groups) to CPIX, effective from 1 April 2018. However, no provision was made in the Income

Tax Act 2007 to automatically revert back to the CPI (all groups) measure[4]. We recommend that you agree to include in the Bill a remedial amendment to the Income Tax Act 2007 to update the CPI measure used for FTC and BSTC CPI indexation from CPIX to CPI all groups, effective from March 2021, in order to be consistent with the CPI measures used for other similar social support adjustments.

52 FTC and BSTC rates going forward have been forecast in line with the policy decision to use CPI (all groups). For FTC recipients, continuing to use CPIX would equate to an increase of approximately $0.13 per week, per child. While agreeing this technical change does not have a fiscal cost, continuing to use CPIX would have a fiscal cost of approximately $18 million over the forecast period.

53 We also recommend that, for the sake of efficiency, the scheduled CPI adjustment to the FTC and BSTC payments outlined in paragraph 33 be made via the Bill, rather than by Order in Council as would otherwise be required.

Increasing Minimum Family Tax Credit via legislation rather than Order in Council

54 Cabinet previously agreed to:

54.1 increase the 1 April 2022 MFTC[5] threshold to reflect increases to main benefits from the same date;

54.2 change the approach to calculating the 1 April 2022 MFTC threshold so that the Winter Energy Payment component of the formula equates to five months of payments rather than 12 months of payments; and

54.3 give effect to the 1 April 2022 MFTC threshold increase (at the time forecast to be $32,760) via Order in Council by 1 December 2021 [CAB-21-MIN-0116.33 refers].

55 We propose to make the above MFTC threshold increase via the Bill as this is more efficient than making the increase using a separate Order in Council.

56 We note that the MFTC threshold that would apply from 1 April 2022 is now forecast as being $32,864, reflecting additional wage growth increases to 2022 benefit rates.

[4] This is unlike the Social Security Act 2018. The Social Security Act 2018 s453 required the CPI excluding tobacco to be used for the period 2018 to 2021 (inclusive). This provision has now expired and s453 requires to CPI (all groups) to be used.
[5] The MFTC is support providing a guaranteed minimum income for people with children who work at least 20 hours per week and no longer receive a main benefit. It "tops up" income from work, so that families have a higher income than they would receive while receiving a benefit.

Implementation

57 The following proposed changes will be implemented by Inland Revenue as part of its annual system roll-over and will go live from 1 April 2022:

57.1 the FTC increase (reflecting both the CPI indexation increase and the $5 p/w increase);

57.2 the FTC and IWTC abatement rate increase;

57.3 the BSTC CPI indexation increase; and

57.4 the MFTC threshold increase.

58 The effect of the CPI remedial amendment will be reflected in the calculation of the CPI indexation increases for FTC and BSTC included in the Bill.

59 Passing on the FTC increase to the rates of the OB, UCB, and FCA will occur from 1 April 2022 alongside the Annual General Adjustment of benefit rates.

Financial Implications

60 The fiscal implications of the policy changes proposed are **$272.485 million** over the forecast period. These are broken down as follows:

60.1 $239.690 million to increase the FTC by $5 per child and increase the abatement rate from 25% to 27%, including the flow-on impact to other MSD assistance, and

60.2 $32.794 million to increase the base rates of OB, UCB and FCA.

61 The other related technical policy changes proposed have already been factored into forecasts. No additional funding is being sought.

Legislative Implications

Legislative implications of increasing the FTC

62 The proposed $5 increase to the FTC and associated FTC and IWTC abatement rate increases, together with the other changes proposed in this paper, will require amendments to the Income Tax Act 2007 via urgent primary legislation before 1 December 2021. This is to ensure Inland Revenue has sufficient time to make the required system changes, and to implement the changes that would otherwise require Orders in Council to be made by that date.

63 We recommend that urgent legislation be introduced on 23 November 2021 and that it moves through all stages in the House under urgency by 25 November 2021.

64 Because of time constraints, we propose that the Minister of Revenue return to Cabinet to seek approval to introduce the Taxation (COVID-19 Support Payments and Working for Families Tax Credits) Bill containing the amendments agreed to by Cabinet.

Legislative implications of passing on the FTC increase to the rates of OB, UCB and FCA

65 The rates of the OB and UCB are prescribed in Schedule 4 of the Social Security Act 2018. Enacting the increase to the base rates of these payments requires an amendment to the Social Security Act 2018 via an Order in Council. Subject to Cabinet agreement to the proposal, the Minister for Social Development and Employment will report back separately to Cabinet Legislation Committee to progress this Order in Council in early 2022.

66 Increasing the base rate of the FCA can be done administratively under the Oranga Tamariki Act 1989, and therefore legislative change is not required.

Impact Analysis

Regulatory Impact Statement

67 The Regulatory Impact Statement (RIS) requirements apply to the proposals in this paper. A RIS has been prepared and is attached.

68 The Quality Assurance reviewers at Inland Revenue have reviewed Regulatory Impact Statement: April 2022 Working for Families changes and consider that the information and analysis summarised in it **partially** meets the quality assurance criteria of the Regulatory Impact Statement framework

69 This RIS has been prepared in a constrained timeframe. There was no public consultation on these proposals. However, we note that the direction of the proposals was signalled in the WEAG report and are consistent with the Government's targets for child poverty. The changes will not have any significant adverse impacts on stakeholders given the changes are to systems which are already in place.

Climate Implications of Policy Assessment

70 There are no climate implications arising from this paper.

Population Implications

71 Approximately 57% of all families with children receive WFF, and 35% receive the In-Work Tax Credit (using administrative and TAWA outputs).

72 The impact of the changes proposed in this paper will be modest. Those expected to benefit from the changes will be low income families with children. Sole parents, who are predominately women, make up a large proportion of low-income families. For the 2020 tax year, 52% of WFF recipients were sole parent families. For the Family Tax Credit specifically, around 58% of recipients are sole parent families.

73 As Māori people with children are overrepresented amongst low income households they are likely to benefit from the WFF changes. For example, as at November 2018, Māori made up 15% of the New Zealand population, but 36% of benefit recipients (Welfare Expert Advisory Group 2018 Welfare System: statistics). Passing on the FTC to the rates of the OB, UCB and FCA would also impact children and Māori.

Over half of children living with caregivers[6] are Māori, and a significant proportion of their caregivers are also Māori.

74 The impact of the WFF changes on other groups may be proportionate to their representation in the target group of low-income families. Pacific people with children are overrepresented amongst low income households. Children in households where someone has a disability are over-represented amongst low income families. These families will be likely to benefit from the changes.

Human Rights

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

Consultation

76 The Treasury and Inland Revenue have been consulted in the development of this paper.

Communications

77 Subject to Cabinet decisions, we intend to make a media statement introducing these changes in November 2021.

Proactive Release

78 This Cabinet paper will be proactively released, with redactions made consistent with the Official Information Act 1982. Proactive release will follow the media statement.

[6] There are around 24,000 children being cared for by around 15,000 caregivers, both inside and outside of the State care system.

Recommendations

1. **note** that in 2019, SWC agreed to a review of Working for Families as part of the Welfare Overhaul work programme [SWC-19-MIN-0168];

2. **note** that on 12 May 2021, SWC noted that the review of Working for Families had been brought forward on the Welfare Overhaul work programme [SWC-21-MIN-0068];

3. **note** that we are committed to fundamental changes to Working for Families to improve the structure and design of Working for Families payments, with a focus on support for additional in-work costs, particularly childcare costs, and administrative, operational and client experience improvements;

4. **note** that under section MF(7)(2)(b) and MF(7)(2BA)(a) of the Income Tax Act 2007, the rates of the Family Tax Credit and Best Start Tax Credit must be adjusted once the cumulative increases in the Consumer Price Index (CPI) reach 5%, since the last adjustment;

5. **note** that increases to the CPI have now reached 8.57% and under current settings, the Family Tax Credit and Best Start Tax Credit will automatically increase by 8.57% on 1 April 2022;

6. **note** that there is a strong case to take immediate additional action to improve income adequacy for families on our lowest incomes as part of our review of Working for Families, as:

   6.1 we know that COVID-19 and the associated alert level restrictions have created additional pressures for some families,

   6.2 the CPI adjustment of payments scheduled for April 2022 provide an opportunity to make changes to target assistance to those on lower incomes,

   6.3 changes need to be implemented through Budget 2022 to have a full impact on our current three-year child poverty targets;

7. **agree** to the following changes to take effect from 1 April 2022:

   7.1 increase the Family Tax Credit rates by $5 per child per week,

   7.2 increase the Family Tax Credit and In Work Tax Credit abatement rate to 27 percent,

   7.3 pass on the $5 increase to the Family Tax Credit to increase the base rates of the Orphan's Benefit, Unsupported Child's Benefit, and Foster Care Allowance by $5 per week per child;

8. **agree** to increase the abatement rate, as outlined in rec 7.2 via an amendment to the Income Tax Act 2007;

9. **note** that making these changes together ensures support is targeted to those on the lowest incomes at a reduced fiscal cost, while ensuring that no families will be worse off compared to what they currently receive;

10. **note** that the changes to Working for Families are forecast to reduce child poverty by 5,000 (+/- 4,000) children on the before-housing-costs, moving line measure, and 6,000 (+/- 5,000) children on the after-housing-costs, fixed line measure;

11. **approve** the following changes to appropriations to give effect to the policy decision in recommendation 7 above, with a reduction in the operating balance and increase in net core Crown debt:

	$m - increase/(decrease)				
	2021/22	**2022/23**	**2023/24**	**2024/25**	**2025/26 & Outyears**
Vote Social Development					
Minister for Social Development and Employment					
Benefits or Related Expenses:					
Childcare Assistance					
Hardship Assistance	(0.621)	(2.617)	(2.639)	(2.545)	(2.545)
Orphan's/Unsupported Child's Benefit	1.478	6.215	6.593	6.923	7.293
Minister of Housing					
Benefits or Related Expenses:					
Accommodation Assistance	(0.735)	(2.853)	(3.030)	(3.618)	(3.618)
Vote Housing and Urban Development					
Minister of Housing					
Non-Departmental Output Expense:					
Purchase of Public Housing	(0.599)	(2.552)	(2.555)	(2.141)	(2.141)
Vote Oranga Tamariki					
Minister for Children					
Investing in Children and Young people MCA:					
Departmental Output Expense:					
Statutory Intervention and Transition (funded by revenue Crown)	0.252	1.009	1.012	1.009	1.009
Vote Revenue					
Minister of Revenue					
Benefits or Related Expenses:					
Family Tax Credit PLA	22.250	89.000	85.000	81.000	81.000
In-Work Tax Credit PLA	(5.000)	(20.000)	(21.000)	(21.000)	(21.000)
Independent Earner Tax Credit PLA	0.250	1.000	1.000	1.000	1.000
Total Operating	**17.275**	**69.202**	**64.381**	**60.628**	**60.998**

12. **agree** that the proposed changes to appropriations above be included in the 2021/22 Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply;

13. **agree** that the expenses incurred under recommendation 11 above be charges as a pre-commitment against the Budget 2022 operating allowance;

Changes to the measure used to index the Family Tax Credit and Best Start Tax Credit

14. **note** that a technical amendment is needed to change the CPI measure used for this calculation from the New Zealand Consumers Price Index all groups *excluding cigarettes and other tobacco products* (CPIX) to New Zealand Consumers Price Index all groups, consistent with previous Cabinet decisions [CAB-16-MIN-0189 refers];

15. **note** that forecast cost associated with indexation have been calculated in line with the policy decision noted in recommendation 14, and to continue using CPIX going have a fiscal cost of $18 million over the forecast period, as CPIX is higher than CPI all groups;

16. **agree** to update the CPI measure used to calculate the indexation of the Family Tax Credit and Best Start Tax Credit to the *New Zealand Consumers Price Index all groups* from the March 2021 quarter, and this be used for the Family Tax Credit and Best Start Tax Credit indexation increases required from 1 April 2022;

17. **agree** to give effect to the change in CPI measure via an amendment to the Income Tax Act 2007;

Giving effect to rates of Family Tax Credit and Best Start Tax Credit from 1 April 2022

18. **note** that as a result of the 5% CPI threshold being reached, and based on the decision above at rec 16, the Family Tax Credit and Best Start Tax Credit must be increased by 8.57% from 1 April 2022;

19. **note** that the combined impact of policy changes to the FTC agreed in recommendation 7 and the CPI indexation noted in recommendation 18 result in the following Family Tax Credit and Best Start Tax Credit rates from 1 April 2022:

Payment	**Annual Amount (as set out in the Act)**	**Equivalent weekly rate**
Family Tax Credit "eldest dependent child"	$6,642	$127.73
Family Tax Credit "additional dependent child"	$5,412	$104.08
Best Start Tax Credit	$3,388	$65.15

20. **agree** to give effect to the new Family Tax Credit and Best Start Tax Credit rates noted above in recommendation 19 via amendments to the Income Tax Act 2007 rather than by Order in Council as would otherwise be required;

Increasing the Minimum Family Tax Credit via primary legislation

21. **note** that Cabinet previously agreed to implement the adjustment to the 1 April 2022 Minimum Family Tax Credit threshold (then forecast to be to $32,760) to align with the increase to main benefit via an Order in Council [CAB-21-MIN-0116.33 refers];

22. **note** that the Minimum Family Tax Credit threshold is now forecast to be $32,864 from 1 April 2022;

23. **agree** to give effect to the adjustment to the Minimum Family Tax Credit on 1 April 2022 via an amendment to the Income Tax Act 2007 rather than via an Order in Council as previously agreed by Cabinet;

Legislation implications

24. **agree** that the legislative amendments outlined in recommendations 8, 17, 20 and 23 be included in legislation introduced and progressed under urgency on 23 November in order to meet the 1 April 2022 implementation date;

25. **agree** to delegate authority to the Minister of Revenue, Minister of Social Development and Employment, and Minister of Finance to make any minor and technical amendments to these changes to the Working for Families settings;

26. **note** that the Minister of Revenue will seek Cabinet approval to introduce the Taxation (COVID-19 Support Payments and Working for Families Tax Credits) Bill (the Bill);

Minor flow-on consequences to the Community Services Card

27. **note** there is a flow-on to the Community Services Card (CSC) from increasing the Family Tax Credit, which may change the eligibility to the CSC for a small number of families;

28. **agree** to delegate authority for the Minister of Finance, Minister of Health and Minister for Social Development and Employment to make decisions on any consequential changes to the CSC income thresholds.

Authorised for lodgement

Rt Hon Jacinda Ardern

Minister for Child Poverty Reduction

Hon Carmel Sepuloni

Minister of Social Development and Employment

Regulatory Impact Statement: April 2022 Working for Families changes

Coversheet

Purpose of Document	
Decision sought:	Analysis produced for the purpose of informing: final Cabinet decisions
Advising agencies:	Inland Revenue, Ministry of Social Development, The Treasury, The Department of Prime Minister and Cabinet
Proposing Ministers:	The Minister for Child Poverty Reduction and the Minister for Social Development and Employment
Date finalised:	28/10/2021

Problem Definition

The Government is reviewing the Working for Families scheme in response to recommendations from the Welfare Expert Advisory Group (WEAG). Phase one of the review has considered a redistributive package of changes through Budget 2022 to provide further support to low-income families and contribute toward the Government's child poverty reduction targets.

Executive Summary

Overview of proposals discussed

Options for phase one of the WFF review

The proposed options for phase one of the Working for Families (WFF) review are discussed in this Regulatory Impact Statement (RIS). These consist of modest-cost options for Budget 2022 that increase and redistribute support to low-income families alongside an anticipated adjustment of family tax credit (FTC) and Best Start tax credit (BSTC) rates in April 2022 in line with CPI inflation. These options are intended to contribute towards the Government's child poverty reduction targets and the objectives of the WFF review.

Related changes outside of the WFF review

A proposed remedial adjustment to how Consumer Price Index (CPI) increases are calculated will proceed under the counterfactual and is discussed in this RIS for context and completeness.

Increases to Orphan's Benefit (OB), Unsupported Child's Benefit (UCB) and Foster Care Allowance (FCA) payment rates as a consequence to a proposed increase in FTC rates are also discussed in this RIS. Income Support Ministers have agreed to these consequential increases.

The costs associated with the annual minimum family tax credit (MFTC) threshold change are noted in this RIS for context but the change is not analysed as it has previously been agreed to by Cabinet [CAB-21-MIN-0116].

Background to the WFF review

In 2018, the Government established the Welfare Expert Advisory Group (WEAG) to advise them on the future of New Zealand's social security system, including the WFF scheme. The WEAG recommended fundamental changes to the design and targeting of WFF as well as significant increases to main benefits and the FTC.

Following the WEAG's report, *Whakamana Tāngata: Restoring Dignity to Social Security in New Zealand*, the Minister for Child Poverty Reduction requested a broader review of WFF. The WFF review is part of the broader Welfare Overhaul work programme.

Ministers have agreed the original objectives for WFF [Cabinet minute (04) 13/4 refers] remain important. These were to:

- make work pay by supporting families with dependent children, so that they are rewarded for their work effort
- ensure income adequacy, with a focus on low and middle-income families with dependent children to address issues of poverty, especially child poverty
- achieve a social assistance system that supports people into work, by making sure that people get the assistance they are entitled to, when they should, and with delivery that supports them into, and to remain in, employment.

Ministers have also agreed the following objectives for the review of WFF:

- Objective 1: target support more to lower-income families rather than more universal support
- Objective 2: focus on low-income working families, while maintaining support for beneficiary families
- Objective 3: help make work pay and assist with the costs for people in work.

These objectives cannot all be met at the same time, and Ministers will need to consider the relative balance between the objectives throughout the review.

There are two phases to the review:

- Phase one will consider modest-cost options for Budget 2022 that increase and redistribute support to low-income families alongside the planned CPI adjustment in April 2022
- Phase two will consider more fundamental changes to the structure and design of WFF payments, with a particular focus on in-work support, and changes to improve administration, operations and client experience.

Phase one is the subject of this RIS and canvasses the following options:

- Increases to the FTC
- Increases to the WFF abatement rate

CPI adjustment

Under the status quo, FTC and BSTC rates are increased by a corresponding amount once cumulative increases to CPI (since the rates were last increased) reach 5%. This policy is forecast to trigger increases in FTC and BSTC rates for 1 April 2022.

All options considered in phase one of the review would be implemented in April 2022, coinciding with the CPI indexation increases to the FTC and BSTC rates. Therefore, the impacts of these options have been modelled both including and excluding the impact of counterfactual indexation to demonstrate what customers will experiences and the real value of the options themselves respectively.

CPI remedial

A remedial amendment to the way in which CPI increases are calculated for the purposes of indexation is proposed and would apply from 1 January 2021. This remedial would remove the exclusion of increases in the prices of cigarettes and other tobacco products from the calculation of increases in the CPI for the purposes of indexing FTC and BSTC rates and returns the calculation of indexation to increases in CPI all groups. Cabinet only intended the exclusion of cigarettes and other tobacco products for the purposes of indexing social assistance to last until the end of the 2020 calendar year so the impact of this remedial is included in the counterfactual for the purpose of analysing the options for phase one of the WFF review.

Modelling the impact of CPI indexation

The impacts of each option were modelled using the Treasury's micro-simulation model (TAWA).[1] Modelling the options was required to inform advice to Ministers before the September 2021 quarter update for CPI was released.[2] Therefore, in advice provided to Ministers all outputs were calculated using a counterfactual based upon the CPI increases forecast in the 2021 Budget Economic and Fiscal Update (BEFU). Thus, all outputs were subject to change.

An updated costing for Ministers' chosen option is used in the Cabinet paper, based on a counterfactual that was calculated using the actual CPI increase for the September 2021 quarter. This updated costing is included below. However, all other outputs in this RIS match those originally provided to Ministers. We note that the actual CPI increase for the September 2021 quarter was materially higher than forecast, which will flow through to the distributional impacts of the policy agreed.

FTC rates and WFF abatement rate changes

Initially, agencies provided advice to Income Support Minsters on a range of options for changes to the FTC which varied by cost and the approach to abatement. Based on this advice, Ministers chose a set of parameters which were used to develop a final set of four options for them to decide between. These final options are summarised in the following table. Note that, unless otherwise stated, all outputs do not include the impact of CPI indexation.

- Options A1 - A3 relate to a $5 FTC increase
- Option B relates to a $7.50 FTC increase

[1] These TAWA modelling results use data from the IDI, which was provided by Stats NZ under conditions designed to give effect to the security and confidentiality provisions of the Statistics Act 1975. The results are the work of the author, not Stats NZ or individual data suppliers.

[2]An increase in FTC & BSTC rates is triggered once cumulative increases to the CPI since the last adjustment of FTC and BSTC rates reaches 5%. Once the 5% threshold has been reached, FTC and BSTC rates will be scheduled to increase from 1 April of the upcoming year. The percentage they are increased by is based on the cumulative actual increase in CPI up until the end of the September quarter after the 5% threshold was reached.

FTC rate and abatement rate options	FTC increase per child		Abatement rate	Annual cost	Children lifted from poverty[3]		Gains and losses for households			
	Rate change	Total with CPI (eldest & subs. child)			BHC50[4]	AHC50[5]	Winners	Average gain	Losers	Average losses
A1 ($5 FTC, 25% abmt)	$5	$11.71 and $10.42	25% (No change)	$158m	5,000 (± 4,000)	9,000 (± 6,000)	316,000	$10	S[6]	S
A2 ($5 FTC, 26% abmt)	$5	$11.71 and $10.42	26%	$111m	5,000 (± 4,000)	9,000 (± 6,000)	287,000	$8	26,000	-$1
A3 ($5 FTC, 27% abmt)	$5	$11.71 and $10.42	27%	$68m	5,000 (± 3,000)	8,000 (± 6,000)	223,000	$8	89,000	-$6
B ($7.50, 28% abmt)	$7.50	$14.21 and $12.92	28%	$103m	7,000 (± 5,000)	10,000 (± 6,000)	223,000	$12	89,000	-$8

Options A2, A3 and B explore changes to the WFF abatement rate. The WFF abatement rate applies to a family's in-work tax credit (IWTC) (or CTC[7]) and FTC entitlements once their annual income surpasses the WFF abatement threshold. The abatement rate determines the rate at which a family's WFF entitlement is reduced once their income crosses the threshold, i.e. how many cents in each dollar earnt over the threshold a family will lose from their entitlement. Currently, the WFF abatement rate is 25% (25c in each dollar) and the abatement threshold is $42,700.

Abatement rate increases reduce the fiscal cost of an FTC rate increase and target support more towards lower-income families. Abatement rate increases meet the WFF review's objective to "target support more to lower-income families rather than more universal support".

Updated impacts of the final option agreed by Ministers

Ministers have chosen to progress option A3 (a weekly increase in FTC rates of $5 and an abatement rate of 27%). The following are the updated modelled outputs of option A3 using a counterfactual calculated with the updated CPI figure. Note that, unless otherwise stated, all outputs for this option do not include the impact of the FTC and BSTC rates increase due to CPI indexation.

[3] Note there is significant statistical uncertainty in the child poverty reduction estimates.

[4] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income before housing costs are deducted.

[5] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income after housing costs are deducted (for the 2017/18 base financial year).

[6] S = suppressed due to Statistics NZ confidentiality rules.

[7] The Child Tax Credit (CTC) was 'grandparented' once it was replaced by the In-Work Tax Credit. Very few families still receive it.

FTC rate and abatement rate options	FTC increase per child		Abatement rate	Annual cost	Children lifted from poverty[8]		Gains and losses for households			
	Rate change	Total with CPI (eldest & subs. child)			BHC50[9]	AHC50[10]	Winners	Average gain	Losers	Average losses
A3	$5	$14.69 and $12.83	27%	$66m	5,000 (± 4,000)	6,000 (± 5,000)	223,000	$8	91,000	-$6

Option to pass on increase to other caregivers (Oranga Tamariki comment)

There is also the option to extend the FTC increase to the rates of Orphan's Benefit (OB), Unsupported Child's Benefit (UCB), and Foster Care Allowance (FCA), costing an average of $8.2m per annum for a $5 increase to rates, or an average of $12.3m per annum for a $7.50 increase to rates. By convention, any FTC increase is passed on to these payments – this is because caregivers are not able to receive the FTC, and the FTC makes a partial contribution towards the costs of raising children.

[8] Note there is significant statistical uncertainty in the child poverty reduction estimates.

[9] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income before housing costs are deducted.

[10] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income after housing costs are deducted (for the 2017/18 base financial year).

Limitations and Constraints on Analysis

The options presented in phase one have been limited by:

- The scope of the review and the specific parameters set by Ministers for phase one options
- The modest fiscal envelope of the review
- The tight timeframes required to make system changes before April 2022
- No public or stakeholder consultation
- The desire to minimise design constraints on phase two
- Data uncertainty

Phase one parameters

The proposed changes were prepared within the final parameters set by Ministers, following earlier advice. These parameters were that the options:

- have modest increases to the rate of FTC
- cost around $50 - $100 million per year
- retain a single abatement threshold at the current level of $42,700
- reduce child poverty
- minimise the number of losing families, particularly for those with incomes below $100,000 per year.

The fiscal envelope

There is limited funding available for Budget 2022 due to the tight fiscal environment and prior Government expenditure on support to mitigate the effects of the COVID-19 pandemic.

Ministers originally agreed that any changes to WFF should be broadly within the existing fiscal envelope. Officials provided advice in August 2021 where modelling demonstrated that the level of redistribution required to make income adequacy-focused options fiscally neutral resulted in many of the lowest-income working families being financially disadvantaged. It is also difficult to reduce the costs of WFF increases without high abatement rates which can result in very high effective marginal tax rates (EMTRs), countering the objective of making work pay.

To avoid financially disadvantaging low-income working families and creating very high EMTRs, officials provided advice on changes to the FTC to coincide with the scheduled CPI indexation round. Following this advice, Income Support Ministers decided that phase one options would include modest FTC increases costing up to $100m per year. Modelling suggests that medium-cost redistributive options can reduce child poverty.. In addition, when the proposed changes are combined with the scheduled CPI increases, the estimated numbers of recipients who would be worse off are reduced. However, the modest fiscal envelope for phase one still limits the ability of options to reduce child poverty without increases to abatement rates (which result in much higher EMTRs).

Tight timeframes

Policy development has been constrained by the tight timeframes required to make system changes in time for an April 2022 implementation. To avoid confusion and reduce administrative complexity, all system changes are made prior to January each year to ensure the changes can be incorporated into the annual “rollover” process which calculates WFF entitlements for the coming tax year and issues notices of entitlement to customers. To meet this deadline, Inland Revenue requires Cabinet decisions on policy settings by the end of November 2021. This significantly limits opportunities for analysis and consultation, meaning that more substantial, structural changes could not be considered in phase one.

No consultation on phase one

Ministers have agreed to defer public engagement with the WFF review until April/May 2022. This aligns with the longer development timeframe for the more substantial options canvassed in phase two. The options canvassed in phase one cannot be submitted for consultation as they are budget sensitive.

Impact on phase two

Options for phase one of the review also need to be considered within the context of the broader review. Options which do not unnecessarily limit the scope for phase two, which will consider more fundamental changes to the structure and design of WFF, are preferred.

Data uncertainty

These options have been modelled by Treasury's Tax and Welfare Analysis (TAWA) model. Treasury warns that there are significant uncertainties when estimating future poverty metrics due to the underlying data and economic forecasts. When Inland Revenue modelled the same outputs for quality assurance the following differences appeared. This comparison is based on TAWA outputs using unequivalised family taxable income, and Inland Revenue administrative data.

Option	Losers (N)	Winner (N)	average loss per week $	average win per week $	Cost $m
A1	N/A	30,000	N/A	-1	-2
A2	13,000	15,000	0	-1	-8
A3	18,000	9,000	0	-1	-10
B	-1,000	28,000	-2	-1	14

These differences most likely reflect the fact that, unlike Inland Revenue modelling, TAWA modelling assumes full take up and does not take relationship changes into account, leading to an overestimation of the impact of changes on the population.

TAWA modelling does not take into account any behavioural changes that may result from the policy changes, such as changes in employment.

The MFTC threshold changes were forecast by Inland Revenue's forecasting team according to their usual annual process, based on the data available.

Responsible Managers	
Maraina Hak Policy Lead, Policy and Regulatory Stewardship Inland Revenue s 9(2)(a) 28/10/2021 Polly Vowles Manager, Income Support Policy Ministry of Social Development s 9(2)(a) 28/10/2021	

Quality Assurance	
Reviewing Agency:	Inland Revenue
Panel Assessment & Comment:	The Quality Assurance reviewers at Inland Revenue have reviewed Regulatory Impact Statement: April 2022 Working for Families changes and consider that the information and analysis summarised in it **partially** meets the quality assurance criteria of the Regulatory Impact Statement framework This RIS has been prepared in a constrained timeframe. There was no public consultation on these proposals. However, we note that the direction of the proposals was signalled in the WEAG report and are consistent with the Government's targets for child poverty. The changes will not have any significant adverse impacts on stakeholders given the changes are to systems which are already in place.

Section 1: Diagnosing the policy problem

What is the context behind the policy problem and how is the status quo expected to develop?

Government commitment to improving child poverty

In 2018, the Government passed the Child Poverty Reduction Act whose purpose is to help achieve a significant and sustained reduction in child poverty in New Zealand by provisions that:

- encourage a focus by government and society on child poverty reduction
- facilitate political accountability against published targets
- require transparent reporting on levels of child poverty.

This Act bound the Government to set:

- long-term targets for reducing, over a long-term period (10 financial years), child poverty
- intermediate targets that support, over an intermediate period (three financial years), current long-term targets.

In line with these requirements, the Government has so far set one set of long-term, 10-year targets and two sets of intermediate, three-year targets to lower the rate of child poverty. These targets, measured against the AHC50[11] and BHC50[12] poverty thresholds, are outlined in the following table. [13]

Poverty measure	Unit	Baseline year (2018)	Current rate	First three-year target	Second three-year target	Ten-year target
		2017/18	2019/20	2020/2021	2023/2024	2027/28
AHC50	Child poverty rate	22.8%	18.4%	18.8%	15%	10%
	Number of children in poverty	253,800	210,500	218,000	174,000	~120,000
BHC50	Child poverty rate	16.5%	13.8%	10.5%	10%	5%
	Number of children in poverty	183,400	157,800	122,000	116,000	~60,000

[11] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income after housing costs are deducted (for the 2017/18 base financial year).

[12] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income before housing costs are deducted.

[13] Government has also set targets measured against material hardship but the AHC50 and BHC50 measures are the only ones that will be used in this document for the sake of simplicity and consistency with the modelling of outputs by TAWA.

The Government has a series of mechanisms at its disposal with which it could reduce child poverty to meet its targets and improve income adequacy for low- and middle-income families generally. Examples of these are the minimum wage, rent controls, benefit rates and the WFF scheme. These tools do not necessarily target the same population groups.

The introduction of the Families Package in 2018, along with significant recent increases to the minimum wage and benefit rates, have helped the Government towards achieving its targets. The following table outlines child poverty rates since the introduction of the Child Poverty Reduction Act in 2018.

Poverty measure	Year	Rate		Annual change in rate		Number		Annual change in number		Total number of children
		Percent	Level sampling error	Percentage points	Sampling error on the change	(000s)	Level sampling error	(000s)	Sampling error on the change	(000s)
AHC50	**2018**	22.8	1.9	0.4	2.8	253.8	21.6	6.3	31.0	1,113.3
	2019	18.3	1.1	-4.5	2.4	207.7	12.9	-46.1	27.4	1,132.8
	2020	18.4	1.3	0.1	1.8	210.5	15.2	2.8	20.0	1,144.2
BHC50	**2018**	16.5	1.1	2.3	1.6	183.4	12.2	27.1	17.4	1,113.3
	2019	13.5	0.9	-2.9	1.7	153.2	10.1	-30.1	19.6	1,132.8
	2020	13.8	1.2	0.3	1.5	157.8	13.5	4.5	16.7	1,144.2

The Government recognises the current WFF review as an important opportunity to further reduce child poverty rates.

The WFF scheme

The WFF scheme has two primary objectives:

- to support income adequacy and reduce child poverty
- to improve financial incentives for low-income earners to participate in the labour market.

It must achieve these objectives at a sustainable cost to government.

The scheme was introduced between 2004 and 2007 and has undergone multiple changes under successive governments.

Increases to the FTC rates are a particularly useful way to address child poverty and income adequacy as the credit's eligibility requirements make it well targeted to low- and middle-income families with children, regardless of their work status.

Background to the WFF review

In 2018, the Government established the WEAG to advise on the future of New Zealand's social security system, including the WFF scheme. The WEAG recommended fundamental changes to the design and targeting of WFF, and significant increases to main benefits and the FTC.

Following the WEAG's report *Whakamana Tāngata: Restoring Dignity to Social Security in New Zealand*, the Minister for Child Poverty Reduction requested a broader review of WFF. The WFF review is part of the broader Welfare Overhaul work programme.

Scope of the WFF review

The WFF review will explore whether policy settings can be adapted to better address the scheme's objectives.

Ministers have set the scope of the review to:

- Working for Families settings (including the Independent Earner Tax Credit (IETC))
- The Accommodation Supplement
- Options for supporting disabled people in work, including consideration of a Disability Tax Credit.

The impacts of related workstreams, progressing in parallel to the review, will also be considered.

Income Support Ministers have agreed the review should focus on:

- low-income working families, while maintaining support for beneficiary families
- options that target support more to lower-income families rather than more universal support
- the principle of making work pay and assisting with the costs for people in work.

These objectives have been noted by Cabinet. Cabinet has indicated that the review will be the primary vehicle for achieving the second, three-year child poverty targets. However, making significant improvements via phase one will be challenging given the tight fiscal environment.

Review phases

Following advice in August 2021, which covered initial options in line with Minister's objectives for the review, officials have split advice on the review into two phases. These are:

- phase one, which will consider modest-cost options for Budget 2022 that increase and redistribute support to low-income families alongside the planned CPI adjustment of FTC and BSTC rates in April 2022
- phase two, which will consider more fundamental changes to the structure and design of WFF payments, with a particular focus on in-work support, and changes to improve administration, operations and client experience.

Phase one is the subject of this RIS and includes the following options

- increases to the FTC to support income adequacy
- WFF abatement rate changes to target assistance more tightly to lower-income families.

The counterfactual

In the absence of government changes, the number of children living in poverty is expected to slightly increase.[14] Although benefit and some WFF rates are indexed to inflation (wage growth and the CPI respectively), these maintain the real value of payments over time; i.e., these indexation adjustments lower the likelihood that child poverty rates would increase, rather than actively reduce them.

Developments in the wider economy could influence child poverty rates, positively or negatively. However, the only way to ensure that poverty rates reduce is by making changes targeted to achieve this end. The WFF review is a key opportunity to do so.

Option to pass on increase to other caregivers (Oranga Tamariki comment)

There is also the option to extend the FTC increase to the rates of the OB, UCB and FCA. Increases to the FTC have been applied to the rates of OB, UCB, and FCA in 2005, 2007, and 2018, as caregivers receiving these payments cannot receive the FTC in respect of the same child, and the FTC makes a partial contribution towards the costs of raising children.

[14] According to TAWA forecasts.

What is the policy problem or opportunity?

The problem

The central issue which phase one of the WFF review seeks to address is the persistence of child poverty and income inadequacy for low- and middle-income families in New Zealand. Although poverty and income inadequacy exist for individuals without children, the scope of this review is limited to families with children.

In the year ended June 2020, 207,700 children, 18.4% of the children in New Zealand, were living in AHC50 poverty.[15] This means these children were growing up in families whose annual household equivalised disposable income (HEDI[16]), after deducting housing costs (AHC), was less than 50% of the median HEDI in New Zealand.[17] If housing costs are not deducted, 157,800 children, 13.8% of children in New Zealand, were living in BHC50 poverty.[18] [19]

In the same year, 165,400 households, 9% of all households in New Zealand, reported that the adequacy of their income was "not enough" to support their needs. A further 432,600 (24%) reported that their income was "only just enough" to support their needs.[20]

Part of the government's role (as emphasised by the Child Poverty Reduction Act 2018) is to alleviate issues of poverty and income adequacy in society. It does so through various means, but most explicitly by targeting financial transfers to affected groups of the population via the welfare system and the WFF scheme. The fact that poverty, particularly child poverty, and income inadequacy persist demonstrates that these tools have not solved the problem. Although the Government has not committed to eliminating these issues, it has set targets to significantly reduce the number of children in poverty.

The stakeholders

The primary stakeholders in this issue are the families and children living in poverty or with inadequate income. They have a significant, personal interest in this issue as living in poverty or without income adequacy has the potential to restrict or negatively influence all aspects of their lives. Restricted access to material goods or restricted capacity for social participation can have significant flow on effects to other areas of life such as physical and mental health, educational outcomes and thus work opportunities.

In many ways, wider society is also a stakeholder in this issue. The consequences of poverty lead to greater public expenditure, particularly on healthcare and the justice system, as well

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[15] According to Stats NZ..

[16] HEDI is household total income, net of tax, adjusted to allow comparison of income adequacy between households with different composition. This involves an equivalisation factor that accounts for the number and age of household occupants and economies of scale. TAWA and official child poverty metrics use OECD equivalisation, where HEDI = DI/(1+0.5*(N_GTE14-1) + 0.3*N_LT14). It is essentially a per-person, disposable income where the first person 14 or older counts as 1 person, subsequent people 14 or older count as 0.5 and each child under 14 years counts as 0.3.

[17] According to Stats NZ.

[18] According to Stats NZ.

[19] Note that the AHC50 poverty measure is fixed-line (the median HEDI is calculated using the 2017/18 base financial year then adjusted for CPI inflation up to the financial year in which poverty is being measured), whereas the BHC50 poverty measure is moving-line (the median HEDI is calculated using the financial year in which poverty is being measured).

[20] According to Stats NZ.

as the loss of potential tax revenue. Although increased expenditure on welfare may appear to negatively impact the taxpayer, reductions in poverty rates will lead to savings in other areas.

Disproportionally affected groups

Māori, Pacific people, people with disabilities and women are overrepresented in low-income earners and evidence indicates these groups are likely to be among the hardest hit by COVID-19 economic impacts. Māori and Pacific women in particular are over-represented in low-wage employment as well as casual, temporary and other forms of insecure employment. COVID-19 has only exacerbated the situation for these groups, who are also more likely to be in industries impacted by COVID-19 restrictions. Women with caring responsibilities, especially sole parents, are also exposed to the adverse effects of economic recessions that can lock in long-term unemployment and poverty (including in-work poverty) and lead to increased rates of child poverty.

Changes to the FTC considered in this RIS provide increases to families with the lowest incomes. They are therefore likely to disproportionately benefit Māori, Pacific people and women.

Another key consideration is the impact of any solutions specifically on children. Contributing to child poverty reduction is one of the main objectives of the WFF scheme. Better targeting of WFF aims to increase the income adequacy of families in which the most vulnerable children live, and greater work incentives help to provide pathways for families out of poverty. This may include increased opportunities for their children as they move into education and work. Research indicates people who come onto benefits before the age of 20 are more likely to stay on benefit longer.

Option to pass on FTC increase to other caregivers population - (Oranga Tamariki comment)

There are around 15,000 families caring for around 24,000 children supported by the OB, UCB, and FCA. Around half of caregivers outside of the State care system (6,000 families) are earning less than $43,000.

Targeting the problem

The eligibility criteria of the WFF tax credits are designed to target support to low- and middle-income families through income thresholds at which entitlements begin to abate. Out of these, the FTC best targets families experiencing poverty and income inadequacy as it is not linked to work or benefit status.

The changes to the FTC rate and abatement rate that are considered in this RIS are redistributive options within the WFF scheme. Ministers have indicated that changes to WFF should be a primary lever to help meet child poverty reduction targets. The options are aimed at more effectively targeting WFF payments to support lower income families and to reduce child poverty.

An increase in the base FTC rate is most closely aligned to the WFF review's objective of supporting low income working families, while a change to the abatement rate is more closely aligned to the objective of targeting financial assistance rather than providing more universal support.

What objectives are sought in relation to the policy problem?

The three primary objectives to be considered for any policy changes to WFF are to:

1. Improve income adequacy for beneficiaries and low-income people
2. Improve financial incentives to work
3. Pay welfare support at a sustainable cost to government

These objectives must be considered when evaluating any proposed changes to WFF along with any more specific objectives that are being sought in relation to a particular proposal or set of proposals.

1. Improving income adequacy for beneficiaries and low-income people

While recent changes to the welfare system (including the Families Package, the $25 increase to main benefits on 1 April 2020 and the indexation of main benefits to average wage) will help to improve the living standards of low-income people, income adequacy and child poverty issues remain. Any changes to the WFF should have a net positive impact on these issues, particularly as these credits are an important tool with which to meet the Government's child poverty targets.

2. Improving financial incentives to work

Improving financial incentives to work will encourage people who are able to work to seek employment. For most people, paid work is a key means of achieving improved wellbeing. However, financial incentives are only one (and not necessarily the most important) of many factors that influence people's decisions on whether, or how much, to work.

3. Paying welfare support at a cost that is sustainable to government

The Government is required to act and pursue its policy objectives in accordance with the principles of responsible fiscal management as set out in the Public Finance Act 1989, such as managing fiscal risks facing the government, having regard for the impact on present and future generations and ensuring the Crown's resources are managed effectively and efficiently.

Any changes proposed in this RIS must be at a sustainable cost to government, particularly given the current tight fiscal environment following the range of initiatives implemented by the Government in response to COVID-19.

The iron triangle

These three objectives make up the "iron triangle" of trade-offs inherent to income support. It is generally possible to achieve two of the three objectives for any given policy change, but not all three.

The current WFF review

Income Support Ministers have agreed, and Cabinet has noted, that the current review of WFF should focus on:

- income support for low-income working families, while maintaining support for beneficiary families
- targeting support more to lower-income families rather than more universal support
- considering the principle of making work pay and assisting with the costs for people in work.

Ministers also agreed, following initial advice, that options for phase one must be modest-cost. Ultimately, Ministers narrowed the fiscal envelope of the final options analysed in this RIS to between $50 -100m.

Although these review objectives maintain the original objectives, their focus on targeting and the modest fiscal envelope indicate that objective 3 (to pay welfare support at a sustainable cost to government) is a priority. As phase one’s scope is limited to options which improve income adequacy and child poverty, objective 1 (to improve income adequacy for beneficiaries and low-income people) must also be a priority. Therefore, options have been designed to fulfil objectives 1 and 3, even if that comes at the expense of objective 2 (to improve financial incentives to work).

Section 2: Deciding upon an option to address the policy problem

What scope will options be considered within?

Options were presented in two stages: initial and final. Subsequent to the confirmation of the WFF review objectives in April 2021 and the setting of the second set of three-year child poverty targets in June 2021, the scope for initial options was defined as modest-cost options for Budget 2022 that increase and redistribute support to low-income families.

After analysing initial advice, Ministers narrowed the scope for final options. The following table summarises the factors considered by Ministers in initial advice and their decisions on the scope for final options. These are discussed in more detail below.

	Scale of package	Approach to abatement
Link to criteria	Fiscal cost Impacts on child poverty	Impacts on work incentives Impacts on future reform
Options canvassed in initial advice	A range of options for an FTC increase were presented to Ministers ranging from a $5 to $15 per child increase. The options were broadly grouped into low cost ($50-$200m p.a.), and high cost ($200-$400m p.a.). The larger increases to the FTC had greater impacts on child poverty.	There were three broad sets of approaches to abatement explored: - Modest two-tier structure - Sharper two-tier structure - One-tier abatement structure
Constraints from Ministers for final advice	As a result of initial advice, Ministers agreed the following constraints around the **scale of the package:** - Modest increases to the rates of FTC - Cost around $50 - $100 million per year - reduce child poverty	As a result of initial advice, Ministers agreed the following constraints on the **approach to abatement:** - retain a single abatement threshold at the current level of $42,700 - minimise the number of losing families, particularly for those with incomes below $100,000 per year.

Initial advice on options for phase one

An initial, broader series of options for phase one was presented to Ministers in the 17 September *Working for Families Review: update and options for Budget 2022* report. These options included:

- a redistributive package focused on changes to the FTC
- and concurrently

- the alignment of the BSTC abatement scheme with the WFF abatement scheme
- smoother indexation arrangements
- an extension to the BSTC

The redistributive package

Options for the redistributive package included $5, $7.50, $10 and $15 FTC rate increases combined with a series of abatement rate and threshold options that included the possibility of introducing a second tier of abatement threshold. The details of these options and their outputs (modelled by TAWA) are outlined in the table below.

Option	FTC increase		Children lifted from poverty		Two tier abatement approach			Single tier abatement approach		
	FTC increase above CPI	FTC increase with CPI (eldest & subs. child)	BHC50[21]	AHC50[22]		Second abatement threshold	Second abatement rate		Abatement threshold	Abatement rate
Lowest cost ($60-90m)	$5	$11.71 and $10.42	5,000	7,000-8,000	A	$60,000	29%	C	$42,700	27%
						$65,000	31%		$45,200	29%
					B	$75,000	33%			
						$75,000	35%			
Lower cost ($130-170m	$7.50	$14.21 and $12.92	7,000-8,000	11,000 - 12,000	A	$60,000	29%	C	$42,700	27%
						$65,000	31%		$45,200	29%
					B	$75,000	33%			
						$75,000	35%			
Higher cost ($200-240m)	$10	$16.71 and $15.42	11,000-13,000	15,000-16,000	A	$60,000	29%	C	$42,700	27%
						$65,000	31%		$45,200	29%
					B	$75,000	33%			
						$75,000	35%			
High cost ($360-400m)	$15	$21.71 and $20.42	16,000-17,000	22,000-23,000	A	$60,000	29%	C	$42,700	27%
						$65,000	31%		$45,200	29%
					B	$75,000	33%			
						$75,000	35%			

Ministers were advised that:

- The single-tier options redistribute funding from a much broader range of middle-higher income families and have a more modest impact on EMTRs.
- The two-tier options redistribute funding from a smaller group of comparatively higher income families, and a significant increase in EMTRs is concentrated within this group.
- Some of the impacts on work incentives created by the options in this paper could potentially be mitigated by further changes progressed as part of phase two of the review. However, such options may turn out to be limited if fiscal, operational, or other constraints arise in the intervening period, and some of the more expensive options in this paper may limit ‘headroom’ for further WFF reform.

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[21] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income before housing costs are deducted.

[22] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income after housing costs are deducted (for the 2017/18 base financial year).

Options that increase the FTC rate by $10 or $15 and most of the $7.50 increase options have the greatest impact on child poverty but are also relatively higher cost. Ultimately, Ministers ruled these out.

Options that change the existing WFF abatement threshold or which introduce a second WFF abatement threshold are more significant structural changes that could pre-empt the work that will take place in phase two. They often resulted in high increases to EMTRs and a significant number of losers. These options were also ruled out by Ministers.

Most of the options that were progressed in the *Working for Families Review: further advice on options for Budget 2022* (A2, A3 and B) were chosen for their lower fiscal cost, minimal impact on EMTRs and relative simplicity. Although option A1 was outside of the fiscal envelope Ministers outlined for options in this stage of advice, it was included to allow for comparison with an option that did not tighten targeting.

Concurrent options

The following options were presented to Ministers as part of initial advice alongside the redistributive package.

Best Start tax credit (BSTC) alignment

Aligning the BSTC abatement scheme with the WFF abatement scheme, so that BSTC, IWTC and FTC payments abate one after the other, was suggested so that a second tier of WFF abatement threshold would not coincide with the abatement of the BSTC.

Ministers were advised that aligning the BSTC abatement scheme with the WFF scheme would involve winners and losers, as well as additional fiscal costs, and further work would be required to understand the distributional impact and costs of the change. As with the possible introduction of a second WFF abatement threshold, Inland Revenue would need a decision on this kind of structural change by the end of September 2021 for April 2022 implementation to be possible. For this reason, officials recommended further analysis and advice on whether to proceed with this option as part of phase two.

Ministers chose not to progress this option under phase one.

Smoother indexation

Ministers expressed interest in shifting to smoother indexation changes over time. Options to do this included:

- *Annual CPI indexation ($58m p.a. for FTC and BSTC)* – this would not substantially change FTC rates over the long term but would be smoother and mean slightly higher rates in the years between scheduled adjustments. Consequently, this would come at some additional cost.
- *Annual wage indexation ($85m p.a. for FTC and BSTC)* This would support the Government's child poverty objectives, but would come at a greater cost, particularly over the longer term: The impact and the fiscal cost of wage indexation is initially small, but 'snowballs' over time and becomes increasingly substantial. If Ministers wished to ensure the incomes of low-income families keep pace with middle-income families, officials recommended wage-adjusting the FTC and BSTC and indexing the IWTC to maintain work incentives over time.

Both options would incur additional fiscal costs, which could limit options for the second phase of the review. Officials suggested that Ministers might wish to consider permanent indexation changes as part of phase two.

Ministers chose not to progress this option under phase one.

BSTC extension

Officials considered including an option to extend the BSTC to 3- and 4-year-olds at a $40 p/w rate with the same abatement regime into the *Working for Families Review: further advice on options for Budget 2022* report. This option had initially been presented to Ministers in Appendix three of the *Working for Families Review: update and options for Budget 2022* report.

Although the value for money in terms of its child poverty impact was attractive, officials ultimately excluded this option because it did not meet the scope Ministers had outlined. Implementation of this option would also have involved significant administrative complexity within the proposed timeframe.

Subsequent advice to Ministers on final options for phase one

Following the first round of advice, Ministers requested further advice on Budget 2022 options which:

- have modest increases to the rate of FTC
- cost around $50 - $100 million per year
- retain a single abatement threshold at the current level of $42,700
- reduce child poverty
- minimise the number of losing families, particularly for those with incomes below $100,000 per year.

This commissioning, combined with timing considerations, has limited options to minor increases to the FTC rate and changes to the WFF abatement rate. Phase one will also include the annually required MFTC threshold increase to reflect 2022 increases in benefit rates.

The options canvassed for phase one of the review are Budget sensitive, meaning that no stakeholder engagement has taken place (other than with other government agencies).

No in-depth review of international literature has taken place in relation to the options in this RIS. This is due to timing constraints and that the options considered consist of simple changes to rates within the existing WFF regime, rather than substantive policy changes.

Non regulatory options have not been considered because financial transfers from government need appropriation, which requires legislative authority.

What criteria will be used to compare final options to the counterfactual?

Fiscal cost

Ministers prefer options of $100m or less, in line with the modest fiscal envelope available for phase one of the review. This limits the impact of options on the criteria of child poverty and work incentives.

Impacts on child poverty

These will be measured using fixed line AHC50[23] and BHC50.[24] Options which have greater reductions in the number of children in AHC50 and BHC50 poverty are preferred. Options should not be so tightly targeted that they push more children into poverty or deepen the poverty of those already under the line.

Impacts on work incentives

The impact of these proposals on financial incentives to work are considered. These will be measured using EMTRs, which are incentives to earn an additional dollar, and participation tax rates (PTRs) which are incentives to enter employment. Ministers have indicated they prefer options that will not significantly increase already high EMTRs.

Impacts on future reform

Changes should not be so substantial that they limit the scope of options available for Ministers to consider through phase two of the review.

Weighting

The fiscal cost and child poverty impact criteria will be given the highest weighting as they are prioritised in this phase of the review. Incentives to work will be addressed in phase two of the review.

[23] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income after housing costs are deducted (for the 2017/18 base financial year).

[24] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income before housing costs are deducted.

What options are being considered?

The counterfactual

Currently, the FTC rates are $113 p/w ($5,878 p/a) per eldest child and $91 p/w ($4,745 p/w) for each additional child. For every dollar of income a family earns above $42,700, they will lose 25c of their annual FTC entitlement.

Under the status quo, FTC and BSTC rates are increased by a corresponding amount once cumulative increases to CPI (since the rates were last increased) reach 5%. This is forecast to trigger increases in FTC and BSTC rates for the income year starting 1 April 2022.

All options considered in phase one of the review would be effective from 1 April 2022, coinciding with the CPI indexation increases to the FTC and BSTC rates. Therefore, the impact of these options has been modelled both including and excluding the impact of counterfactual indexation to demonstrate what customers will experience and the real value of the options themselves respectively.

Because modelling took place ahead of time, officials do not know the final rate of CPI inflation up to April 2022. Therefore, all outputs relating to counterfactual indexation were calculated using the CPI increases forecast in the 2021 BEFU. Thus, all outputs that include the impact of (forecast) counterfactual indexation are subject to change.

CPI measure – remedial amendment

A CPI remedial amendment, updating the CPI measure used in the FTC and BSTC CPI indexation provisions of the Income Tax Act 2007, will be required. Legislation currently requires FTC and BSTC rates to be increased in line with cumulative increases to all groups of the CPI excluding tobacco and cigarette products (CPIX). However, Cabinet only intended the exclusion of tobacco to last the duration of the 10% annual increases to tobacco excise taxes, the last of which took place in 2020 (CAB-16-MIN-0189). Therefore, the remedial amendment would return FTC and BSTC indexation to CPI (all groups) from quarter 1 of 2021. Although increases measured by CPI (all groups) are slightly different than under CPIX, the remedial amendment is not expected to materially change the fiscal impact of the FTC and BSTC indexation increases. This remedial is considered part of the counterfactual for analysis of the options in phase one of the WFF review.

Annual MFTC adjustment

The purpose of the MFTC is to ensure that families who are in-work and off-benefit are financially better off than they would be on a benefit. This is done by “topping-up” families’ earned income to a prescribed level (the MFTC threshold) that is higher than what their income could be when on a benefit. This intends to incentivise sole parent families with children to move off-benefit and into greater amounts of paid work.

If the MFTC threshold is not adjusted in line with benefit changes, the policy objective would not be met. Therefore, the MFTC threshold should be adjusted to reflect increases to main benefit rates (which are indexed to wage growth) that will take place under the status quo.

In April 2021, Cabinet agreed to an April 2022 increase in the MFTC threshold to reflect increases in main benefits [Cab-21-Min-0116].

Forecast changes to the MFTC threshold are summarised in the table below. Changes to the FTC rate or WFF abatement rate will not impact the MFTC threshold.

Tax year	**1 April 2022**	**1 April 2023**	**1 April 2024**	**1 April 2025**
MFTC threshold	$32,864	$33,280	$33,644	$34,112

Adjustments to the MFTC threshold are not being considered as part of phase one of the WFF review and are therefore not analysed further.

Options A and B

The following make up the final options that were presented to Income Support Ministers for phase one of the WFF review:

- A1: $5 FTC increase and no abatement change
- A2: $5 FTC increase and 26% abatement rate
- A3: $5 FTC increase and 27% abatement rate
- B: $7.50 FTC increase, 28% abatement rate

Each of these options is mutually exclusive but all would take place on top of the indexation changes anticipated in the counterfactual.

The impacts of these options are outlined below. All outputs, except the settings (produced by Inland Revenue), have been produced using Treasury's TAWA model.

Settings

The following table demonstrates what the WFF settings would look like in April 2022 under each option. The status quo FTC and BSTC rates have increased from current settings due to indexation. All amounts are annual.

Scenario	FTC eldest child	FTC subsequent child	IWTC per family	IWTC extra child	WFF abatement rate	BSTC	MFTC
CF	$6,227	$5,027	$3,770	780	25%	$3,306	$32,864
A1	$6,487	$5,287	$3,770	780	25%	$3,306	$32,864
A2	$6,487	$5,287	$3,770	780	26%	$3,306	$32,864
A3	$6,487	$5,287	$3,770	780	27%	$3,306	$32,864
B	$6,617	$5,417	$3,770	780	28%	$3,306	$32,864

Child poverty impacts

The following tables demonstrate the reduction in child poverty that would take place under each scenario when measured against the AHC50[25] and BHC50[26] poverty thresholds. As TAWA modelling assumes full take up, results will overestimate the number of families impacted. Some numbers may seem not to correspond due to rounding.

[25] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income after housing costs are deducted (for the 2017/18 base financial year).

[26] The percentage of children living in households with less than 50 percent of the median equivalised disposable household income before housing costs are deducted.

Scenario	Population (,000) with income below the AHC50 poverty threshold		Difference (,000) from counterfactual	
	Families[27]	Children[28]	Families	Children
CF	323	160	-	-
A1	320	151	-4	-9
A2	320	151	-4	-9
A3	320	152	-3	-8
B	319	150	-4	-10

Scenario	Population (,000) with income below the BHC50 poverty threshold		Difference (,000) from counterfactual	
	Families[29]	Children[30]	Families	Children
CF	183	92	-	-
A1	181	87	-3	-5
A2	181	87	-3	-5
A3	181	87	-3	-5
B	179	84	-4	-7

Option B, with its greater weekly increase of $7.50, has the greatest positive impact on child poverty measured by either threshold. When measuring against AHC50, option A3, which combines the smaller increase of $5 with a 2% abatement rate increase, has the smallest positive impact on child poverty. When measuring against BHC50 options A1-3 appear to have the same impact.

Fiscal impact

The following table breaks down the annual fiscal impact of each option by source. Although the FTC is the only payment rate which would change, the interlinked abatement and eligibility settings of social assistance payments mean these increases have flow-on effects to the accommodation supplement (AS), the IWTC and the IETC.

Option	Total ($m)	AS ($m)	FTC ($m)	IWTC ($m)	IETC ($m)
A1	$158	-$3	$143	$20	-$1
A2	$111	-$3	$115	-$1	$0
A3	$68	-$3	$90	-$20	$1
B	$103	-$5	$136	-$29	$1

Option A1 has the greatest fiscal cost as, although it consists of the smaller $5 increase, it offsets none of the extra cost with increased targeting (abatement). This means expenditure will be spread higher up the income scale. Option A3 has the smallest cost as it offsets the costs of its payment rate increase with a 2% abatement rate increase, more tightly targeting expenditure. Although option B has the highest payment rate increase of $7.50, the fiscal cost of this is partially offset by the largest abatement rate increase of 3%.

[27] Out of the 2,691,000 families in New Zealand.

[28] Out of the 1,155,000 children in New Zealand.

[29] Out of the 2,691,000 families in New Zealand.

[30] Out of the 1,155,000 children in New Zealand.

Winners and losers

The following table summarises the average gains and losses and the total winners and losers seen under each option. Results are presented both including and excluding the impact of counterfactual indexation.

Option	FTC increase per child		Abatement rate	Gains and losses for households (excluding CPI indexation)				Gains and losses for households (including CPI indexation)			
	Rate change	Total with CPI (eldest & subs. child)		Winners	Average gain	Losers	Average losses	Winners	Average gain	Losers	Average losses
A1	$5	$11.71 and $10.42	25% (No change)	316,000	$10	S	S	345,000	$20	s	s
A2	$5	$11.71 and $10.42	26%	287,000	$8	26,000	-$1	340,000	$18	s	s
A3	$5	$11.71 and $10.42	27%	223,000	$8	89,000	-$6	330,000	$16	8,000	-$1
B	$7.50	$14.21 and $12.92	28%	223,000	$12	89,000	-$8	309,000	$20	27,000	-$3

To assess the targeting of the gains and losses of these options these results have been modelled by income distribution. The following graphs are divided by their exclusion or inclusion of the impacts of counterfactual indexation and by their income measure in the following order:

- Exclusion of counterfactual, by taxable income
- Exclusion of counterfactual, by HEDI[31]
- Inclusion of counterfactual, by taxable income
- Inclusion of counterfactual, by HEDI

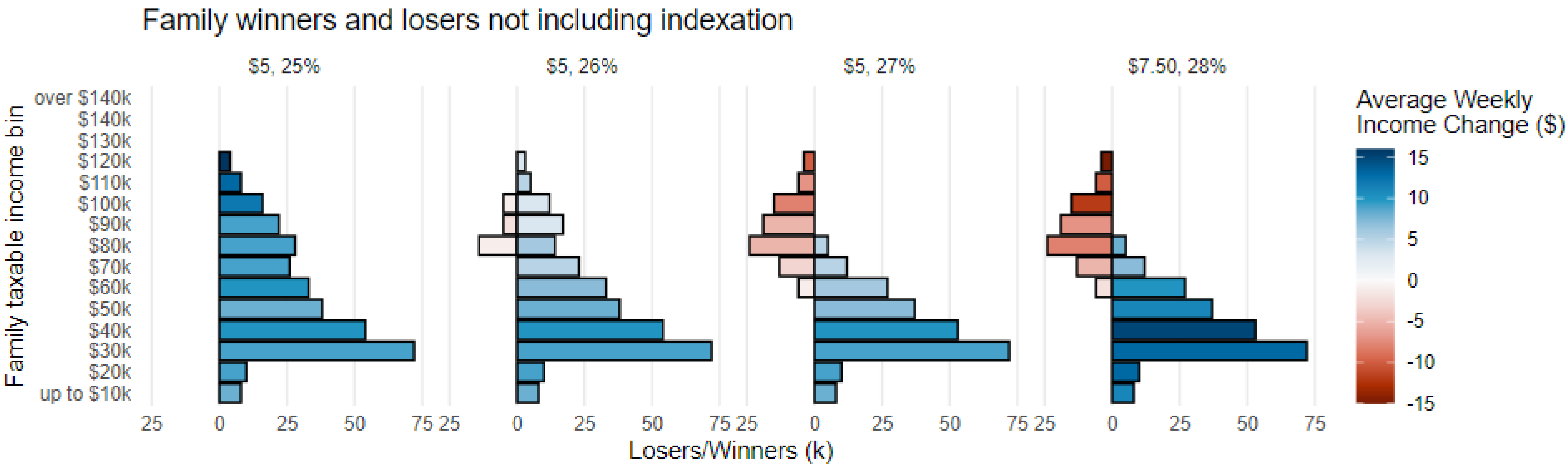
Graphs excluding the impacts of counterfactual indexation will demonstrate the real value of each option versus doing nothing. Graphs including these impacts will demonstrate what customers will experience if one of these options is introduced alongside indexation in April 2022.

Graphs using taxable income band demonstrate the actual income available to families who are experiencing the gains or losses. Graphs using household equivalised disposable income (HEDI) adjust income for household size. This removes anomalies seen in taxable income graphs where greater average gains appear to be received by higher income bands when this is merely a result of larger families receiving greater entitlements to meet their greater needs.

[31] HEDI refers to Household Equivalised Disposable Income which is household total income, net of tax, adjusted to allow comparison of income adequacy between households with different composition. This involves an equivalisation factor that accounts for the number and age of household occupants and economies of scale. TAWA and official child poverty metrics use OECD equivalisation, where HEDI = DI/(1+0.5*(N_GTE14-1) + 0.3*N_LT14). It is essentially a per-person, disposable income where the first person 14 or older counts as 1 person, subsequent people 14 or older count as 0.5 and each child under 14 years counts as 0.3.

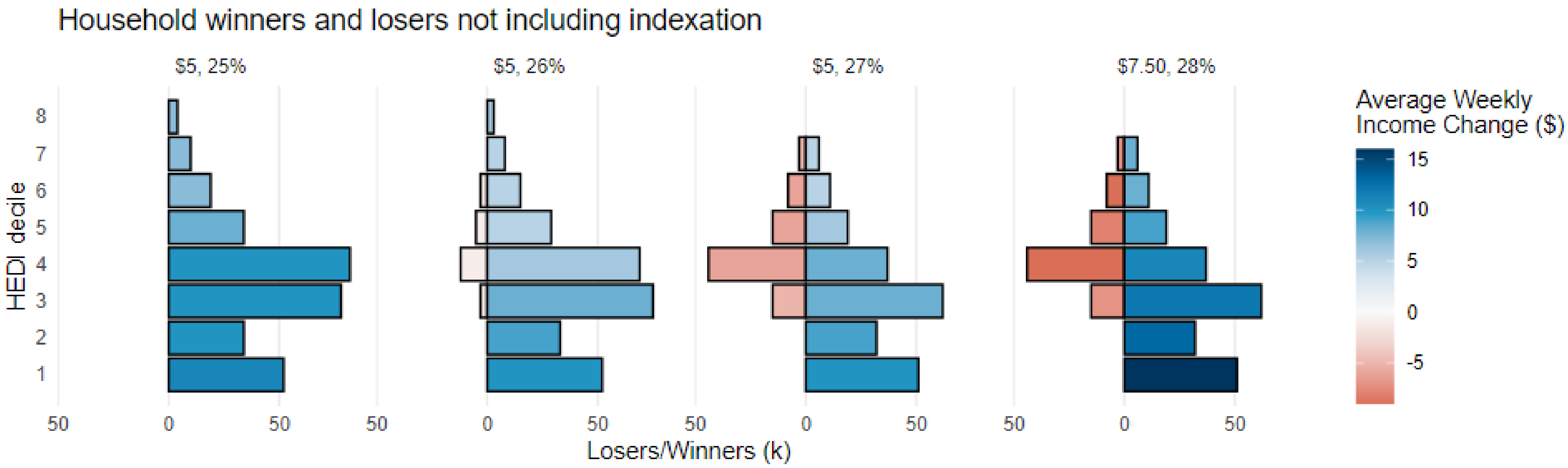
Impacts excluding counterfactual indexation, by taxable income

Options are in order from A1 on the left to B on the right.



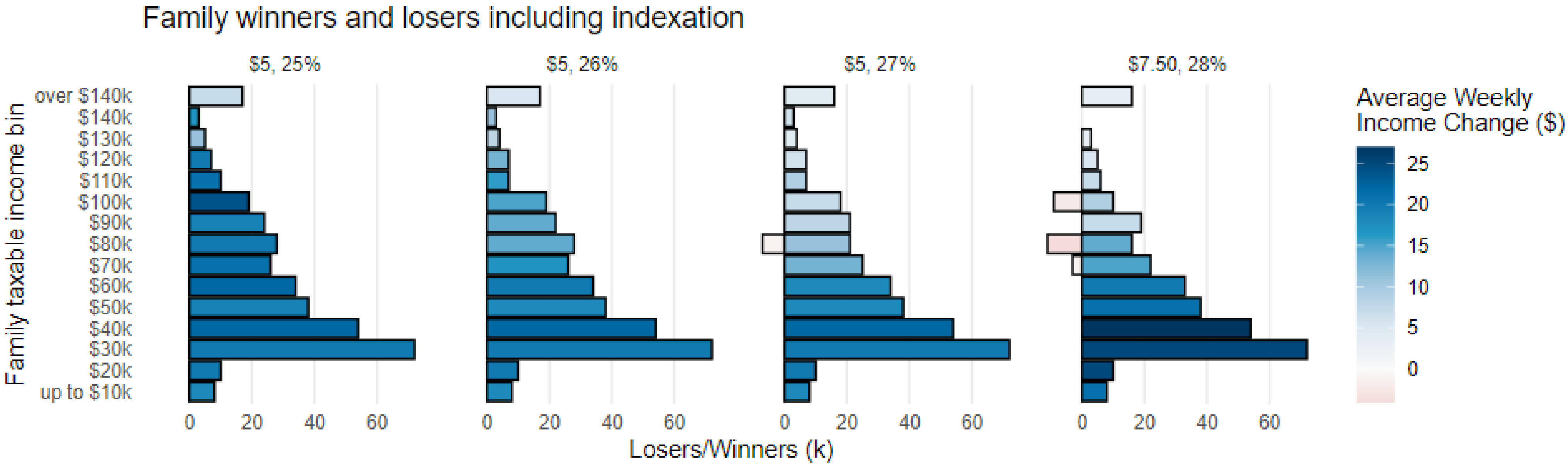
A1 is the only option without losers as it is the only option that does not increase targeting through abatement rate increases. However, A1's greatest weekly increases appear to be in the highest income bands. This may be because families who are receiving the FTC with higher incomes have multiple children, and therefore they would receive the $5 increase per child per week. Option B creates the greatest weekly gains, albeit with the greatest losses. However, the gains are targeted to benefit low-income families, with increases averaging from $11 to $15 p/w in the $0-60k income bands while losses only occur for families earning $60k or more a year.

Impacts excluding counterfactual indexation, by HEDI



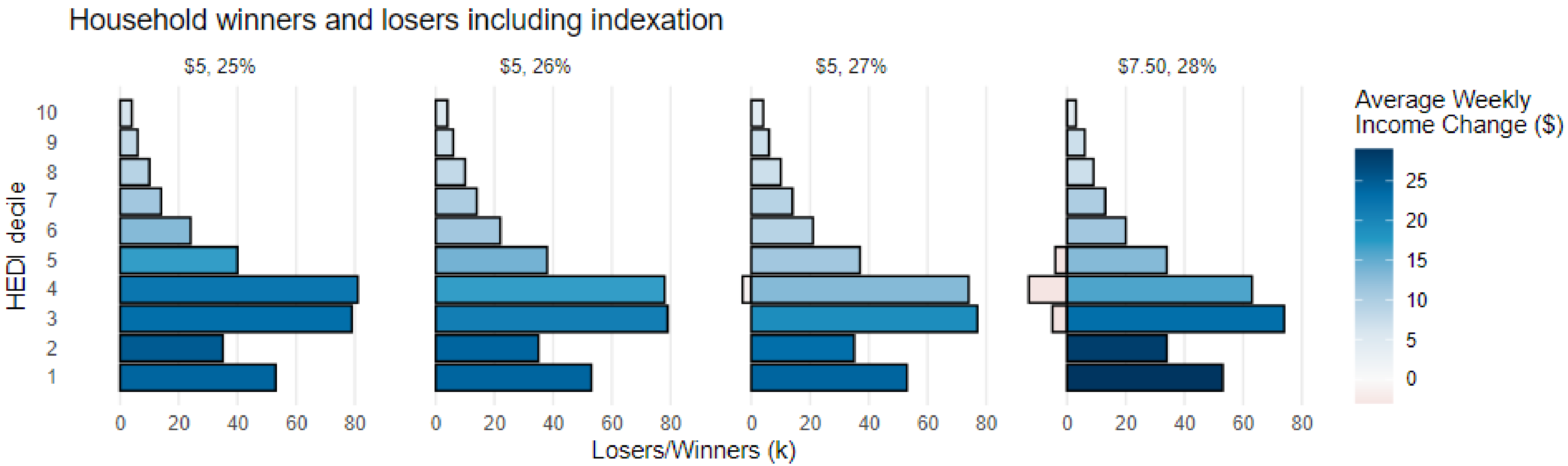
Measuring by HEDI demonstrates that, despite what the previous graph might imply, option A1 provides the greatest gains ($10 to $11 p/w) to families with the greatest need. However, it still spreads expenditure higher up the income bands than other options as it is not combined with an abatement rate increase. This makes it less effectively targeted than the other options as a smaller proportion of its (much larger) fiscal cost is concentrated towards lifting children out of poverty. However, this less targeted expenditure will still be beneficial to other low- and medium-income families as it will improve their income adequacy.

Impacts including counterfactual indexation, by taxable income



When options are combined with counterfactual indexation very few customers experience losses. Similar to the results in the previous graphs, option B produces the largest weekly increases (from $20 to $27 p/w) for families in the bottom income bands ($0-60k) while options A2 and A3 produce lower increases ($18 to $22 p/w for the same bands). Although option B still produces some losers in the >$60k income bands, on average customers in these bands experience increases of $3 to $15. When combined with indexation, option A1 produces average gains of around $20 p/w spread reasonably evenly across income bands.

Impacts including counterfactual indexation, by HEDI



As was also demonstrated by the previous HEDI graph, most of the expenditure for each option will be concentrated in families with the greatest need. Although A1 (when combined with indexation) appeared to provide a total average gain of $20 when measured by family taxable income, when measured by HEDI, the first four deciles see average gains of $22 to $25 p/w with $6 to $17 gains in the upper deciles. The targeting of option B also appears tighter when measured by HEDI, with average gains of $23 to $29 pw in the first three deciles and $4 to $16 in the higher deciles. However, this graph does raise concern that option B creates losers in the low- to middle-income deciles of 3, 4 and 5.

Work incentive impacts

The impact each option would have on a family's total income has been modelled to assess how the changes affect EMTRs[32] and PTRs[33] at different hours of work for different family types. The three example families are a sole parent, a couple with one earner and a couple with two earners. The

[32] How much of each extra dollar of income an individual will lose to tax, levies and abated social assistance.

[33] How much of the income received when entering work an individual will lose to tax, levies and abated social assistance.

examples assume each family has two children aged 2 and 5, has weekly rental costs of $500 and receives Accommodation Supplement (area 1) if eligible, earns $20 per hour, and pays ACC levy.[34]

The following table outlines the impact of the options on income and work incentives.[35]

Option	Impact		Sole parent	Couple with one earner	Couple with two earners[36]
	On income	By hours worked			
CF (excluding indexation)	Income after taxes and rental costs[37]	20	$731.06	$742.02	$939.66
		40	$767.88	$775.62	$1046.27
A1 ($5 FTC, 25%)	Income gain from work at	0-10 hours	$150.22	$134.22	$96.98
		10 to 20 hours	$99.77	$19.05	$67.07
		20 to 40 hours	$36.82	$33.60	$106.60
	Income change from CF	20	$9.10	$9.10	$9.10
		40	$9.10	$9.10	$9.10
	Change to EMTRs and/or PTRs		**None**	**None**	**None**

[34] These example families are for illustrative purposes only. The assumptions around rental costs follow the approach used by the WEAG; they assumed the families used were based in Manurewa, South Auckland (Accommodation Supplement Area 1), and that the families were paying rent in the lower quartile. As at September 2021, lower quartile rent for Manurewa is $500 per week.

[35] All data in the following table is taken from TAWA excluding PTR's which are taken from Inland Revenue internal data.

[36] Assumes that the primary earner works a fixed amount at 40 hours at $20 per hour, and the second earner earns $20 per hour.

[37] Status quo refers to 1 April 2022, post-CPI indexation.

A2 ($5 FTC, 26%)	Income gain from work at	0-10 hours	$150.22	$134.22	$96.30
		10 to 20 hours	$99.77	$18.80	$62.07
		20 to 40 hours	$36.82	$32.73	$102.60
	Income change from CF	20	$9.10	$8.84	$5.29
		40	$9.10	$7.97	$1.29
	Change to EMTRs and/or PTRs		**This option would minimally increase EMTRs by 1% beyond 40.95 hours of work once $66,956 of net income is exceeded.**	**This option would minimally increase EMTRs by 1% beyond 42.25 hours of work once $66,993 of net income is exceeded.**	**This option would increase EMTRs by 1% between 2.25 hours and 56.44 hours of work once $67,157 of net income is exceeded. Similarly, this option would increase PTRs by around 1% for the second earner entering the workforce.**
A3 ($5 FTC, 27%)	Income gain from work at	0-10 hours	$150.22	$134.22	$95.61
		10 to 20 hours	$99.77	$18.54	$63.07
		20 to 40 hours	$36.82	$31.86	$98.60
	Income change from CF	20	$9.10	$8.58	$1.48
		40	$9.10	$6.84	-$6.52
	Change to EMTRs and/or PTRs		**This option would increase EMTRs by 2% beyond 40.95 hours of work once $66,956 of net income is exceeded.**	**This option would minimally increase EMTRs by 2% beyond 42.25 hours of work once $66,979 of net income is exceeded.**	**This option would increase EMTRs by 2% between 2.25 hours and 54.35 hours of work once $67,143 of net income is exceeded. This option would increase PTRs by around 2% for the second earner entering the workforce.**

B ($7.50 FTC, 28%)	Income gain from work at	0-10 hours	$150.22	$134.22	$94.93
		10 to 20 hours	$99.77	$18.28	$61.07
		20 to 40 hours	$36.82	$30.99	$94.60
	Income change from CF	20	$13.65	$12.88	$2.22
		40	$13.65	$10.26	-$9.79
	Change to EMTRs and/or PTRs		**This option would increase EMTRs by 3% beyond 40.95 hours of work once $67,193 of net income is exceeded.**	**This option would increase EMTRs by 3% beyond 42.25 hours of work once $67,202 of net income is exceeded.**	**This option would increase EMTRs by 3% between 2.25 hours and 53.55 hours of work once $67,366 of net income is exceeded. This option would increase PTRs by around 3% for the second earner entering the workforce.**

This table demonstrates that the options have minimal or no impacts on work incentives due to the minor nature of their increases to the abatement rate. Option A1 will have no impact on work incentives and options A2, A3 and B will not impact the work incentives for a single earner family working full time on minimum wage.

However, options A2, A3 and B will impact families with higher wages and secondary earners in low-income households. They will have a minor (1-3%) impact on the EMTRs of single earner families who cross the abatement threshold (i.e. who earn above minimum wage). They will also impact the participation tax rate of secondary earners who already have very low work incentives, although this impact will also be limited to a 1-3% increase.

Overall, the increase in EMTRs is minimal and therefore unlikely to materially impact financial incentives to work.

Cumulative impact of changes

However, consideration should be given to the accumulation of abatement rate changes over time. For example, as part of the Families Package changes in 2018, the WFF abatement rate increased from 22.5% to its current 25% setting. When WFF was first introduced (between 2004 and 2007), the abatement rate was 20%. These changes, particularly when considered with the Ministers' preferred option, represent a significant increase in abatement rate in a relatively short period.

Distributional impacts

These options are targeted towards low-income families (beneficiary or otherwise) receiving the FTC. Modelling has taken place for their impact on families in different income bands (all positive for those earning <$60k annually[38]) and children in poverty (all positive) but not for other specific groups such as Māori, women, or those with disabilities.

It is likely that there will be a disproportionate impact on Māori when any changes are made within the tax and transfer system because they are over-represented in the benefit system. As at November 2018, Māori made up 15% of the New Zealand population, but 36% of benefit recipients (Welfare Expert Advisory Group 2018 Welfare System: statistics).

The impact of the options on other groups may be proportionate to their representation in the target group of low-income families. Inland Revenue cannot model these impacts as it does not collect data on gender, ethnicity, or disability. Time constraints have further limited the ability to access and analyse relevant data that may be held by external sources.

Option to pass on FTC increase to other caregivers – distributional impacts (Oranga Tamariki comment)

Passing on the FTC increase to the rates of the OB, UCB and FCA would also impact children and Māori - There are around 24,000 children being cared for by around 15,000 caregivers, both inside and outside of the State care system. Over half of children living with caregivers are Māori, and a significant proportion of their caregivers are also Māori.

Stakeholder support

No stakeholder feedback is available for these options as they are budget sensitive. Previous feedback from the WEAG supports increases to the FTC with a preference for universalism over tight targeting which indicates that they would not be in favour of options which increase abatement rates (options A2, A3 and B).

Option to pass on an increase in FTC to other caregiver payments

There is also an option to pass on any increases to the FTC to rates of OB, UCB and FCA. There are around 24,000 tamariki being cared for by around 15,000 caregivers, both inside and outside of the State care system. Caregivers who received OB, UCB and FCA do not qualify for FTC for the same child. However, increases to FTC rates have resulted in commensurate increases to the base rates for OB, UCB and FCA in 2005, 2007 and 2018. Most recently OB, UCB and FCA rates were increased in July 2020 by $25 per week, in line with increases to main benefits, to support caregivers against the impacts of COVID-19 and support placement stability.

[38] This reflects the impact of the options alone, without including the impact of counterfactual indexation.

Currently rates of OB, UCB and FCA are between $89 and $152 higher than the eldest child rate of FTC. This reflects the higher levels of support provided to caregivers who are caring for children when their parents are unable to, and reflects that caregivers receiving OB, UCB and FCA do not have access to some of the same supplementary assistance as other families, such as the dependent child rate of Accommodation Supplement.

The costs associated with passing on the FTC rate increase to other caregiver payments are summarised in the table below.

Increased base payment ($,000s)	2021/22	2022/23	2023/24	2024/25	2025/26 & outyears	Forecast period Total	Average per annum
Increase of $5	$1,730	$7,224	$7,605	$7,933	$8,302	$32,794	$8,199
Increase of $7.50	$2,595	$10,836	$11,408	$11,899	$12,453	$49,191	$12,298

The payments made to caregivers are not taxable. The payments made are outside the WFF regime and they do not directly affect the WFF review phase one options considered in this RIS.

How do the options compare to the counterfactual?

	CF	A1 ($5 FTC, 25%)	A2 ($5 FTC, 26%)	A3 ($5 FTC, 27%)	B ($7.50 FTC, 28%)
Child poverty impact	0	+ *Modelling suggests that this option will lift 9,000 children from AHC50 poverty or 5,000 from BHC50 poverty.*	+ *Modelling suggests that this option will lift 9,000 children from AHC50 poverty or 5,000 children from BHC50 poverty.*	+ *Modelling suggests that this option will lift 8,000 children from AHC50 poverty or 5,000 children from BHC50 poverty.*	+ *Modelling suggests that this option will lift 10,000 children from AHC50 poverty or 7,000 children from BHC50 poverty.* ***Of the options, this has the greatest impact on child poverty.***
Fiscal cost	0	- *This option has an estimated fiscal cost of $158m for T22/23. It is the most expensive option and outside of Minister's preferred fiscal envelope.*	- *This option has an estimated fiscal cost of $111m for T22/23.*	- *This option has an estimated fiscal cost of $68m for T22/23.* ***This is the least expensive option.***	- *This option has an estimated fiscal cost of $103m for T22/23.*
Work incentive impact	0	0 ***No impact***	- *Minor (maximum of 1% increase in EMTRs over an income threshold)* .	- *Minor (maximum of 2% increase in EMTRs over an income threshold)* .	-- *Minor (maximum of 3% increase in EMTRs over an income threshold)* .
Phase two impact	0	- *This option may limit the range of options available under phase two to a*	- *This option may limit the range of options available under phase two to a*	- *This option may limit the range of options available under phase two to a*	-- *This option may limit the range of options available under phase two to a minimal degree*

		minimal degree due to its fiscal cost (not design solution).	*minimal degree due to fiscal cost and increase of the abatement rate.*	*minimal degree due to its fiscal cost and increase of the WFF abatement rate*	*due to its fiscal cost and increase of the WFF abatement rate*
Overall assessment		*This option improves child poverty without creating losers or decreasing work incentives. However, its fiscal cost is outside of the range set by Ministers.*	*Although this improves child poverty, it reduces fiscal cost at the expense of work incentives, phase two options and support for medium-income families.*	*Although this improves child poverty, it reduces fiscal cost at the expense of work incentives, phase two options and support for medium-income families.*	*Although this improves child poverty, it reduces fiscal cost at the expense of work incentives, phase two options and support for medium-income families.*

Key:

++	much better than doing nothing/the status quo/counterfactual
+	better than doing nothing/the status quo/counterfactual
0	about the same as doing nothing/the status quo/counterfactual
-	worse than doing nothing/the status quo/counterfactual
- -	much worse than doing nothing/the status quo/counterfactual

What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

The narrow scope for final options means all are essentially minor variations on the same changes (an increase in FTC rates and the WFF abatement rate). Consequentially, the differences between options are relatively minor. The minor nature of these differences increases the impact of the statistical uncertainty involved in modelling. This is particularly true of the child poverty impacts.

Option B lifts the greatest number of children from poverty: 10,000 when measured against AHC50 which is 1,000 more than the next best option (A1). At an annual cost of $103m, option B also roughly meets the modest fiscal budget set for phase one due to its 3% abatement rate increase, which effectively targets the greatest support to those most in need.

However, although option B best fits Ministers' commissioning and most of their objectives, it has several drawbacks. Compared to the counterfactual, it makes losers of some medium-income families, and of all the options, it has the largest negative impact on EMTRs and PTRs which are already very high. It may also limit the range of options available under phase two of the review due to its 3% increase of the WFF abatement rate. Options A2 and A3 face the same issues to lesser degrees, but with lower child poverty impacts.

Option A1 increases support without changing abatement settings. This would lift 9,000 children from AHC50 poverty without creating losers or reducing incentives to work. However, option A1 has the largest annual fiscal cost of $158m and therefore falls outside the fiscal cost parameters set by Ministers. The high fiscal cost may also potentially limit the range of options available under phase two of the review

What are the marginal costs and benefits of the option?

Ministers have indicated that they prefer option A3: a $5 FTC increase and 27% abatement threshold.

All impacts of this option have been modelled using Treasury's TAWA which assumes full take-up and does not account for relationship changes. All outputs relate to the impact of the options excluding CPI indexation.

Option	Affected groups	Comment	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action				
A3 ($5 FTC increase, 27% abatement rate)	WFF recipients	*89,000 households will see a decrease in weekly income, compared to the counterfactual. This assumes full take-up*	*Average weekly decrease of -$6*	*Medium certainty as assuming full take-up impacts accuracy.*
		Increase in EMTRs of 2% above 42 hours at minimum wage[39]	*Low*	*High*
	The government	*Ongoing, annual fiscal cost. This assumes full take-up.*	*$68m*	*Medium certainty as assuming full take-up impacts accuracy.*
	Total monetised costs	*Ongoing, annual fiscal cost. This assumes full take-up.*	*$68m*	*Medium certainty as assuming full take-up impacts accuracy.*
		Average weekly decrease in income	*-$6*	*Medium certainty as assuming full take-up impacts accuracy.*
	Non-monetised costs	*Increase in EMTRs and PTRs of 2% above 42 hours at minimum wage*[40]	*Low*	*High*

[39] Once FTC/IWTC payments start to abate. This reflects the couple with one earner family type.

[40] Once FTC/IWTC payments start to abate. This reflects the couple with one earner family type.

	Additional <u>benefits</u> of the preferred option compared to taking no action			
A3 ($5 FTC increase, 27% abatement rate)	WFF recipients	*223,000 households will benefit from an ongoing, weekly increase in income. This assumes full take-up.*	*Average weekly increase of $8.*	*Medium certainty as assuming full take-up impacts accuracy.*
	Children in poverty	*Although the rate increase is ongoing, we cannot predict the duration of its impact. Lifting the income of a child's family above a threshold does not guarantee that they will no longer suffer the effects of poverty or that their income will remain above the threshold permanently.*	*8,000 children lifted out of AHC50 poverty or 5,000 out of BHC50 poverty.*	*Low. There are significant uncertainties with TAWA modelling for poverty metrics.*
	Total monetised benefits	*223,000 households will benefit from an ongoing, weekly increase in income. This assumes full take-up.*	*Average weekly increase of $8.*	*Medium certainty as assuming full take-up impacts accuracy.*
	Non-monetised benefits	*Although the rate increase is ongoing, we can not predict the duration of its impact. Lifting the income of a child's family above a threshold does not guarantee that they will no longer suffer the effects of poverty or that their income will remain above the threshold permanently.*	*8,000 children lifted out of AHC50 poverty or 5,000 out of BHC50 poverty.*	*Low. Treasury warns that the uncertainties of TAWA modelling are particularly significant for poverty metrics.*

Section 3: Delivering an option

How will the new arrangements be implemented?

The proposals would require amendments to the Income Tax Act 2007. The preferred option will be included in urgent primary legislation prior to December 2021. The proposed timeframe allows sufficient time for Inland Revenue and MSD to implement the necessary system changes.

Inland Revenue will be responsible for the implementation of the proposed changes, and as part of its business-as-usual function. MSD will be responsible for implementing the proposed changes for those who receive their WFF payments from MSD.

The new FTC rates and/or WFF abatement thresholds will be used to calculate recipients' entitlements from 1 April 2022 and will be reflected in the notices of entitlement that Inland Revenue sends to recipients from February as part of the annual 'rollover' process

How will the new arrangements be monitored, evaluated, and reviewed?

The effects of the proposed changes can be monitored using data Inland Revenue currently collects as part of administering WFF. This data includes the number of WFF recipients, the makeup of those families, the amount and type of payments made, and end of year assessment data on under and overpayments. This administrative data provides descriptive information about WFF recipients, and the actual fiscal cost to the Government of the chosen settings. MSD holds data about the WFF payments (FTC and Best Start) they make to main benefit recipients.

The agencies who are involved in the WFF review are currently discussing how any changes that are progressed as part of the broader WFF review will be evaluated.

Item 10

Inland Revenue
Te Tari Taake

MINISTRY OF SOCIAL DEVELOPMENT
TE MANATŪ WHAKAHIATO ORA

Tax policy report: Working for Families Review – Public Engagement

Date:	21 July 2022	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2022/274 REP/22/7/676

Action sought

	Action sought	**Deadline**
Minister of Revenue	**Note** the contents of this report	25 August 2022
Minister for Social Development and Employment	**Note** the contents of this report	25 August 2022

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**
Murray Shadbolt	Policy Lead (Acting), Inland Revenue	s 9(2)(a) s 9(2)(a)
Leah Asmus	Principal Analyst, Ministry of Social Development	s 9(2)(a)

21 July 2022

Minister of Revenue
Minister for Social Development and Employment

Cc: Rt Hon Jacinda Ardern, Prime Minister/Minister for Child Poverty Reduction
Hon Grant Robertson, Minister of Finance
Hon Kelvin Davis, Minister for Children

Working for Families Review – Public Engagement

Executive summary

1. Public engagement to inform the Review of Working for Families (WFF) took place from April to June 2022. The engagement sought feedback on how the current system of WFF could be improved to better meet the needs of whānau in Aotearoa. It did not seek feedback on proposed options for change and was not intended to be a representative sample.

2. We received 585 survey responses, 53 written submissions and ran 16 sessions with key stakeholders. The majority of feedback was from advocacy groups (or individuals connected to such groups) concerned with child poverty and broader social policy concerns, both in written submissions and targeted sessions with key stakeholders, and this is reflected in the feedback we received.

3. Through engagement we heard fairly consistent feedback from a large number of stakeholders and submitters that:

   3.1 Many whānau are struggling with inadequate incomes, and the recent increase in the cost of living and the housing crisis are putting pressure on whānau.

   3.2 Reducing child poverty and improving outcomes for children is important (although stakeholders had differing views on how to achieve better outcomes).

   3.3 Indexation of payments and thresholds is important to maintain support over time.

   3.4 Current rates of abatement are too high, and act as a disincentive to work or to increase hours.

   3.5 Supporting whānau with the costs of work is important, particularly childcare and transport costs.

   3.6 Debt is a significant issue that acts as a barrier to take-up and has a negative impact on whānau wellbeing.

   3.7 The current system is too complex to navigate, and is not designed for diverse family types or families with variable income and circumstances.

4. However, in other areas we heard opposing views from stakeholders and submitters, for example:

   4.1 Roughly half of stakeholders and submitters told us that reducing child poverty and improving income adequacy should be the sole objectives of

WFF, while other stakeholders urged us to retain the objective of supporting work incentives.

4.2 Around half of stakeholders and submitters argued the In-Work Tax Credit (IWTC) should be paid to all families, regardless of work and benefit status, while a minority cautioned against this due to the reduction in incentives to move off benefit and into paid employment.

4.3 About 30% of submitters and almost half of targeted engagement stakeholders were supportive of increasing rates of payment, especially for those on the lowest incomes, while a minority thought more support should be provided to working families or through alternative labour market mechanisms which do not increase the cost of welfare.

5. The whānau Māori groups whom officials met with through targeted engagement also provided feedback on various aspects of WFF, including:

5.1 The high costs of living and the financial stress faced by many whānau, in particular due to debt. Some whānau Māori emphasised the important role of other family members (such as grandparents) in caring for tamariki, and the need to provide these family members with financial support.

5.2 Many whānau Māori want to work but face barriers, such as the lack of certainty posed by variable income/hours and the need to support the wider community through unpaid 'heart mahi'. Whānau Māori highlighted the value of unpaid mahi and wanted this to be recognised as 'work'.

5.3 Trust and relationships are important to Māori, and they had a general preference for face-to-face meetings. They noted the impact that past negative experiences with government support can have on WFF take-up. Māori emphasised the need to improve communications with them, and proactively at that, to improve take-up.

5.4 The obligations the Crown has under Te Tiriti o Waitangi to support equitable outcomes for tamariki Māori and their whānau should be acknowledged.

6. The suggestions for change raised through engagement are broadly consistent with the types of options officials are exploring. The engagement provided useful insight into the types of changes stakeholders with different objectives are likely to support.

7. Stakeholders and submitters with a focus on child poverty reduction and income adequacy suggested options for change such as:

7.1 Removing the paid work requirements from WFF so all payments are available regardless of benefit/work status, and renaming the system to reflect a focus on children.

7.2 Increasing the rate of payment, in addition to rolling the IWTC and the Minimum Family Tax Credit (MFTC) into the Family Tax Credit (FTC).

7.3 Increasing the FTC abatement threshold and reducing the abatement rate.

7.4 Providing greater support through childcare subsidies and subsidised transport to work.

8. Stakeholders and submitters who supported the objective of improving work incentives and making work pay suggested options such as:

8.1 Reducing the abatement rates of the FTC and IWTC, to incentivise increasing hours of work and reduce effective marginal tax rates.

8.2 Providing support for income adequacy through mechanisms outside of welfare support, such as support for training/study and wage increases.

8.3 Providing more support when people are transitioning into work, such as temporarily providing extra support when a person resumes work.

8.4 Providing support for the costs of work, such as childcare and transport costs.

8.5 Making changes to the system to allow for greater variations in income and changes in circumstances.

9. Other suggestions to improve how the system functions included:

9.1 Making changes to reduce debt creation, such as shorter income assessment periods, and the introduction of grace periods or a buffer credit.

9.2 Increased debt write-off and hardship provisions.

9.3 Improving access to information and support, especially for families with a disability or where English is a second language.

9.4 Moving to a single payment agency, preferably Inland Revenue (IR).

10. In conjunction with this report, Ministers will receive a report covering evidence and key concerns relating to WFF, and high-level options for change. Feedback from engagement has been used to support the development of those options, and a summary of relevant feedback from consultation has also been provided in that report to support your assessment of the options.

Recommended action

We recommend that you:

11. **note** the contents of this report.

Noted Noted

12. **agree** to publicly release this report, subject to any redactions under the Official Information Act

Agreed / Disagreed Agreed / Disagreed

s 9(2)(a)

Murray Shadbolt
Policy Lead (Acting)
Inland Revenue

s 9(2)(a)

Leah Asmus
Principal Analyst
Ministry of Social Development

Hon David Parker
Minister of Revenue
/ /2022

Hon Carmel Sepuloni
Minister for Social Development and Employment
/ /2022

Background

13. In February 2022, Ministers agreed to proceed with both written and public engagement on the Review of Working for Families (REP/22/2/067; IR2022/053 refers). Public engagement on Working for Families (WFF) with submitters and stakeholders took place from 20 April to 31 May 2022. Members of the public were able to respond to an online survey and/or provide a written submission via email. We received 53 written submissions and 585 survey responses. For privacy reasons, we have not linked the specific feedback to individual stakeholders/submitters.

14. Officials held 16 targeted engagement sessions over May and June 2022, four of which were specifically with whānau Māori. A total of 41 stakeholder groups attended the targeted engagement sessions overall. Appendix 4 sets out the key questions officials asked stakeholders at these sessions.

15. The majority of feedback we received through written submissions and targeted engagement was from advocacy groups, and individuals connected to these groups, who have a strong focus on reducing child poverty. A very small number of submitters and stakeholders provided feedback with a more business-focussed or work incentive lens. This is reflected in the feedback we received and should be taken into account when reading this report.

Purpose of this report and key themes from engagement

16. This report briefs Ministers on the feedback received from the public engagement. The feedback is presented as the view of the stakeholder/submitter, with no supplementary commentary from officials. It is divided into ten sections, which are written so they can be read independently of each other:

    16.1 Objectives of WFF (page 5).

    16.2 Work incentives and the cost of work (page 6).

    16.3 Income adequacy and the level of support provided (page 9).

    16.4 Changing circumstances and variable income/hours (page 10).

    16.5 Debt (page 11).

    16.6 Complexity of WFF (page 14).

    16.7 Different types of families and whānau (page 14).

    16.8 Perspectives from Māori whānau (page 16).

    16.9 Perspectives from Disabled people and their families (page 17).

    16.10 Administration, accessibility, and take up (page 19).

17. The first three appendices contain further comments from submitters and stakeholders on WFF:

    17.1 Appendix 1 - Additional feedback from Māori on WFF (page 22).

    17.2 Appendix 2 - Technical comments on the specific WFF tax credits (page 23).

    17.3 Appendix 3 - Other points raised in submissions and targeted engagement (page 25).

18. Alongside this report, Income Support Ministers will receive a report summarising evidence and key issues relating to WFF, and high-level options to address these. Where relevant, findings from engagement have also been included in that report.

Objectives of WFF

Child poverty and making WFF more child-centric

19. Roughly half of stakeholders/submitters expressed a strong preference for WFF to become more child-centric and equitable, and said that its objectives should be to reduce child poverty and ensure income adequacy rather than to provide work incentives. A small number of people referred to the Child Poverty Reduction Act 2018, the United Nations Convention on the Rights of the Child, the Universal Declaration of Human Rights, and the Child and Youth Wellbeing Strategy.

> *"To make WFF 'work' for families and in particular effective in reducing child poverty, this income support needs to be about children first and foremost and completely disconnected from incentives to work."*

20. Many of these stakeholders/submitters thought the same amount of WFF should be paid regardless of work or benefit status, to ensure children received the same level of support. They emphasised the value of unpaid work, such as parenting and voluntary work, and recommended that this unpaid work qualify as 'work' for WFF. Some said that current settings were discriminatory for families in receipt of benefits, and that families should not be kept in poverty to incentivise them to work. A number of these stakeholders/submitters recommended changing the name of WFF, so that its emphasis was on supporting children (or families with children) rather than on paid work.

> *"WFF discriminates against parents who receive benefits. There is a lack of acknowledgement of the importance of WFF tax credits in reducing child poverty. And WFF fails to acknowledge the valuable unpaid work of parenting. Families on benefits must receive the full package of WFF tax credits."*

Support for providing financial incentives to work

21. A small number of people supported work incentives remaining one of WFF's objectives. At one session, stakeholders commented that while many may recommend paying the IWTC to all families including those not in paid work, the underlying issue of benefits not providing families with adequate incomes should be kept separate from financial incentives to work. That is, if incomes are not adequate, this is a separate issue to how and whether work incentives should be provided. These stakeholders suggested that using different tools to address these two distinct issues could help prevent the issues being conflated, and instead of using WFF to fulfil both objectives, separate support could be put in place to address each issue (see paragraph 39 for comments regarding an Earned Income Tax Credit).

> *"[Organisation] recognises the social, emotional and financial benefits of being employed, and supports that the tax credits policy remains as an incentive to encourage people into paid work."*

22. At another session, stakeholders argued that removing the IWTC's work requirement would undermine the policy intent of WFF, which was largely about work incentives and making work pay. They suggested that people who advocated for removing the work requirement did so because it was easier to modify an existing tax credit than to introduce a new one (such as a universal child tax credit).

23. Half of survey respondents thought the objectives of financially supporting low/middle-income families regardless of whether they were in paid work, and supporting families to get into and stay in paid work, were both equally important.

Work incentives and the cost of work

Cost of work

24. Work-related costs (such as childcare and transport costs, and having to purchase new clothes for work) were raised at more than half of the targeted engagement sessions. It was noted that the cost of childcare was now very expensive, and that it was "very devaluing" if a parent's income from work was less than what they paid for childcare. One submitter said childcare costs were greater for sole-parent families, because there were no other adults in the family available to look after children while the sole-parent was at work.

> *"On top of the abatement will often be childcare fees. Therefore, the total cost of a parent returning to the workforce will be the reduction in WFF payments plus the cost of childcare. This could easily be sufficient to dissuade many parents from returning to the workforce."*

25. Some mentioned the opportunity cost of returning to work. Working parents could not look after their children, might not be able to take children to/from school, and had less time to source affordable food/essentials. They said this made some parents feel that work was not worthwhile, and could result in some only returning to work if they were promoted or offered flexible work hours.

> *"For parents the decision to engage in work brings with it a series of trade-offs for both them and their tamariki, that add to the already demanding and important mahi of caring for the next generation."*

26. Some noted that while discounted public transport could help with work-related costs, public transport was not available in all areas and fuel was now very expensive. Some stakeholders said that people in shift work, or with multiple jobs, often incurred comparatively greater costs, because they had to travel between job sites or pay for childcare outside of usual work hours. Some also noted the extra work costs and challenges disabled people face (see paragraph 89 for more information).

Current settings and work incentives

27. A number of people said current settings did not sufficiently reduce barriers to work, and therefore failed to effectively incentivise work. One stakeholder group felt that more support was needed for people on benefit transitioning into work, including when WFF recipients were still partially on benefit but in work as well.

28. Two submitters were concerned that providing WFF to people on benefit reduced work incentives too much, as the level of income received while on benefit could make working not worthwhile for some people. Another submitter said WFF and other support created incentives for recipients to misrepresent their incomes, so that they could continue to receive the same level of WFF/support even if they also received other income (e.g., from work). This submitter expressed concern about generational welfare, and the impact providing extra support for multiple children in a family could have on incentives.

29. Most survey respondents thought the availability of WFF was something people thought about when considering whether to take part in work. The majority of

respondents agreed that the IWTC, MFTC and the Best Start Tax Credit (BSTC) were important considerations for families when considering whether to take part in work. Most respondents also thought the amount of money a family received from WFF influenced the number of hours they worked.

Impacts of abatement on work incentives

30. A fifth of submitters said that the current abatement system is problematic. They said WFF currently begins abating at too low an income level, and that the abatement rates are too high. This resulted in high effective marginal tax rates (EMTRs) and a low return from work or increased hours, which was a barrier to work for some families. The current settings could result in there being little incentive to maintain or increase hours, especially given the trade-off of time spent with whānau.

> *"The Government also needs to change abatement thresholds, so that those with part-time work or low paid work can keep more of the money they earn. When abatement happens, it should be at a much lower rate, so that work becomes a worthwhile investment."*

31. One submitter said that WFF 'has all the makings of a poverty trap'. They said that WFF, and current abatement settings in particular, could make accepting promotions at work less worthwhile:

> *"The disincentives for lower-paid earners to raise their incomes above the abatement threshold mean that while the package has short-term benefits as a cash boost to incomes, it has marginal if not negative benefits over the medium to long term."*

32. A couple of people highlighted the compounding effect of abatement when WFF and the Accommodation Supplement were combined, because they abate at 27% and 25% respectively. They noted that this exacerbated existing issues with high EMTRs, and had a negative impact upon income adequacy and work incentives. High EMTRs were seen as particularly problematic, and it was suggested that improving the abatement system could help decrease EMTRs.

33. Most survey respondents thought it was more important for WFF to support as many families as possible while abating slowly, rather than providing more support to people on the lowest incomes but abating quickly.

Mixed views on IWTC as a work incentive

34. One stakeholder group said the IWTC positively impacted on sole-parent participation but negatively impacted on second-earner participation. Overall, they felt the IWTC was not a particularly effective work incentive tool, but that it helped with in-work costs. A small number of people said some customers were motivated to transition off benefit because they were tired of having their life examined by MSD, or took pride in coming off benefit, so preferred receiving tax credits when they returned to work (instead of remaining partially on benefit).

35. Many wanted to repeal the IWTC, or merge it into the FTC, so that all families on WFF received the IWTC whether they were on benefit or in paid work (refer to paragraphs 19 and 20 for discussion on making WFF more child-centric). They felt that removing the IWTC would have little impact on work incentives.

> *"Other factors that determine a parent's propensity for work include previous labour force engagement, skills and education, the restraints*

and costs of childcare and transport, mental and physical health, [and] workplace culture."

36. One submitter said current settings assumed parents lacked incentives to work and therefore required financial incentives, but that this was not supported by research.

> *"[T]he central premise of WFF around supporting only whānau that are in employment is discriminatory and does not achieve the intended goal of encouraging people into paid employment, or support whānau who are in poverty."*

Ideas from submitters and stakeholders

37. Various ideas were put forward on how to improve work incentives and reduce barriers to work:

37.1 **Provide a higher entitlement rate or lump sum, or phase support payments out over a longer period, when a parent first returns to work.** This could be done for the first six to twelve months of employment, for example. This would help with the costs of going back to work, similar to how students receive support for course-related costs when they start studying.

37.2 **Raise and index the abatement thresholds.** People suggested raising the thresholds to between $47,000 and $60,000. One submitter disagreed with increasing thresholds, and suggested decreasing thresholds instead, to minimise the disincentives to work for low-income families.

37.3 **Change the abatement rate.**

37.3.1 **20% of submitters supported lowering abatement rates**, because doing so could improve EMTRs and work incentives. Most suggested lowering the rate to 20%.

37.3.2 **Around 10% of submitters suggested having multiple abatement rates**, such as having two rates or the tiered rates Welfare Expert Advisory Group (WEAG) suggested. This would ease the pressure for low/middle-income families, but ensure higher rates applied to high-income families for whom WFF was less likely to make a material difference.

37.3.3 A small number of submitters strongly recommended **aligning WFF with other income support thresholds and abatements to moderate interactions with tax thresholds**. These currently created very high EMTRs for low/middle-income earners, which was particularly problematic. One suggestion was to apply an overall abatement rate of 25% (and no more than 30% if a greater rate were preferred) to the Accommodation Supplement and WFF.

37.4 **There were mixed views on what changes, if any, should be made to the IWTC.** As mentioned above, many wanted to repeal the IWTC or merge it into the FTC. A small number of people recommended increasing the IWTC. One suggestion was adjusting the IWTC for inflation to $82 per week, plus $17 for the fourth and additional children. However, a couple of people cautioned against this because the IWTC abated last, and was therefore received by some families with relatively high incomes.

37.5 **Allow people to receive support if they are on benefit but also work part-time**, to help families transition off benefit and towards full-time work.

37.6 **Provide extra support to people with multiple jobs, who work outside of standard business hours, as well as to disabled people in work**, because they face extra costs.

38. **Some stakeholders suggested making employment-related costs, like public transport and childcare, more affordable**. Another idea was to give employers a tax break or an incentive to provide childcare, particularly for shift workers and people who work outside of standard business hours. It was noted that work could also be done to help people better understand what support they could receive when they returned to work.

39. **Some stakeholders and submitters supported introducing an earned income tax credit (EITC) as an alternative to the IWTC and the MFTC**, as recommended by the WEAG. An EITC would provide a work incentive for all people, and would reward part-time work performed while on benefit. A small number of people did not support introducing an EITC.

Income adequacy and the level of support provided

40. Many people commented on recent rises in the cost of living, including the impact of COVID-19 and high inflation. They said income inadequacy could cause families significant stress and WFF did not provide sufficient support. One stakeholder said some families really struggled to withstand even the most minor life shocks. Many were very concerned about increased housing costs, and some referred to recent high interest rates. They said that current abatement rates and payment levels did not provide enough support to keep children out of poverty, even for parents on the median wage. One submitter expressed concern that the lack of adequate support for working parents with children would lead to more families moving to Australia, because Australia had better systems for working parents with children.

> *"Whānau are unable to make changes and achieve their aspirations within a system which fails to acknowledge the increasing financial pressures they face."*

41. A small number of people emphasised how income inadequacy had to led to families getting into debt to meet basic needs, often borrowing money from predatory lenders, and that this could lead to extreme financial stress. One submitter referred to the WEAG sample budgets (as updated by Fairer Futures earlier this year) for various household types, which highlighted income deficiencies. They emphasised that despite a modest real improvement in incomes, families still experienced income deficiencies. A small number of people said some WFF recipients struggled with wanting to be honest about income changes but also not wanting to risk losing support, with some working under the table to keep their entitlements.

42. Current abatement settings were also raised as an issue for income adequacy. Refer to paragraphs 30 to 33 for more discussion on abatement.

Ideas from submitters and stakeholders

43. Many submitters had suggestions regarding the level of support provided by WFF.

43.1 **Increase WFF, and index both WFF payments and abatement thresholds annually to wages and the Consumer Price Index (CPI).** WFF was currently only partially indexed, and any adjustments made were small and happened too slowly, which resulted in many families experiencing food insecurity and material hardship. Many wanted WFF to be indexed like NZ Superannuation and core benefits, although one stakeholder group said more frequent adjustments could be necessary in the current high inflation environment. Indexation would help ensure the level of support provided by

WFF, and its impact on reducing income inequality, did not erode over time. For more ideas regarding improving the current abatement system, see subparagraphs 37.2 and 37.3.

43.2 **Regularly calculate the level of support families need to achieve income adequacy**. Ideally, these calculations would be done by someone independent. The Government should ensure that families' incomes are topped-up, so they reach the calculated level of income adequacy. Current housing, transport and food costs need to be carefully considered. Some recognition also needs to be given to the different and rising costs associated with children of different ages. Babies cost more, as is recognised by the BSTC, but so do children at high school.

43.3 A small number of stakeholders suggested **adjusting the level of support provided to families that experience higher costs of living or costs of work because of where they live**. For example, people in rural areas may incur greater work costs because they live further from their workplaces, and others may live in areas where the cost of living is particularly high (such as people who do not live on the two main islands of New Zealand).

43.4 A small number of stakeholders **cautioned against increasing the level of support provided**. They said that increasing WFF could result in the cost of housing increasing, with the extra support just being passed on to landlords through higher rents. They said it could also increase clawbacks, create cliff faces, worsen EMTRs, and make it harder to achieve WFF's objectives. These stakeholders emphasised the importance of considering the long-term impacts/gains, rather than just focussing on providing extra short-term support to families. One submitter disagreed, however, and said carefully targeting WFF should minimise such risks, and that poverty-reduction policies should not be responsible for mitigating inflation risks.

44. Stakeholders at a quarter of targeted engagement sessions, and a couple of written submitters, were in favour of **allowing families to capitalise on their WFF entitlements**, because this would help families accumulate the money required to purchase their own homes. Many referred to previous family support that could be capitalised, and said this had helped their parents and grandparents purchase homes. One stakeholder said the BSTC could be a good candidate for capitalisation, given its universal application in the first year of a child's life, and that universality could be extended to cover all three years the BSTC is available. Alternatively, the FTC could be capitalised instead.

Changing circumstances and variable income/hours

WFF does not work well for families with variable incomes/hours

45. Many people were concerned that the current system did not work well for people with variable income/hours. Increasing amounts of part-time, shift, and casual insecure work, as well as the rise of the gig economy, had contributed to difficulties with WFF. Stakeholders said reporting income changes was difficult, and that the pandemic had exacerbated existing issues. People said families with variable incomes often struggled to budget, and did not know what their income was going to be in a given period. In addition, families struggled to determine how income changes might affect their entitlements, so could not necessarily make informed decisions about whether working more would be worthwhile.

> *"People with irregular incomes currently find it extraordinarily challenging to navigate WFF (and indeed the wider welfare system),*

which all too often seems predicated on an outdated view of work being almost entirely permanent and full-time."

46. Survey respondents reported mixed experiences when asked whether payments adjusted easily to changes in family circumstances or income.

More WFF support needed for seasonal workers

47. Some people said WFF presented challenges for seasonal workers, because they often only received income for part of the year. Some families had to relocate regularly to obtain more work, which negatively impacted on children. People said providing more support to these families could help them relocate less often.

Impact of new relationships on WFF

48. A small number of people were concerned with how changes in a parent's relationship status could negatively impact upon their WFF entitlements, and potentially put families into debt if they were overpaid WFF after a relationship commenced. They did not consider it appropriate for entitlements to be reduced just because of a parent's new relationship, as the new partner might not provide the parent or their child with support. One stakeholder disliked how currently a parent's entitlement could be reduced if they were 'dobbed in' for being in a relationship. They suggested only adjusting entitlements if a parent notifies IR/MSD of a relationship themselves. They also suggested updating the definition of relationship.

Ideas from submitters and stakeholders

49. **Introduce a tolerance threshold or grace periods.** This would enable families to work a certain amount of overtime, or retain the same entitlement for a certain period (e.g., four weeks or 90 days) after their circumstances change.

50. **Make the system more flexible, so that it deals with changing circumstances better**. It needs to be hyper-responsive to changes, and this should be reflected in the user interface technology. A web-based system with a very simple user interface could replace the current forms, which are confusing and difficult. Assistance could be provided for those who struggle with literacy.

51. **Support families with parents in seasonal work more**, so they can relocate less often. This could help improve outcomes for children in these families.

52. **Only adjust WFF entitlements after a parent notifies IR/MSD of a new relationship, and update definition of 'relationship'.**

53. Some ideas put forward by submitters regarding debt are also relevant to changing circumstances - see from paragraph 59 below.

Debt

Fear and stress of debt

54. A recurring theme was that debt was stressful and had a large impact on affected families. This was echoed by survey respondents, most of whom thought that debt creation was a significant issue. Fear of getting into debt impacted upon work incentives, as families worried about incomes from work causing overpayments and debt. Lump sum payments made debt less likely to form, but were not viable for low-income families as they needed regular support during the year.

"We are concerned that the WFF structure is driving the creation of debt for whānau who access support when they are most in need, only to be penalised for an increase in income, regardless of how desperately they needed financial assistance at the time."

55. Some families avoided WFF altogether because of its complexity and their fear of debt. Two stakeholder groups noted that overpayments could put low-income families into crisis, and that some families with WFF debt borrowed money from loan sharks to service that debt. One stakeholder said sole-parent families often had the most debt, so needed the most support. Some stakeholders felt debt just seemed punitive, and did not contribute positively towards the WFF objectives.

56. Survey respondents had mixed views regarding whether it was fair to make families repay overpayments caused by a change in circumstances or income.

Income estimates can lead to debt

57. Some people said it was difficult to accurately estimate income for the year in advance, and that estimates could result in debt if circumstances changed during the year. They said WFF debt penalised people for income increases (e.g., from pay rises, changing jobs, bonuses, or working overtime). One stakeholder felt it was unfair to expect customers to know how income changes would affect entitlements. One submitter said constantly adjusting their income and thinking about whether they would receive the correct amount of WFF was degrading and exhausting.

Families do not understand what creates debt

58. People said some customers did not understand what created debt, and did not know when to notify IR/MSD of changes to their income or circumstances. Some felt debt was created because of WFF's structure and system. Others said that some customers assumed entitlements changed automatically because IR was aware of income changes. Digital exclusion and a lack of in-person service access affected some customers' abilities to report changes, which could result in some families ending up in debt. Some people said that IR sometimes paid families the wrong amount of WFF even after being notified of a change in income or circumstances, so these families ended up in debt through no fault of their own.

Ideas from submitters and stakeholders

59. **WFF entitlements should be calculated more 'speedily', ideally in real-time** IR should also perform income calculations, especially where customers have struggled to report changes in their income.

60. **The year could be broken up into shorter periods of assessment, such as quarterly, biannually, monthly, or weekly.** This would help minimise overpayments and debt.

61. **Withhold a small amount of a family's entitlement during the year, then provide a lump sum at the end of the year.** People could be paid a base rate (which would be guaranteed) and then receive any extra amounts they are entitled to at the end of the year. This may not work for all families, as some may prefer to receive more during the year and risk being overpaid at the end of the year.

62. **Remove late payment penalties and interest**, except where a person is obviously gaming the system. Additional fees should not apply if a customer pays for late payment fees via the telephone when talking to IR.

63. **Families should be able to offset debt using future entitlements. Shift away from calling it debt - view WFF as over/under-payments over time instead.** This would reduce hardship, by ensuring families could continue to receive support even if they had already reached their entitlement for the year.

64. **Communicate with families more effectively**, so that they are more aware of when they need to notify IR/MSD of changes. Use multiple communication channels, including non-digital and person-to-person channels (such as live support from people online or on the phone). Use plain language, and ensure communications are friendly and supportive. There should be more thorough case management, or more effective use of staff to provide services that help households avoid debt. Enable customers to request calls from IR/MSD, and if a call back is delayed customers should not be required to repay overpayments that occur in the interim.

65. **Improve access to support and help people understand how to avoid debt and pay it off over time**. Stakeholders said that many families with debt did not know what options were available to them. They said that it needs to be easier for people in debt to deal with the system, and support needs to be streamlined.

66. **Prioritise certainty and stability over accuracy. Focus on ensuring people receive their entitlements instead of collecting debt.** Stability and certainty should be the core focus, so that families know how much they are going to receive each week. To this end, a couple of people suggested that entitlements should be based on prior year income. One stakeholder said entitlements should only be revised if there is a major change in a family's circumstances (for example, if the number of children in the family changes), in which case the recipient would be required to notify IR/MSD of the change. Another submitter suggested that for recipients who receive salaries or wages, investment income from non-associated parties of up to $1,000 should be exempt. They said if the end of year square-up resulted in an underpayment, the recipient should receive a lump sum (as is currently the case), but any overpaid amounts should not be collected.

67. **Improve hardship and debt write-off provisions**:

    67.1 **Debt incurred below a certain threshold should not be pursued.**

    67.2 **Put hardship policies/arrangements in place.** Families in severe and persistent poverty should have debt forgiven, similar to how beneficiaries' debts are forgiven.

    67.3 **Assess debt for all periods at the same time**. Families in hardship should not have to repeatedly apply for debt to be written off.

    67.4 **Write-off debt incurred through no fault of the recipient**. For example, where IR/MSD have not updated an entitlement despite being notified of a change in circumstances or income. Also, families should not be expected to repay debt if they fail to do something many families would not necessarily think to do.

    67.5 **Ensure expenses relevant to a child's wellbeing are accurately accounted for when assessing the affordability of WFF debt repayments.** Including WFF as income when assessing affordability could result in families having inadequate income to support their children.

68. **Split debt between parents**, instead of one parent having to repay all WFF debt.

69. **Use KiwiSaver to satisfy WFF debt**. One stakeholder suggested IR/MSD could dip into customers KiwiSaver accounts to satisfy WFF debt.

Complexity

70. Many people said the scheme was too complex and should be simplified. Having multiple WFF tax credits was confusing, and the rules around work hours, abatement, and care arrangements made WFF difficult. The complexity of the scheme sometimes made it difficult to calculate a person's entitlement. One stakeholder group expressed concern that the scheme must be overcomplicated if even well-educated people who provide advice on WFF struggled to understand and explain WFF. A small number of people said complexity led to greater inequity amongst WFF recipients; negatively impacted upon take-up, work incentives, and income adequacy; and made planning ahead difficult.

> *"The complex design of WFF has meant rather than helping a family into some essential support, it can leave them confused and without the proper payments they should be receiving."*

71. A couple of people emphasised the need for simple rules and systems that customers could understand, so that customers could insist on receiving their entitlement. They said the complex rules currently in place aimed to stop people taking advantage of the system, but this complexity resulted in those most in need of WFF not receiving support. In a similar vein, one submitter emphasised the need for complexity to be balanced against the overall return on investment in children through WFF. They felt reducing complexity should reduce administration costs.

72. Survey respondents had mixed views on whether WFF should provide support which reflected different circumstances but be more complex, or if it should instead be simple but less responsive to different circumstances.

Ideas from submitters and stakeholders

73. **Switch to a more universal payment for families**. This was mentioned at half of targeted engagement sessions and was supported by a small number of submitters. People liked universality because it would remove issues like debt and inaccurate income estimates, as well as ensuring that no child missed out on support. One submitter said that the greater cost of a universal payment would be offset by reductions in other societal challenges and lower administrative costs. One stakeholder group noted that high-income families would also receive support under a universal model, but one submitter thought this was not a problem because higher income families could donate their payments or choose not to claim them.

74. **Simplify WFF by merging the IWTC and/or MFTC into the FTC**. Those who were in favour of making WFF more child-centric so that no distinction was made between families on benefit and in paid work (see paragraphs 19 and 20) would support this approach.

75. **Align abatement under WFF**, so that the tax credits abate uniformly and WFF abatement is better aligned within the wider welfare system.

Different types of families and whānau

76. **Sole-parent families:** A small number of people said that WFF was designed for two-parent families, but there were now many more sole-parent families. They said sole-parents needed the most support, because they would likely have lower leave provisions and greater costs. In a two-parent family, one parent could look after the children, but working sole-parents did not have this option. It was noted that WFF did not acknowledge that sole-parents could only work during the opening hours of childcare centres, whereas two-parent families were better able to work non-standard hours. One stakeholder group said the gendered element to sole-

parent families should be recognised. Women led over 80% of sole-parent families, and many women were in part-time or low-paid work.

77. **Shared care:** A small number of people said the rules and systems for shared care arrangements needed improvement. They emphasised that despite children only spending some time at each parent's home, both parents had to bear the same base costs associated with having a child (e.g., providing the child with a bed and a home). One submitter said family arrangements could change monthly, weekly, or daily, many families found the current system confusing, and many were unclear as to whom and when they needed to provide information. One stakeholder raised concerns regarding some of the terminology used in the WFF scheme (e.g., 'primary caregiver' and 'bed nights'), and the negative impact these terms could have on already strained relationships between (separated) parents.

78. **Grandparents:** Some stakeholders said it was becoming more common for grandparents to help raise grandchildren, and that grandparents needed support. They said some parents passed on WFF to grandparents, but others did not. Some stakeholders said that grandparents might not want parents to stop receiving WFF tax credits but still needed extra support themselves. One stakeholder group said Pasifika grandparents in particular might not understand what WFF support they were entitled to. Another stakeholder commented that the Government provided support for formal childcare costs but did not provide support if grandparents looked after a child instead. This stakeholder suggested that if grandparents effectively provided a service the Crown would otherwise have had to pay for, such as looking after a child, this should be recognised.

79. **Whāngai and other care arrangements:** Some people said WFF should recognise whāngai and other cultures' care arrangements. They said it was not always obvious who WFF should be paid to as care may be provided informally/without legal basis.

Ideas from submitters and stakeholders

80. **Introduce more flexible settings so that sole-parent families have more certainty about what support they will receive.** Also amend the abatement system to provide more equitable outcomes for these families.

81. **Support parents who share the care of a child, regardless of the proportion of time the child spends at each parent's home**. Each parent needs the whole amount of WFF because the needs of children cannot always be halved. Settings should be modified so that parents who have their children on weekends can receive WFF.

82. **Grandparents should receive financial support if they care for their grandchildren.** One idea was providing a tax credit to parents, which they could use to pay for formal childcare or pass on to grandparents.

83. **Whoever actually cares for a child should receive WFF**, even if they are not legally the child's caregiver.

84. **Make the system flexible regarding family settings and responsive to frequent changes in family arrangements**, without imposing onerous requirements. One suggestion was a colour-coded calendar app, which caregivers could use to provide information about which parent in a shared care arrangement had care of their children and when they were caring for the children.

Perspectives from Māori whānau

85. Officials had four targeted engagement sessions with whānau Māori, and some written submissions provided feedback relating to Māori whānau. Key points made specifically by or regarding Māori whānau are set out below.

> *"Māori must be supported to have authority over taonga such as their tamariki and over the affairs of their whānau, with financial support for whānau being a key aspect of addressing historic injustice. We commend this review of WFF as a means of identifying opportunities to better address inequalities for tāngata whenua."*

85.1 **The Crown has obligations to Māori under Te Tiriti o Waitangi and the United Nations Declaration on the Rights of Indigenous People. WFF also needs to take into account Te Ao Māori.** Comments and suggestions included:

85.1.1 The Crown has a responsibility to consider and address debt traps created by the system for tāngata whenua.

85.1.2 Support whānau Māori, to address historic injustice and reduce the number of tamariki living in poverty. Article two guarantees Māori tino rangatiratanga over their kaīnga (homes), whenua (lands) and taonga (all things of value). Article three promises protection for Māori and guarantees equality with British subjects. Taken together, these articles may create an obligation to ensure Māori have sufficient resources to support their whānau and achieve equitable outcomes for tamariki Māori.

85.1.3 WFF policy should reflect the importance of tino rangatiratanga (independence and self-determination) at a whānau or hapū level. Policy should be designed by Māori for Māori, and incorporate matauranga and tikanga Māori (Māori knowledge and customs).

85.2 **Family is a broad concept for Māori**. It can include extended family members, such as uncles/aunties, nieces/nephews, and grandparents. One whānau Māori group said that Māori felt obligated to support family, and would take in other people's children even if they already did not have much available to support themselves. They emphasised that the system needed to be flexible, so that it could keep up with changes in whānau circumstances.

85.3 **Trust and relationships are important to Māori.** Some whānau Māori highlighted the good relationships they have with IR. They said having dedicated people within IR supporting whānau Māori made it significantly easier for them to access information about things like WFF.

85.4 **Proactively communicate to Māori that they are eligible for WFF.** Whānau Māori said generally Māori were very uncomfortable asking for help despite being entitled to support. However, they noted that some Māori might feel apprehensive about receiving communications from IR. One whānau Māori group said some people were too humble/proud to accept support, and would decline it as they thought other people were more in need of help.

> *"Whānau are hesitant coming into the IR or MSD office because they feel as if both organisations had labelled them as "bludgers" always looking for a handout before they had even walked through the door."*

85.5 **Many Māori prefer talking to IR/MSD in person,** but appointments at IR/MSD offices often did not work because of transport issues, or because appointments were too rushed or were at unsuitable times. Face-to-face interactions through home visits and locally-held workshops would help with take-up. Some said they preferred dealing with trusted local IR/MSD staff, whereas others preferred engaging with staff from out of town because they preferred not to disclose personal information to local people they knew.

85.6 **Sharing data on Māori communities could help increase take-up.** If data were shared with whānau Māori, they could use it to help ensure others in their community were aware of the support they were entitled to (e.g., through holding workshops, running education programmes, or putting information in local newsletters). Without this data, whānau Māori said it was hard to know what extra information or support Māori might benefit from.

86. Whānau Māori also provided some feedback that was similar to points made by other submitters and stakeholders. Below is a high-level summary of this feedback; more detail on these points is set out in Appendix 1.

86.1 Pay WFF recipients the same amount regardless of work status. "Work" should take into account unpaid "heart mahi" undertaken to support the wider community, such as marae mahi.

86.2 Increase and index WFF, increase abatement thresholds, and provide extra support to people living in rural or remote parts of New Zealand. Rurality particularly affects some whānau Māori, as it can impact how whānau access support as well as increase both the cost of living and the cost of work.

86.3 The cost of work and variable income/hours are barriers to work.

86.4 Debt is scary and causes stress. It disadvantages low-income families, many of whom are Māori.

86.5 Māori often live intergenerationally. Other family members who care for children should receive support.

86.6 Simplify WFF and improve communications.

86.7 Previous bad experiences applying for support can affect take-up.

Perspectives from Disabled people and their families

More support is needed for disabled people and their families

87. A small number of people expressed concern that insufficient financial support was provided to disabled people and their families, who generally faced higher costs. For example, extra costs to attend medical appointments/therapy sessions, or to purchase medication that is not Government-funded. They said the first thousand days were very important for infants with disabilities, but families received little financial support to stay home during this time.

Disabled people and their families face greater barriers to work

88. Some people said that disabled families were particularly disadvantaged by the scheme's current focus on work incentives. Many disabled parents wanted to work but were discriminated against by potential employers, so for the Government to say they needed to try harder to find work was very demoralising. Some parents and extended family members might not be able to return to work, or might find it difficult to work consistently, because they had to look after a disabled child or

adult. Disabled households were therefore more likely to be poorer, in part-time or casual work, underemployed, and less likely to qualify for the IWTC and the MFTC.

> *"It is not always possible for parents to enter or return to paid work for a myriad of reasons, including health and disability among parents and/or children. For whānau with children with disabilities, pursuing adequate income through paid work could circumvent the pursuit of a thriving whānau."*

89. Stakeholders said some disabled people, or their families, might decide that it was better to be on benefit than to work. This was because of the greater certainty and consistency associated with the benefit, and unlike work, it involved no extra costs. One stakeholder said it was harder for disabled people to actually attend work consistently, because some needed support to prepare for, and get to, work. They said an added barrier for disabled people was Government support for personal care and household management ceasing after they returned to work.

90. Providing more financial support could help more parents in families with disabilities return to work, however one stakeholder said they thought this on its own would be insufficient to address the barriers to work faced by disabled people. They suggested implementing separate measures to reduce barriers for disabled people, such as an allowance for employers to help with the costs associated with hiring disabled people.

Accessibility and administration for families with disabilities

91. Some stakeholders expressed concern that disabled people and their families experienced difficulty accessing WFF. One stakeholder highlighted the issues that tāngata whaikaha and whānau whaikaha Māori, as well as Pasifika disabled people, had accessing WFF, compared with Pakeha disabled people. They said this meant Māori and Pasifika disabled people tended to receive less support. This stakeholder said ethnic disparities became worse as complexity increased, and stressed the importance of simplifying WFF to minimise ethnic disparities. They also said the onus should not be on disabled people to apply for support or provide information to IR/MSD. Some people said there was a lack of specialised assistance for disabled people, and that the shift to online Government services had created a divide between those who were digitally capable and those who were not. However, one stakeholder said IR's website was already surprisingly accessible for blind people.

Ideas from submitters and stakeholders

92. **Provide more financial support to disabled people and their families**, to help with the extra costs they face. Ideas included providing a top-up WFF payment, or a tax credit, specifically to these families. Support should be available whether a family has a disabled child or adult, and people should not have to 'jump through hoops' to prove how disabled they are to qualify.

93. **WFF should take into account the impact of looking after a disabled child or adult**. Family members who support a disabled child or adult may have variable hours, or may not be able to return to work at all. More generous abatement rates might be one way to help with this.

94. **Minimise ethnic disparities amongst disabled people by simplifying WFF**, **and improve accessibility for disabled people.** For example, the deaf community needs interpreters and advocates. Disabled people may struggle with digital literacy and with communicating over the phone. Blind people may also struggle with some websites, depending on how they are designed.

Communications and take-up

95. Some people emphasised the effect of the tone used in communications on take-up. A quarter of stakeholders raised communication issues for non-native English speakers and/or disabled people, and how this affected engagement and understanding. Some preferred talking to real people, while others said digital communication channels, such as apps, would be helpful.

96. Stakeholders said difficulties applying for WFF affected take-up, as did limited digital literacy/access. One stakeholder said some people may be hesitant or unwilling to share personal information to receive WFF. Others said fear/distrust of the Government affected take-up, which particularly affected Asian, Māori, and Pasifika families, as well as non-New Zealand citizens. They also said some customers shared their WFF experiences, and bad experiences could impact take-up by others.

97. One stakeholder group said WFF was not sufficiently promoted to certain customer populations, which affected take-up; IR/MSD made assumptions without actually listening to customers, and failed to properly explain what support customers could receive; and some customers felt both discriminated against and demoralised.

98. Most survey respondents found it easy to find general information about WFF, however, they had mixed views on how easy it was for families to understand what they were entitled to. Most survey respondents would look for information about WFF through the IR website.

Administration by IR and MSD

99. **Inconsistencies caused by dual-agency model:** Some said that having two different agencies administer WFF resulted in gaps and inconsistency, and that customers should be treated the same regardless of the agency they dealt with. Another stakeholder felt there were two systems: one for people in paid work or business (IR), and another for welfare recipients (MSD), and that this was inequitable.

100. **IR**: People who provided feedback in this area generally preferred dealing with IR. They said IR was less punitive, easier to deal with regarding issues, more knowledgeable, and more likely to both get WFF payments right and provide favourable outcomes. They liked how IR offered different payment frequency options, could write-off debt, and could enter into repayment arrangements. Some said getting through to IR could be hard because of long wait times on the phone, engaging with IR could be stressful, and IR did not always communicate effectively.

101. **MSD**[1]: One stakeholder said in-work support from MSD motivated people more, and another said MSD staff were normally helpful. One stakeholder said blind people had issues transitioning between the blind benefit and WFF through MSD. Another stakeholder said MSD failed to clearly communicate and deliver customers' entitlements and did not have a mana-enhancing approach. MSD was more likely to have overpayment issues, and its website seemed to prioritise repaying debt over wellbeing. Issues with long wait times on the phone were also mentioned.

Payment frequency

102. A small number of people commented on payment frequency. They liked how IR provided various options, and generally preferred regular payments during the

[1] Comments about MSD include those made about Work and Income.

year because they helped with budgeting. There was no expressed preference for receiving payments on particular days of the week (e.g., on the same days as other support payments from the Government).

> *"Higher-income families can receive WFF annually which avoids debts, but for lower-income families who rely on regular payments, this is not a feasible option."*

103. Most survey respondents thought weekly or fortnightly WFF payments were better than end of year lump sums. Responses were mixed when asked if weekly or fortnightly payments were still better if it meant families were overpaid and would later have to repay some of the WFF they had received. Most respondents thought concern about incurring debt influenced when people decided to receive their payments.

Ideas from submitters and stakeholders

104. **Improve communications to reduce language barriers.** See paragraphs 92 and 94 for more feedback on supporting disabled people.

105. **Make information about WFF more accessible**. Introduce more communication channels (e.g., texting, and online channels such as apps, Tiktok and Facebook). Some people may have limited digital access/literacy, however, and many customers (particularly Pasifika and Māori) prefer engaging in person.

106. **Make it easier for people to apply for WFF and use the system.** One submitter said means-testing should not be so administratively burdensome that it prevents families accessing WFF. Another suggested introducing a direct phone line for customers to connect with financial advisors.

107. **Automate more of the system, including families' entitlements, and notify customers when they are eligible for support**. Many people supported more automation, except when entitlements were reduced, in which case a real person should process the change in entitlement. They thought automation would improve take-up, reduce overpayments, and require customers to provide less information.

108. **Improve understanding and awareness of WFF** to improve take-up, as some customers did not fully understand WFF. For example, some people did not know that they had to cancel their benefits to receive the IWTC. One stakeholder suggested raising awareness through local MPs, champions, and case workers.

109. **Make the Government more joined up so that customers only have to submit information once**, to reduce stress and ensure families received the support they were entitled to. Ideas included a centralised application portal, or agencies automatically sharing eligibility information when people applied for support. People also suggested standardising definitions across agencies.

110. **Have only one agency administer WFF**, to reduce gaps and ensure consistent treatment. The small number of stakeholders who suggested this generally preferred IR administering and paying WFF. This was because it would reduce delays and gaps when people transitioned on/off benefit; IR already holds various information; IR is more flexible and reliable; and IR has tools such as IRD numbers it can use to ensure WFF is administered correctly. One stakeholder suggested if IR were sole administrator, the ringfence around the FTC (which traditionally applies when the FTC is received by someone on a benefit) should remain.

111. **Retain both agencies but modify their roles and responsibilities.** A few stakeholders suggested this. For example, IR could collect information and calculate entitlements, and MSD could engage with and pay customers.

112. **Improve the culture at IR/MSD and commit to mana-enhancing service.** Some people said a culture-shift and commitment to service delivery guided by manaakitanga was needed, so that customers were respected, received their full entitlements, and could better avoid debt.

Next steps

113. A separate options report on WFF will be provided to Ministers alongside this report. Both reports will be discussed at a joint Ministers meeting proposed for 9 August 2022. Officials will also follow up with the stakeholders who attended the targeted engagement sessions after this report is publicly released, to acknowledge their contributions and (to the extent possible) update them on the next steps of the WFF review.

Appendix 1: Additional feedback from Māori

114. **Pay WFF recipients the same amount regardless of work/benefit status.** One whānau Māori group emphasised that in rural areas it could be difficult for whānau to get paid work due to limited job opportunities, as many of the jobs available were for people with greater qualifications. They suggested a training tax credit could help Māori in these areas upskill and increase their likelihood of finding employment. They also said that 'heart mahi', such as marae mahi, was very important to Māori, but was unpaid. The whānau Māori group thought that this sort of unpaid work should qualify as 'work' for WFF. One submitter said that Māori were more likely to be in caregiving roles within their whānau, and that existing settings exacerbated stigma around Māori as welfare recipients. They noted that financially disadvantaged Māori were less able to afford formal care or were likely to have fewer labour market resources.

115. **Increase and index WFF, increase abatement thresholds, and provide extra support to people living in remote parts of New Zealand.** Concerns with the cost of living were mentioned at each session with Māori. They said some whānau lived in garages, and others could not build houses on their own land because it was so expensive. Ideas to help with the cost of living included allowing whānau to capitalise WFF to help with purchasing homes; providing people in remote areas with extra support to help with greater living costs; and providing Best Start as a lump sum at the beginning of the year when a child is born.

116. **The cost of work and variable income/hours are barriers to work**. Childcare and transport costs were particularly expensive (especially for Māori in rural areas), and extra support for Māori to transition into work would be welcomed. Seasonal, uncertain, or limited work opportunities sometimes made staying on benefit more appealing, because the benefit was predictable. Some settings discouraged people from earning more, which was contrary to WFF's objective of incentivising work.

117. **Debt is scary and causes stress. It disadvantages low-income families, many of whom are Māori**. Some Māori took deliberate steps to avoid debt, and were apprehensive about WFF because they had previous bad experiences with WFF debt. Some Māori did not know when IR/MSD had to be notified of changing circumstances or that repayment arrangements were available. Ideas to reduce debt included WFF case managers regularly checking in with families regarding their circumstances; automating entitlements; and removing penalties.

118. **Māori often live intergenerationally. Other family members who care for children should receive support.** Some Māori parents had to care for their children and the elderly. Other whānau members who look after children (e.g., grandparents and aunties/uncles) often had difficulties accessing financial support.

119. **Simplify WFF and improve communications**. Ideas included using apps to declare income changes or to request contact from IR/MSD, while still recognising that some Māori were not digitally literate or had limited digital/internet access. Māori may be less likely to engage with complicated information, so presenting information simply is important, as is the tone used in communications. Whānau Māori suggested take-up could be improved by providing information in various places in the community, using campaign vehicles, and via online platforms.

120. **Previous bad experiences applying for support can affect take-up.** Some Māori experienced prejudice, hostility, and condescension when engaging with IR/MSD. Ideas included improving relationships between MSD connectors and staff, and improving the treatment of Māori by IR/MSD staff so that Māori feel valued and respected.

Appendix 2: Technical comments on the specific tax credits

Family Tax Credit (FTC)

121. People expressed support for the FTC, with some saying it was as important as New Zealand Superannuation but for children. Some suggested merging some or all the other WFF tax credits into the FTC, to simplify WFF and shift its emphasis away from work incentives and towards alleviating child poverty. Ideas included:

121.1 **Increase the FTC and index it annually to wages and prices**. **Also increase the abatement threshold and lower the abatement rate.** 10% of submitters recommended increasing the credit to $170 for one child and $120 for subsequent children.

121.2 **Pay a flat-rate per child.** Larger families experienced more poverty, and different rates indirectly discouraged people from having more children.

Best Start Tax Credit (BSTC)

122. Some stakeholders mentioned that they felt BSTC was important. Ideas for change included:

122.1 **Better integrate the BSTC into WFF**. A few stakeholder groups said keeping BSTC separate increased complexity. Abatement could be particularly severe depending on a child's age. One idea was to align the BSTC's abatement system with that of the other WFF tax credits.

122.2 **Provide the BSTC in the first 1,000 days even if a parent has returned to work**. **Also provide it to parents on paid parental leave (PPL), and pay the BSTC before a baby is born.** One stakeholder group said ceasing the BSTC because a parent returned to work was punitive and deprived them of helpful extra support. A submitter said the BSTC should be provided to people on PPL, because PPL addressed income lost following a pause in employment whereas the BSTC provided support for the extra costs of raising another child. A small number of people suggested paying the BSTC before babies were born to ensure they received the 'best start' in life.

122.3 **Provide greater support for younger children and a top-up for low-income families**. **Consider extending support to children under five**.

122.4 **There were mixed views on universality.** A small number of people favoured better targeting towards low-income families. Others supported universality in year one and then targeting the BSTC in subsequent years, while some supported the BSTC applying universally for all three years.

122.5 **Increase the eligibility thresholds for years two and three.** One stakeholder group said $79,000 was too low a threshold, because few families would be able to survive on one pre-tax income of that level.

122.6 **The BSTC needs to cater for large families better.** One stakeholder group said the BSTC did not seem to cater for large families particularly well.

In-Work Tax Credit (IWTC)

123. Many people suggested repealing the IWTC or merging it with the FTC, so families received the same support regardless of work/benefit status[2]. Other ideas included:

123.1 **Make the eligibility criteria as accessible and broad as possible, and increase the IWTC.** One stakeholder group said there needed to be more emphasis on the IWTC. A small number of people suggested increasing the IWTC to $82 per week, plus $17 for fourth and additional children.

123.2 **Only provide the IWTC to salary/wage earners and sole traders.** One submitter said if others (e.g., self-employed people) wanted to claim WFF, they should be on payroll records and show as wage earners.

123.3 **Pay a flat-rate per child.** One stakeholder group disagreed with having different rates, as these indirectly discouraged people from having more children. However, another stakeholder questioned whether the IWTC should even provide extra amounts for additional children.

123.4 **Provide the IWTC to people partially on benefit and working**, **and provide it to parents in training or study**. Alternatively, provide a separate training/study tax credit.

Minimum Family Tax Credit (MFTC)

124. Some people suggested repealing the MFTC because few families received it, it caused high EMTRs, it discriminated against people on benefit, and it could result in families getting into debt. However, one stakeholder felt the MFTC was particularly valuable for people transitioning off benefit. Ideas for change included:

124.1 **Change the hours test or completely remove it.** Some suggested allowing the test to be applied over a longer period, e.g., fortnightly or annually. One submitter said failing the hours test caused significant stress, and that illness or public holidays could prevent people satisfying the test.

124.2 **Adjust the abatement rate**. The current rate was challenging for people with variable hours/income, and made working more hours less worthwhile.

124.3 **Increase and index the MFTC**. A few recommended this to make working more worthwhile, compared with staying on benefit. It was noted that $632 was less than the amount that would be paid for 30 hours of work on the minimum wage, and might not provide enough support to achieve income adequacy.

124.4 **Provide the MFTC to people on benefit and working.**

124.5 **There were mixed views about whether it was preferable for people transitioning off benefit and into work to receive the MFTC or a partial benefit instead**. One stakeholder group said people should be able to stay on benefit as they transitioned into work, instead of receiving the MFTC. Another stakeholder group disagreed, and said people took pride in coming off benefit, so would rather receive the MFTC than a partial benefit. This was the case even if the same amount of financial support were to be provided via the partial benefit or the MFTC.

[2] See paragraphs 19 and 20 for discussion regarding making WFF more child-centric, and paragraphs 34 to 36 above regarding work incentives and the IWTC.

Appendix 3: Other points raised in submissions and targeted engagement

What people like about WFF

125. One stakeholder **liked that work incentives were still an objective of WFF**.

126. About 20% of submitters and 25% of stakeholder groups **expressed support for WFF**. Many felt WFF provided important support for low/middle-income families, especially given increased living costs. One submitter thought WFF was important for Māori, who were more likely to both have low incomes and access welfare.

118. One stakeholder group said **some of the WFF tax credits provided good support**, but the abatement thresholds made it hard to realise the benefit of the credits. Another stakeholder **liked how WFF had increased**, but that WFF should increase more. One stakeholder **liked how tax credits were progressive**. They said tax credits were an effective way to provide support to low-income people.

119. A few people had **positive comments about the IWTC**. They appreciated recent changes to the IWTC, and how it supported parents who returned to work to improve their family's life/situation. One stakeholder said the IWTC 'feels like the right thing' because it acknowledged work costs and helped make work sustainable. A couple of people had **positive comments about the BSTC**. One submitter said they liked how the BSTC is universal. Another said they thought the BSTC was important. One stakeholder group **liked the FTC**, and thought it was particularly important because New Zealand would likely face a "deep recession" soon.

120. One submitter said **WFF was administered well**. Another liked WFF's payment frequency and its broad eligibility criteria. One stakeholder group liked the WFF application process, because it was kinder, less invasive, and more transactional than other application processes. Two people liked IR's updates and alerts.

Other feedback on WFF

121. **WFF reforms must take into account the wider welfare and support system:** A small number of people said WFF should be considered holistically alongside the wider welfare and support system. One stakeholder group said there needed to be a cross-Government collaborative approach for children. One submitter said many support payments did not fit well together, because they partially or completely negated each other, and encouraged a joint IR/MSD review of family income support payments to consider how they fit together. A few stakeholder groups said other welfare and support changes have had unintended consequences for WFF. For example, minimum wage increases might increase a person's work income but reduce their WFF by a greater amount because of abatement settings. Some mentioned WFF could also affect the Accommodation Supplement.

122. **Long-term impacts must be considered:** One stakeholder said sometimes providing support could do more harm than good. They said long-term impacts were not focussed on, and people were often viewed critically if they asked about long-term impacts. They provided the housing crisis as an example, and said providing more money to pay rent could result in increased rents, which benefited landlords, but the actual recipients of Government support ended up no better off themselves.

123. **Caution against greater targeting:** One submitter said there were various problems with targeting, including greater complexity; high abatements rates and sudden cliffs/drops in support; more gaming of the system by people seeking to artificially reduce their incomes; and the greater stigma attached to more targeted

payments. They said New Zealand’s welfare system was already highly targeted, and there was no compelling argument to make WFF even more targeted.

124. **WFF compensates for low wages:** A few people said WFF subsidised employers by topping up low wages received by WFF customers, and this meant taxpayers took on a burden that should instead be borne by employers. If wages increased then WFF could better focus on supporting children, issues with abatement rates and work incentives would likely be minimised, and WFF would cost less.

125. **WFF negatively impacts business and economic growth:** One submitter said WFF discouraged people from accepting promotions, or encouraged employees to demand greater pay increases, because abatement settings made pay increases less worthwhile. They said unions had sought to convert overtime payments into time in lieu entitlements because of WFF, to prevent income increases which would reduce WFF and negatively impact overall family incomes. They were concerned that over time, WFF would result in unsustainable wage claims, which would be exacerbated if increases to the minimum and living wages put upwards pressure on wages generally. They said WFF acted directly counter to the goal of economic growth, by discouraging people to increase their skills and productivity.

126. **WFF negatively impacts retirement savings:** One submitter said the effect of KiwiSaver contributions on families receiving WFF could disincentivise saving and reduce KiwiSaver take-up. They said the Government had not assessed the interrelationship between KiwiSaver and WFF to see what inefficiencies might exist.

127. **Repeal WFF:** Three submitters did not support WFF. Two suggested repealing it. Alternative ideas to WFF including adjusting personal tax rates and thresholds, or resolving the housing crisis and then targeting support to low-income families.

128. **Eligibility criteria for non-citizens/residents:** One submitter said currently, families were excluded from WFF where the New Zealand citizen/resident in the family worked full-time but their partner and children were not citizens/residents. Whether a family with one resident/citizen parent qualified depended on which parent was the primary caregiver. They said given the delays and backlogs with processing residency applications, eligibility for WFF should not be dependent on individual family circumstances.

129. **Definition of income:** A couple of people said child support should not count as ‘income’ for WFF because often child support was not paid, so families missed out on WFF support during the year. One submitter recommended reviewing the definition of family scheme income because of its complexity, especially when trusts were taken into account. They recommended the scheme focus on standard scenarios and have de minimis thresholds for certain income types, and that a separate system be introduced for people with business income. Another idea was removing the business test for payments, which looks through to businesses and trusts, because most people were unlikely to commit fraud and the current rules were overly complex.

130. **Community groups and intermediaries:** Some people said community groups had to help customers because of failures by IR/MSD, and because WFF was so complex. One stakeholder said community groups could help improve agencies’ cultures. Intermediaries and community groups helping agencies to improve take-up was discussed at some sessions. However, one stakeholder cautioned against the Government partnering with non-governmental organisations (NGOs) to provide WFF, because of potential issues with transparency and accountability. This stakeholder preferred the Government having contracts with NGOs instead of partnerships with them. They stressed it was also important not to reduce the number of choices people had, and that if WFF were to be partially delivered through NGOs, customers should retain the ability to receive their entitlements directly from the Government if they preferred.

Appendix 4: Key questions asked at targeted engagement sessions

131. The key questions officials asked stakeholders at the targeted engagement sessions included:

    (a) How can we better support:

    - Low-income working families?
    - Families with changing hours, shift-work, or part-time hours?
    - Different family and whānau make-up and care arrangements, such as the shared care of children?

    (b) What are your views on how WFF is administered?

    (c) What do you like about WFF and would like to ensure is retained?

    (d) What concerns do you have about WFF?

    (e) What changes would you make to WFF and why?

    (f) Do you have any comments about the specific WFF tax credits?

    (g) Do you agree with the policy intent or objectives of Working for Families?[3]

    (h) Do you have any comments on the current structure and impacts of financial work incentives?

[3] Officials asked questions (g) and (h) at the more technical targeted engagement sessions, such as those with academics and WFF experts.

MINISTRY OF SOCIAL DEVELOPMENT
TE MANATŪ WHAKAHIATO ORA

DEPARTMENT OF THE PRIME MINISTER AND CABINET
TE TARI O TE PIRIMIA ME TE KOMITI MATUA

Inland Revenue
Te Tari Taake

TE TAI ŌHANGA
THE TREASURY

Update on Working for Families – October Income Support Ministers meeting

Date:	27 September 2022	**Report no.:**	REP/22/9/913 DPMC-2022/23-313 IR2022/444 T2022/2143
Security level:		**Priority:**	High

Action Sought

Rt Hon Jacinda Ardern **Hon Grant Robertson** **Hon Kelvin Davis** **Hon Carmel Sepuloni** **Hon David Parker**	Note the contents of the attached A3s.	7 October 2022

Contact for telephone discussion

Name	*Position*	*Telephone*
Deborah Tucker	Principal Analyst, Child Wellbeing and Poverty Reduction Group, DPMC	s 9(2)(a)
Polly Vowles	Policy Manager, MSD	s 9(2)(a)
Keiran Kennedy	Manager, The Treasury	s 9(2)(a)
Eina Wong	Principal Policy Advisor, IR	s 9(2)(a)
Report prepared by	Daniel Frischknecht, MSD; Deborah Tucker, DPMC (CWPRG); Eina Wong, IRD; Laura Browne, Treasury.	

Minister's office comments

☐ Noted ☐ Seen ☐ Approved ☐ Needs change ☐ Withdrawn ☐ Not seen by Minister ☐ Overtaken by events ☐ Referred to (specify) ____________________	***Comments***

Date received from MSD ____________________

Date returned to MSD ____________________

MINISTRY OF SOCIAL DEVELOPMENT
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DEPARTMENT OF THE PRIME MINISTER AND CABINET
TE TARI O TE PIRIMIA ME TE KOMITI MATUA

Inland Revenue
Te Tari Taake

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THE TREASURY

Report

Date: 27 September 2022 **Security Level:**

To: Rt Hon Jacinda Ardern, Prime Minister / Minister for Child Poverty Reduction
Hon Grant Robertson, Minister of Finance
Hon Kelvin Davis, Minister for Children
Hon Carmel Sepuloni, Minister for Social Development and Employment
Hon David Parker, Minister of Revenue

Update on Working for Families – October Income Support Ministers meeting

Purpose of the report

1 As part of the Working for Families (WFF) review, the attached A3s:

1.1 provide a high-level overview of the detailed advice and modelling that will be included in the substantive advice in November

1.2 present initial modelling to show how the variations of options address specific concerns raised, and highlight the different choices for Ministers on the design of WFF and the benefit/tax credit interface

1.3 seek feedback on the direction of travel, or whether there are any particular areas of interest for further work, to help inform the November advice.

2 The modelling included in the A3s will continue to be refined over time as we work through the detailed policy design of each option.

Recommended actions

It is recommended that you:

1 **note** the contents of the attached A3s.

s 9(2)(a)	s 9(2)(a)	s 9(2)(a)	s 9(2)(a)
Clare Ward	Polly Vowles	Keiran Kennedy	Eina Wong
Department of the Prime Minister and Cabinet	Ministry of Social Development	The Treasury	Inland Revenue
27/09/22	27/09/22	27/09/22	27/09/22
Date	Date	Date	Date

Rt Hon Jacinda Ardern	Hon Grant Robertson	Hon Kelvin Davis	Hon Carmel Sepuloni	Hon David Parker
Prime Minister, Minister for Child Poverty Reduction	Minister of Finance	Minister for Children	Minister for Social Development and Employment	Minister of Revenue
Date	Date	Date	Date	Date

Update on Working for Families – October Income Support Ministers meeting

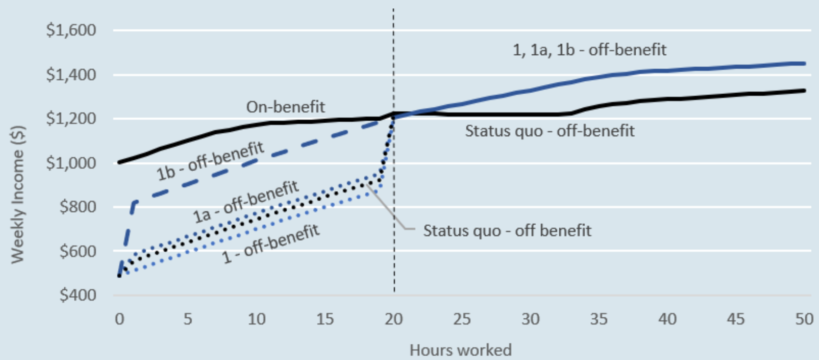
BUDGET SENSITIVE

1. Purpose of this update

- Provide a high-level overview of the detailed advice and modelling that will be included in the substantive advice in November.
- Present initial modelling to show how the variations of options address specific concerns raised, and highlight the different choices for Ministers on the design of WFF and the benefit/tax credit interface.
- Seek feedback on the direction of travel, or whether there are any particular areas of interest for further work, to help inform the November advice.

2. An updated options set is being developed for Ministers to consider in the substantive November advice

	1. Maintaining an in-work payment			5. A single tax credit		
Context and options	**Option Summary:** Maintains an in-work payment and has a strong focus on making work pay by also increasing the generosity of this payment. **Request for more advice:** how can this option (a) better support families who don't meet the hours test and (b) improve its BHC50 outcomes. **Variations of options:** The new in-work payment would only be available to families off-benefit who regularly meet the hours test (to support off-benefit outcomes). Alternative variations will consider allowing families who are off-benefit to receive some, or all, of the payment before the hours test is met to reduce the number of families worse off and improve BHC50 outcomes.			**Option summary:** Removes the in-work payments and enhances the FTC. It improves income adequacy and makes work pay through more generous FTC payment rates and abatement settings. **Request for more advice:** how can this option (a) better support 'making work pay', (b) reduce the number of families worse off and (c) mitigate the impacts from any increased reliance on the benefit system. **Variations of options:** Options that better make work pay, either through more generous FTC settings or through changes to the benefit system. Additional structural changes could also be made to reduce the number of families being made worse off.		
	Option 1: Not entitled to payment unless hours test is met (option presented in previous advice)	**Option 1a:** Entitled to a portion of payment before hours test is met	**Option 1b:** Entitled to entire payment regardless of hours worked	**Option 5:** Remove IWTC and make FTC payment rates and abatement settings more generous	**Option 5a:** Further changes to WFF abatement settings to help make work pay	**Option 5b:** 5a but also rebalancing some of main benefits into FTC to further make work pay
Child poverty	9,000 (BHC50) 28,000 (AHC50)	10,000 (BHC50) 29,000 (AHC50)	14,000 (BHC50) 31,000 (AHC50)	24,000 (BHC50) 27,000 (AHC50)	27,000 (BHC50) 41,000 (AHC50)	20,000 (BHC50) 29,000 (AHC50)
Costs (p.a)	$675m	$716m	$800m	$540m	$882m	$686m
Gainers / losers	170,000 HHs gain by $81pw. 24,000 HHs lose by $34pw*.	178,000 HHs gain by $80pw. 16,000 HHs lose by $32pw*.	181,000 HHs gain by $87pw. 13,000 HHs lose by $32pw*.	235,000 HHs gain by $46pw. 24,000 HHs lose by $23pw^.	265,000 HHs gain by $65pw. 18,000 HHs lose by $27pw^.	262,000 HHs gain by $53pw. 34,000 HHs lose by $23pw^.
	*Around 12,000 of these HHs are estimated to be worse off due to the modelling applying different ringfencing rules for the current IWTC and the proposed new in-work payment. Further modelling for the November advice will determine whether these losses reflect desired policy or are due to the modelling assumptions used.			^These families are worse off due to the removal of the IWTC and flow-ons to AS. For many of these families it may become financially advantageous to move onto benefit to prevent being worse off. Further advice and options will be provided.		
Make work pay / incentives to work	Option 1 and its variations increase the incomes of employed HHs by between $80pw - $87pw on average (depending on the option), while the incomes for non-working HHs remain the same. It will increase the returns from working compared to the status quo and option 5. For example, it increases the gap between benefit and 40 hours work by $131pw for a sole parent with two children earning the minimum wage. The average gains are lower for families with relatively higher earnings. However, similar to the WFF changes in 2005/06, option 1 and its variations may incentivise second earners in couples to reduce their work hours.			Option 5 provides larger gains for non-working HHs ($66pw) compared to working HHs ($39pw).	Option 5a provides similar gains for non-working and working HHs ($67pw and $65pw respectively).	Option 5b provides smaller gains for non-working HHs ($41pw) compared to working HHs ($57pw).
				Option 5 reduces the returns from working more for many low to middle-income workers compared to the status quo; option 5a has more mixed impacts; and option 5b generally increases the returns from working (particularly for couples and those with earnings above the minimum wage). Like option 1, but to a lesser extent, option 5 and its variations may incentivise second earners to reduce their work hours.		
Income by hours worked For sole parent with two children earning minimum wage						



Notes: The variations of option 1 provide different levels of income for those off-benefit working less than 20 hours a week, but the same income for 20 or more hours of work. It would be financially advantageous to be on benefit when working less than 20 hours, however some families remain off benefit instead. This could be for various reasons, such as personal choice or lack of awareness of supports available.

Notes: Incomes drop slightly around 35-40 hours worked as this is when families would move off benefit and lose WEP (families without children face this drop currently). During summer months, there won't be a drop in income under this option and the returns from working would be stronger.

Incomes under Option 5 is the same as option 5a for lower levels of hours worked.

3. There are trade-offs within options…

	1. Maintaining an in-work payment			5. A single tax credit		
Option	**Option 1:** Not entitled to payment unless hours test is met	**Option 1a:** Entitled to a portion of payment before hours test is met	**Option 1b:** Entitled to entire payment regardless of hours worked	**Option 5:** Remove IWTC and make FTC payment rates and abatement settings more generous	**Option 5a:** Further changes to WFF abatement settings to help make work pay	**Option 5b:** 5a but also rebalancing some of main benefits into FTC to further make work pay
Pros and cons	Has the strongest incentives to work the desired number of hours. However, non-beneficiary sole parents working less than 20 hours (or 30 hours for couples) are financially disadvantaged.	More closely reflects current system, where all low-income non-beneficiaries are eligible to receive the IWTC and receive a top-up at 20 or 30 hours worked (through the MFTC). Compared to option 1, this option reduces the number of families worse off, has slightly greater child poverty impacts, but is slightly more costly.	This variation of option 1 further reduces child poverty and the number of families worse off, is the easiest to administer and reduces debt. However, this option is the most costly and has weaker incentives to work full-time. For those off-benefit, it also provides relatively generous levels of assistance with minimal work requirements.	Provides larger income gains for non-working households (HHs) ($66pw) compared to working HHs ($39pw). Of all the variations of option 5, it reduces the gap between benefit and work the most.	Provides similar income gains for non-working and working HHs ($67pw and $65pw respectively). Is less targeted than option 5 and has higher costs. It will only 'get you so far' with improving incentives as it provides greater benefits to relatively higher income families and may encourage second earners to reduce their work hours.	Provides smaller gains for non-working HHs ($41pw) compared to working HHs ($57pw). Increasing FTC, and reducing benefits by a smaller amount, is better for work incentives. Benefit and FTC rates would be more similar to, but higher than, what WEAG recommended. Improves incentives more cost effectively than option 5a, however, has lower child poverty reductions.

…as well as trade-offs across options

	1. Maintaining an in-work payment		5. A single tax credit	
Trade-offs across options	This option only **benefits working families** (around half of families in poverty), so has lower BHC50 impacts compared to option 5 in the short-term. It also increases the depth of poverty on this measure because it increases median incomes.	→ You could complement this option with a modest increase to other adequacy payments for beneficiary families – progressed at the same time or at a later stage.	Some **families will be worse off** from rebalancing IWTC into FTC given the two payments have different apportionment rules, eligibility settings and flow-on impacts to AS and TAS.	→ This could be addressed by changing the FTC rate structure to a 'per family' amount, plus a 'per child' amount. In practice, this is a structural change that doesn't affect entitlement for many families, but could help families disadvantaged from multiple complex interactions (such as shared care).
	This option is likely to have **higher longer-term costs** if payment settings are indexed to ensure families remain 'better off' off-benefit over time, especially if main benefits are increased in the future.	→ Officials will provide advice on different options for indexing – including advice on the trade-offs between regular indexation and ad-hoc adjustments.	Depending on the design, this option is **likely to reduce the financial incentives to work** for some families.	→ Changing benefit abatement settings is another relatively targeted way to incentivise part-time work. However more families will then be eligible for a benefit under option 5. Officials can provide further advice on additional options to make work pay, including interactions with options being considered through the review of Childcare Assistance.

4. Important considerations

Benefit interface	Although highly uncertain, it is estimated that up to 20,000 additional working families would financially benefit from receiving a benefit under option 5, but this would reduce slightly under option 5b. We expect actual take-up to be lower in practice. Option 5 would likely require a legislative change to allow JS recipients to work full-time (30 hours or more) and receive a benefit until it abates to zero (like Sole Parent Support currently). These working families would interact with the higher compliance benefit system, including declaring income weekly. MSD are exploring ways to improve the client experience for this group to help mitigate any negative impacts, and advice will be provided in November.
Overseas tax credits	Overseas tax credits differ in design, with Australia (and the UK once it moves to Universal Credit) having a tax credit system that is more consistent with option 5. On the other hand, the US and Canada both have in-work payments like option 1, but these are set at much more modest levels.

5. Buffer tax credit vs increased automatic debt write-off threshold

	Buffer Tax Credit	Increased debt write-off threshold
Description	Essentially a refundable tax credit made available at the end of the income year. It would be first applied against any WFF debt a customer may have accrued due to over-payments. Where a customer has not accrued any WFF debt, the balance of the buffer tax credit could be paid as a one-off lump sum at the end of the tax year.	Increasing the threshold for automatic write-offs for WFF debt (currently $50) would clear low-value WFF debt. An increased write-off threshold could either apply to all customers or could be targeted to smaller groups with greater need (e.g. customers with income under a certain amount).
Initial advice on trade-offs	• Benefits customers with and without debt, so less targeted towards families with debt. However, is more equitable than an increased debt write-off threshold because customers who have kept IR informed of changes receive the same dollar amount as other customers who have been overpaid during the year and have debt written off. This also means it doesn't create perverse incentives. • More costly than increasing the debt write-off threshold by the equivalent dollar amount. • More complicated to administer due to the requirement to pay out unused portion of the tax credit if the customer has no debt or their debt is less than the amount of the credit.	• Targeted as it is only available to customers with debt, but may create perverse incentives and would be less equitable than the buffer tax credit. • Likely to be lower cost than the buffer tax credit. • Less complicated to administer because no further steps are required after the debt write-off has been applied.

6. Next Steps

Next steps

If Ministers have any feedback on this update we can reflect this in the substantive November advice. If Ministers are generally comfortable with the direction of the advice, officials will provide two reports on Working for Families for the November Income Support Ministers meeting. The two reports will cover detailed advice on:

- **Paper One: Further advice on options 1 and 5**, expanding on the content covered in this brief update
- **Paper Two: Administrative and operational improvements**, including more detailed advice on the buffer tax credit and increased debt write-off threshold.

At the November Ministers meeting, officials recommend Ministers choose a preferred option for redesign – this would allow officials and Ministers to focus on more detailed policy parameters that comes with significant redesign.

November advice content

Paper One: Further advice on options 1 and 5	Paper Two: Administrative and operational improvements
In addition to more detail on the options included in this update, Paper One will also respond to the following questions and feedback. **Option One:** • What impact the removal of the IWTC hours test has had, and advice on how to soften any reintroduction of this test. • Expected increased employment effects of this option. **Option Five:** • What is the impact of this option on sole parent households relative to other households? • How can this option reduce the reliance on some families moving onto a main benefit, and/or be more customer friendly for people on benefit? • Would lower income tax rates at the bottom help to improve work incentives for this option? **Across options:** • How do the options align with OB, UCB, and FCA? • Analysis of any potential savings, including any reduced supplementary/hardship payments. **Officials will also consider more detailed advice on:** • Child poverty, financial incentives / making work pay, and fiscal costs (including longer-term costs). • Behavioural impacts / labour supply. • Indexation and longer-term settings. • Phasing-in or sequencing of options (including using existing CPI adjustments). • Interactions of options with NZ Income Insurance Scheme.	In addition to more detailed advice on the buffer tax credit and increased debt write-off threshold, Paper Two will respond to the following requests for further advice: • giving WFF recipients a longer period of time in which to inform Inland Revenue of a change in circumstances ('grace periods') • improving information exchange between Inland Revenue and the Ministry of Social Development for people moving on and off benefit • other miscellaneous administrative changes to improve customer experience, as set out in the WFF advice provided in July 2022. This paper will also respond to the question on how widespread overpayments are resulting from the complexity of WFF.

Item 12

Inland Revenue
Te Tari Taake

MINISTRY OF SOCIAL DEVELOPMENT
TE MANATŪ WHAKAHIATO ORA

Report

Date:	27 April 2023	**Security Level:**	
To:	Hon Carmel Sepuloni, Minister for Social Development and Employment Hon Dr Deborah Russell, Associate Minister of Revenue		

Future direction of the Working for Families Review

Purpose of the report

1 This report provides you with a draft Cabinet paper for Ministerial consultation on the Working for Families Review (the Review) to date and the direction of further work towards a new, enhanced in-work payment.

Recommended actions

It is recommended that you:

1 **agree** to forward the attached draft Cabinet paper to your Ministerial colleagues for consultation and provide officials with feedback by 3 May 2023

Agree / Disagree	**Agree / Disagree**
Hon Carmel Sepuloni	**Hon Dr Deborah Russell**

2 **note** agency consultation on the draft Cabinet paper will occur concurrently to Ministerial consultation

3 **note** the Ministry of Social Development intend to lodge the paper late to Cabinet Office on 5 May 2023 for consideration by the Cabinet Social Wellbeing Committee on 10 May 2023

The Aurora Centre, 56 The Terrace, PO Box 1556, Wellington
– Telephone 04-916 3300 – Facsimile 04-918 0099

4 **note** that if agreed by Cabinet, officials will work with your Offices on communication material to announce the future direction of the Working for Families review.

s 9(2)(a)

27 April 2023

Polly Vowles
Policy Manager
Income Support Policy

Date

s 9(2)(a)

27 April 2023

Maraina Hak
Policy Lead
Inland Revenue

Date

Hon Carmel Sepuloni
Minister for Social Development and Employment

Date

Hon Dr Deborah Russell
Associate Minister of Revenue

Date

Background

2 Recent advice to Ministers in March 2023 as part of the Review focused on the option to introduce a new, enhanced in-work payment, as this option was most consistent with the objectives of the Review [REP/23/3/169; IR2023/018 refers].

3 Given the scale of the changes proposed, there was insufficient time to develop and model the detailed settings for a new payment in order to provide comprehensive advice for Budget 2023, and it could not be implemented in 2024. For this reason, more modest changes to In-Work Tax Credit settings were also explored that are broadly consistent with the direction of travel towards the new in-work payment design, while also being sensible standalone options. These changes were not progressed in Budget 2023.

4 In order for any Working for Families changes to be implemented in time to impact the ten-year child poverty targets, the new in-work payment would need to be implemented by 2025.

5 This means work would need to continue to progress at pace. In-principle decisions would need to be made at the end of 2023, and detailed parameters would need to be confirmed by April 2024 with funding provided at Budget 2024. Implementation timeframes will also depend on the final design of the option chosen and what other priorities Inland Revenue and the Ministry of Social Development are asked to progress over the same timeframes.

6 The Cabinet paper seeks agreement to the direction of further work towards a new, enhanced in-work payment, noting that simpler changes could be made if significant investment isn't possible in Budget 2024.

Announcing the possible direction of the Review on Budget Day

7 If agreed by Cabinet, you may wish to signal the possible direction of the Review on Budget Day. This would provide an update following the public engagement process last year and to key stakeholders' who have an ongoing interest in the Review.

8 Due to the complexity of the potential change, detailed settings have not been confirmed and there may be other policy issues that are yet to be identified, therefore officials do not recommend you announce option details. At most, we recommend you indicate that a new in-work payment is a possible direction of travel that is being explored further.

9 The paper notes that subject to Cabinet decisions, Ministers intend to respond reactively and make a media statement and/or engage with stakeholders indicating that a new in-work payment is the direction of travel that is being explored further as part of the Review, alongside consideration of changes to current settings.

10 Treasury may advise that this stronger wording ('the direction of travel') will trigger WFF changes being incorporated in the next fiscal forecasts. The paper now also does not address Treasury's feedback that Cabinet should explicitly agree to Budget Day communications.

Next Steps

11 It is recommended that you agree to conduct Ministerial consultation on the attached Cabinet paper from 28 April to 3 May 2023. Agency consultation will occur concurrently to Ministerial consultation.

12 The paper will then be lodged late to Cabinet Office on 5 May 2023 for consideration by the Cabinet Social Wellbeing Committee on 10 May 2023. You will be provided with an aide-memoire for this meeting.

13 If agreed by Cabinet, we will work with your Offices on communications material, signalling the future direction of the Review.

14 You will also report back to Cabinet on the final design of the new in-work payment by the end of 2023.

Appendix

Draft Cabinet paper - *Future direction of the Working for Families Review*

File ref: REP/23/4/348; IR2023/146

Author: Kahu Te Kani, Policy Analyst, Income Support Policy

Responsible manager: Polly Vowles, Policy Manager, Income Support Policy

In Confidence

Office of the Minister for Social Development and Employment

Office of the Associate Minister of Revenue

Cabinet Social Wellbeing Committee

Future direction of the Working for Families Review

Proposal

1 This paper provides an update on the progress of the Working for Families review (the Review) to date and seeks agreement to the direction of further work towards a new, enhanced in-work payment.

Relation to government priorities

2 The Government is focused on supporting New Zealand families with the rising cost of living. Changes as part of the Review will help lift the standard of living for families as they have a particular focus on supporting income adequacy, reducing child poverty and improving financial incentives to work.

3 Reducing child poverty is critical to the Government's priority of improving child wellbeing and laying the foundations for the future. Child poverty is a long-term enduring issue that is affecting New Zealand children now and continues to impact them into the future.

4 Improving child wellbeing is an area of cooperation under the Cooperation Agreement between The New Zealand Labour Party and The Green Party of Aotearoa New Zealand.

Executive Summary

5 Working for Families (WFF) is a suite of tax credits that provide additional support to low-income families. Following the Welfare Expert Advisory Group's (WEAG) report recommending significant changes to WFF, the Government agreed to review WFF as part of the Welfare Overhaul work programme. The Review now forms part of the priority Welfare Overhaul work over the next 12 months, with a particular focus on:

5.1 Low-income working families, while maintaining support for beneficiary families.

5.2 Options that shift more towards targeting support to low-income families rather than more universal support.

5.3 The principle of people being better off in work and assisting with costs for people in work.

6 Recent changes to WFF have focussed on broad rate increases to both working and beneficiary families through the Families Package, including increases to the Family Tax Credit (FTC) and introduction of the Best Start Tax Credit (BSTC). Increases to main benefit rates from 2020 to 2023 have also significantly increased incomes for families receiving benefits.

7 The In-Work Tax Credit (IWTC), on the other hand, was last increased in Budget 2015, the real value of the IWTC has decreased over time, and the numbers of families eligible for the payment have decreased as wages have risen. The IWTC is the key instrument to 'make work pay' within the wider context of the current WFF scheme and it was designed to address in-work poverty.

8 In-work poverty is an increasing issue for New Zealand suggesting there is a strong case for increased support for working families, particularly in the current climate. For a significant number of working families, the cost of living will have risen faster than incomes this past year.

9 Options progressed through the Review present the best opportunity to achieve substantial reductions in measured child poverty and to make significant headway towards achieving the ten-year targets, which are due to be achieved in 2027/28. In order for any WFF changes to be implemented in time to impact these targets, they would need to be implemented in 2025.

10 Overall, the evidence suggests that New Zealand's model of tax credits is not an outlier internationally, and the broad structure and targeting of WFF is largely fit-for-purpose, and generally effectively balances different objectives. However, improvements are needed to address identified issues with the design of the system, with fundamental change to the structure of the system most likely to address these issues.

11 To provide additional support to low-income working families and ensure people are better-off in work we recommend officials progress further work to develop a new, enhanced in-work payment. The new payment would be available to working families who are off-benefit and would replace the IWTC and MFTC. Given more detailed advice and decisions are required to determine detailed settings for a new in-work payment, the earliest this option could be implemented is April 2025.

12 There are smaller-scale options that could be progressed for April 2025 if fiscal conditions do not allow for significant investment in WFF through Budget 2024, including options that increase the IWTC rate or the abatement threshold, which could be packaged with administrative and operational improvements.

13 If agreed, Budget Day announcements could indicate that further advice will focus on exploring a new, in-work payment to replace the MFTC and IWTC as a potential direction of the Working for Families Review, alongside other changes to current settings to better support families.

14 In order for any new in-work payment to be implemented in April 2025, in-principle decisions would need to be made by the end of 2023 and detailed decisions by April 2024. We will report back to Cabinet on a proposed design of the new in-work payment by the end of 2023.

Background

15 The Working for Families (WFF) scheme was implemented between 2004 and 2007 to support income adequacy and reduce child poverty, and to improve financial incentives for low-income earners to participate in the labour market.

16 We made immediate changes when we came into Government to improve WFF through our Families Package. This increased income support to around 330,000 working and beneficiary families in the first year and included Family Tax Credit (FTC) increases and the introduction of a new Best Start tax credit.

17 Building on this, in 2017, the Government committed to overhauling the welfare system, including the WFF scheme, with a vision for a welfare system that ensured people in need are able to have an adequate income, are treated with respect and dignity, and are able to participate meaningfully in their communities. This was informed by the advice and recommendations of the Welfare Expert Advisory Group (WEAG). In its report in 2019, the WEAG recommended significant changes to WFF as part of a wider suite of changes to income support settings. Cabinet agreed to a review of WFF as part of the medium-term Welfare Overhaul work programme [CAB-19-MIN-0578].

18 On 12 May 2021, the Cabinet Social Wellbeing Committee (SWC) noted that Income Support Ministers[1] had agreed to bring forward the Review in order to prioritise reducing child poverty and determined its scope [SWC-21-MIN-0068].

19 In April 2021, given the recent and proposed increases to rates of benefits for beneficiary families at the time, Income Support Ministers agreed that there be a focus in the Review on:

19.1 Low-income working families, while maintaining support for beneficiary families.

19.2 Options that shift more towards targeting support to low-income families rather than more universal support.

19.3 The principle of people being better off in work, and assisting with costs for people in work [CAB-21-MIN-0167 refers].

20 Income Support Ministers also agreed that the original WFF objectives of supporting income adequacy and reducing child poverty, and improving financial incentives for low-income earners to enter the labour market remain important.

Summary of Working for Families payments[2]

Around 56% of all families in New Zealand receive WFF, at a cost of $2.7 billion for the 2022 income tax year. WFF is made up of the following tax credits:

[1] Income Support Ministers included the Minister for Child Poverty Reduction, Minister of Finance, Minister for Social Development and Employment and the Minister of Revenue.
[2] Note, figures are for the 2022-2023 tax year are provisional.

- **Family Tax Credit** (256,700 families, \$1.9 billion): the main payment received by both beneficiary and non-beneficiary families and is not dependent on work status. As of 1 April 2023, families receive \$136 per week for the eldest child and \$111 per week for each subsequent child. This payment begins to abate at \$42,700 of annual family income at 27%.

- **In-Work Tax Credit** (162,600 families, \$481m): the main in-work payment for families who do not receive a benefit. It pays \$72.50 per week for families with 1 to 3 children, with an extra \$15 per week for each subsequent child. After the Family Tax Credit is fully abated, it is abated at 27%.

- **Best Start Tax Credit** (119,200 families, \$299m): this payment provides \$69 per week to all families with a child under one year old, and for lower income families with a child under 3. For children aged 1 to 2 years, this payment begins to abate at \$79,000 of annual family income at 21%.

- **Minimum Family Tax Credit** (3,150 families, \$13m): this payment tops up incomes of working families and guarantees a minimum income level for low-income families working at least 20 hours per week who do not receive a benefit. The minimum income is currently set at \$34,216 of annual family income after tax.

21 We have already made short term changes as a first step of the WFF review which was estimated to increase incomes for 346,000 families by an average of \$20 per week. This was through an increase to FTC, as well as inflation adjusted increases to both FTC and Best Start. There was an additional increase on 1 April this year to both FTC and Best Start, further increasing incomes for families. In addition, there have been consecutive discretionary increases to main benefit rates each year from 2020 to 2023 above indexation, increases to the benefit abatement thresholds, and the indexation of main benefits to wages/CPI.

22 The IWTC, on the other hand, was last increased in Budget 2015, from \$60 to \$72.50 per week alongside a benefit rate increase for families with children.[3] There are no requirements to automatically increase the rate of the IWTC, meaning its real value has decreased over time, and the numbers of families eligible for the payment have decreased as wages have risen. The IWTC is the key instrument to supporting lower-income working families within the wider context of the current WFF scheme and it was designed to reduce in-work poverty. Alongside the Minimum Family Tax Credit (MFTC), it helps ensure that people are better off in work.

Evidence suggests improvements to the design of the system are needed to better support families

23 As part of the Review, officials brought together a range of evidence and analysis on issues relevant to WFF. A summary of this is provided in Appendix One.

[3] Since 2020 there have been some changes to eligibility settings of the IWTC: the hours test was removed from 1 July 2020 and grace periods were introduced from 1 April 2021.

24 Officials also conducted public engagement to inform the Review from April to June 2022. Findings were collated across survey responses, written submissions and sessions with key stakeholders.[4] Key messages heard through this process were:

24.1 The objective of income adequacy and reducing child poverty is important and payments need to keep up with the cost of living to provide adequate support.

24.1.1 For example, around half of stakeholders and submitters argued the IWTC should be paid to all families regardless of work and benefit status to support child poverty reduction.

24.2 Abatement of WFF payments means people often see little or no return from working more.

24.3 Supporting whānau with the costs of work is important, particularly childcare and transport costs.

24.4 The system is complex and can be difficult for families to access and navigate.

24.5 Debt is a significant issue that acts as a barrier to take-up and has a negative impact on whānau wellbeing.

25 Overall, the evidence suggests that New Zealand's model of tax credits is not an outlier internationally, and we face similar issues to other countries that use tax credits in terms of balancing objectives such as income adequacy and making work pay. Within current fiscal constraints, the broad structure and targeting of WFF is largely fit-for-purpose, and generally effectively balances different objectives.

26 However, improvements are needed to address identified issues with the design of the system. Firstly, there is an ongoing need to improve the adequacy of incomes for families both on benefit and in work. While this Government has made positive progress on child poverty, there are still too many children living in hardship in New Zealand. We still need to reduce these numbers by ### (AHC) and ### (BHC) in order to meet the 10-year targets.

27 Secondly, there are issues with the design of our tax credits that mean that some groups see little return to no return when they work more hours. Our abatement settings mean that multiple payments across the tax and benefit system withdraw at the same time, and the Minimum Family Tax Credit (MFTC) in particular has serious design issues.[5] For example, a sole parent in receipt of the MFTC and earning minimum wage is financially no better off working 35 hours a week compared to 20 hours a week. Receipt of the various payments also occurs across a complex 'benefit-

[4] The majority of feedback we received through written submissions and targeted engagement was from advocacy groups, and individuals connected to these groups, who have a strong focus on reducing child poverty. A very small number of submitters and stakeholders provided feedback with a more business-focussed or work incentive lens.

[5] These issues include 100% abatement meaning the MFTC can negatively impact decisions to work more hours and lack of flexibility for people with variable hours.

work interface' that impacts not just on people's experiences of the system but also on their outcomes.

Working families are a key group to support to help achieve child poverty targets

28 In-work poverty is an increasing issue in New Zealand, particularly for sole earners (both sole parents and couples with only one parent working). Rates of poverty have been increasing for this group, indicating a single income is becoming less sufficient for providing economic security and meeting basic needs. We also know around half of all children in poverty are from households where someone is in employment.

29 There is an even stronger case for supporting working families in the current climate. For a significant number of working families, the cost of living will have risen faster than incomes this past year. Inflation, as measured by the all-groups CPI, was 7.2% for 2022, whereas the net average wage increased by 6.2%.

30 The Review is currently the primary vehicle for achieving substantial reductions in measured child poverty and to make significant 'headway' towards achieving the ten-year targets, which are due to be achieved in 2027/28.

31 As discussed further below, and if Cabinet agrees to progress it, the Review will present options for funding consideration in Budget 2024 with likely implementation in 2025. This means these changes will not be implemented in time to contribute to achievement of the current three-year targets (which cover the period 2021/22 – 2023/24) but would contribute to progress in the third target period, which covers the 2024/25, 2025/26, and 2026/27 years. After the final three-year target period, there is one more financial year before the ten-year targets are due to be achieved (2027/28).

Over the past 12 months Income Support Ministers have received advice on options for reform

32 In July last year, officials provided Income Support Ministers with a summary of evidence and issues related to WFF tax credits, as well as a selection of high-level options to address some of the key issues identified. This advice included two options for significant structural reform:

32.1 The introduction of a new, enhanced in-work payment to replace the MFTC and IWTC, or

32.2 The removal of in-work payments through the creation of a single tax credit and greater support for low-income working families through the benefit system.

33 In early 2023, we requested that subsequent advice focus on the option to introduce a new, enhanced in-work payment. This was focused on ensuring parents would be better off when they work more hours, and targeted at continuing to reduce child poverty. This option was most consistent with one of the objectives of the Review to focus on working families, while maintaining support for beneficiary families.

We proposed a new, enhanced in-work payment be explored to address key issues with the structure of the system

34 To provide additional support to low-income working families and ensure people are better-off in work we recommend Cabinet agree in principle to this approach to develop a new, enhanced in-work payment. The new payment would be available to working families who are off-benefit and would replace the IWTC and MFTC.

35 The impact of a new in-work payment will depend on the design settings chosen. However, initial work by officials shows that a payment like this could substantially increase the incomes of low to middle-income working families and reduce child poverty. For example, an in-work payment of $386 a week to families off-benefit would cost around $703m per year of additional funding, benefit 170,000 families by an average of $79 a week compared to what they receive now and reduce the number of children in poverty by 18,000 (BHC50) and 29,000 (AHC50).

36 This option would potentially support families with variable working hours (if there is no 'hours test'[6]) and help to simplify the system by reducing the number of tax credits. It also presents an opportunity to address core design issues with the MFTC.

37 A shift to a new and more generous in-work payment is a fundamental change to the welfare system and is likely to have significant fiscal costs. This year, the Review will focus on further work to develop options for the in-work payment that balance trade-offs around fiscal cost, poverty reduction and incentives to work.

38 There are also a number of other detailed policy matters that would need to be worked through for the new payment design, including settings for parents in shared care situations; eligibility for the self-employed, and for recipients of Orphans Benefit, Foster Care Allowance, Unsupported Child's Benefit (OB/FCA/UCB); and detailed rules about how income and abatement settings are operationalised. Further work will also examine the equity of the changes for different groups and any legal implications, including comparing people without children and families with children, and support and requirements for those in and out of the benefit system.

39 Given more advice and decisions are required to determine detailed settings for a new in-work payment, the earliest this option could be implemented is April 2025.

Simpler changes could be made if significant investment is not possible in Budget 2024

40 Given the significant fiscal cost of fundamental changes to WFF, there are smaller-scale options that could be progressed if fiscal conditions to do not allow for a significant investment in WFF in Budget 2024. These options are broadly consistent with the direction of travel towards a new in-work payment, while also being sensible standalone options that could be implemented from 1 April 2025. This includes options that increase the IWTC rate or the WFF abatement threshold, which could be packaged with administrative and operational improvements.

Timing implications

[6] An 'hours test' is where people must work a minimum number of hours to be eligible for a payment, for example the MFTC currently has an 'hours test'.

41 Changes to the WFF system are needed in 2025 to contribute to the next targets for child poverty reduction. It is also important to note that in 2026 current projections show the MFTC threshold will exceed the WFF abatement threshold ($42,700), meaning the effective marginal tax rate for some families will be well over 100% and existing issues with WFF, particularly the MFTC, will be exacerbated. There is already some overlap in abatement between some main benefit rates and the WFF abatement threshold which means a small number of working families receiving benefits face effective marginal tax rates above 100%.

42 In order for a new in-work payment to be implemented in April 2025, work would need to continue to progress at pace. In-principle decisions would need to be made at the end of 2023, and detailed parameters would need to be confirmed by April 2024 with funding provided at Budget 2024. Implementation timeframes will also depend on the final design of the option chosen and what other priorities Inland Revenue (IR) and the Ministry of Social Development (MSD) are asked to progress over the same timeframes. Smaller scale changes could also be implemented in 2025.

43 We will report back to Cabinet on a proposed design of the new in-work payment by the end of 2023. Further decisions will be required to refine the new payment in time for Budget 2024 decisions. These timeframes are ambitious and rely on a quick Government formation following the election. It also means there is limited scope for further consultation on what would potentially be a fundamental reform to WFF.

Financial Implications

44 There are no financial implications arising from this Cabinet paper. Further work on the Review may have financial implications, which will be considered through future budget processes.

Legislative Implications

45 There are no direct legislative implications arising from this Cabinet paper. However, subject to Cabinet decisions, we intend to report back on options as part of the Review, which may have legislative implications.

Impact Analysis

Regulatory Impact Statement

46 Cabinet’s impact analysis requirements apply to the proposal to explore a new in-work payment alongside other smaller changes to current settings, but there is no accompanying Regulatory Impact Statement and the Treasury has not exempted the proposal from the impact analysis requirements. Therefore, it does not meet Cabinet’s requirements for regulatory proposals.

47 Officials from MSD and IR will prepare a regulatory impact statement to support Cabinet's decisions on a specific proposal later in the year.

Climate Implications of Policy Assessment

48 The Climate Implications of Policy Assessment (CIPA) team has been consulted and confirms that CIPA requirements do not apply to this proposal as it not expected to result in any significant, direct emissions impacts.

Population Implications

49 The impacts on different population groups will depend on the option chosen to progress, however we have included high-level impacts on WFF changes generally.

50 Approximately 56% of all families with children receive WFF[7], and 35% receive the In-Work Tax Credit (using administrative and TAWA outputs).[8] Those expected to benefit from potential changes to WFF are low and middle-income families with children. Sole parents, who are predominately women, make up a large proportion of low-income families. For the 2020 tax year, 52% of WFF recipients were sole parent families.

51 As Māori with children are overrepresented amongst low-income households they are likely to benefit from potential WFF changes. For example, as at June 2022, Māori were estimated to make up approximately 17% of the New Zealand population,[9] but 39% of benefit recipients.[10]

52 The impact of potential WFF changes on other groups may be proportionate to their representation in the target group of low and middle-income families. Pacific people with children are overrepresented amongst low-income households. Children in households where someone has a disability are over-represented amongst low-income families. These families will be likely to benefit from the changes.

Human Rights

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

Consultation

54 The Department of the Prime Minister and Cabinet, Oranga Tamariki, Treasury and Inland Revenue have been consulted in the development of this paper.

Communications

55 Subject to Cabinet decisions, we intend to respond reactively and make a media statement and/or engage with stakeholders indicating that a new in-work payment is the direction of travel that is being explored further as part of the Review, alongside consideration of changes to current settings.

[7] Using provisional data for the 2022-2023 tax year.
[8] Using data for the 2020-2021 tax year.
[9] Māori population estimates: At 30 June 2022 | Stats NZ
[10] As at March 2023, available at monthly-benefits-update-march-2023.pdf (msd.govt.nz)

Proactive Release

56 This paper will be proactively released within 30 business days of decision being confirmed by Cabinet, in accordance with Cabinet Office Circular CO (18)4, with any appropriate redactions.

Recommendations

The Minister for Social Development and Employment recommends that the Committee:

1 **note** that the Working for Families Review is priority work on the Welfare Overhaul work programme over the next 12 months;

2 **note** that the Working for Families Review has a particular focus on:

2.1 low-income working families, while maintaining support for beneficiary families

2.2 options that shift more towards targeting support to low-income families rather than more universal support

2.3 the principle of people being better off in work and assisting with costs for people in work;

3 **note** recent changes to Working for Families have focussed on broad rate increases to both working and beneficiary families through the Families Package, including increases to the Family Tax Credit and introduction of the Best Start Payment, and beneficiary families have gained from significant increases to main benefits in recent years;

4 **note** in-work poverty is an increasing issue for New Zealand and evidence suggests there is a strong case for increased support for working families;

5 **note** options progressed through the Working for Families Review are our primary vehicle to achieve substantial reductions in measured child poverty and to make significant headway towards achieving the ten-year targets, which are due to be achieved in 2027/28;

6 **agree** in principle to the Working for Families Review focusing on a new in-work payment to support working families;

7 **invite** officials to continue/ begin detailed work on a new in-work payment to support working families

8 **note** there are smaller-scale options that could be progressed for April 2025 if fiscal conditions do not allow for significant investment in Working for Families in Budget 2024, including increases to the rate of the In-Work Tax Credit and/or the Working for Families abatement threshold, which could be packaged with administrative and operational improvements;

9 **note** that in order for any Working for Families changes to be implemented in time to impact the ten-year child poverty targets, the new payment would need to be implemented in 2025;

10 **note** that in order for any new in-work payment to be implemented in April 2025, in-principle decisions would need to be made by the end of 2023 and detailed decisions by April 2024;

11 **invite** the Minister for Social Development and Employment and the Associate Minister of Revenue to report back to Cabinet on options for progressing a new in-work payment, alongside other changes to current settings, by the end of the year.

Authorised for lodgement

Hon Carmel Sepuloni

Minister for Social Development and Employment

Hon Dr Deborah Russell

Associate Minister of Revenue

Appendix: Summary of evidence

As part of the Review, officials brought together a range of evidence and analysis on issues relevant to WFF. This evidence helps assess the effectiveness of the current WFF payments and/or better understand the context the payments operate in.

Across this evidence, there are some issues which can be grouped around similar themes:

- **New Zealand's model of tax credits is not a significant outlier, and faces similar issues to many other countries.** Officials reviewed the design of different models of tax credits overseas, including Australia, the United Kingdom, the United States and Canada, and concluded that the design of WFF in New Zealand fits broadly within the spectrum of tax credit design in these countries. Other countries are similarly grappling with issues of balancing adequacy for working and non-working low-income families, while also maintaining incentives to work and making work pay.
- **In-work poverty is an increasing issue, as in many other countries.** Sole earners (both sole parents and couples with only one parent working) have higher rates of income poverty and material hardship compared to households with two parents in paid work. Rates of poverty have also been increasing for this group, indicating a single income is becoming a less viable option for providing economic security and meeting basic needs.
- **WFF tax credits are an effective poverty alleviation tool for families with children, but choices about targeting involve trade-offs.** Children in poverty are broadly evenly split between beneficiary families and the working poor, and can also be found across a range of low-to middle-income families. This means there are a range of different choices about how to target child poverty reduction, with different trade-offs around 'coverage' and cost-effectiveness, as well as different impacts on the relative levels of benefit and work.
- **While the gap between benefit and work has increased over the past two decades, issues with the design of WFF tax credits (and other income support payments) mean some groups see little return from working more.** Between 2003 and 2022, the gap between benefit and work increased for all family types, primarily because of the implementation of WFF between 2004 – 2007 and subsequent increases both to the minimum wage and to wages more generally. However, some groups of families currently face very high Effective Marginal Tax Rates (EMTRs), particularly low-income sole parents and second earners. This often means work does not 'pay' and sometimes even means they are worse off the more they work – particularly if they have childcare costs. The extent to which 'work pays' is just one factor that influences employment decisions, but the evidence suggests that changes to financial incentives do have modest impacts on employment decisions, with sole parents and second earners responding more than primary earners.
- **There is a case for investment in the early years of a child's life.** The evidence has demonstrated that this is when children are the most vulnerable to the consequences of poverty, and when caregivers are least able to support themselves through employment in the labour market. There are also affordability issues associated with

childcare for low-income families in New Zealand, and that the costs of childcare make a considerable difference on the extent to which 'work pays'.

- **Administrative issues impact not just on client experience, but also on adequacy and incentives.** The policy objectives of improving income adequacy and making work pay is more difficult if clients are not receiving their entitlements, and there is room for improvement in 'take-up' of in-work payments. The administration of WFF is also a contributor to overall debt to government, which can be a considerable cost burden on low-income families and can also discourage work.

High-level assessment of Working for Families

Income Support Ministers requested a high-level assessment of WFF, with a particular focus on whether the structure of WFF is 'fit-for-purpose' for low and middle-income families, and whether particular families have not benefited from the payment system who should:

- The introduction of WFF between 2004 and 2007 benefited low-income working families more than beneficiary families, and the significant reductions in child poverty it achieved were primarily for low income working households with children. However more recent changes as part of the Families Package in 2018 also provided gains for beneficiary families, and successive benefit increases in 2020, 2021 and 2022 have increased beneficiary incomes further. Both beneficiary and working families have benefited from WFF, though issues of income adequacy and poverty persist for both groups.
- Since the late 2000s, WFF has become progressively more targeted to those on lower incomes, as incomes have increased faster than the abatement thresholds and abatement rates have been increased. While this ensures money is generally well directed to those who need it more, it has now reached the point where payments are beginning to abate for those on very low incomes - even for some families supported by benefits. Abatement now overlaps with other income support payments, creating pockets of very high marginal tax rates.
- The 2004-07 WFF changes increased the margin between benefit and work and helped to 'make work pay', but the immediate impact on employment was relatively modest. Sole parents' paid employment increased, but second earners decreased, which suggests an incentive payment has modest impacts on decisions to work in aggregate.
- Officials believe there are significant issues with the design of in-work assistance, particularly the MFTC but also to a lesser extent the IWTC. There is also significant complexity in the system, not just in the number of payments and the design of their policy settings, but also in the delivery of some payments across two different agencies.

Overall, the broad structure and targeting of WFF currently achieves an effective balance between key objectives of income adequacy, fiscal cost, and maintaining financial incentives to work. However, further changes are recommended to address identified issues.

Inland Revenue
Te Tari Taake

MINISTRY OF SOCIAL DEVELOPMENT
TE MANATŪ WHAKAHIATO ORA

Report

Date: 20 July 2023 **Security Level:**

To: Hon Carmel Sepuloni, Minister for Social Development and Employment

Hon Dr Deborah Russell, Associate Minister of Revenue

Working for Families Review: Preferred approach for December Cabinet report back

Purpose of the report

1 The purpose of this report is to seek decisions on the preferred option for the Working for Families (WFF) Review. This will enable a Cabinet report back by the end of 2023 on the next steps of the Review.

Executive summary

2 The decisions in this report on the preferred option/s for the WFF Review will enable a report back to Cabinet in December 2023. If Ministers would like to progress a WFF option for consideration in Budget 2024, timely decisions on the advice in this report will be required.

3 Ministers have indicated that their preferred direction for structural reform was a scaled version of an option referred to in previous advice as Option 1B – a new in-work payment. Previous options considered by the Review are set out in Appendix One.

4 Through further work on the Review, officials have determined that there is insufficient time to develop a structural reform option for Budget 2024 (with an implementation date of 1 April 2025), though smaller-scale changes within the current system could still be considered. Options for structural reform could be considered in Budget 2025, with an implementation date of 1 April 2026. This report presents:

- a set of structural reform options illustrating key choices about the design of the in-work payment, and
- a set of smaller-scale changes within the current system focused on addressing issues with the current abatement threshold.

Structural reform of Working for Families - a new in-work payment

5 This new in-work payment combines the current work-related tax credits – the Minimum Family Tax Credit (MFTC) and In-Work Tax Credit (IWTC) into a single, more generous in-work payment. This new system also retains the Family Tax Credit (FTC) and the Best Start Tax Credit (BSTC) which go to both beneficiary and non-beneficiary families with children.

6 The new in-work payment would continue to be available for low to middle-income working families not receiving a main benefit. It also switches the order of abatement compared to the current system, with the new in-work payment abating first from a lower starting point, and the FTC abating after the in-work payment. This is illustrated in a diagram in **Appendix Two**.

7 The new in-work payment provides significant income gains to low and middle-income working families (meeting a key objective of the Review). At the same time, it would reduce the number of children in poverty. A core improvement of the new in-work payment is that it removes effective marginal tax rates (EMTRs) of above 100% created by the MFTC, improving work incentives for the approximately 3,000 current MFTC recipients.

8 The full-cost version of Option 1 was estimated in previous advice to cost around $1,055m per year (not including operational costs). Given this significant cost, a scaled option was also provided that reduced the annual fiscal cost to $703m[1] by increasing abatement settings to target increases more to lower-income working families, consistent with the objectives of the Review.

In-work payment variations

9 This report provides updated costings of the scaled option provided in previous advice[2] – referred to in this report as the "base case" (**IWP(base)**) – as well as four variations that adjust key parameters to address issues with the base option that:

- further reduce the high fiscal cost
- reduce high effective marginal tax rates (EMTRs), and
- reduce tensions with the benefit system.

[1] This costing was prepared for the March 2023 advice using a different Economic and Fiscal forecast update than the forecast update used for this paper.
[2] REP/23/3/169; IR2023/018

10 A key parameter that is varied to reduce cost is the payment rate - the IWP(base) option for the in-work payment option has a **high payment rate**.

11 The variations:

- Address the high cost of the IWP(base) option - **IWP(a)** and **IWP(b)**: A **medium or low payment rate** set in relation to **sole parents** receiving a broadly equivalent amount of income as the current system
- Address the high EMTRs of the IWP(base) option - **IWP(c)**: A **medium payment rate** with more **gradual abatement**
- Address the tension with the benefit system and high cost of the IWP(base) option - **IWP(d)**: A **medium payment rate** and a **partial hours test**.

12 The table below provides a summary of the main impacts of each in-work payment option. Costings in this report do not include operational costs – these will be provided in further advice.

	IWP(base)- high IWP	**IWP(a) – medium IWP**	**IWP(b) – low IWP**	**IWP(c) – medium IWP + gradual abatement**	**IWP(d) – medium IWP + partial hours test**
Fiscal impact[3] **Tax year 25/26**	$690m	$343m	$221m	$617m	$240m
Average gains/losses	170,000 HHs gain $78pw	148,000 HHs gain $45pw 5,000 HHs lose $20pw	136,000 HHs gain $33pw 11,000 HHs lose $18pw	173,000 HHs gain $68pw	142,000 HHs gain $34pw 11,000 HHs lose $20pw
Child poverty reduction	21,000 (BHC50) 26,000 (AHC50)	14,000 (BHC50) 14,000 (AHC50)	8,000 (BHC50) 7,000 (AHC50)	19,000 (BHC50) 23,000 (AHC50)	9,000 (BHC50) 10,000 (AHC50)

13 The base option for the new in-work payment and the variations presented in the report still meet the objectives of the Review outlined in paragraph 41 of

[3] Fiscal costs in this report use outputs from Treasury's Tax and Welfare Analysis model. Inland Revenue have also modelled these costs. There is some variance between the two modelling outputs, largely due to the differences in underlying populations between the models. Officials will determine the best source of costings for Cabinet papers and Budget proposals.

the main body of the report. However, when making choices between these options, the key trade-offs relate to managing fiscal cost against:

- the impact a reduced payment rate has on couples
- impacts on effective marginal tax rates and financial incentives to work, and
- achieving significant reductions in child poverty.

14 The variations are intended to illustrate the key choices about the parameters of the new in-work payment in order for Ministers to indicate their preferred settings in this advice and enable the next report to focus on detailed design issues.

15 Further assessment of each of the variations of the in-work payment is provided in **Appendix Three**, and **Appendix Four** provides further detail on the parameters of each option.

Variations - payment rate and impacts on couples

16 Setting the payment rate in relation to sole parents – at a **medium or low payment rate** (IWP (a) – (d)) – compared to the **high payment rate** in IWP(base), reduces the overall costs of the payment but perpetuates an existing issue with the benefit system in relation to the MFTC. With the current rate of MFTC, couples are not necessarily better off leaving the benefit system at 30 hours of work at the minimum wage than they are receiving an abated benefit.

17 The lower the payment rate is set, the more that couples would need to work to be better-off receiving it. Also, the "30-hour rule" in the benefit system means that a small number of couples may not be able to continue to receive Jobseeker Support beyond 30 hours of work a week, so may need to come off benefit and be worse off. To ensure these couples aren't worse off at 30 hours, changes to primary legislation are recommended to enable couples to continue to receive an abated benefit for longer.

18 Officials will provide further advice on this issue depending on the option chosen.

Variations - abatement settings and targeting of fiscal costs

19 The IWP(base) option and most of the variations have abatement settings that increase EMTRs compared to the current system for most recipients of WFF tax credits (other than current MFTC recipients). Providing more **gradual abatement** rates (IWP(c)) maintains the EMTRs at or below the current levels (maintaining financial incentives to work). However, the more gradual abatement means that this option is significantly costlier than the other variations and has a similar scale of fiscal costs compared to the base option. Further, the large fiscal costs are less targeted towards low-income working families compared to other options.

Variations - introducing an hours test to reduce tension with the benefit system

20 The new in-work payment provides a level of income that is much closer to what is received by a main benefit compared to the current system. Having a large payment with minimal work requirements creates a tension with the benefit system given the work obligations and sanctions attached to the receipt of main benefit. Without an hours test, the new payment could be argued to undermine the purpose and principles of the benefit system and in particular the work obligations and sanctions laid out in the Social Security Act 2018.

21 However, it is not easy to address this issue without facing significant trade-offs. The key advantage of an hours test is that it mitigates tensions with the work obligations and sanctions in the benefit system and provides greater incentives to work more by retaining the hours test for the full amount of weekly payment.

22 The key disadvantages of an hours test are that it would reintroduce complexity, uncertainty and potentially increase debt for a larger number of WFF recipients who have fluctuating employment arrangements. For this reason, Inland Revenue (IR) do not recommend this option as it would be unlikely to improve the current system overall.

Considerations to be worked through in subsequent advice on structural reform with a new in-work payment

23 There are further considerations for the new in-work payment that will be provided in subsequent advice. These considerations require a considerable amount of further detailed policy work.

24 These include: indexation of the in-work payment rate and/or abatement settings, implications for the costs of any future discretionary increases to main benefits or the FTC, eligibility of self-employed families; how shared care arrangements are dealt with; eligibility for Orphans Benefit/ Unsupported Childs Benefit /Foster Care Allowance recipients; consideration of 4+ children rate, detailed abatement and ring-fencing rules (including abatement thresholds), and payment settings in relation to the MFTC within the transition period.

25 Ministerial decisions on many of these aspects would be needed to inform a future Budget Bid.

Emerging issues to address if structural reform is not progressed

26 If no changes are made to Working for Families in the next two years, overlapping abatement will increasingly undermine the functioning of the system. It is anticipated that by 1 April 2026 the MFTC and the WFF abatement thresholds will overlap, creating effective marginal tax rates (EMTRs) of over 100% for a small group of low-income working families that would grow without continual adjustments.

27 In addition, an increasing number of beneficiaries will also face overlapping abatement of their main benefits and the Family Tax Credit (FTC). Finally, inflation and wage growth have been significant since the WFF abatement threshold was last adjusted in 2018. Increases in the abatement threshold are recommended by officials to both address overlapping abatement and ensure that WFF continues to support both low and middle-income working families. These issues could be addressed by either structural reform or smaller-scale changes to Working for Families progressed in Budget 2025 at the latest.

Options to address overlapping abatement thresholds

28 There are four options that are presented that address the abatement threshold overlap and progress complementary increases to IWTC and/or remove the MFTC completely. These are summarised in the table below.

	AT(a) Abatement threshold to $50,000 pa only	**AT(b)** $10 pw IWTC increase + abatement threshold to $50,000 pa	**AT(c)** $25 pw IWTC increase + WFF abatement threshold to $50,000 pa + MFTC removed	**AT(d)** $10 pw IWTC increase + WFF abatement threshold to $50,000 pa + MFTC removed
Fiscal impact **Tax Year (24/25)**[4]	$238m	$309m	$406m	$291m
Average gains/losses	152,000 HHs gain $30pw	173,000 HHs gain $34pw	173,000 HHs gain $46pw 6,000 HHs lose $35pw	167,000 HHs gain $35pw 7,000 HHs lose $36pw
Child poverty reduction	4,000 (BHC50) 11,000 (AHC50)	6,000 (BHC50) 17,000 (AHC50)	8,000 (BHC50) 19,000 (AHC50)	5,000 (BHC50) 16,000 (AHC50)

29 The abatement threshold options could be progressed in lieu of wider structural reform or as a first step progressed in either Budgets 2024 or 2025, and structural reform options considered through later Budgets.

30 As with the in-work payment options, further assessment of each of the variations of the in-work payment is provided in **Appendix Three**, and **Appendix Four** provides further detail on the parameters of each option.

Preferred approach for December Cabinet paper

31 Choices between higher and lower-cost options depend primarily on the Government's wider fiscal strategy and desired progress towards the ten-year child poverty reduction targets.

[4] Fiscals costs only, does not include implementation or operational costings.

32 **Appendix Three** sets out key trade-offs for consideration of the in-work payment options and the abatement threshold options discussed in this report:

- High-cost options for an in-work payment: IWP(base) / IWP(c)
- Lower-cost options for an in-work payment: IWP(a) / IWP(b) / IWP(d)
- Abatement threshold increase and complementary changes: AT(a) – (d).

33 When considering between the IWP options, variations have been provided to reduce costs and address key issues with the base option. However these variations also introduce more trade-offs. While the in-work payment removes effective marginal tax rates (EMTRs) of above 100% for the small number of MTFC recipients, the overall impact of the new IWP is that it increases EMTRs for the much larger group of FTC recipients. However, maintaining EMTRs at current levels results in significantly higher fiscal costs and less targeting to lower-income families.

34 Some of the variations of the IWP also create losers (IWP(a), IWP(b) and IWP(d)) and provide lower child poverty reductions. The higher cost options, IWP(base) and IWP(c) provide the largest child poverty reductions. Finally, there are differing agency views on whether or not there is an hours test with the in-work payment.

35 IR do not recommend re-introducing a partial hours test as it would reintroduce complexity, uncertainty and potentially increase debt for a larger number of WFF recipients who have fluctuating employment arrangements. For MSD, the decision on whether or not to introduce an hours test is finely balanced but given the large in-work payment, providing it without an hours test represents a large philosophical change to the welfare system as noted in paragraph 20 above.

36 If Ministers are interested in progressing changes that cost between $200 - $400m then the trade-offs and losers associated with the lower cost IWP options begin to outweigh the benefits associated with the new in-work payment. For a similar fiscal envelope, officials recommend considering the abatement threshold options, AT(a) or AT(b), instead.

37 While the abatement thresholds options do not provide large structural reform, they help to maintain the policy intent of WFF by adjusting the abatement thresholds to allow for recent wage and inflation increases. Abatement threshold options also provide a key change that most stakeholders are interested in. By not removing the MFTC, option AT(a) and AT(b) do not create any losers and are comparatively simpler to administer. Officials do not recommend abatement threshold options that remove the MFTC unless further changes are made to reduce the number of families financially disadvantaged.

38 The implementation dates outlined in this report are indicative. Once policy and implementation dates are available, consideration of the deliverability of

this initiative within MSD and Inland Revenue's wider policy change portfolio would need to be made.

Next steps

39 Given the scale of some of the options presented in this report, we recommend this advice is forwarded and discussed with a group of Ministers that replicates the previous Income Support Ministers. This group would include the Prime Minister, Minister for Children, Minister of Finance, Ministers of Child Poverty Reduction and the Minister of Revenue.

Recommended actions

It is recommended that you:

1 **note** that as requested by Ministers, this report provides further advice on options for structural reform of Working for Families focussed on a new in-work payment

2 **note** you are expected to report back to Cabinet outlining the next steps for the Working for Families Review by the end of 2023

3 **note** a new in-work payment has a strong focus on making working pay and would provide significant gains in incomes for low-income working families and simplification of the system for working families

4 **note** the new in-work payment also has high fiscal costs and it also represents a fundamental shift in the welfare system, with flow-on impacts that may need to be addressed within benefit settings

5 **note** although costings for the new in-work payment have assumed a 1 April 2025 implementation date, officials do not consider there is sufficient time between now and the election to undertake the detailed design and analysis on the preferred option that will be required to progress a Cabinet paper by the end of 2023

6 **note** that if Ministers would like to progress a new in-work payment, officials will provide advice in late 2023 or early 2024 to enable decisions in Budget 2025 with an implementation date on or after 1 April 2026

7 **note** if a structural reform option is not progressed due to fiscal constraints or implementation timings, officials recommend progressing an option to increase the abatement threshold of WFF to avoid overlapping abatement thresholds and ensure that WFF continues to support both low and middle-income working families

8 **agree** to progress as an end-point of the review an option that either:

8.1 results in structural reform of the Working for Families system by introducing a new in-work payment

AGREE / DISAGREE

OR

8.2 addresses an anticipated issue related to overlapping abatement thresholds for Working for Families tax credits

AGREE / DISAGREE

If you agree to structural reform options for a new in-work payment

9 **note** that, due to the high cost of the new in-work payment proposed in previous advice [REP/23/3/169; IR2023/018 refers], officials have outlined variations to the proposed new payment

10 **note** that these options scale costs and address key issues of high effective marginal tax rates and tensions with the benefit system

11 **note** alternative options for the new in-work payment vary across the following parameters:

11.1 how the payment rate is set;
11.2 how the payment will abate;
11.3 how the payment will interact with main benefits

12 **note** recommendations 13 - 16 below seek your preferred approach within these parameters

13 **indicate** whether the payment rate should be set:

13.1 at a high payment rate to ensure that couples are better off off-benefit at 30 hours of work on the minimum wage: IWP(base)

YES / NO

OR

13.2 a medium or low payment rate to ensure that sole parents would be better off off-benefit when working at least 20 hours of work on the minimum wage: IWP(a), IWP(b), IWP(c), IWP(d)

YES / NO

14 **note** the dollar figures for the medium and low rates are illustrative and can vary depending on exact parameters

15 **indicate** whether the two-tier abatement settings should:

15.1 increase EMTRs but target the payment towards low-income families: IWP(base), IWP(a), IWP(b), IWP(d)

YES / NO

OR

15.2 provide lower abatement rates to maintain EMTRs at or just below current levels: IWP(c)

YES / NO

16 **indicate** whether, in order to address interactions with main benefits, there should be:

16.1 no hours test: IWP(base), IWP(a), IWP(b), IWP(c) [Inland Revenue preferred option]

YES / NO

OR

16.2 a partial hours test: IWP(d)

YES / NO

17 **note** that based on preferences indicated in recommendations 13 - 16 further advice will be provided on detailed design issues related to the payment

If you agree to addressing the anticipated overlapping abatement of Working for Families tax credits

18 **note** that to address anticipated overlapping abatement thresholds of the Working for Families tax credits by 2026, there are options to increase abatement thresholds with or without increases to the IWTC and removal of the MFTC

19 **note** consistent with previous advice, options to increase abatement thresholds could be progressed as a first step to further structural reform, in particular because the new in-work payment cannot be implemented until on or after 1 April 2026

20 **note** the costings in the report for the abatement threshold (AT) options are the same costings used in the March advice and assumed a 1 April 2024 implementation date

21 **indicate** your preferred approach to address the overlapping abatement thresholds by:

21.1 increasing the abatement threshold to $50,000 only [AT(a)]

YES / NO

OR

21.2 increasing the abatement threshold to $50,000 and a $10 per week increase to the IWTC [AT(b)]

YES / NO

OR

21.3 increasing the abatement threshold to $50,000 and a $25 per week increase to the IWTC and removal of the MFTC [AT(c)]

YES / NO

OR

21.4 increasing the abatement threshold to $50,000 and a $10 per week increase to the IWTC and removal of the MFTC [AT(d)]

YES / NO

22 **agree** that officials provide advice on further changes to mitigate the issue of overlapping abatement thresholds in future, such as indexing the WFF abatement threshold, and potentially increasing or indexing the threshold for the Best Start Tax Credit

AGREE / DISAGREE

23 **note** options AT(a) and AT(b) set out in recommendation 21 could be implemented from 1 April 2024 if a Budget 2024 pre-commitment is agreed

24 **note** options AT(c) and AT(b) set out in recommendation 21 could not be implemented before 1 April 2025 due to the removal of the MFTC within these options

25 **indicate** your preferred implementation date of the preferred option in recommendation 21, either:

25.1 1 April 2025, with funding sought through Budget 2024

YES / NO

OR

25.2 1 April 2026, with funding sought through Budget 2025

YES / NO

Next steps

26 **note** officials will provide further advice to the Minister for Social Development and Employment and the Associate Minister for Revenue on the administrative/operational improvements for Working for Families when officials next report back on the wider package

27 **agree** to forward a copy of this report to the Prime Minister, Minister for Children, Minister of Finance, Minister for Child Poverty Reduction, and the Minister of Revenue

AGREE / DISAGREE

28 **agree** that a meeting is set up with the Ministers outlined in recommendation 27 to discuss the advice in this report.

AGREE / DISAGREE

s 9(2)(a) [redacted]

20/07/2023

Polly Vowles
Policy Manager, Ministry of Social Development

Date

s 9(2)(a) [redacted]

20/07/2023

Maraina Hak
Policy Lead, Inland Revenue

Date

Hon Carmel Sepuloni
Minister for Social Development and Employment

Date

Hon Dr Deborah Russell
Associate Minister of Revenue

Date

Advice to date on Working for Families

40 The Working for Families Review (the Review) has been progressing since April 2021 and has provided advice on a range of options to improve the system based on a review of evidence and literature.[5]

41 In 2021, given recent and proposed increases to rates of main benefits for beneficiary families at the time, Income Support Ministers[6] agreed that there be a focus of the Review on:

- Low income working families, while maintaining support for beneficiary families
- Options that shift more towards targeting support to low-income families rather than more universal support
- The principle of people being better off in work, and assisting with the costs for people in work [CAB-21-MIN-0167].

42 Income Support Ministers also agreed that the original WFF objectives of supporting income adequacy and reducing child poverty, improving financial incentives for low-income earners to enter the labour market, and providing timely and accurate entitlement remain important.

43 Further details on the options previously considered in the Review can be found in paragraphs 120 - 123 below, and a full list of options is provided in **Appendix One**.

44 Based on advice provided in November 2022, the Minister for Social Development and Employment and the Minister of Revenue received advice in March 2023 [REP 23/3/169] outlining:

- a potential Budget 2023 initiative for smaller-scale changes to current settings
- high-level advice for longer term-term structural change for Budget 2024 in the form of a new in-work payment.

45 The Working for Families Budget 2023 initiative was not successful. In May 2023, the Minister for Social Development and Employment and the Associate Minister of Revenue took a paper to Cabinet, providing an update on the progress of the Review to date [CAB-23-MIN-0178].

46 The paper noted that the next steps of the Review will consider exploring a potential new in-work payment (IWP) to support working families alongside consideration of other changes to current settings. The paper also noted the

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[5] March 2023 (REP/23/3/169; IR2023/018); November 2022 (REP/22/11/1097; DPMC-2022/23-547; T2022/2489; IR2022/511); July 2022 (REP/22/7/682; T2022/1644; IR22/145; DPMC-2021/22-2539)

[6] Income Support Ministers included the Minister for Child Poverty Reduction, Minister of Finance, Minister of Social Development and Employment and the Minister of Revenue.

Review provides the best opportunity to make progress on meeting the Government's long-term child poverty targets. The Minister for Social Development and Employment and the Associate Minister of Revenue were invited to report back to Cabinet by the end of the year on the next steps of the Review.

Purpose and structure of this report

47 The decisions in this report on the preferred option/s for the WFF Review will enable a report back to Cabinet in December 2023. If Ministers would like to progress a WFF option for consideration in Budget 2024, timely decisions on the advice in this report will be required.

48 Through further work on the Review, officials have determined that there is insufficient time to develop a structural reform option for Budget 2024 (with an implementation date of 1 April 2025), though smaller-scale changes within the current system could still be considered. Options for structural reform could be considered in Budget 2025, with an implementation date of 1 April 2026.

49 Furthermore, if no changes are made to Working for Families in the next two years overlapping abatement will increasingly undermine the functioning of the system. This issue could be addressed by either structural reform or smaller-scale changes to Working for Families progressed in Budget 2025 at the latest.

50 Officials note that these initiatives will need to be considered as part of the Government's wider policy work programme to mitigate potential deliverability risk, particularly where agencies are asked to deliver other changes within a similar timeframe.

51 This report is separated into four parts to address the above issues and related work:

- Section One: Options for structural reform of Working for Families
- Section Two: Smaller scale options to address anticipated overlapping abatement thresholds
- Section Three: Economic and fiscal context and the child poverty reduction targets
- Section Four: Further work and timeframes for Cabinet report back

Section One: Options for structural reform of Working for Families

52 Option 1 introduces a new in-work payment, which combines the MFTC and IWTC into a single, more generous payment, and retains the FTC. It would continue to be available for low to middle-income working families not receiving a main benefit. It also switches the order of abatement compared to the current system, with the new in-work payment abating first, from a lower

starting point and the FTC abating after the in-work payment. This is illustrated in a diagram in **Appendix Two**.

53 Option 1 provides significant income gains to low and middle-income working families (meeting a core objective of the Review) and reductions in child poverty. A core improvement of the new in-work payment is that it removes effective marginal tax rates (EMTRs) of above 100% created by the MFTC, improving work incentives for the roughly 3000 families currently receiving MFTC. Previous advice has canvassed two variations of this option:

- Option 1A: allows families to receive <u>some</u> of the payment before the hours test[7] is met, before being topped up to the full amount.
- Option 1B: allows families to receive all of the payment without an hours test.

54 It is worth noting that a new payment that is targeted towards families off benefit is not the preferred direction of the Review for a large group of stakeholders. From public engagement conducted in 2022, around half of stakeholders and submitters, including the Child Poverty Action Group, argued that the IWTC should be paid to all families regardless of work and benefit status to support child poverty reduction.

55 In the March advice, Option 1B was estimated to cost $1,055m a year in 2025/26.[8] Ministers previously indicated that a fiscal envelope of $200m to $400m a year was likely to be appropriate in Budget 2023. Updated advice on the current economic and fiscal context is provided later in the report in paragraphs 146 - 147.

56 A scaled version of Option 1B was also provided to reduce costs to closer to the suggested envelope. The scaled version of Option 1B had the same payment rate but had higher abatement compared to the full-cost version of Option 1B, targeting the increase in payments more towards lower-income families, consistent with the objectives of the Review. However, the scaled version also provides for smaller income gains and reductions in child poverty and increases EMTRs slightly for many families compared to the current system. The scaled version of Option 1B was estimated to cost $703m in 2025/26 [REP 23/3/169].

57 Ministers have indicated that their preferred direction for structural reform of WFF was a scaled version of Option 1B. This section provides updated costings of the scaled Option 1B (with a higher two-tier abatement regime)

[7] The hours test relates to the minimum number of hours a family needs to work before they are eligible for the full rate of payment. For this payment the hours test is 20 hours a week for sole parents and 30 hours a week for couples. For families that work below the hours test are eligible for a partial payment.

[8] Costings for this report used the Half Year Economic and Fiscal Update 2022 (HYEFU 22) as a base.

which will be referred to as the "base case" in-work payment option – IWP(base) - for the remainder of the report.[9]

58 The key parameters of the IWP(base) are:

- A **high payment rate** of $384 per week (set at a level so that couples are better off receiving the IWP working 30 hours on minimum wage[10])
- The payment abates at 55% from working 20 hours a week on minimum wage ($26,500 per annum (pa)), reducing to 30% from the Accommodation Supplement abatement threshold ($49,500 pa)[11]
- has no hours test.

59 It also presents four alternative options related to this option which adjust key parameters of the new in-work payment to address issues with the current IWP option – its high cost, high abatement rates and tension with the benefit system. All of these options have a lower payment rate that only ensures that sole parents are better off moving off-benefit at 20 hours of work on the minimum wage and does not ensure that couples are better off. This issue is described in more detail in paras 76 - 79 below.

60 The report presents four alternative options to the IWP(base). These are set out below with the key differences to the parameters of the base option described in paragraph 58 bolded:

- To address the high cost - IWP(a) and IWP(b): A **medium payment or low payment rate** set in relation to **sole parents** receiving broadly equivalent amount of income as the current system
- To address the high EMTRs - IWP(c): A **medium payment rate** with more **gradual abatement**
- To address the tension with the benefit system - IWP(d): A **medium payment rate** and a **partial hours test** to address tension with the benefit system.

[9] Costings have used the Budget and Fiscal Update 2023 (BEFU 23) forecasts and an implementation date of 1 April 2025 and do not include operational costings.
[10] The modelling for the IWP options has assumed a minimum wage of $25.50 per hour from 1 April 2025.
[11] This is to avoid EMTRs over 100% once the Accommodation Supplement starts to abate at 25c/$1.

61 A summary of key impacts of the parameters of each option is provided in Appendices Two and Three and in the table below:

	IWP(base)- high IWP	**IWP(a) – medium IWP**	**IWP(b) – low IWP**	**IWP(c) – medium IWP + gradual abatement**	**IWP(d) – medium IWP + partial hours test**
Payment rate	High - $384pw	Medium - $335pw	Low - $316pw	Medium - $335pw	Medium - $335pw
Payment rate – who is better off	Couple	Sole parent	Sole parent	Sole parent	Sole parent
Abatement rates	Base	Base	Base	Less severe	Base
Hours Test	No	No	No	No	Yes
Fiscal impact (25/26)	$690m	$343m	$221m	$617m	$240m
Average gains / losses	170,000 HHs gain $78pw	148,000 HHs gain $45pw 5,000 HHs lose $20pw	136,000 HHs gain $33pw 11,000 HHs lose $18pw	173,000 HHs gain $68pw	142,000 HHs gain $34pw 11,000 HHs lose $20pw
Child poverty reductions	21,000 (BHC50) 26,000 (AHC50)	14,000 (BHC50) 14,000 (AHC50)	8,000 (BHC50) 7,000 (AHC50)	19,000 (BHC50) 23,000 (AHC50)	9,000 (BHC50) 10,000 (AHC50)

62 Fiscal costs in this report use outputs from Treasury's Tax and Welfare Analysis model. Inland Revenue have also modelled these costs. There is some variance between the two modelling outputs, largely due to the differences in underlying populations between the models. Officials will determine the best source of costings for Cabinet papers and Budget proposals.

63 The base option for the new in-work payment and the variations presented in the report still meet the objectives of the Review outlined in paragraph 41. However, when making choices between these options, the key trade-offs relate to managing fiscal cost against:

- achieving significant reductions in child poverty
- impacts on effective marginal tax rates and financial incentives to work, and
- the impact a reduced payment rate has on couples.

64 Another key tension the new in-work payment creates is with the benefit system if there is no hours test. Without an hours test, the new payment could be argued to undermine the purpose and principles of the benefit system and in particular the Social Security Act 2018, which is centred around work with strong obligations and sanctions. However, an hours test would reintroduce complexity, uncertainty and potentially increase debt for a larger number of WFF recipients who have fluctuating employment arrangements.

65 These trade-offs are summarised in a table in **Appendix Three** and discussed further in each section of the alternative options below.

In-work payment, base option - IWP(base): A new, enhanced in-work payment, with two-tier abatement

66 The IWP(base) option provides the new in-work payment for working families with children who are off-benefit. The payment is set at $384 pw (high payment rate). This payment rate is set at this level to ensure that couples with a single earner working 30 hours a week at the minimum wage will be better off receiving the payment than remaining on a main benefit. These are similar payment settings to the MFTC prior to 2021, but with more gradual abatement.

67 The high payment rate means that the number of hours of work where sole parents are better off will be much lower. Assuming a minimum wage of $25.50 at 1 April 2025, a sole parent would be better off moving off-benefit working 15 hours a week.

68 The key feature of the base option is that there is no hours test meaning that families would receive the full in-work payment ($384 pw) when they are in paid work and off-benefit. This means that there are no minimum number of hours of work required to receive the full amount like the current IWTC, but unlike the MFTC.

69 Modelling[12] indicates that IWP(base) (scaled from the full option 1B) would:

- Cost $690m in 2025/26 (the first full year of payments)
- See 170,000 households gain an average of $78 per week, and
- Reduce child poverty by 21,000 children on the BHC50 measure, and 26,000 on the AHC50 measure.

70 The base option meets the objectives of the Review and provides the greatest reduction in child poverty and the greatest weekly gain to households of the options costed for this report.

[12] In the March Report, this option cost $703m. Fiscal modelling provided in the March report has been updated using BEFU 23.

71 Despite the benefits of this option, the main trade-offs related to this option are:

- **Cost** – even with the two-tier abatement settings this option still has a high fiscal cost of $690m per year which may not be feasible. Options IWP(a) and IWP(b) present ways to reduce the payment rate and lower the overall cost of this option.
- **Effective marginal tax rates** – the rate at which the in-work payment abates creates higher EMTRs for many families. Option IWP(c) provides an alternative setting for the two-tier abatement to lower EMTRs (noting that this increases the cost)
- **Tension created with the benefit system** – having a large weekly payment with no hours test creates tensions with the benefit system in relation to work obligations and sanctions for a near-equivalent rate of payment in the benefit system. To mitigate this, Option IWP(d) includes a partial hours test.

Lower payment rates to address the overall costs of the base option: IWP(a) and IWP(b)

72 The two lower payment rate options costed for this report are:

- A **medium payment rate** of $335 per week – IWP(a), and
- A **low payment rate** of $316 per week – IWP(b).

73 Assuming a 1 April 2025 implementation date, IWP(a) would:

- cost $343m in 2025/26
- see 148,000 households gain an average of $45 per week and see 5,000 households lose an average of $20 per week[13], and
- reduce child poverty by 14,000 children on the BHC50 measure and 14,000 on the AHC50 measure.

74 Assuming a 1 April 2025 implementation date, IWP(b) would:

- cost $221m in 2025/26
- see 136,000 households gain an average of $33 per week and see 11,000 households lose an average of $18 per week[14], and
- reduce child poverty by 8,000 children on the BHC50 measure and 7,000 on the AHC50 measure.

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[13] The losers for this option are in-work couple families who lose more in IWTC than the gain in the combined new in-work payment plus the FTC. This includes anyone not receiving a full year of the IWP (for example those with shared care arrangements and higher income families with more than four children).

[14] The losers for this option are in-work couple families who lose more in IWTC than the gain in the combined new in-work payment plus the FTC.

75 These lower cost options still largely meet the objectives of the reform (see **Appendix One**) with much lower fiscal costs. IWP(a) is approximately 50% of the cost of the base option for the first full year of payment and IWP(b) is approximately 32% of the cost.

76 However, both IWP(a) and IWP(b) provide for more modest gains for families and smaller reductions in child poverty than IWP(base), with the lower payment rate resulting in the smallest income gains and lowest reductions in child poverty.

Trade-offs for payment rates - couples

77 Both the medium and low payment rates reflect the current MFTC settings which have prioritised the payment rate towards sole parents being better off, due to decisions to only partially increase the MFTC abatement thresholds in 2020 [CAB-20-MIN-0152 refers].

78 Sole parents make up around 86% of current MFTC recipients. Setting the payment at a rate that means sole parents will be better off will likely meet the policy intent for the majority of recipients. Previous advice has also noted that the available evidence in New Zealand and overseas suggest that sole parents have more significant responses to changes in financial incentives to work than primary earners in couples. This evidence also suggests that greater in-work payments can work in the opposite direction for couples, by reducing the labour force participation of secondary earners in couples overall.

79 However, a key trade-off with a payment rate below $384 per week means that a couple will no longer be better off moving off-benefit and receiving the IWP working 30 hours a week on minimum wage. The lower the rate, the more couples will need to work – for example, a couple with a single earner on the minimum wage would need to work for 38 hours a week on the minimum wage[15] to be better off receiving the IWP (with a medium payment rate). For an IWP with the lower payment rate, a couple with a single earner on the minimum wage would need to work 41 hours a week on the minimum wage to be better off off-benefit.

80 Further, the "30-hour rule" in the benefit system means that a small number of couples may be ineligible for Jobseeker Support at this point, so may need to come off benefit (before it fully abates) and be worse off because their employment earnings alone are not equivalent to the amount received through the benefit system.[16] To ensure these couples aren't worse off at 30

[15] Assuming a minimum wage of $25.50 on 1 April 2025
[16] Jobseeker Support recipients cannot continue to receive the benefit if they are working full-time, which is deemed to be 30 hours or more per week. There are exceptions for sole parents and grandparented clients who were transferred to Jobseeker Support during Welfare Reform, who can work full time for up to 26 weeks.

hours of work or more, changes to primary legislation are recommended to enable couples to continue to receive an abated benefit for longer (ie. remaining eligible when working more than 30 hours per week). Officials will provide further advice on this issue depending on the option chosen.

Trade-offs for payment rates – between medium and low payment rates

81 The exact dollar figures of the medium and lower rates are illustrative and can vary, both higher and lower, depending on other variables. The two key considerations for how payment rates could be set are comparisons with existing levels of payments (MFTC and IWTC) and the minimum wage.

82 The **medium payment rate** provides families working 20 hours a week on the minimum wage with an equivalent amount of support from the IWP as the combined value of the MFTC and IWTC on 1 April 2024.

83 The **low payment rate** provides these families with a lower amount of IWP than the current system would on 1 April 2025. However, if there are increases in the minimum wage (for the purposes of these costings we have assumed a minimum wage on 1 April 2025 of $25.50), then sole parents overall incomes would not fall and they would still be better off overall off-benefit at 20 hours of work.

84 For this report the **low payment rate** means that sole parents working 20 hours a week at the minimum wage would see a $5 increase in net weekly income on 1 April 2025, compared to what they would be receiving on 31 March 2025 if they were working 20 hours and receiving the MFTC and IWTC, because they receive higher income from the minimum wage increase. However, this effectively means they do not gain from the increase in the minimum wage. **The medium payment rate** means that these families retain more of the gain from an increase in the minimum wage and are $24 per week better off, comparing 31 March and 1 April 2025.

85 If the payment rate is set even lower, below $310 per week, then sole parents would see a reduction in income on 1 April 2025, compared to 31 March 2025. Lower payment rates reduce the fiscal cost considerably - based on modelling, a $10 per week reduction in the payment rate translates roughly to a decrease in the fiscal cost of around $65 to $75 million per year.

A medium payment rate with more gradual abatement settings to address high EMTRs: IWP(c)

86 The two-tier abatement settings of the base option (outlined in paragraph 58) were introduced to reduce costs for the full-scale Option 1B. However, the rates of the two-tier abatement settings creates higher EMTRs for families earning above $50,000 per year and receiving both the Accommodation Supplement and WFF. High EMTRs reduce the amount of income that families retain from increases in wages – and this means that financial incentives to work are reduced.

87 There are also some scenarios where families could face EMTRs that exceed 100% particularly if they are repaying Student Loan debt (which is repaid at 12c in the dollar for income above $21,000) and/or receiving Best Start (abates at 21% for family income above $79,000 at the same time as WFF payments).

88 One option to reduce the high EMTRs of the base option is to have more gradual abatement settings. IWP(c) has the same weekly payment rate as IWP(a) ($335 pw) and two-tier abatement settings, however for income above $26,500 the payment would abate at 50% (instead of 55%) and for income above $49,500 the payment would abate at 27% (instead of 30%).

89 Assuming a 1 April 2025 implementation date, IWP(c) would:

- cost $617m in 2025/26
- see 173,000 households gain an average of $68 per week
- reduce child poverty by 19,000 children on the BHC50 measure and 23,000 on the AHC50 measure.

90 The key benefit of this option is that it reduces the very high EMTRs for people earning above $50,000 a year. It also has the greatest reductions in child poverty of all the scaling options.

91 However this option provides only an 11% reduction in fiscal costs ($73 million) for 2024/25 compared to the base option, which may not be sufficient.

92 In addition to the high fiscal costs, this option has a greater proportion of gains going to higher-income families so it targets less of the overall fiscal cost towards working families on the lowest incomes.

- For IWP(c), approximately 38% of the total fiscal cost goes to households with income under $42,700 (the lowest two income deciles), with an average gain across all households of $68 per week.
- In comparison, IWP(a) which has the same payment rate, has 47% of the total fiscal costs going to households in two lowest income deciles and an average gain across all households of $45 per week, at a considerably lower fiscal cost.

93 This option, as with IWP(a) and (b) maintains an existing issue where couples are not necessarily better off leaving the benefit system at 30 hours of work at the minimum wage and receiving a payment for people in work (either the MFTC or a new IWP), than they are receiving an abated benefit.

To address tensions with the benefit system: IWP(d)

94 Having a large payment with minimal work requirements (i.e. as little as an hour a week) creates a tension with the benefit system given the work obligations and sanctions attached to the receipt of main benefit.

95 IWP(d) reintroduces a partial hours test[17] and would allow families with children off-benefit to receive a portion of the payment ($100 pw) before the hours test is met, then receive a higher amount (up to $335 pw) if the hours test is met (20 hours a week for sole parents, 30 hours a week for couples). This mirrors the current system, where families can receive $72.50 pw[18] from the IWTC with no hours test but must meet an hours test to receive the MFTC (up to $253 per week).

96 The payment rate for IWP(d) is set at the same point as IWP(a) and IWP(b) described above, the medium payment rate. It also has the base settings for the two-tier abatement regime (55% and 30%).

97 Assuming a 1 April 2025 implementation date, IWP(d) would:

- cost $240m in 2025/26[19]
- see 142,000 households gain an average of $34 per week and 11,000 households lose an average of $20 per week[20]
- reduce child poverty by 9,000 children on the BHC50 measure and 10,000 on the AHC50 measure

98 IWP(d) is one of the lowest cost options of the Option 1 variations and is 35% of the costs of the base option. IWP(d) largely meets the objectives of the reform, however there are smaller reductions to child poverty and significant additional complexity in customer compliance and administration.

Tensions with the benefit system – obligations and sanctions

99 Under the base rate and variants, working families could receive up to $335 per week but would have no work obligations beyond being in paid work in a given week.[21] Work obligations in the benefit system require sole parents (and partners in couples with children) to be seeking part-time work (20 hours a week) when their youngest child is aged between 3 and 13 years and to seek full-time work (30 hours a week) once they reach 14 years of age. For couples, the primary recipient of Jobseeker Support must have full-time work obligations, unless they have reduced work capacity because of a health

[17] The hours test was removed from the IWTC from 1 July 2020 but remained for the MFTC.
[18] Families with four or more children can receive an additional $15 per child with the IWTC.
[19] IR have provided a costing estimate of $393m for this option. The variability between IR and the Treasury's costing for this option will be investigated as part of further work to develop this option.
[20] As with IWP(a) and IWP(b) those that lose assistance are couple families who lose more in the IWTC than they gain in the IWP + FTC and there are also single and couple families that lose because they work fewer hours than the hours test.
[21] To be eligible for the current IWTC, a principal caregiver and/or their partner must normally be an earner and derive an income in the week they are an earner (e.g., be in paid work in a week). This paragraph assumes the IWP would operate in the same way if there is no hours test.

condition, injury or disability, in which case they either have part-time work obligations or have their work obligations deferred.

100 The example below illustrates the scale of change from the current system if the full payment rate is available without an hours test.

- Under the current system, at one hour of work a week a sole parent on the minimum wage will be better off receiving a main benefit by **$441.97 pw**. This is a strong incentive to remain on a main benefit despite its more stringent requirements.
    - They would get $591.77 pw[22] without receiving a main benefit and $1,033.74pw if receiving a main benefit.
- Under the new IWP with a medium payment rate (IWP(a)), they are better off receiving a main benefit by only **$179.47 pw** as they now can receive $854.27[23] without receiving a main benefit.

101 With no hours test, MSD also considers that there are increased incentives for the self-employed to manipulate their hours to be eligible for the payment. This is essentially exacerbating an existing risk with the IWTC, but with a much larger payment.

102 The hours test in IWP(d) provides greater incentives to work more hours and better manages benefit system integrity, by requiring a certain level of hours worked to receive the full amount of the significantly higher new payment. From a proportionality perspective, the partial hours test is also fairer as it targets a higher payment rate towards recipients who work more hours and who would likely have higher in-work costs.

Trade-offs with an hours test – compliance costs and complexity

103 However, there are considerable trade-offs associated with an hours test. It would mean higher compliance costs for clients with fluctuating hours and is significantly more complex to administer than the current system.

104 Introducing an hours test for the new IWP creates greater complexity for recipients as there is an increased likelihood that they would need to navigate between MSD and IR systems as hours change. If a recipient has variable or unpredictable hours, they may experience gaps in support for the IWP and would be better off switching to a main benefit. This is demonstrated by the example provided below.

[22] This assumes they are receiving Accommodation Supplement from MSD as a non-beneficiary client. This also includes the FTC and IWTC.

[23] As above, this assumes they are receiving Accommodation Supplement from MSD as a non-beneficiary client. This also includes the FTC and new IWP.

Example: Hospitality worker receiving IWP with variable hours

Kate is a sole parent working casually at a Dunedin restaurant on minimum wage. Her hours of work vary week to week depending on the time of year and availability of other staff.

During the university term, the restaurant is busy, and she is generally rostered on for 25 hours per week. This means she earns $567.50 per week before tax. As she meets the hours test of 20 hours per week, she also receives the full $386 per week of IWP.

However, the restaurant is very quiet during university holidays, so Kate is only rostered to work 10 hours per week. Her income reduces to $227 per week before tax, and as she no longer meets the hours test, she only receives a partial IWP of $100 per week.

The gap in support created by the varying rate of IWP means she would be better off going on benefit (and continuing to work, reporting her income, and getting an abated sole parent support payment) during the quiet period. Kate would then need to navigate between MSD and IR's systems when her hours picked up again.

105 Further, evidence suggests that generally people respond more to incentives to enter work (the extensive margin) than incentives to increase hours of work (intensive margin). Accordingly, an hours test may not be a well-targeted payment.

106 In addition to the increased complexity for clients, there are operational considerations for Inland Revenue and potentially some additional compliance costs for employers. Primarily, Inland Revenue does not hold or collect data to administer an hours test well. This is an existing design issue for the MFTC (and for the IWTC previously), however this issue is limited to 3,000 people. Introducing an hours test for the new IWP would extend the issue for a broader group of families.

107 Inland Revenue modelling indicates that between 15,000 – 30,000 families would fall below the threshold of a 20 hours per week test for at least one month of the tax year[24]. If ceasing to qualify (even temporarily) is not proactively declared by recipients, it may be picked up by IR's early intervention process or at the end of year square up. This creates an increased likelihood of overpayments because these checks must be retrospective in nature. If (as with the previous IWTC hours test) the hours test was required to be met weekly, the administrative burden and associated costs for IR and for recipients would be substantial.

108 Because an hours test would reintroduce complexity of the system policies, complexity for recipients, increase the uncertainty of outcomes for families, and potentially increase debt for a larger number of WFF recipients who have

[24] Based on IR using minimum wage multiplied by 20 hours per week as a proxy for meeting the hours test.

fluctuating employment arrangements, Inland Revenue do not recommend this option as it would be unlikely to improve the current system overall.

Further considerations for introducing a new in-work payment

109 There are a set of further choices about the settings of these options that will be covered in future advice but are set out at a high level here. These considerations require a considerable amount of further detailed policy work.

Indexation of the in-work payment

110 Indexation of the new IWP should maintain the policy intent of payments as benefits increase. The policy intent of the IWP is that work pays more than being on benefit. For this report, we have costed the indexation of IWP(a) only for the 2026/27 year and have assumed the IWP is maintained in line with benefit and wage increases, which is a relatively complex interaction.

111 For tax year 2026/27 it is estimated that IWP(a) will cost $361m for the second full year of payment, an $18m increase on the first year costs.

112 Indexation could apply to either the payment rate or the lowest abatement threshold, or indexation could be applied to both settings. Once a preferred option has been identified, further consideration and modelling of indexation options will be included in the next set of advice.

113 It should be noted that this effectively indexes the FTC as well and would eventually have a threshold cross-over with the BSTC. The FTC abatement threshold in the highest-cost IWP(base) option is already only $5,000 below the BSTC threshold in 2025/26.

Implications for discretionary benefit and/or Family Tax Credit increases

114 In the past, when discretionary increases to main benefit rates have been made (i.e. in 2020 and 2021), an equivalent increase to the MFTC has also been made to ensure that low-income working families remain better off off-benefit at 20 hours of work a week on the minimum wage.

115 To maintain the work incentives for the group of families who previously received the MFTC and the policy intent of the payment, similar increases would need to be applied to the new IWP. It is estimated approximately 50 – 80,000 families would receive the new IWP. This would represent a much larger flow-on fiscal cost compared to the status quo.

116 Officials have not costed the fiscal impacts for the new IWP of discretionary increases to benefits or the FTC, however scenarios using the preferred option can be provided in the next round of advice.

Flow on impact of the new in-work payment

117 As indicated in previous advice [REP 23/3/169] the new IWP and the two-tier abatement settings will create interactions and policy issues with other forms of assistance that will need to be worked through. The key areas of further advice relate to eligibility for the self-employed, shared care,

OB/UCV/FCA, 4+ IWTC and detailed abatement and ring-fencing rules. **Appendix Five** provides further advice on these flow-ons.

118 As officials work through the detailed design for the new IWP, decisions are likely to be required on the above issues. Additional issues may also arise during the detailed design process.

Bill of Rights implications for IWP variations

119 Initial advice from MSD Legal is that prima facie, there is a likelihood that the inequities from the new IWP related to: people who are single vs people who are in a couple; people with children vs those without children, could have implications under the New Zealand Bill of Rights Act 1990. However, the policy justifications likely mean that the risk of challenge is low, and even if challenged, the justifications can likely be considered as justified limitations under section 5 of the Act. Further advice will be provided when eligibility settings and design parameters are confirmed.

A single WFF tax credit with no in-work payment has previously been considered as a significant structural change option

120 In previous advice, an alternative option for significant structural change was considered - a single tax credit with no IWP (referred to as Option 5 in previous advice). The single tax credit removes all in-work payments and redirects the funding into the FTC. The option supports income adequacy for families with children (both in-work and on benefit) and aims to make work pay by making FTC abatement settings more generous, instead of having an IWP.

121 Compared to the new IWP, the single tax credit would be simpler, both from a client's perspective and for agencies to administer, but would be likely to cost more in the long term. It would also mean that low-income working families would remain on an abated benefit for longer.

122 The key impacts of this option were:

- comparable gains to both beneficiary and non-beneficiary families
- reductions in child poverty of 24,000 children on the BHC50 measure and 27,000 children on the AHC50 measures
- Costings provided in the November report estimated the cost of the first year of the full option would be $686m in 2024/25, but if the option was phased in, the first full year cost would reduce to $365m in 2024/25.
    - Note these costings used BEFU 22, so are likely to underestimate the fiscal costs compared to the options provided in this advice.

123 **Appendix One** provides further information about the single tax credit option and the other options that have been considered as part of the Review.

Section Two: Smaller scale options to address anticipated overlapping abatement thresholds

124 If you do not want to progress structural reform for the Review, or fiscal conditions do not allow for significant investment in WFF in Budget 2025, options could be progressed to help future proof WFF.

125 Inflation and wage growth have been significant since the WFF abatement threshold was last adjusted in 2018. Increases in the abatement threshold are recommended by officials to ensure that WFF continues to support both low and middle-income working families.

126 In addition, officials estimate that by 1 April 2026 the MFTC and the WFF abatement threshold will overlap, creating EMTRs over 100% for a small group of low-income working families. With strong wage growth and increases to the MFTC, this could occur even earlier than anticipated. This would undermine the function and policy intent of the MFTC.

127 An increasing number of beneficiaries will also face overlapping abatement of their benefit and the FTC. At a minimum, changes to the WFF abatement threshold are needed to address this in the absence of structural reform.

128 Indicative modelling from March 2023 of potential changes to current settings that address the anticipated overlapping abatement is used in this section. These costings are calculated using the 2022 Half-Year Economic Fiscal Update and assume a 1 April 2024 implementation date. If you wish to progress an option to help future proof WFF in lieu of structural reform, updated modelling and advice on implementation dates could be provided in subsequent advice.

An increase to the WFF abatement threshold would help future proof WFF and could be progressed alongside complementary changes to current settings

129 The WFF abatement threshold, currently $42,700 per annum (pa), was last increased from 1 July 2018 and is not periodically adjusted. This means that the annual increases to the MFTC[25] will continue to lift the MFTC until it overlaps with the WFF abatement threshold, causing some low-income working families to be financially disadvantaged. It also means that WFF payments effectively become more targeted over time as wage growth pushes families out of eligibility.

130 An increase to the WFF abatement threshold is needed to mitigate these issues. As per previous advice[26], officials recommend the threshold is increased to $50,000 to ensure that a single earner on the minimum wage

[25] To reflect anticipated wage growth indexation of benefits.
[26] March 2023: REP/23/3/169; IR2023/018

does not face significant abatement of WFF payments (as 40 hours of work a week means the current minimum wage is equivalent to $47,216 pa and future increases to the minimum wage will increase this annual income further).

131 Alongside addressing anticipated overlapping thresholds, changes to the WFF abatement threshold would also reduce the extent to which abatement of benefits and WFF overlap. IR estimate this would reduce debt for approximately 2,400 beneficiary families and eliminate it for approximately 1,200 beneficiary families.

Summary of options to address anticipated overlapping and modelling from March 2023

132 A summary of the options to address abatement thresholds is provided in **Appendix Three** and in the table below.

	AT(a) Abatement threshold to $50,000 pa only	**AT(b)** $10 pw IWTC increase + abatement threshold to $50,000 pa	**AT(c)** $25 pw IWTC increase + WFF abatement threshold to $50,000 pa + MFTC removed	**AT(d)** $10 pw IWTC increase + WFF abatement threshold to $50,000 pa + MFTC removed
Fiscal impact **Tax Year (24/25)**[27]	$238m	$309m	$406m	$291m
Average gains/losses	152,000 HHs gain $30pw	173,000 HHs gain $34pw	173,000 HHs gain $46pw 6,000 HHs lose $35pw	167,000 HHs gain $35pw 7,000 HHs lose $36pw
Child poverty reduction	4,000 (BHC50) 11,000 (AHC50)	6,000 (BHC50) 17,000 (AHC50)	8,000 (BHC50) 19,000 (AHC50)	5,000 (BHC50) 16,000 (AHC50)

133 The March 2023 advice presented the following options for consideration through Budget 2023, which assumed a 1 April 2024 implementation date:

- **AT(a)**: increase the WFF abatement threshold to $50,000 pa.
- **AT(b)**: increase the WFF abatement threshold to $50,000 pa + a $10 pw increase to the IWTC rate.

134 These options were presented as both potential interim measures broadly consistent with further structural change and also sensible standalone options to address anticipated overlapping abatement if structural reform is not

[27] Fiscal costs only, does not include implementation or operational costings.

desirable. Compared to the IWP options, there are lower fiscal costs associated with these changes, but also smaller reductions in child poverty.

135 The Review objectives of supporting income adequacy and reducing child poverty, as well as improving financial incentives to work, are met under both options. However, they are not focused on simplifying the system, so do not address the core design issues with the MFTC and the complexity of the tax/benefit interface would remain.

136 The option that best supports income adequacy and lifts the most children out of poverty on the AHC50 measure per dollar of fiscal cost combines an IWTC increase of $10 pw with an increased abatement threshold (AT(b)). This option is estimated to reduce child poverty by 17,000 on the AHC50 measure at a cost of $309 million in 2024/25.[28]

137 Increasing the abatement threshold only means that overlap is likely to occur again in the future without further changes being made to mitigate this, such as indexing the WFF abatement threshold. Increasing or indexing the threshold for the BSTC could also be considered as overlapping abatement will increase with these options. Officials can provide further advice on this if requested.

138 These options (AT(a) and AT(b)) could be implemented from 1 April 2024 if urgent legislation is passed before the end of 2023.

139 You may also wish to remove the MFTC, but this is not recommended without changes to avoid families being worse off. In the absence of structural reform, core design issues with the MFTC remain, including its high EMTRs. You may wish to address these by removing the MFTC, alongside the required changes to address anticipated overlapping abatement.

140 Previous advice explored options that remove the MFTC alongside increasing the WFF abatement threshold to $50,000 pa and increasing the IWTC. These options were:

- **AT(c)**: remove the MFTC, increase the WFF abatement threshold to $50,000 pa and increase the IWTC rate by $25 pw. This option:
  - had a cost of $406 million in 2024/25
  - was estimated to reduce child poverty by 19,000 on the AHC50 measure.
- **AT(d)**: remove the MFTC, increase the WFF abatement threshold to $50,000 pa and increase the IWTC rate by $10 pw. This option:
  - reduced the cost to $291 million but had slightly smaller reductions in child poverty – 16,000 on the AHC50 measure.

[28] Costings from March 2023 do not include operational costs.

141 While still meeting the objectives of supporting income adequacy and reducing child poverty, as well as improving financial incentives to work, these options (AT(c) and AT(d)) would also help to simplify the system. As these options include the removal of the MFTC they would require longer to implement than AT(a) and AT(b) and could be implemented by 1 April 2025.

142 Officials recommend against removing the MFTC unless further changes are made to reduce the number of families financially disadvantaged. Removing the MFTC would create difficulty and confusion for those currently in receipt of the payment and is likely to result in some families being financially disadvantaged. Previous modelling[29] estimates that AT(c) would result in:

- 6,000 households losing on average $35 pw (using TAWA modelling)
- 3,000 families currently receiving the MFTC would lose on average $79 pw (using IR modelling, which is not directly comparable to the TAWA modelling above).

143 To reduce the number of people made worse off by the changes, agencies would advise those eligible to transfer to benefit. This would likely eliminate most of the losses estimated above, as The Treasury and IR's models cannot estimate families moving onto benefit. A small group of very low-income working families would not be eligible for benefit and would be financially disadvantaged, for example Jobseeker Support couples, due to working 30 or more hours a week. As noted earlier, complementary changes to the benefit system would be required to enable couples to receive an abated benefit for longer.

144 An alternate option to removing the MFTC completely is to freeze the rate of MFTC or alternatively grandparent the current recipients and eventually remove the payment when all families have moved off. These types of options would have lower fiscal costs but would increase administrative complexity and have negative impacts for MFTC customers. Officials have not costed these options but can do so if Ministers are interested in future advice.

Section Three: Economic and fiscal context and child poverty reduction targets

145 Choices between higher and lower cost options depend on the Government's wider fiscal strategy and progress towards the ten-year child poverty reduction targets.

[29] The number of families estimated to be financially disadvantaged are likely to be over-stated, as both estimates do not account for the fact that many affected families would be eligible to receive an abated benefit to offset their losses. However, there would be a small group of families who would not be eligible for benefits, for example, Jobseeker Support due to working more than 30 hours a week.

146 In the Budget Economic and Fiscal Update 2023, The Treasury estimated that the Budget 2024 operating allowances should be sufficient to cover cost pressures to existing services but will leave limited headroom for other operating investments. Further to this, pre-existing challenges such as demographic changes are expected to put pressure on the public finances in the coming years. As such, ongoing fiscal discipline and potentially difficult choices will be necessary to ensure a sustainable operating balance before gains and losses (OBEGAL) trajectory both during the forecast period and over the medium term.

147 This means that available funding for any potential changes to WFF in Budget 2024 will be significantly constrained, as spending will need to remain within allowances to maintain the fiscal strategy and help ensure a sustainable fiscal trajectory across the short and medium-term

148 **Appendix Three** sets out key trade-offs for consideration of the in-work payment options and the abatement threshold options discussed in Sections One and Two of this report:

- high-cost options for an in work payment: IWP(base) / IWP(c)
- lower-cost options for an in work payment: IWP(a) / IWP(b) / IWP(d)
- abatement threshold increase and complementary changes: AT(a) – (d).

Child Poverty targets

149 As officials have noted in previous advice, this review presents the biggest opportunity to make further progress towards child poverty targets in the coming years. Substantial investment since the targets were first set in 2018 has helped to make considerable progress in reducing child poverty, but sizeable reductions are still needed to reach the ten-year targets.

150 This is particularly the case on the before-housing-cost primary measure, which currently needs to be reduced by a further 7 percentage points or ~80,000 children. Large reductions are also still required on the after-housing-cost and the material hardship primary measures – in the order of 4-5 percentage points or ~50-60,000 children on each.

151 All the options in this report provide gains for working families only. Broadly half of children in poverty live in working households, so the benefits of these options are confined to this group. The other half of children in poverty are in households that rely on income from main benefits.

Section Four: Further work and timeframes for Cabinet report back

152 In the recent Cabinet paper "Future Direction of the Working for Families Review" it was noted that you would report back to Cabinet on the next steps of the Review by the end of the year [CAB-23-MIN-0178].

153 Depending on Government formation timelines following the election and other Government priorities during the post-election period, officials anticipate the most likely date for the Cabinet report back is December 2023.

Timing of subsequent advice

154 The decisions in the report on the preferred option/s for the WFF Review will enable a report back to Cabinet in December 2023. If Ministers would like to progress a WFF option for consideration in Budget 2024, timely decisions on the advice in this report will be required.

155 Through further work on the Review, officials have determined that there is insufficient time to develop a structural reform option for Budget 2024 (with an implementation date of 1 April 2025), though smaller-scale changes within the current system could still be considered. Options for structural reform could be considered in Budget 2025, with an implementation date of 1 April 2026.

156 If Ministers still would like to progress the in-work payment, officials will provide advice in late 2023 or early 2024 to enable decisions in Budget 2025 with an implementation date on or after 1 April 2026.

157 If the preferred outcome of the Review is to address the anticipated overlapping abatement of MFTC and WFF by one of the abatement threshold variations, then decisions related to this option could be progressed on standard timeframes. For implementation on 1 April 2025, funding could be sought through Budget 2024. However, as the overlap is not anticipated to occur until April 2026, this decision could be delayed and funding could be sought through Budget 2025 for implementation on 1 April 2026.

158 It would also be possible to implement the abatement threshold options that do not remove the MFTC (AT(a) and AT(b)) more quickly – by 1 April 2024. However, this would require urgent legislation passed by the end of 2023 and a pre-commitment against Budget 2024.

Public announcements related to the next steps of the Review

159 As part of the May 2023 Cabinet paper [CAB-23-MIN-0178 refers], Cabinet noted that any reactive communications about the next steps of the Review would indicate that a new in-work payment is a possible option being explored further, alongside consideration of changes to current settings.

160 Cabinet agreement would need to be sought again to make any further public announcements related to the options outlined in this report.

Next Steps

Inland Revenue advice on administrative improvements

161 In November 2022 (MSD REP/22/11/111) - IR2022/512), the Minister for Social Development and Employment and the Minister of Revenue agreed to some administrative improvements (providing a grace period on the death of a child, removing the historic Child Tax Credit, and improving information

sharing between MSD and IR) which would be $0.48 million over the forecast period and $0.156 million for outyears and which could be implemented as part of the reforms.

162 In March 2023 (MSD REP/23/3/169 - IR2023/018), we noted that we will provide further advice about minor administrative and remedial amendments. Inland Revenue officials are currently working through proposals including how they relate to the debt reduction work. Officials expect these to be in the range of $1 - 2 million a year. The changes identified so far could be implemented in time for an April 2025 start date if decisions are made in Budget 2024. We will provide further advice when we report to you on the broader package.

Ministerial discussion of this advice

163 Officials recommend you forward a copy of this advice to the Prime Minister, Minister for Children, Minister of Finance, Minister for Child Poverty Reduction and the Minister of Revenue and that a Ministerial meeting is set up to consider this advice and the next steps for the Review.

Appendices

- **Appendix One** – Previous options considered
- **Appendix Two** – Illustrative diagram of WFF tax credits – structural reform
- **Appendix Three** – Summary of option impacts and key trade-offs
- **Appendix Four** – Parameters of in-work payment options
- **Appendix Five** - Flow on impacts of the new in-work payment

Report numbers: REP/23/7/669; IR2023/216

Appendix One – Previous options considered (figures from July 2022)

	Child poverty reduction	Household gains and losses	Annual fiscal cost
Improvements to the structure and design of in-work tax credits in order to make work pay			
Option 1: A single in work payment* proposes a significant structural change by introducing a single and more targeted in-work payment that combines the Minimum Family Tax Credit (MFTC) and In-Work Tax Credit (IWTC).	9,000 (BHC50) 28,000 (AHC50)	170,000 HHs gain by $81 per week. 24,000 HHs lose by $34 per week.	$675m
Option 2: An alternative MFTC proposes a smaller-scale change that largely keeps existing settings but replaces the MFTC with a similar, more flexible, payment for sole parents that abates gradually.	2,000 (BHC50) 2,000 (AHC50)	134,000 HHs gain by $5 per week. No HHs lose.	$35m
Option 3: IWTC phase-in removes the MFTC and phases in the IWTC more gradually as incomes increase and allows beneficiaries to receive the payment while on benefit (i.e., removes 'off benefit' rule).	1,000 (BHC) 1,000 (AHC50)	41,000 HHs gain by $33 per week. 20,000 HHs lose by $30 per week.	$38m
Option 4: Change benefit abatement settings removes the MFTC, retains the off-benefit rule for the IWTC and increases benefit abatement thresholds to better support families in part-time work.	1,000 (BHC50) 2,000 (AHC50)	225,000 HHs gain by $8 per week. No HHs lose.	$83m
Option 5: A single family tax credit with variations including: • removes the MFTC and IWTC, but increases the eldest child rate of FTC by $50pw, and subsequent child rate by $15pw • increases the FTC abatement threshold to $50,000 and reduces the abatement rate to 25% to help make work pay • introduces a two-tiered abatement regime to target increases more to lower-income working families and to reduce fiscal costs • options for phased implementation.	24,000 (BHC50) 27,000 (AHC50)	235,000 HHs gain by $46 per week. 24,000 HHs lose by $23 per week.	$540m
Improvements in the early years to assist with the costs of children and support choices around work and childcare			
Extending targeted Best Start payment to eligible families with children up to age five ($40pw).	5,000 (BHC50) 5,000 (AHC50)	49,000 HHs gain by $41 per week. No HHs lose.	$104m
Increasing Best Start by $40pw for eligible families up to age three.	5,000 (BHC50) 8,000 (AHC50)	68,000 HHs gain by $44 per week. No HHs lose.	$156m
Complementary changes that could further reduce child poverty alongside changes to in-work payments			
Increase FTC by $25pw per child.	32,000 (BHC50) 35,000 (AHC50)	267,000 HHs gain by $49 per week. 5,000 HHs lose by $3 per week.	$680m
Increase IWTC by $25pw.	6,000 (BHC50) 8,000 (AHC50)	161,000 HHs gain by $23 per week. No HHs lose.	$192m

* *A version of this option is being proposed in the current advice*

Appendix Two - Illustrative diagram of WFF tax credits – structural reform

Appendix Three – Summary of impacts and key trade-offs

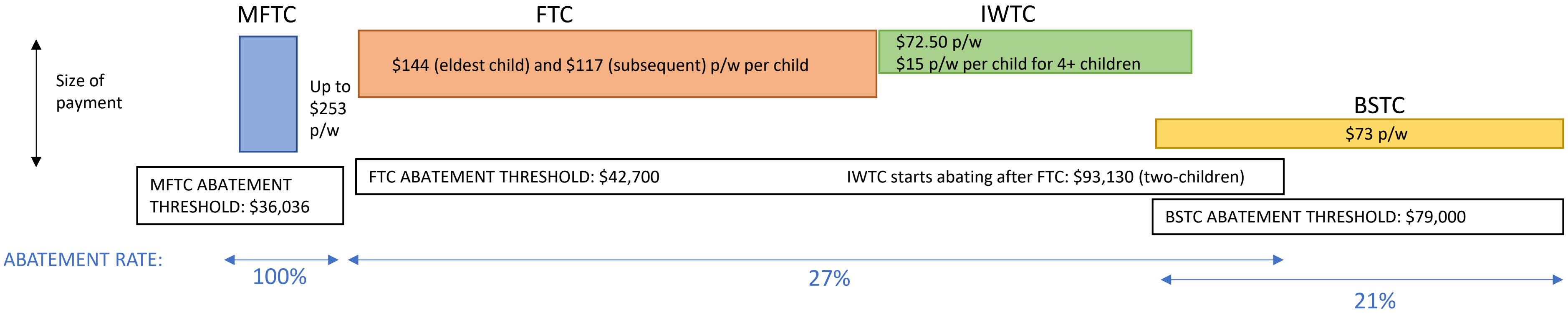
Appendix Four – Parameters of new in-work payments

Appendix Five: Flow on impacts of the new in-work payment

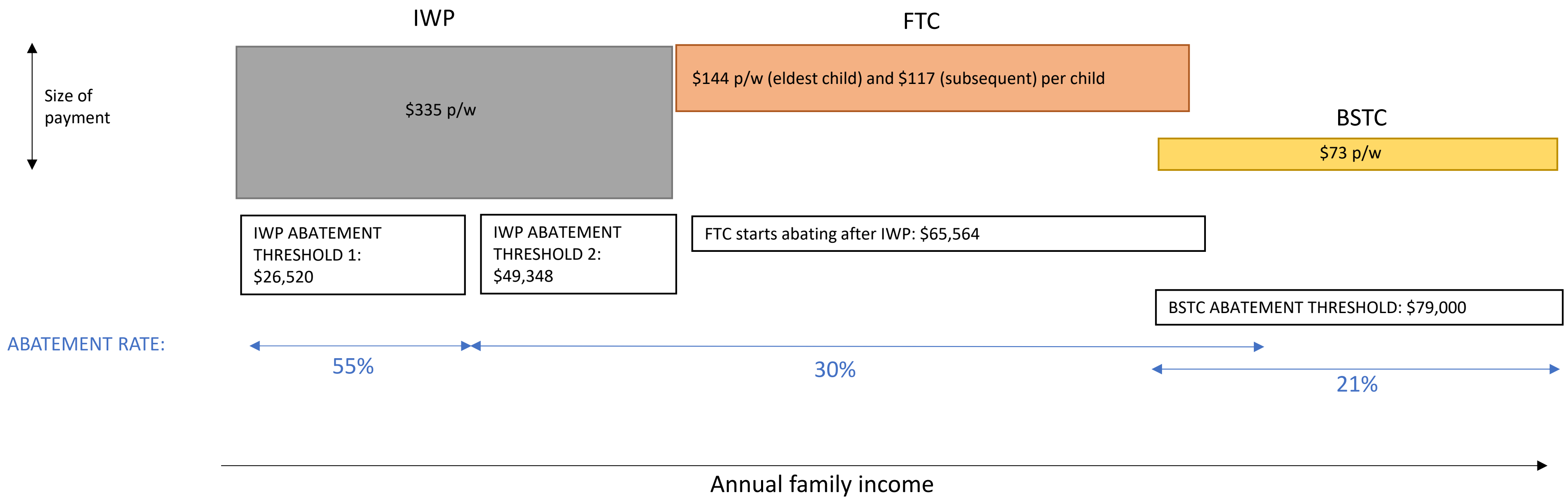
- **Eligibility for the self-employed** – Officials are likely to recommend that the new in-work payment would include self-employed people, but further work would need to be undertaken to confirm this and examine its specific implications. For example, a higher payment may result in more incentives to game. Under the status quo, self-employed people are eligible for the IWTC only and not the MFTC, for reasons that are partly historical in nature, and because of an increased incentive to game for self-employed people.
- **Shared care –** Currently the full amount of IWTC is available for each parent with shared care of a child, whereas the FTC is apportioned between parents depending on the level of care. Modelling for this report has assumed the same rules as the IWTC. There is a question as to how the shared care rules would apply to the new in-work payment, and whether the same rules apply as for the IWTC. The Minister for Social Development and Employment recently received initial advice on options to address split and shared care within the welfare system [REP/23/6/583].
- **OB/UCB/FCA –** Caregivers cannot currently receive OB/UCB/FCA and the FTC for the same child, as these payments are considered analogous. However, caregivers can receive both the IWTC and the OB/UCB/FCA, if they qualify. Decisions would be required on whether the same settings should apply to the new in-work payment.
- **4+ IWTC rate –** The current IWTC includes a per-child rate of $15 pw for the 4th and subsequent children, which did not feature in the original design of Option 1B included in previous advice. There is a policy question as to whether to retain the rate or remove it - removing it would potentially disadvantage some larger working families.
- **Detailed abatement and ring-fencing rules** – The shift from IWTC/MFTC to the new in-work payment may have implications for rules about how income and abatement settings are operationalised in practice. Detailed policy settings are yet to be confirmed. There may be some families who are financially disadvantaged from these changes.

Appendix Two – Illustrative diagram of WFF tax credits – structural reform

Current WFF tax credits (as at 1 April 2025)



New in-work payment (IWP) replaces MFTC & IWTC – IWP (a)



Appendix Three – Summary of impacts and key trade-offs

Summary of impacts

Option	New, more generous, in-work payment (costings for 2025/26)					Abatement threshold increase + complementary changes (costings for 2024/25)			
	IWP(base)	IWP(a)	IWP(b)	IWP(c)	IWP(d)	AT(a)	AT(b)	AT(c)	AT(d)
Costs*	$690m	$343m	$221m	$617m	$240m	$238m	$309m	$406m	$291m
Child poverty	21,000 (BHC50) 26,000 (AHC50)	14,000 (BHC50) 14,000 (AHC50)	8,000 (BHC50) 7,000 (AHC50)	19,000 (BHC50) 23,000 (AHC50)	9,000 (BHC50) 10,000 (AHC50)	4,000 (BHC50) 11,000 (AHC50)	6,000 (BHC50) 17,000 (AHC50)	8,000 (BHC50) 19,000 (AHC50)	5,000 (BHC50) 16,000 (AHC50)
Gainers / losers	170,000 HHs gain $78pw	148,000 HHs gain $45pw 5,000 HHs lose $20pw	136,000 HHs gain $33pw 11,000 HHs lose $18pw	173,000 HHs gain $68pw	142,000 HHs gain $34pw 11,000 HHs lose $20pw	152,000 HHs gain $30pw	173,000 HHs gain $34pw	173,000 HHs gain $46pw 6,000 HHs lose $35pw	167,000 HHs gain $35pw 7,000 HHs lose $36pw
Benefit/work interface	Having a large weekly payment with no hours test creates tensions with the benefit system in relation to work obligations and sanctions for a near-equivalent rate of payment in the benefit system.				Mitigates tension with benefit system and provides greater incentives to work more by retaining hours test for full amount of payment.	Status quo.		A small number of low-income working families will receive benefits for longer – and benefit system changes required.	
Administration	Moderate simplification due to removal of MFTC with hours test. No need to notify IR of changes to work hours (similar to IWTC currently).				Higher compliance costs for clients with variable working hours and is significantly more complex to administer than the current system.	Minor administrative impact. These options could be implemented from 1 April 2024 if urgent legislation is passed before the end of 2023.		Moderate simplification through removal of MFTC. These changes could not be implemented before 1 April 2025 due to the removal of the MFTC.	
Incentives to work / make work pay	Improves the returns from working full-time for sole parents and primary earners in couples, reduces financial incentives for second earners in couples.	Same as IWP(base) for increased financial incentives for sole parents and reduced financial incentives for secondary earners. The lower payment rate perpetuates an existing issue that means couples are not necessarily better off off-benefit at 30 hours on the minimum wage. Benefit system changes could be considered to enable couples to receive a benefit for longer to avoid being worse off.				Generally slightly improves the returns from working more hours (particularly for those with earnings above the minimum wage), reduces financial incentives for second earners in couples.			
EMTRs	Increases abatement rate slightly resulting in higher EMTRs compared to the status quo. Also: Eliminates overlapping abatement of main benefits and FTC. Increases overlapping abatement of FTC with BSTC.	Same as IWP(base)		Maintains EMTRs at or below current levels. Also: Eliminates overlapping abatement of main benefits and FTC. Increases overlapping abatement of FTC with BSTC similar to IWP(base).	Same as IWP(base)	Ensures people don't face overlapping abatement or EMTRs over 100% due to MFTC/FTC. Reduces overlapping abatement of FTC with main benefits. Increases overlapping abatement of IWTC with BSTC.			

* The fiscal costs will continue to be refined as officials work through the detailed policy parameters, include operational/IT costs, and use more up-to-date forecasts (PREFU).

Appendix Three – Summary of impacts and key trade-offs

High-cost options for an in work payment – IWP(base) / IWP(c)

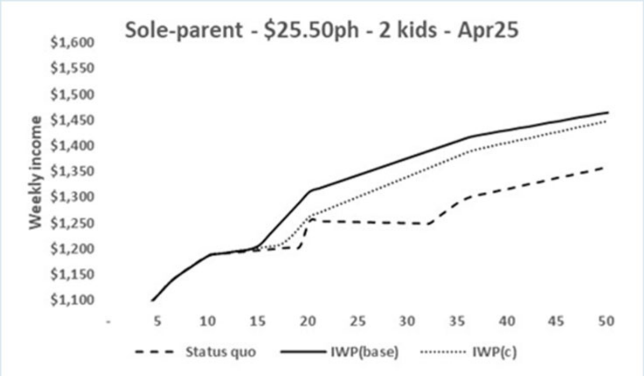
Choice between IWP(base) and IWP(c) is between:

- **A high payment rate, or**
- **A lower abatement rates/EMTRs.**

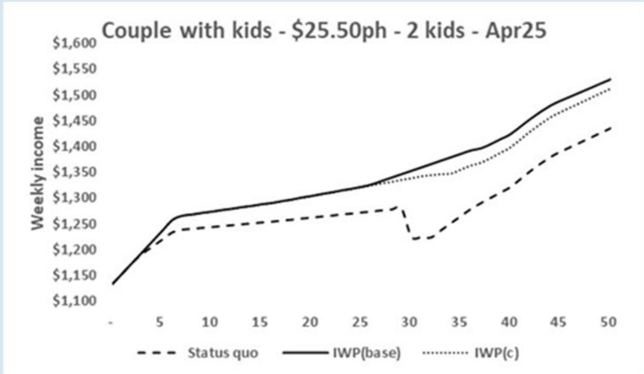
The **high payment rate** ensures that couples as well as sole parents are better off off-benefit at 30 hours of work a week on the minimum wage. However, couples are a small proportion of the target population and higher payments to couples tend to reduce the labour supply of secondary earners overall. The trade-off for the high payment rate requires higher abatement settings than IWP(c) and results in higher EMTRs/reduced financial incentives to work.

A **lower abatement rate** maintains EMTRs at or below current levels, but trade-offs a reducing to a medium payment rate than means couples may not be better off off-benefit.

Sole parent income by hours worked (no WEP)



Couple income by hours worked (no WEP)

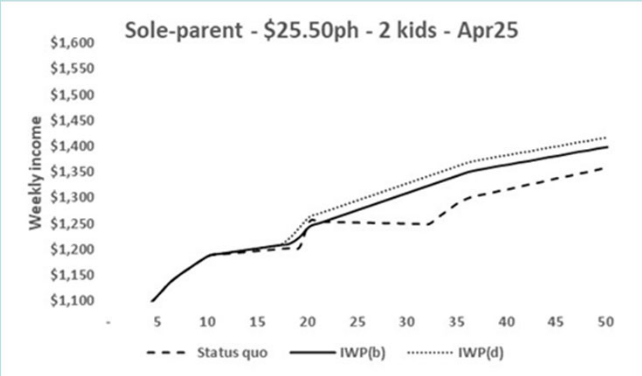


Lower-cost options for an in work payment – IWP(a) / IWP(b) / IWP(d)

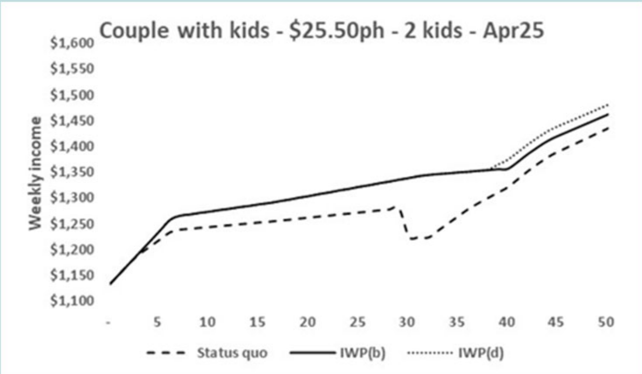
Choices between IWP(a) / IWP(b) and IWP(d) are:

- **The payment rate** – A low payment rate provides a lower amount than the current system on 1 April 2025, but sole parents are still better off overall off-benefit at 20 hours of work if there are increases to the minimum wage. A medium payment rate provides an equivalent amount to the current system and means families retain more of the gains from an increase to the minimum wage.
- Whether to introduce **an hours test** to mitigate the tension with benefit system created by a person being able to receive a similar amount of support from the in-work payment as the benefit system, but with minimal work obligations and no sanctions. However, hours test creates significant administrative complexity for clients and agencies.

Sole parent income by hours worked (no WEP)



Couple income by hours worked (no WEP)



Abatement threshold increase + complementary changes – AT(a)-(d)

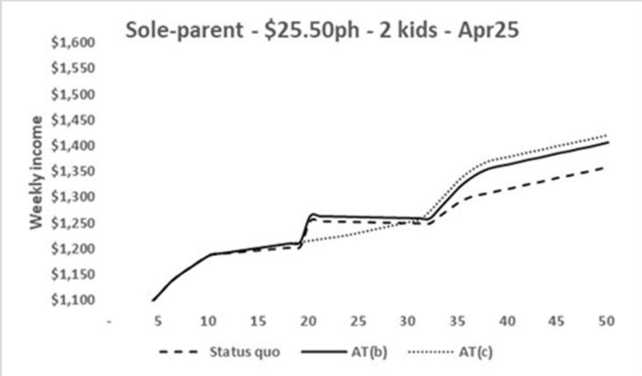
Choices between AT(a)-(c) are:

- Whether to **remove or retain the MFTC**, and
- The **size of the IWTC increase**.

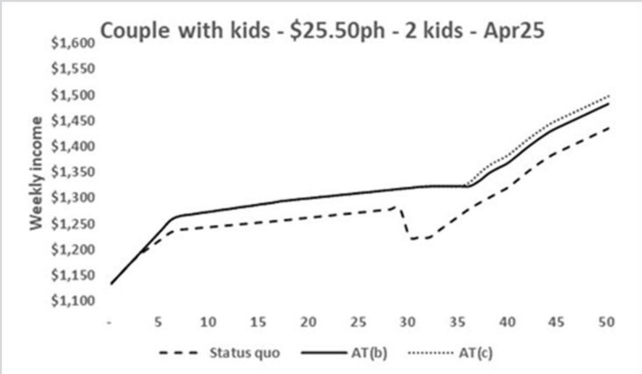
Options that **retain the MFTC** do not address the key issues with this payment (high EMTRs, administrative complexity, debt). Options that remove the MFTC would mean more working families receiving benefits.

Larger **IWTC increases** cost more but have greater reductions in child poverty.

Sole parent income by hours worked (no WEP)



Couple income by hours worked (no WEP)



Appendix Four – Parameters of in-work payment options

Parameters

	Status quo	New, more generous, in-work payment (2025/26)					Abatement threshold increase + complementary changes (2024/25)			
		IWP (base)	IWP(a)	IWP(b)	IWP(c)	IWP(d)	AT (a)	AT(b)	AT(c)	AT(d)
In work payment (annual)	N/A	$19,968	$17,420	$16,432	$17,420	$17,420	N/A			
In work payment (weekly)	N/A	$384pw	$335pw	$316pw	$335pw	$335pw	N/A			
Payment rate based on sole parent or couple	Sole parent	Couple	Sole parent	Sole parent	Sole parent	Sole parent	N/A			
Amount for being 'off-benefit'	$72.50pw	$384pw	$335pw	$316pw	$335pw	$100pw	$72.50pw	$82.50pw	$97.50pw	$82.50pw
Amount for being 'off benefit' and meeting hours test	$72.50pw +MFTC (up to $253pw for min wage earner)	N/A – same as above				Hours test - $335pw	$72.50pw +MFTC (up to $253pw for min wage earner)	$82.50pw +MFTC (up to $253pw for min wage earner)	$97.50pw (MFTC removed)	$82.50pw (MFTC removed)
Abatement threshold(s)	Abates after FTC	$26,520 $49,348	$26,520 $49,348	$26,520 $49,348	$26,520 $49,348	$26,520 $49,348	Abates after FTC			
Abatement rate(s)	27%	55% 30%	55% 30%	55% 30%	50% 27%	55% 30%	27%			
FTC abatement threshold / rate	$42,700 27%	$74,057 30%	$65,564 30%	$62,270 30%	$71,593 27%	$65,564 30%	$50,000 27%			

Item 13

Inland Revenue
Te Tari Taake

Policy and Regulatory Stewardship
Kaupapa me te Tiaki i ngā Ture
55 Featherston Street
PO Box 2198
Wellington 6140
New Zealand

T. 04 890 1500

Briefing note

Reference:	BN2023/229
Date:	2 August 2023
To:	Revenue Advisor, Minister of Revenue – Jason Batchelor Private Secretary, Minister of Revenue – Helen Kuy Revenue Advisor, Associate Minister of Revenue – Harper Burtenshaw
From:	Kathleen Littlejohn
Subject:	**Further information on The Working for Families Review options**

Purpose

1. Enclosed is a copy of additional information which the Ministry of Social Development has provided to the Minster of Social Development and Employment.

2. This information is intended to assist the discussion between yourself and the Minister of Social Development and Employment during your meeting on 3 August 2023.

Kathleen Littlejohn
Senior policy advisor
s 9(2)(a)

Further information on Abatement Threshold options

1 This note provides further information about the Abatement Threshold options presented in the report "Working for Families Review: Preferred approach for December Cabinet report back" [REP/23/7/669 / IR2023/216].

2 It provides information on the:

- earliest implementation dates for abatement threshold options
- explanations of losers associated with options that remove the Minimum Family Tax Credit (MFTC) – AT(c) and AT(d)
- a high-level estimate of how many people impacted by the MFTC removal could be moved onto Jobseeker Support
- high-level information about options to completely remove the MFTC.

Implementation dates

3 The table from the paper has been updated to add an additional row indicating the earliest implementation date for these options.

4 Note, the abatement threshold options were not re-costed from the March 2023 report so the fiscal impacts provided below may vary using updated fiscal and economic forecasts.

	AT(a) Abatement threshold to $50,000 pa only	**AT(b)** $10 pw IWTC increase + abatement threshold to $50,000 pa	**AT(c)** $25 pw IWTC increase + WFF abatement threshold to $50,000 pa + MFTC removed	**AT(d)** $10 pw IWTC increase + WFF abatement threshold to $50,000 pa + MFTC removed
Fiscal impact Tax Year (24/25)[1]	$238m	$309m	$406m	$291m
Average gains/losses	152,000 HHs gain $30pw	173,000 HHs gain $34pw	173,000 HHs gain $46pw 6,000 HHs lose $35pw	167,000 HHs gain $35pw 7,000 HHs lose $36pw
Child poverty reduction	4,000 (BHC50) 11,000 (AHC50)	6,000 (BHC50) 17,000 (AHC50)	8,000 (BHC50) 19,000 (AHC50)	5,000 (BHC50) 16,000 (AHC50)
Earliest implementation	1 April 2024, if • urgent legislation is passed by the end of 2023, and • a pre-commitment is secured against Budget 2024		1 April 2025, with funding sought through Budget 2024, under standard Budget timeframes	

[1] Fiscal costs only (does not include implementation or operational costings).

Options AT(c) and AT(d)

Households that lose

5 The number of families estimated to be financially disadvantaged under option AT(c) and AT(d) are likely to be over-stated, as both estimates do not account for the fact that many affected families would be eligible to receive an abated benefit to offset their losses. However, there would still be a small group of families who may not be eligible for benefits, for example, Jobseeker Support due to working more than 30 hours a week.

6 Officials recommend against removing the MFTC unless further changes are made to reduce the number of families financially disadvantaged. Removing the MFTC would create difficulty and confusion for those currently in receipt of the payment and is likely to result in some families being financially disadvantaged.

7 Previous modelling estimates that AT(c) would result in either:

- 6,000 households losing on average $35 pw (using Treasury's TAWA modelling)

  or

- 3,000 families currently receiving the MFTC would lose on average $79 pw (using Inland Revenue (IR) modelling, which is not directly comparable to the TAWA modelling above).

8 To reduce the number of people made worse off by the changes, agencies would advise those eligible to transfer to benefit. This would likely eliminate most of the losses estimated above, as Treasury and IR's models cannot estimate families moving onto benefit.

Explanation of differences between TAWA and IR modelling

9 Treasury's TAWA model estimates that there are more people receiving the MFTC than there are in reality (as it is based on survey data that then estimates the whole population from this smaller survey sample).

10 For this reason, IR's modelling is better to use for modelling of changes to the MFTC as it is based on administrative data of people receiving MFTC.

11 However, IR's model (as well as Treasury's) cannot estimate the shift of families on to a benefit, but we would expect that most of these families would be eligible for a benefit and would receive approximately the same amount of income support overall (assuming no change in their working hours).

12 Note that officials use TAWA results generally because it is the only model that can estimate child poverty impacts (and any families newly eligible for WFF tax credits).

Estimating how many people impacted by MFTC removal could be moved onto Jobseeker Support

13 In tax year 2021, there were 3,190 MFTC recipients made up of:

- 294 couples
- 2,896 sole parents.

14 Within the benefit system, the 30 hour rule means that the primary recipient in a **couple** cannot receive Jobseeker Support if they are working full-time, which is deemed to be 30 hours or more per week. As the MFTC has an hours test of 30 hours for couples, this means that some couples receiving MFTC **may not be eligible** to move onto Jobseeker Support.

15 Some of these couples may be eligible for a benefit if the partner of the primary recipient can "swap" to become the primary recipient (with their partner now the one working more than 30 hours a week). However, the new primary recipient is subject to full-time work obligations, regardless of the age of their children, which may not be feasible or desirable for some couples (e.g. if they have caregiving responsibilities for a child under 3).

16 **Sole parents** have a slightly different definition of full-time work for their receipt of Jobseeker Support. Sole parents are able to work full-time for a temporary period of up to 26 weeks provided their income, when assessed over a 52-week period, does not fully reduce their benefit.

17 This means that a sole parent working:

- less than 30 hours per week **may be eligible** to transfer to a main benefit
- 30 hours or more per week for 1 – 5 months per year **may be eligible** to transfer to a main benefit
- 30 hours or more per week for 6 or more months per year **may not be eligible** to transfer to a main benefit.

18 The table below summarises potential eligibility for MFTC recipients in different circumstances.

	MFTC recipients			
	Sole parents			Couples
Hours of work	Working less than 30 hours per week	Working 30 hours or more per week, for 1 - 5 months per year	Working 30 hours or more per week, for 6 or more months per year	Working 30 hours or more per week
Assumed eligibility for benefit	May be eligible	May be eligible	May not be eligible	May not be eligible
Approx number	**520**	**1,680**	**700**	**290**

19 Therefore, it is estimated that approximately 31 percent of MFTC recipients, or approximately 990 recipients, may not be eligible for transferring onto a main benefit. This number is made up of approximately 290 couples and 700 sole parents who work 30 or more hours per week for 6 or more months per year.

20 Some of the 700 sole parents may be able to receive Sole Parent Support (instead of Jobseeker Support), if their youngest child is under 14 years old, meaning they may be eligible for a main benefit even if they work for more than 30 hours. Therefore 700 is likely to be an upper estimate of the sole parents who may not be eligible to transfer to a benefit.

21 However, without individual assessment of circumstances and eligibility tests, we cannot be definitive about this number. Exact figures for recipients impacted would need to be provided much closer to the time the MFTC is removed, due to the variable nature of this population.

22 Officials can provide further advice about the options to mitigate the impact of removing the MFTC for this group. The main option is to amend the 30 hour rule or work obligations for Jobseeker Support receipt.

Alternative options to completely removing the MFTC

23 An alternate option to removing the MFTC completely is to freeze the rate of MFTC or alternatively grandparent the current recipients and eventually remove the payment when all families have moved off. These types of options would have lower fiscal costs and smaller losses for recipients but would increase administrative complexity and may have negative experiences for MFTC customers. Officials have not costed these options but can do so if Ministers are interested in future advice.

Note on costings

24 It is important to note that the costings provided in the advice so far have been **high-level estimates** of the most significant costs.

25 They do not include the following:

- Implementation and operational costs, or
- Costs associated with more families transferring on to benefit in the options that remove the MFTC:
    - These costs will also depend on whether benefit system changes are agreed to allow Jobseeker Support recipients with children to continue to receive an abated benefit for longer.

26 We expect that any savings from removing the MFTC would largely be offset by greater costs within the benefit system, with the differences likely to be marginal in the scale of the overall cost. This would be similar if the MFTC is grandparented, as the costs of this would be likely to be mostly offset by reductions in benefit costs. Officials can provide more refined costings, including implementation and operational costs, in future advice.

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Briefing note

Reference:	BN2024/260
Date:	18 June 2024
To:	Revenue Advisor, Minister of Finance – Emma Grigg Revenue Advisor, Minister of Revenue – Lonnie Liu Private Secretary, Minister of Revenue – Helen Kuy
From:	Richard McLaughlan
Subject:	**Response to the impending overlap of the Working for Families abatement threshold and Minimum Family Tax Credit threshold**

Purpose

1. You have requested a response to a media query from Susan Edmunds at Radio New Zealand received on 19 June 2024.

2. The media query concerns an article by Terry Baucher. This article outlines the impending overlap of the Working for Families abatement threshold and Minimum Family Tax Credit threshold, which is expected to result in a small number of families facing Effective Marginal Tax Rates of well over 100%.

3. The direct question asked by Susan Edmunds is whether this is something the Minister of Finance is concerned about.

Issue

The Working for Families abatement threshold

4. The Working for Families abatement threshold is currently set at $42,700. This is the point at which the Family Tax Credit and In-Work Tax Credit entitlements start to reduce at 27%.

5. The Working for Families tax credit abatement threshold is not routinely adjusted. The last time the Working for Families abatement threshold was increased was on 1 July 2018. Working for Families has become progressively more targeted to those on lower incomes, as incomes have increased faster than the abatement threshold.

6. There was a National Party manifesto commitment to increase the Working for Families abatement threshold from $42,700 (before tax) to $50,000 (before tax), from 1 April 2026. However, following coalition negotiations, this was removed from the tax package.

The Minimum Family Tax Credit threshold

7. The Minimum Family Tax Credit is intended to "make work pay" by providing a financial incentive to ensure, at the margin, low income working families remain better off financially in full time work than they would be on a main benefit. Where a person receives the Minimum Family Tax Credit, they will receive a payment increasing their income up to a guaranteed amount. After this point their entitlement will reduce at 100%

8. The Minimum Family Tax Credit is broadly set at a point where someone is $1 dollar better off working and receiving the Minimum Family Tax Credit than they would be on a main benefit. As such, it is required to be increased every year in line with changes to main benefit rates.

9. From 31 July, the Minimum Family Tax Credit threshold will be $35,316 (after tax), or $41,848 (before tax).

Overlap of the two thresholds

10. As a matter of course, the Minimum Family Tax Credit threshold increases every year in line with benefit rates, whereas the Working for Families abatement threshold is not routinely adjusted.

11. This means that without an adjustment, the Minimum Family Tax Credit threshold is forecast to overlap with the Working for Families abatement threshold in April 2027. This will mean that Minimum Family Tax Credit recipients, who are some of the lowest income working families, will face effective marginal tax rates of well over 100%.[1] This would mean that increasing work hours would result in less income.

12. An example of this overlap was included in the Regulatory Impact Statement for the $25 increase to the In-Work Tax Credit (which has been quoted in the media):

Example of overlap:
Under this example the Minimum Family Tax Credit threshold is increased to $43,000 (before tax) and the Working for Families tax credits abatement threshold remains at $42,700 (before tax).

Mila is a sole parent who works at a supermarket for 35 hours per week on minimum wage and earns $42,900 dollars. Following the crossover, she will face an effective marginal tax rate of 128.6%. This means that for an additional $1 she earns, her tax credits reduce by $1.28 and her total income drops as a result. She is not incentivised to work any additional hours.

This is a result of the following reductions of her income via:

- 17.5% personal income tax;
- 82.5% Minimum Family Tax Credit;
- 1.6% ACC levy; and
- 27% Working for Families abatement (the additional abatement once the overlap happens).

This could be made worse if Mila has student loan repayments (12%) or receives the Accommodation Supplement (25%).

[1] Effective marginal tax rates are a measure of the total amount lost from marginal increases in earnings due to taxes, deductions, and social assistance abatements. So, an effective marginal tax rate of 100% means that $1 of the next $1 of income earned is lost to the person, and an individual is no better off working an additional hour.

Suggested response

13. We suggest the following response from Ministers in relation to this issue:

- Ministers are aware of the issue of overlapping abatement of Working for Families tax credits. We have directed officials to provide us with some advice later this year about how we look to address it.

- It should be noted that increasing the Working for Families abatement threshold is only one way to mitigate this issue, and other options are available. We expect that advice from officials will canvass a range of different options.

Richard McLaughlan
Senior Policy Advisor
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