



## Proactive Release

The following document has been proactively released by the Department of the Prime Minister and Cabinet (DPMC) on behalf of Hon Jan Tinetti, Minister for Child Poverty Reduction:

### **Proactive Release: Briefing to the Incoming Minister for Child Poverty Reduction - Supplementary briefings**

The following document has been included in this release:

- **Title of paper:** Aide-Memoire: Working for Families: Briefing to the Incoming Minister for Child Poverty Reduction (DPMC-2022/23-856)

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#### **Key to redaction codes**

- s9(2)(a), to protect the privacy of individuals;
- s9(2)(f)(iv), to maintain the confidentiality of advice tendered by or to Ministers and officials.



## Coversheet

### Aide-Mémoire: Working for Families: Briefing to the Incoming Minister for Child Poverty Reduction

Date:	17/02/2023	Report No:	DPMC-2022/23-856
		Security Level:	<del>IN CONFIDENCE</del>
		Priority level:	Routine

	Action sought	Deadline
Hon Jan Tinetti Minister for Child Poverty Reduction	discuss with officials at officials' meeting	22 February 4.15pm

Name	Position	Telephone	1 <sup>st</sup> Contact
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#### Departments/agencies consulted on Briefing

Ministry of Social Development, the Treasury, Inland Revenue.

#### Minister's Office

Status:

Signed

Withdrawn

#### Comment for agency

Attachments: Yes/No

# Aide-Mémoire

## Working for Families: Briefing to the Incoming Minister for Child Poverty Reduction

<b>To:</b>	Hon Jan Tinetti, Minister for Child Poverty Reduction		
<b>From:</b>	Clare Ward, Executive Director Child Wellbeing and Poverty Reduction	<b>Date:</b>	17/02/2023
<b>Briefing Number:</b>	DPMC-2022/23-856	<b>Security Level:</b>	<del>IN CONFIDENCE</del>

### Purpose

1. The purpose of this aide-mémoire is to provide background information on:
  - the Working for Families (WFF) tax credits
  - the current review of WFF and the options being considered.<sup>1</sup>

### WFF was implemented almost 20 years ago and is now being reviewed

2. WFF was implemented between 2004 and 2007 with the dual objectives to:
  - support income adequacy and reduce child poverty
  - improve financial incentives for low-income earners to enter the labour market.
3. There was a third delivery objective to support people into work (and to remain in work) by making sure they get the assistance they're entitled to in a timely manner.
4. Around 57% of all families in New Zealand receive WFF, at a cost of \$3 billion for the 2022 financial year. WFF is made up of the following tax credits.
  - **Family Tax Credit** (273,900 families, \$2.1 billion): the main payment that supports beneficiary and working families and is not dependent on work status. Currently, families receive \$127 per week (pw) for the eldest child and \$104 pw for each subsequent child. At the point the family income reaches \$42,700, it begins to be abated at 27% (ie for each dollar earned over \$42,700, the Family Tax Credit payment is reduced by 27 cents).
  - **In-Work Tax Credit** (182,000 families, \$542m): the main in-work payment that supports families in work, if they do not receive a main benefit. It pays \$72.50 pw for families with 1 to 3 children, with an extra \$15 pw for each subsequent child. After the Family Tax Credit is fully abated, the In-Work Tax Credit is abated at 27%.
  - **Minimum Family Tax Credit** (4,320 families, \$15m): the other in-work payment that tops up the incomes of working families who go off benefit to a guaranteed minimum

<sup>1</sup> For background on the current policy settings for the benefit/work interface see **Attachment B**.

income level threshold (currently set at \$34,216). This ensures these families are not worse off when they leave benefit. As a family earns an extra dollar over the income threshold, they lose a dollar of MFTC until the tax credit is fully abated away.

- **Best Start Tax Credit** (112,300 families, \$339m): introduced as part of the Families Package in 2018. It provides \$65 pw to all families with a child under one year old, and for lower income families with a child under three. After the first year, it begins to abate at 21% for each dollar earned over \$79,000.
5. The Government agreed to review WFF as part of the Welfare Overhaul work programme [CAB-19-MIN-0578 refers]. In May 2021, Income Support Ministers<sup>2</sup> agreed that the original objectives remain important, and that the Review should focus on:
    - low-income working families, while maintaining support for beneficiary families
    - options that target support to lower-income families rather than more universal support
    - the principle of making work pay and assisting with the costs for people in work.
  6. In April 2022, Ministers agreed to two themes for further advice on 'making work pay':
    - improving the settings for in-work assistance and the work-benefit interface
    - assisting with the costs of children in the early years.

### **WFF is a significant lever to achieve direct reductions in child poverty**

7. The WFF Review presents a key opportunity in the coming years to achieve substantial reductions in measured child poverty and to make progress towards achieving the ten-year child poverty targets, which are due to be achieved in 2027/28. The 2022 Child Poverty Budget Report indicates significant policy interventions aimed at increasing incomes for low-income households with children will be required to reach these targets.
8. The Government's second set of three-year intermediate targets (to be assessed in 2023/24) aim to support the achievement of the ten-year targets. If a simple change, such as a straightforward tax credit increase, were to be implemented in mid-2023, it would still have some impact on progress towards the second intermediate targets. However, current reporting methods mean that only around half of the impacts of an initiative would be reflected in the measured rates in the 2023/24 target year.<sup>34</sup> Changes implemented in 2024 would have a full impact in the first year (2024/25) of the third intermediate target period.

### **WFF has had a positive impact for low-income families, but there are areas for improvement**

9. As part of the current review of WFF, officials undertook a literature scan of the tax credits and concluded that New Zealand's model of tax credits is not an outlier. We face similar issues to other countries that use tax credits, in terms of balancing the objectives of income adequacy, reducing child poverty, and improving incentives to work. Within

<sup>2</sup> As outlined in our initial BIM, the Income Support Ministers have included the Ministers for Child Poverty Reduction, Social Development and Employment (lead Minister), Finance, Revenue, Children and, more recently, the Minister of Education.

<sup>3</sup> Stats NZ's current approach to reporting child poverty data is based on a "2-year rolling reference period". This creates a lag between the time that a policy is implemented and the impacts being fully reflected in the data. In 2024/25 Stats NZ's reporting will shift to a 12 month fixed reference period which will mean that impacts of policies implemented in full before the start of the financial year will be fully reflected in the poverty rates for that financial year.

current fiscal constraints, the broad structure and targeting of WFF is largely fit-for-purpose. However, improvements are needed to address identified issues with the design of the system (see **Attachment A** for a summary of the evidence).

10. 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, payments are beginning to abate for those on very low incomes. Our abatement settings mean that multiple payments across the tax and benefit system can withdraw at the same time, meaning that some groups see little return from working more, particularly if they are also paying for childcare costs.
11. Officials believe there are significant issues with the design of the two work-focused payments, particularly the Minimum Family Tax Credit (MFTC) and, to a lesser extent, the In-work Tax Credit (IWTC). The MFTC is particularly complex and not well understood by customers, so has lower take-up and awareness compared to the other WFF tax credits. The rigidity of the eligibility criteria makes entitlement sensitive to changes in work circumstances, and can result in under- and over-payments during the year.
12. There is also significant complexity in the system, particularly in relation to the number of payments, different eligibility rules, difficulty in navigating the system between the two delivery agencies (Ministry of Social Development and Inland Revenue), and knowing when you are better off (for example, with abatement settings).

### **The overriding concern from stakeholder engagement related to child poverty**

13. An engagement process was carried out last year as part of the WFF review. The majority of survey respondents were of the view that WFF does not currently pay enough to support families. Through targeted engagement, many stakeholders, including a number of academics and those representing groups that advocate for children, emphasised the importance of broader social policy concerns. From these groups, we heard that:
  - the objective of income adequacy and reducing child poverty is important and that the payments need to keep up with the cost of living to provide adequate support
  - the IWTC should be paid to all families and not just those who are off a benefit and in paid work. These stakeholders argued that the payment is discriminatory and unfair, particularly given children are unable to choose whether their parents are working. This is a particular and longstanding concern of the Child Poverty Action Group.
14. Many argued the IWTC is not effective as a work incentive, and that it is more important to remove barriers to employment (such as the costs of travel and childcare). Other stakeholders, by contrast, emphasised the importance of financial incentives to work, and argued that, if anything, they should be strengthened. Stakeholders from a range of different perspectives noted that the current abatement of WFF payments means some people see little or no return from working more.

### **There have been a number of changes to WFF since 2018**

15. The Families Package in 2018 increased and simplified the Family Tax Credit (FTC) payment rates, and introduced the Best Start payment for new-born children. In Budgets 2020 and 2021, Ministers prioritised benefit increases over changes to the tax credits. In late 2021, in recognition of the additional economic pressures from COVID-19 and the need to make further progress on the child poverty targets, the Prime Minister announced

an FTC increase to coincide with the scheduled Consumer Price Index (CPI) adjustment on 1 April 2022.<sup>5</sup> The abatement rate was also increased from 25% to 27%, which helped to concentrate the greater gains to households on the lowest incomes.

16. Last year, inflation triggered another CPI adjustment to the FTC and Best Start payment rates, meaning that both payments will increase again from 1 April this year. These increases have already been factored into the Treasury's child poverty forecasts released in May 2022.
17. Other changes have been made to improve the IWTC for working families.
  - From 1 July 2020 the hours test was removed, meaning people can continue to be eligible even if they work as little as an hour a week. Previously, the hours test was a minimum of 20 hours for sole parents and 30 hours for couple parents.
  - From 1 April 2021, two-week 'grace periods' were introduced as part of the response to COVID-19. This meant families could continue to receive the IWTC payment for up to two weeks while not working. This ensures people transitioning between jobs, or with contracts built around school terms, for example, continue to be eligible.

**More recently, a suite of reform options has been developed for the Review**

18. More recently, advice has been commissioned by the Income Support Ministers for significant reform options that support the objectives and focus areas. This has included more structural options that aim to improve the design of the tax credit system s9(2)(f)(iv)  
[Redacted]
19. As with any changes in the tax credit space, there are always trade-offs between the competing goals of poverty reduction, work incentives, and fiscal restraint (the 'iron triangle'). Adequacy-focused changes s9(2)(f)(iv) can help achieve direct and immediate reductions in child poverty rates. Improvements to the design and structure of settings, and making work pay, can also improve work incentives and reduce barriers to employment. While the impact on child poverty rates is likely to be more gradual and less significant, at least in the short term, such changes are also part of any comprehensive approach to child poverty reduction.

s9(2)(f)(iv)  
[Redacted]

<sup>5</sup> Under the WFF legislation, the FTC and BS payment rates must be increased to match inflation at specified times – the rates are increased once the cumulative value of quarterly increases in the CPI reaches 5% since the rates were last adjusted.

s9(2)(f)(iv)  
[Redacted]

s9(2)(f)(iv)

[Redacted]

[Redacted]

**Next steps**

24. Officials are currently working through the new commissioning and will provide advice in March for Budget 2023 options. The lead Minister for the Review is considering governance options for the work programme going forward.

25. We will discuss this with you in our upcoming meeting on Wednesday 22 February.

s9(2)(a)

[Redacted]

**Clare Ward**  
Executive Director, Child Wellbeing and Poverty Reduction

17/02/23



**Hon Jan Tinetti**  
Minister for Child Poverty Reduction

18 / 02 / 2023  
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<b>Attachments:</b>	<b>Title</b>	<b>Security classification</b>
<b>Attachment A:</b>	Summary of evidence	UNCLASSIFIED
<b>Attachment B:</b>	Current policy settings for the benefit/work interface	UNCLASSIFIED

<b>Contact for telephone discussion</b>			
<i>Name</i>	<i>Position</i>	<i>Telephone</i>	<i>1<sup>st</sup> Contact</i>
Clare Ward	Executive Director, Child Wellbeing and Poverty Reduction	s9(2)(a)	✓
Deborah Tucker	Principal Analyst	s9(2)(a)	

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## Attachment A: Summary of evidence

26. As part of the Review, officials have brought together a range of evidence and analysis on issues relevant to WFF. This evidence helps us 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 that 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 have 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 is 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 and 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.** The immediate impact of the WFF package 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 the aggregate.
- **The introduction of WFF between 2004 and 2007 benefited low-income working families more than beneficiary families.** The significant reductions in child poverty WFF 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.

- **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 to 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 are 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.

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# Current policy settings for the benefit/work interface | As at 12 July 2022

## Payments for people on benefit

JS

SPS

### Main Benefit settings

#### Eligibility

Sole Parent Support (SPS) is available for sole parents with children 13 and under. Jobseeker Support (JS) is available for sole parents with children over 13 and couples with children.

#### Abatement

Abatement settings are different for different family types, based on different expectations about the level of work encouraged.

- Couples on JS can earn up to \$160 before their benefit begins to abate (~8 hours min wage). For every dollar earned above this threshold, the net rate reduces by 70 cents.
- For sole parents (SPS or JS) their benefit reduces by 30 cents for every dollar earned over \$160 a week, and by 70c above \$250.

Sole parents generally move off-benefit at 20 hours worked when they are better off receiving the IWTC and MFTC instead.

For couples, historically they were better off moving off benefit at 30 hours worked but in recent years couples may be financially better off remaining on benefit if one member of the couple is in full-time work (provided the primary recipient of benefit is the one that does not work 30 hours or more).

WEP

### Winter Energy Payment

#### Eligibility

All main benefit recipients qualify for the rates of WEP.

#### Abatement

There is no gradual abatement of WEP. As people move off benefit they lose entitlement to WEP.

## Payments for people both on or off benefit

FTC

### Family Tax Credit

#### Eligibility

The FTC is available to both beneficiaries and working families. It is \$127.73 for the eldest child, and \$104.08 for subsequent children.

#### Abatement

The FTC abates at 27c in the dollar if a family earns over \$42,700. Increases to the minimum wage (and non-adjustment to the threshold) has meant that the FTC now begins abating at 39 hours on the minimum wage, or for some couples while they are receiving a main benefit.

AS

### Accommodation Supplement

#### Eligibility

The AS is available to both low-income beneficiaries and working families if they have high housing costs.

#### Abatement

AS is abated at 25 cents from each dollar of income above the benefit cut-out point. This is \$842 a week for a sole parent, and \$926 a week for a JS couple with children.

BSTC

### Best Start Tax Credit

#### Eligibility

BSTC is a payment of \$65.15 per child a week for families with children under 3. It is universal in the first year of a child's life, and in the second and third years it is income tested.

#### Abatement

Payment abate at 21% in the second and third year once the family earns above \$79,000 a year. It abates outside of other WFF payments.

## Payments for people not receiving a benefit

MFTC

### Minimum Family Tax Credit

#### Eligibility

The MFTC is a 'top up' for low-income working families to ensure they are better off in-work than when on a benefit. The MFTC threshold ensures a weekly income of \$632 per week and is paid to around 3,500 of the lowest income working families. To be eligible, parents must meet an hours test, of 20 hours of work for sole parents and 30 hours of work for couples.

#### Abatement

For every dollar a family earns over the MFTC amount, their entitlement reduces by more than one dollar (due to ACC levies) which can mean no additional income from an extra hour of work.

IWTC

### In-Work Tax Credit

#### Eligibility

The IWTC is a payment for low- and middle-income working parents and provides \$72.50 per week for the first three children and \$15 for each child after that.

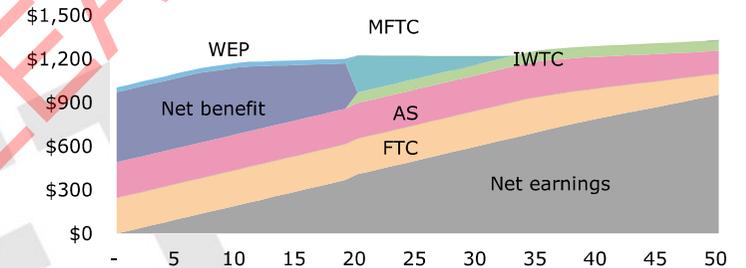
IWTC recipients are no longer required to meet an hours worked test, but IWTC is only available to families in work and not receiving a main benefit.

#### Abatement

The IWTC starts to abate at 27c in the dollar after FTC is fully abated (around \$65,000 for a one child family, and \$84,500 for two child family).

## Income by hours worked, by payment type

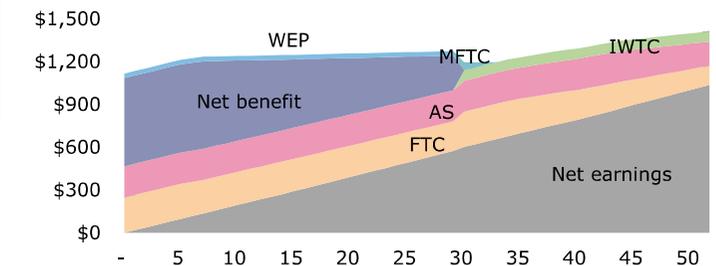
### Sole parent with two children (aged over 3)



When working no hours, this family's income is made up of their main benefit, AS, FTC, and WEP. At around 8 hours of work, their benefit starts to reduce at 30c for every \$1 earned. At around 12 hours, their benefit abates at a much higher rate (70c for every \$1 earned), which means they see little return for working more.

At 20 hours of work, they become eligible for the IWTC and the MFTC. The MFTC reduces dollar for dollar so means no financial gain for increasing hours of work until they pass the MFTC threshold at around 35 hours.

### Couple with two children (aged over 3)



When working no hours, this family's income is made up of their JS benefit, AS, FTC and WEP. At 8 hours their benefit starts to abate at 70%.

When the primary benefit recipient works 30 hours a week they no longer qualify for a main benefit and instead become eligible for the IWTC and MFTC. This means a drop in income because the MFTC no longer ensures couples are better off moving off benefit. However, most couples continue to qualify for a benefit at this point provided the partner of the primary recipient is not working more than 30 hours, which means they don't face a drop in income.