

Coversheet: Increasing main benefit abatement thresholds on 1 April 2021 and consequential adjustments to the Minimum Family Tax Credit

Advising agencies	<i>Ministry of Social Development and Inland Revenue</i>
Decision sought	<p><i>Agreement to increase main benefit abatement thresholds on 1 April 2021 and consequentially adjust the Minimum Family Tax Credit for 2020/21 and 2021/22.</i></p> <p><i>Note that on 30 November 2020, Cabinet agreed to adjust the Minimum Family Tax Credit for 2020/21 [CAB-20-MIN-0490 refers]. However, a Regulatory Impact Assessment could not be undertaken due to time constraints. Under Cabinet’s regulatory impact analysis requirements, this document is:</i></p> <ul style="list-style-type: none"> <i>- the Supplementary Analysis Report for the adjustment to the Minimum Family Tax Credit for 2020/21; and</i> <i>- the Regulatory Impact Assessment for the abatement threshold increases and the adjustment to the Minimum Family Tax Credit for 2021/22.</i>
Proposing Ministers	<i>Minister for Social Development and Employment Minister of Revenue</i>

Summary: Problem and Proposed Approach

Problem Definition

What problem or opportunity does this proposal seek to address? Why is Government intervention required?

The current abatement thresholds provide limited work incentives for beneficiaries

The amount that beneficiaries can earn before their benefit reduces has declined substantially over time as benefit abatement thresholds have not been increased in line with wage growth. This has reduced financial incentives to enter the labour market and to work part-time for people receiving benefits. For example, a person receiving Jobseeker Support in 1997 could work around 11.4 hours on minimum wage before their benefit abated; in 2019, this has reduced to around 4.5 hours on minimum wage.

There are trade-offs in making consequential adjustments to the Minimum Family Tax Credit

Under current policy, the Minimum Family Tax Credit (MFTC) thresholds are adjusted annually to account for changes to relevant settings, such as changes to benefit rates, abatement thresholds and the minimum wage.

The MFTC threshold for 2020/21 was not adjusted to reflect the \$25 benefit rate increase made on 1 April 2020 in response to COVID-19 due to time constraints at the time. This has resulted in the current MFTC threshold being misaligned with the current benefit rate.

Increasing main benefit abatement thresholds on 1 April 2021 has flow-on implications for the MFTC threshold in 2021/22 and subsequent tax years. To maintain financial incentives provided by the MFTC for families with children to enter work, the MFTC threshold for 2021/22 requires adjustments alongside abatement threshold increases under current policy. However, given the proposed increases to the abatement thresholds are significant, the adjustment required for the MFTC to align would be much higher than previous adjustments. This may exacerbate known issues with the MFTC, mainly reducing financial incentive for sole parents to work more than the minimum hours required. It may also increase the cost of options [§ 9\(2\)\(f\)\(iv\)](#) in the upcoming review of Working for Families.

Summary of Preferred Option or Conclusion (if no preferred option)

How will the agency's preferred approach work to bring about the desired change? Why is this the preferred option? Why is it feasible? Is the preferred approach likely to be reflected in the Cabinet paper?

Abatement threshold increases will improve financial work incentives

Increasing benefit abatement thresholds to \$160 and \$250 per week increases the number of hours a beneficiary can work before their benefit begins to reduce. This will improve the financial incentives to enter the labour market and work part-time for people receiving benefits. Part-time work can provide a pathway to full-time work by providing opportunities to connect with the labour market, get work experience and become familiar with the demands that can come with employment.

There are different agency views on making adjustments to the Minimum Family Tax Credit

Under current policy, changes to benefit settings would lead to an adjustment of the MFTC threshold to ensure the financial work incentives provided by the MFTC are maintained. However, given the extent of the recent and proposed benefit changes, full adjustment of the MFTC incurs significant fiscal costs. Additionally, a significant increase to the MFTC threshold may increase the cost of options [§ 9\(2\)\(f\)\(iv\)](#) as part of the upcoming review of Working for Families (WFF).

2020/21 MFTC threshold adjustment

Retrospectively adjusting the 2020/21 MFTC threshold to reflect the increases to main benefits that came into effect on 1 April 2020 means the work incentives provided by the MFTC will be maintained for the 2020/21 tax year. This ensures that low-income families with children (both sole parents and two parent families) are better off in work and receiving the MFTC than working and receiving the benefit.

Note that on 30 November 2020, Cabinet agreed to retrospectively increase the 2020/21 MFTC threshold to \$29,432 from 1 April 2020 to reflect the increases to main benefits that came into effect on 1 April 2020 [CAB-20-MIN-0490 refers].

2021/22 MFTC threshold adjustment

Inland Revenue (IR), Ministry of Social Development (MSD) and the Treasury have differing views on the most appropriate options relating to the alignment of the MFTC threshold:

- **MSD prefers the partial prospective alignment option. This is the proposed option in the Cabinet paper.** MSD considers that a partial prospective alignment maintains the work incentives MFTC provides to the majority of MFTC recipients (ie, sole parents), but at a significantly lower fiscal cost than full alignment. MSD notes that fully aligning the MFTC threshold may exacerbate existing MFTC issues such as high Effective Marginal Tax Rates (EMTRs)¹. MSD considers partially aligning the MFTC threshold would increase the cost of options § 9(2)(f)(iv) as part of the upcoming WFF review, particularly if there is a desire to avoid people being financially disadvantaged by future changes. However, these effects will be less than under full alignment.
- **IR prefers the full prospective alignment option.** Although the fiscal cost of full alignment is greater than under other options, IR considers it necessary to maintain the work incentives provided by the MFTC, ensuring low-income families with children (both sole parents and two parent families) are better off in work and receiving the MFTC than working and receiving the benefit. IR does not consider the potential effects of aligning the MFTC threshold on any future WFF review to be a significant enough issue to warrant reducing the work incentives currently provided by the MFTC.
- In advice to Ministers, the Treasury recommended the no prospective alignment option due to the tight fiscal environment. The Treasury also did not consider that the policy decision [to align the MFTC threshold with benefit rates] meets the threshold to be progressed as a Budget pre-commitment. While the Treasury acknowledged that it was likely to introduce greater complexity for clients, the Treasury did not agree that these adverse effects were sufficient to justify funding the initiative ahead of the Budget process given the tight fiscal environment. § 9(2)(f)(iv)

Section B: Summary Impacts: Benefits and costs

Who are the main expected beneficiaries and what is the nature of the expected benefit?

Monetised and non-monetised benefits

Beneficiaries working part-time and non-beneficiary recipients of the Accommodation Supplement gain from abatement threshold increases

The main people to gain are beneficiaries working part-time and non-beneficiary recipients of the Accommodation Supplement (these are low to middle-income working families). MSD estimates that around 82,900 individuals and families will gain an average of \$18 per

¹ Effective Marginal Tax Rate shows how a dollar increase in gross income translates to an increase in income in hand (after taxation and the reduction of income-tested assistance).

week in extra income support payments as a result of increasing benefit abatement thresholds.

Non-monetised benefits include:

- Improved financial incentives to enter the labour market and work part-time for people receiving benefits
- A modest reduction in the number of children in poverty (it is estimated that the proposed increases to the abatement thresholds will reduce child poverty by around 6,000 (+/- 3,000) on the AHC50 fixed line measure² and 2,000 (+/- 3,000) on the BHC50 measure³ in 2021/22), and
- Broader improvements in health and wellbeing where eligible people are engaged in work (provided the work is safe, stable and financially beneficial).

MFTC recipients and newly eligible recipients will gain from the adjustments to the Minimum Family Tax Credit

Retrospective change – increasing the 2020/21 MFTC threshold to reflect the \$25 benefit rate increase on 1 April 2020

Approximately 3,200 families receiving the MFTC in the 2020/21 tax year would gain an additional \$32 for each week they received the MFTC. The maximum MFTC increase a family could receive would be \$1,664 (\$32 x 52 weeks). However, it is estimated that the average MFTC increase for the year would be approximately \$1,280 per family.

Approximately 400 additional families would become newly eligible for the MFTC in the 2020/2021 tax year as a result of the threshold increase. Because newly eligible families will have incomes above the current threshold, the average increase for these families will be less than \$32 a week.

A full retrospective increase will also maintain financial incentives for families to move off benefit and into work for the remainder of the 2020/21 tax year. It also addresses the potential equity issue whereby some families who remained off benefit and in work following the benefit rate increase on 1 April 2020 are financially disadvantaged relative to those who are on benefit.

Prospective change – partially increasing the 2021/22 MFTC threshold

Approximately 4,000 families are expected to receive the MFTC in the 2021/22 tax year. Of these, around 400 families would be newly eligible to the MFTC. Families would gain an additional \$22 for each week they receive the MFTC. The maximum MFTC increase a family could receive in the 2021/22 tax year would be \$1,144 (\$22 x 52 weeks). However, because not all families will receive the MFTC for every week of the tax year, the average MFTC increase is estimated to be less than \$1,144.

² AHC50 measures the number of children in households with incomes much lower than a typical 2018 household, after they pay for housing costs, and is measured by the threshold line set at 50 per cent of the median income in 2017/18, after housing costs are removed.

³ BHC50 is a moving-line income measure, with the poverty threshold taken the year the data is gathered (low income, before housing costs – moving-line measure). BHC50 measures the number of children in households with much lower incomes than a typical household, and is measured by the threshold line set at 50 per cent of the median household income in the year measured.

A partial increase of the MFTC threshold ensures that sole parents, who make up around 90 percent of the MFTC recipients, continue to be financially better off working and receiving the MFTC than working and receiving a benefit.

Where do the costs fall?

Monetised and non-monetised costs; for example to local government or regulated parties

Abatement threshold increases are primarily a cost to the Government

The cost to the Government of increasing benefit abatement thresholds is \$387.496 million in income support payments and \$6.4 million in operating costs over the forecast period. There is an additional cost of \$80,000 for 12 months for providing a Transitional Assistance Payment (TAP) to people who may be financially disadvantaged as a result of the abatement threshold increases on 1 April 2021.

Non-monetised costs include a small reduction in financial incentives to work full-time for some beneficiaries.

Adjustments to the Minimum Family Tax Credit are primarily a cost to the Government

Retrospective change – increasing the 2020/21 MFTC threshold to reflect the \$25 benefit rate increase on 1 April 2020

The cost to the Government of increasing the 2020/21 MFTC threshold is \$4.6 million for the 2020/21 tax year and \$24.1 million for the forecast period.

Prospective change – partially increasing the 2021/22 MFTC threshold

The cost to the Government of partially increasing the 2021/22 MFTC threshold is \$17 million over the forecast period, assuming the retrospective increase is agreed to.

The financial work incentives provided by the MFTC would be reduced for two-parent families (approximately 10 percent of MFTC recipients) as they would theoretically be better off working and receiving a main benefit than working and receiving the MFTC. There may be a small net fiscal cost to the Government from two-parent families moving onto a benefit. This net fiscal cost has not been calculated due to time constraints. The behavioural impacts are uncertain.

What are the likely risks and unintended impacts? How significant are they and how will they be minimised or mitigated?

Abatement threshold increases may financially disadvantage a small number of people but a Transitional Assistance Payment can be provided

Increasing benefit abatement thresholds will mean that a small number of people will be financially disadvantaged due to complex interactions in the income support system. TAP, a temporary non-taxable payment, is proposed to be available for up to 12 months for the small number of people who may be financially disadvantaged on 1 April 2021 as a result of the abatement threshold increases.

Retrospective and prospective adjustments to the Minimum Family Tax Credit each have unintended impacts

A retrospective increase (paid in lump sum for the portion of the year for which payments have already been made) may lead to debts being created for some people as the MFTC is chargeable income for some types of financial assistance paid under the Social Security Act 2018 (such as Temporary Additional Support). It is also assessable income for Public Housing purposes, for assessing eligibility and calculating the rate of Income Related Rent. While this does lead to debts for some clients, these debts are usually less than the value of the lump-sum payment (so clients are still better off overall) and it reflects the appropriate consideration of these payments as income for these families.

The prospective partial increase means that the MFTC would not be fully aligned with its policy intent and some two-parent families may be better off working and receiving a main benefit than working and receiving the MFTC. However, few couples are likely to qualify for a benefit if one person is working 30 hours a week as this is considered working full-time under the Social Security Act 2018⁴.

Section C: Evidence certainty and quality assurance

Agency rating of evidence certainty?

How confident are you of the evidence base?

MSD is confident that increasing benefit abatement thresholds will directly increase incomes for beneficiaries working part-time and low to middle-income working families receiving the Accommodation Supplement. Holding all else equal, MSD is also confident that these increases are likely to modestly reduce child poverty.

The evidence base on financial incentives to work (for both abatement threshold increase and MFTC) indicates that financial incentives are only one of many factors that influence people's decisions on whether to work and how much to work and they are not usually the most important factor. However, empirical evidence suggests small but statistically significant impacts on labour market participation and intensity from changes in financial incentives to work, with larger impacts for some groups compared to others.⁵ The modelling of the increases to benefit abatement thresholds and the MFTC assumes no behavioural impacts, i.e. no increases in labour market participation or hours worked, as these impacts are likely to be modest and are difficult to quantify.

While increasing financial incentives to work part-time, the changes also reduce financial incentives to work full-time for some. Again, this impact has not been quantified. There is reasonably strong evidence that suitable work has broader positive impacts on wellbeing⁶,

⁴ This is due to the '30-hour rule', where a person (or couple) are not eligible for Jobseeker Support if they are working full-time (defined as 30 hours a week).

⁵ Kostøl, A, & Mogstad, M. (2012) How Financial Incentives Induce Disability Insurance Recipients to Return to Work. IZA Discussion Paper No. 6702 (<http://ftp.iza.org/dp6702.pdf>);
Card, David E., (2000) Reforming the Financial Incentives of the Welfare System. IZA Discussion Paper No. 172.

⁶ The Royal Australasian College of Physicians and the Australasian Faculty of Occupational and Environmental Medicine (2015) Realising the health benefits of work – An evidence update. (<https://www.racp.edu.au/docs/default-source/advocacy-library/pa-health-benefits-of-work-evidence-update.pdf?sfvrsn=4>)

Waddell, G., Burton, A.K. (2006) *Is Work Good For Your Health And Well-Being?* TSO, London

but given the difficulty of modelling any increases in labour market participation or hours of work there has been no attempt to quantify these broader impacts.

To be completed by quality assurers:

Quality Assurance Reviewing Agency:

The reviewing agencies were:

- Ministry of Social Development
- Inland Revenue

Quality Assurance Assessment:

The Quality Assurance reviewers at Inland Revenue and Ministry of Social Development have reviewed the *Increasing main benefit abatement thresholds on 1 April 2021 and consequential adjustments to the Minimum Family Tax Credit RIA* and considers that the information and analysis summarised in it **partially meets** the quality criteria of the Regulatory Impact Analysis framework.

Reviewer Comments and Recommendations:

It partially meets the quality criteria for the following reasons:

- There has been no analysis of the behavioural impacts. This is understandable given the timeframes and difficulties undertaking this analysis. However, the abatement thresholds and the MFTC are intended to encourage people to engage in work. Ideally, RIA would include an estimate of how many people will move into work as a result of the changes. The team notes the employment impacts will be monitored following implementation.
- There is minimal discussion of alternative options to the abatement threshold increases, such as the staged increases committed to by the Government as part of Budget 2019. However, the Treasury RIA team advised MSD that a full RIA for the abatement threshold increases was not required because the increases were a manifesto commitment.
- In terms of the MFTC, the status quo is based on a long-established policy of full alignment of the MFTC with benefit changes. There are now differing views on the appropriateness of this automatic linkage when there are significant increases in benefit entitlements and the case for change does not adequately consider the impact on the identified group of people who would be relatively worse off if the MFTC is not increased. Moreover, the analysis relies on certain assumptions about the fiscal cost, which could benefit from further explanation, such as the degree of behavioural response that could lead individuals to shift from paid employment with MFTC to paid employment with welfare support. The behavioural responses are uncertain. The team notes the employment impacts will be monitored following implementation.
- We note that the options have administrative implications but there is little discussion of the impacts, for example from backdating MFTC payments.

Curnock E, Leyland AH, Popham F. (2016) The impact on health of employment and welfare transitions for those receiving out-of-work disability benefits in the UK. *Soc Sci Med*. Aug;162:1-10. doi: 10.1016/j.socscimed.2016.05.042.

OECD (2015) *Fit Mind, Fit Job: From Evidence to Practice in Mental Health and Work*. OECD Publishing, 1–178. <http://doi.org/10.1787/9789264228283-en>

- Consultation with stakeholders – beyond government departments – has not happened due to time constraints and budget sensitivities.

The team recommends MSD and IR monitor the behavioural outcomes of the changes, especially the employment outcomes.

Impact Statement: Increasing main benefit abatement thresholds on 1 April 2021 and consequential adjustments to the Minimum Family Tax Credit

Section 1: General information

1.1 Purpose

Ministry of Social Development (MSD) and Inland Revenue (IR) are solely responsible for the analysis and advice set out in this Regulatory Impact Statement, except as otherwise explicitly indicated.

This analysis and advice have been produced for the purpose of informing final decisions to be taken by Cabinet in relation to increasing the abatement thresholds and consequential adjustments to the Minimum Family Tax Credit (MFTC).

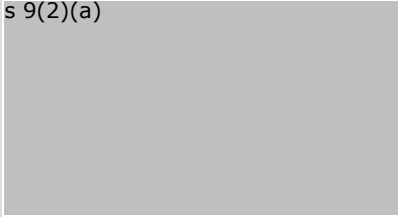

1.2 Key Limitations or Constraints on Analysis

Limitations and constraints on the analysis in this document include:

- The Labour Party committed to increasing the thresholds to \$160 and \$250 per week from 1 April 2021 in its 2020 manifesto commitment. Therefore, other options have been ruled out, such as increasing the thresholds by a different amount, or changes to the abatement rates. (It should be noted that abatement rate changes would also have similar trade-offs that apply, and it would be harder to communicate the changes, which means it would be harder to influence people’s behaviour in the direction intended).
- Other options that have been ruled out due to time constraints include extending a part-time abatement regime to Jobseeker Support on the grounds of a health condition, injury or disability to more closely match their work obligations.
- s 9(2)(f)(iv)
- The modelling results for abatement threshold increases are scaled according to the Pre-election Economic and Fiscal Update 2020 recipient and expenditure forecasts.
- The estimates of the impact of the newly eligible for abatement threshold increases are created based off existing work done in the Integrated Data Infrastructure (IDI). However, there is high uncertainty around these numbers.
- Impacts of abatement threshold increases on Special Needs Grants and recoverable assistance have not been modelled. It is expected that the number of these could modestly decrease, but there is a considerable amount of uncertainty.
- Behavioural impacts (ie, increases in labour market participation or hours worked) have not been modelled as there are various factors that influence a person’s work choices and they are difficult to quantify.

- Analysis in this document has been carried out under tight time constraints.
- No consultation (beyond other Government agencies) has taken place as the proposed increases to the abatement thresholds is a Manifesto commitment and the Government's consideration of the proposed changes in this RIA is Budget Sensitive.

1.3 Responsible Managers:

<p>s 9(2)(a)</p>  <p>Income Support Policy</p> <p>Welfare System and Income Support Policy</p> <p>Ministry of Social Development</p> <p>3 December 2020</p>	<p>s 9(2)(a)</p>  <p>Carolyn Elliott</p> <p>Families and Individuals</p> <p>Policy and Strategy</p> <p>Inland Revenue</p> <p>3 December 2020</p>
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Section 2: Problem definition and objectives

2.1 What is the current state within which action is proposed?

The welfare system is structured to assist those most in need and encourage paid work where possible

New Zealand’s welfare system is designed to target people who are unable to fully support themselves through paid work. Almost all income support in New Zealand is targeted on the basis of family income (and family assets), with the family defined as the nuclear family (i.e. adults and any dependent children). Income and asset tests are determined by a combination of the abatement settings of payments (how fast they are reduced) and the rates of the benefit payments. Generally, the full rate of a payment will be available to people earning up to a certain amount (known as the abatement threshold). Above this amount, payments reduce (abate) as people’s incomes increase.

The welfare overhaul involves a range of changes including changes to abatement thresholds and Working for Families tax credits

The Welfare Expert Advisory Group (WEAG), in its report *Whakamana Tāngata*, proposed a comprehensive package of substantial changes to income support, while broadly maintaining the existing structure of income support. The WEAG package emphasised improving income adequacy and simplifying and rationalising the purpose of particular payments. The WEAG recommended that abatement thresholds for main benefits be increased to \$150 and \$250 per week.

In 2019, Cabinet agreed to overhaul the welfare system to achieve its vision for a system that ensures people have an adequate income and standard of living, are treated with respect, can live in dignity, and are able to participate meaningfully in their communities [CAB-19-MIN-0578 refers]. On 6 November 2019, Cabinet endorsed a high-level short, medium, and long-term work programme to achieve this vision, but did not detail when work would be progressed.

As part of the welfare overhaul work programme, the Government also agreed to a review of Working for Families (WFF) tax credits, including the MFTC.

COVID-19 has caused significant economic disruption in New Zealand

COVID-19 has caused major economic disruption in New Zealand and globally. With great uncertainty in the economy and with extended border closures, unemployment is forecast to rise, peaking at 7.8 percent in the March 2022 quarter.

As a result of the weaker economic outlook, beneficiary numbers are forecast to increase. In October 2020, 369,860 people were receiving a main benefit, at 11.8 percent of the estimated New Zealand working-age population. This is 69,623 more than October 2019. Of the 369,860 receiving a main benefit, 203,371 were Jobseeker Support recipients (6.5 percent of the working-age population), which is 61,241 more than October 2019. The number of people on a benefit is expected to peak in May 2021 at around 443,000, with another peak later in January 2022 reaching around 453,800.

The economic impacts of COVID-19 are expected to disproportionately impact Māori, Pacific people, disabled people (including people with health conditions) and sole parents, who are more likely to be employed in areas affected by job losses and have additional barriers to accessing employment. COVID-19 will certainly increase poverty and hardship rates, although it is too soon to estimate the size of these impacts. The sudden loss of all employment income, or reduced employment income, can tip many families into financial hardship, especially if they have limited cash or near-cash assets to maintain existing commitments (e.g. rent, mortgage and consumer debt).

Government's response to COVID-19

As part of the Government's response to COVID-19, on 1 April 2020, main benefit rates increased by \$25 per week. The Winter Energy Payment (WEP), which is paid from 1 May to 1 October each year, was doubled for the 2020 winter period.

Along with work to minimise hardship for families, the Government has introduced a range of initiatives aimed at boosting employment for those who have lost jobs due to COVID-19.

Labour Party's 2020 manifesto commitment

The Labour Party's 2020 manifesto committed to:

- increase abatement thresholds to \$160 and \$250 per week from 1 April 2021;
- progressively increase the abatement threshold year on year in line with minimum wage increases; and
- continue with the welfare overhaul work and to implement WEAG's recommendations to improve the welfare system.

2.2 What regulatory system(s) are already in place?

Benefit abatement thresholds allow people to work some hours while on benefit

New Zealand's welfare system is designed to assist people who are unable to fully support themselves through paid work. Assistance is targeted through the eligibility criteria⁷ and the benefit abatement regime, which gradually reduces payments that people receive as their other income increases.

Generally, the full rate of payment will be available to people earning up to a certain amount; this is the abatement threshold. Above this amount, payments abate as people's other income increases, but payment can abate in different ways and at different rates based on the type of benefit payment. The abatement rules, along with the benefit rate, determine the benefit cut-out point, which is the amount of income at which a benefit is reduced to zero.

The abatement threshold allows people to work for a small number of hours without having their benefit payment affected and is seen as a way to encourage labour market entry. It is also intended to recognise that there are additional costs associated with work, such as transport costs.

⁷ Social assistance payments are typically means-tested, and eligibility is based on family rather than individual income.

Currently there are two main abatement regimes within the welfare system, which seek to align the financial incentives to work with the level of labour force engagement expected of the individual:

- **a part-time regime** has two abatement thresholds, with a relatively low abatement rate of 30 percent applied at the first threshold, and an abatement rate of 70 percent applied at the second threshold. This is designed to incentivise part-time work and applies to people receiving Sole Parent Support (SPS) and Supported Living Payment (SLP), as well as to those under 65 receiving the Veteran’s Pension (VP). The assumption is that part-time work is often the best option for recipients of these payments.
- **a full-time regime** has a relatively high abatement rate of 70% which is designed to incentivise full-time work. This mainly applies to people on Jobseeker Support (JS)-related benefits, as well as Non-Qualifying Partners (NQP) of New Zealand Superannuation (NZS) and VP recipients. The assumption is that people receiving these benefits are able to undertake full-time work where it is available.

The current abatement thresholds and rates are set out below:

Abatement rate at different thresholds	Current amount beneficiaries can earn per week before their benefit begins to abate
JS (abatement rate of 70%)	\$90
NZS/VP with non-qualifying partner (abatement rate of 70%)	\$115
SPS, SLP and VP (under 65) – Threshold One (abatement rate of 30%)	\$115
SPS, SLP and VP (under 65) – Threshold Two (abatement rate of 70%)	\$215

Under the current settings, a JS recipient would have their benefit reduce by 70 cents for every dollar earned over \$90. For a SPS recipient, their benefit would reduce by 30 cents for every dollar earned over \$115, and by 70 cents for every dollar earned over \$215.

The Minimum Family Tax Credit incentivises families with children to move off benefit and into greater amounts of work

The MFTC is one of the WFF tax credits. The MFTC aims to incentivise families with children (in particular, sole parents) to move off benefit and into greater amounts of paid work⁸ by ensuring people who move from working and receiving a main benefit into working and receiving the MFTC are not financially worse off from doing so. This is done by “topping-up” families’ earned income to a prescribed level (the MFTC threshold) that means they are financially better off by working a greater amount and receiving the MFTC than working and receiving a benefit. This effectively creates a guaranteed income for families, above what they would receive if they were on a benefit. Around 90 percent of MFTC recipients are sole parent families.

⁸ Families with children qualify for the MFTC when they work 20 hours of more per week for sole parents, and 30 hours or more for couples.

The MFTC abates at 100 percent for every dollar earned over the MFTC threshold. This means that for every dollar a family earns over the prescribed amount, their MFTC entitlement reduces by one dollar.

The MFTC threshold, as at 30 November 2020, is \$27,768 per year (after tax). This is \$534 per week. Approximately 3,800 families were paid nearly \$12 million in the 2020/21 tax year. The average MFTC payment amount was \$3,100 per family. IR forecasts that there will be a decrease to approximately 3,200 families in the 2021/22 tax year.⁹

As part of the introduction of WFF, on 26 April 2004, Cabinet agreed to increase the MFTC on 1 April each year by an amount sufficient to ensure that couples do not suffer a reduction in income when moving off benefit into 30 hours of paid work a week, from 1 April 2006 onwards [CAB Min (04) 13/4 refers]. Consequently, the MFTC threshold has been increased each year since 2006 to reflect the latest changes to relevant settings (such as benefit rates, the minimum wage and abatement thresholds).

The MFTC threshold is set by calculating the total income a two-parent family could receive if they were working less than 30 hours and receiving an abated main benefit (the couple rate for Jobseeker Support) and the Winter Energy Payment. This amount is then increased by \$1 and rounded up to the next multiple of \$52 (as expressed for the weeks in the year). Sole parents face the same MFTC threshold as two-parent families. As the sole parent benefit is lower than the couple rate of Jobseeker Support, this means that sole parents gain significantly more than two-parent families by moving onto the MFTC.

Roles of government agencies

The Ministry of Social Development administers and provides information on financial assistance, employment and housing. MSD's role includes paying financial assistance, providing support for getting people into and maintaining employment and housing.

Inland Revenue administers New Zealand's tax system, collecting Crown revenue, as well as collecting and distributing social support programme payments, such as WFF tax credits.

⁹ Some reasons for the decrease in tax year 2021 could be due to the impacts of Covid-19 on employment, or the increase in main benefit payments and temporary doubling of the Winter Energy Payment from 1 April 2020. The latter changes have made the financial incentives to stay on benefit higher.

2.3 What is the policy problem or opportunity?

Abatement thresholds have become out of line with their original settings and offer little financial incentive to enter the labour market or work part-time

Abatement thresholds are increased through one-off changes, rather than being adjusted annually. On 1 April 2020, the abatement thresholds were adjusted through funding secured through Budget 2019. This funding committed to progressively increase the abatement thresholds for main benefits over four years (until 2023, as set out in the below table) in line with minimum wage increases [CAB-19-MIN-0174.36 refers]. The adjustment aimed to ensure that the number of hours a beneficiary could work on minimum wage before abatement began would not reduce any further.

Abatement threshold for:	Prior to April 2020	1 April 2020	1 April 2021	1 April 2022	1 April 2023
Jobseeker Support	\$80	\$90	\$95	\$100	\$105
NZS/VP non-qualifying partner	\$100	\$115	\$120	\$125	\$130
SPS and SLP – Threshold One	\$100	\$115	\$120	\$125	\$130
SPS and SLP – Threshold Two	\$200	\$215	\$220	\$225	\$230

However, prior to the April 2020 adjustment, the last adjustment to main benefit abatement settings occurred in September 2010, when changes were made for recipients of (what was then known as) Domestic Purposes Benefit, Invalid's Benefit, Widow's Benefit as well as for VP (under 65), and NZS and VP with non-qualifying partners. For the full-time abatement regime for JS, the threshold had remained at \$80 since it was last adjusted in 1996.

This has meant that the amount that people could earn before their benefit abated has declined in real terms over time as wages have increased, particularly for JS recipients. For example, a person receiving JS in 1997 could work approximately 11.4 hours on minimum wage (\$7.00 per hour) before their benefit abated. In 2019, a person receiving JS could only work for approximately 4.5 hours on minimum wage (\$17.70 per hour) before their benefit abated. The current settings, despite the adjustments made in April 2020 and subsequent increases set through till 2023, have moved out of line with the original abatement settings and now offer little financial incentive for people to engage in paid work while receiving a main benefit.

The MFTC was not adjusted following COVID-19 related benefit increases

On 1 April 2020, as part of the previous Government's response to COVID-19, main benefit rates were increased by \$25 per week. The Winter Energy Payment was also temporarily doubled for the 2020 winter period.

Under normal circumstances, a consequential increase in the MFTC threshold would likely have been made at the same time. However, the urgent pace at which these benefit changes occurred meant that no decision to change the MFTC threshold was made. This has resulted in the current MFTC threshold being misaligned with the current benefit rate. Under current policy, the MFTC threshold should be increased to account for the increase in benefit rates.

Proposed increases to the abatement thresholds on 1 April 2021 will also require an increase to the MFTC threshold under current policy

Increasing the abatement thresholds on 1 April 2021 (as per the Labour Party's 2020 manifesto commitment) has flow-on implications for the MFTC threshold. Under current policy, a consequential increase to the 2021/22 MFTC threshold would be made to reflect the changes to the abatement thresholds.

If the MFTC threshold does not maintain alignment with the benefit abatement thresholds, this will be inconsistent with the policy intent of the MFTC, that is, to provide a financial incentive to work a greater amount and move off benefit and on to the MFTC. The greater the misalignment of the MFTC threshold and benefits, and the longer the misalignment continues, the greater the impact on the incentives for low income families with children to leave the benefit and work a greater amount and receive the MFTC.

There is also a potential equity issue in that not fully aligning the MFTC threshold financially disadvantages those families who remain off benefit (relative to those who are on benefit). If benefit settings are intended to reflect a minimum level of income for beneficiaries, then implicitly, the guaranteed minimum income provided to working and off-benefit families (via the MFTC) should be at least the same.

The MFTC provides little to no incentive for sole parents to work more than 20 hours a week while receiving the MFTC

The proposed increases to the abatement thresholds on 1 April 2021 are significant, which would require the 2021/22 MFTC threshold adjustment to be much greater than its previous adjustments. This may further exacerbate known issues with the MFTC, mainly that the MFTC provides little to no financial incentive for sole parents to work more than the minimum required hours (20 hours a week) while receiving the MFTC. This is because income earned over the MFTC threshold would reduce the MFTC payment dollar for dollar. This is known as a 100 percent effective marginal tax rate (EMTR); high EMTRs indicate low financial incentives to work.

A significant adjustment to the MFTC threshold would further reward working the minimum number of hours required for the MFTC at the expense of working more than this. This is because the adjustment would mean the income range over which the MFTC is available would be extended, resulting in a larger range of hours worked with a 100 percent EMTR and further reduction in incentives to work greater hours for sole parents on low/minimum wage. For example:

- Fully adjusting the MFTC increases the gain that sole parents receive by moving from working and receiving the benefit to working and receiving the MFTC to around \$125 a week; but reduces the gain from increasing work hours from 20 to 40 hours a week to around \$20 a week.¹⁰
- Partially adjusting the MFTC increases the gain that sole parents receive by moving from working and receiving the benefit to working and receiving the MFTC

¹⁰ This calculation is for a sole-parent family with two children (aged 3 and 5) earning the minimum wage (\$20 per hour) when working, living in Auckland, paying lower quartile rent and receiving the Accommodation Supplement, Temporary Additional Support and relevant tax credits. It does not take into account childcare costs.

to around \$85 a week; but reduces the gain from increasing work hours from 20 to 40 hours a week to around \$60 a week.¹¹

While working 20 hours a week may be desirable for many sole parents due to their caregiving responsibilities and financial incentives being just one of the reasons for labour supply decisions, disincentivising sole parents from working more than 20 hours per week (or taking up higher wage work) may impact on their longer-term labour market trajectories and lifetime earnings. It is important to note that there is also robust evidence to show that the gap between “in work” income and “out of work” income is a stronger driver of behaviour than the incentive to increase work by an additional hour. A significant adjustment in the MFTC would result in a larger gap between “in work” income and “out of work” income (at 20 hours for sole parents and 30 hours for couples) and would potentially provide a stronger financial incentive to go from not working to working the minimum number of hours for the MFTC than partial or no adjustment options.

There is an upcoming review of Working for Families, which includes the MFTC

A review of WFF is planned for 2021, s 9(2)(f)(iv)

This means that any significant adjustments to the current MFTC threshold would likely increase the cost of options for reform. This is largely due to:

- the significant gain that sole parents receive by moving from working and receiving a benefit to working and receiving the MFTC – currently around \$60 a week (for no extra hours of work)
- the likely need to ensure that options for reform do not financially disadvantage low-income working sole parents, as this would be likely to be seen as contrary to the Government’s vision for the welfare system, particularly given its focus on improving income adequacy and reducing child poverty.

s 9(2)(f)(iv)

any significant adjustment to the MFTC threshold would increase the gain that sole parents currently receive by moving onto the MFTC s 9(2)(f)(iv)

¹¹ As above.

¹² Earning minimum wage and therefore, eligible for the maximum amount of the MFTC.

2.4 What do stakeholders think about the problem?

No explicit consultation on these changes beyond Government agencies has taken place

No consultation (beyond other Government agencies) has taken place as the proposed increases to the abatement thresholds is a Manifesto commitment and the Government's consideration of the proposed changes in this RIA is Budget Sensitive.

MSD, IR and the Treasury's views on the adjustments to the MFTC thresholds are set out in Section 5.1.

However, the Welfare Expert Advisory Group informed our analysis

The proposed approach for abatement threshold changes has been informed by the findings of the WEAG, which in turn was informed by the views of stakeholders and those who took part in the engagement process.

The WEAG conducted wide consultation with a variety of groups across New Zealand. This included face to face meetings with more than 1,300 individuals and organisations (such as people receiving welfare payments, employers, service providers, advocates, and community workers), 1,348 written submissions, and additional submissions through online engagement.

In February 2019, the WEAG published its report *Whakamana Tāngata*, which noted that the income support system needs to encourage the outcomes of good and appropriate work by ensuring people are financially better off in paid work.

One element of making work pay is ensuring that abatement settings are reasonable, especially at the point when people are entering work. The WEAG recommended that the abatement thresholds for main benefits be increased to \$150 and \$250 per week.

The WEAG also recommended substantial changes to WFF and other tax credits to improve the adequacy of incomes and returns from paid work for families with children. This included a recommendation to replace the MFTC, In-Work Tax Credit and Independent Earner Tax Credit with a new Earned Income Tax Credit.

2.5 What are the objectives sought in relation to the identified problem?

Three primary objectives to consider are:

- Improve income adequacy for beneficiaries and low-income people
- Improve financial incentives to work
- Pay welfare support at a sustainable cost to government

These objectives should be considered within the overarching government commitment to overhaul the welfare system, in line with the WEAG's recommendations.

Improving income adequacy for beneficiaries and low-income people

Any changes proposed in this RIA should seek to improve income adequacy for low-income people. While the 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 living standards of low-income people, income

adequacy issues are likely to remain for many low-income people. The changes proposed in this RIA should ensure people can receive increased incomes through undertaking paid employment, and keep more of their earnings.

Improving financial incentives to work

Improving financial incentives to work is one component of encouraging people who are able to work to seek employment, alongside other interventions such as active labour market policies. For the majority of people, paid work is a key means of achieving improved wellbeing. For this reason, most income support systems typically aim to ensure that people are financially incentivised to work where this is a possibility.

However, financial incentives are only one of many factors that influence people's decisions on whether to work and how much to work and they are not usually the most important factor. Additionally, different amounts of work may be appropriate for different people given their circumstances.

While the changes proposed in this RIA seek to improve incentives to enter the labour market and to work part-time, the changes also slightly reduce the incentives to work full-time.

Paying welfare 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 RIA 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.

There are significant trade-offs between these three objectives

There are significant trade-offs between these three objectives. It is generally possible to achieve two of the three objectives for any given policy change, but not all three. These three objectives are all important, and any policy will need to balance the trade-offs between these objectives.

Section 3: Option identification

3.1 What options are available to address the problem?

There are two options for abatement threshold increases

Option One – Increase the abatement thresholds to \$160 and \$250 per week on 1 April 2021

This option proposes to increase abatement thresholds to \$160 and \$250 per week from 1 April 2020, as specified in the Labour Party Manifesto 2020. The proposed increases are set out below:

Abatement threshold for:	1 April 2021
Jobseeker Support	\$160
NZS/VP with non-qualifying partner	\$160
SPS and SLP – Threshold One	\$160
SPS and SLP – Threshold Two	\$250

Under this option, beneficiaries will be able to work up to eight hours on minimum wage (based on minimum wage increasing to \$20 per hour on 1 April 2021) before their benefit begins to abate. For recipients of SPS, SLP and VP (under 65), they can work up to 12.5 hours before their benefit begins to abate at the higher rate (Threshold Two).

This would have a fiscal cost to the Government of \$387.496 million in income support payments and \$6.4 million in operating costs over the forecast period.

Option Two – Status quo

This option proposes not to increase abatement thresholds on 1 April 2021, other than the adjustments that have been set to occur for 2021, 2022 and 2023 through funding secured through Budget 2019. This means for the next three years, the abatement thresholds would be adjusted as follows:

Abatement threshold for:	1 April 2021	1 April 2022	1 April 2023
Jobseeker Support	\$95	\$100	\$105
NZS/VP with non-qualifying partner	\$120	\$125	\$130
SPS and SLP – Threshold One	\$120	\$125	\$130
SPS and SLP – Threshold Two	\$220	\$225	\$230

Under this option, the number of hours beneficiaries can currently work up to before their benefit begins to abate (around 4.5 hours on minimum wage) will be maintained (not reduce any further) over the next three years.

There are two options for retrospectively adjusting the Minimum Family Tax Credit threshold

There are two options to consider for retrospective adjustment to the 2020/21 MFTC threshold:

- Option One (status quo) – full retrospective alignment of the 2020/21 MFTC threshold. This is the status quo, as under current policy, the MFTC threshold

would be adjusted in line with changes to benefit rates and abatement thresholds.

- Option Two – no retrospective alignment of the 2020/21 MFTC threshold.

Retrospective adjustment	Detail	Fiscal cost	Number of families affected	Average gain for affected families
Option One – full alignment (status quo)	This would increase the threshold to \$29,432.	\$24.1 million over the forecast period.	Around 3,200 families receiving the MFTC in the 2020/21 tax year would be affected. Around 400 additional families would become newly eligible.	Additional gain of \$32 for each week they receive the MFTC. It is estimated that the average MFTC increase would be \$1,280 per family per year. ¹³
Option Two – no alignment	This would maintain the threshold at \$27,768.	No additional cost.	Around 3,200 families receiving the MFTC in the 2020/21 tax year would continue to receive the same amount of MFTC as currently.	Some families may be better off working and receiving an abated benefit than staying on the MFTC.

There are three options for prospectively adjusting the Minimum Family Tax Credit threshold

There are three options to consider for prospective adjustment to the 2021/22 MFTC threshold:

- Option One (status quo) – full alignment of the 2021/22 MFTC threshold to reflect abatement threshold increases. This is the status quo, as under current policy, the MFTC threshold would be adjusted in line with changes to benefit rates and abatement threshold.
- Option Two – partial alignment of the 2021/22 MFTC threshold.
- Option Three – no adjustment to the MFTC threshold.

¹³ The maximum MFTC increase a family could receive would be \$1,664 (\$32 x 52 weeks). Because newly eligible families will have incomes above the current threshold, the average increase for these families will be less than \$32 dollars a week

Prospective adjustment	Detail	Fiscal cost **	Number of families affected **	Average gain for affected families **
Option One – full alignment (status quo)	This would increase the threshold to \$32,604.	\$51 million over the forecast period.	Around 4,900 families expected to be receiving MFTC in the 2021/22 tax year. Of these, around 1,300 families would be newly eligible for the MFTC.	Additional gain \$61 for each week they receive the MFTC. The maximum possible increase for the year would be \$3,172 per family ¹⁴ .
Option Two – partial alignment	This would increase the threshold to \$30,576.	\$17 million over the forecast period.	Around 4,000 families expected to be receiving the MFTC in the 2021/22 tax year. Of these, around 400 families would be newly eligible for the MFTC.	Additional gain of \$22 for each week they receive the MFTC. The maximum possible increase for the year would be \$1,144 per family ¹⁵ . Two-parent families (10% of the MFTC recipients) would be better off receiving an abated benefit and working than staying on the MFTC.
Option Three – no alignment	This would maintain the threshold at \$29,432 (assuming retrospective change goes ahead).	There may be some working families, who move off the MFTC and on to a benefit (or stay on benefit rather than move onto the MFTC). This would mean reduced MFTC (and In-work Tax Credit) costs, but an increase in benefit costs. These costs have not been quantified and are likely to be small.	Around 3,600 families receiving the MFTC in the 2020/21 tax year would continue to receive the same amount of MFTC as in 2020/21.	Couples (and some sole-parent families) would be better off working and receiving an abated benefit than staying on the MFTC.

** Note that this table assumes the full retrospective alignment for the 2020/21 MFTC threshold, which was agreed by Cabinet on 30 November 2020, has been implemented [CAB-20-MIN-0490 refers].

¹⁴ It is difficult to estimate the number of weeks a family would receive the MFTC on average for a future tax year. The gain would be less for families who do not receive the MFTC for the full year.

¹⁵ As above

3.2 What criteria, in addition to monetary costs and benefits have been used to assess the likely impacts of the options under consideration?

Full assessment of impacts was not completed for abatement threshold increases

As the Labour Party has committed to increasing the abatement thresholds as per Option One, MSD has not undertaken a full assessment of the likely impacts of the options in this RIA.

Criteria for evaluating options for adjusting the Minimum Family Tax Credit

Both the retrospective and prospective alignment options have been evaluated against the following criteria:

- **Work incentives** – the option should ensure the MFTC continues to fulfil its policy objective to financially incentivise low-income families with children to move from working and receiving a benefit to working and receiving the MFTC.
- **Equity** – the option should not financially disadvantage those families receiving the MFTC (ie, in full-time work and off benefit) compared with families who are on benefit.
- **Future reform** – the option should not significantly limit choices for future reform of the MFTC and WFF scheme generally.

3.3 What other options have been ruled out of scope, or not considered, and why?

As the Labour Party has committed to increasing the abatement thresholds as per Option One, MSD has not considered any other options for change, such as increasing the abatement thresholds by different amounts, or changing the abatement rate. Note that changing the abatement rate may be more difficult to influence people's decision to work as it can be harder for people to understand how the changes in the abatement rates affect their payments.

Other options ruled out include possible abatement setting changes for clients on Jobseeker Support on the ground of a health condition, injury or disability (JS-HCD). JS-HCD is available for people assessed as being temporarily unable to work, or able to work only part-time. Therefore, JS-HCD recipients have either part-time or deferred work obligations. However, JS-HCD recipients face the same high abatement rate of 70 percent as other JS clients, aimed at incentivising full-time work, which means current settings may not adequately support JS-HCD recipients to engage in part-time work. Changing the abatement settings for JS-HCD recipients to better support part-time work was ruled out due to time constraints. Further work is required to design and implement any changes in this space to ensure positive outcomes for JS-HCD recipients.

s 9(2)(f)(iv)

Section 4: Impact Analysis

Marginal impact: How does each of the options identified in section 3.1 compare with taking no action under each of the criteria set out in section 3.2?

Adjustment to the Minimum Family Tax Credit - retrospective

	Option One - Full retrospective alignment of the 2020/21 MFTC threshold (status quo)	Option Two - No retrospective alignment of the 2020/21 MFTC threshold
Work incentives	<p style="text-align: center;">0</p> <p>Work incentives for the months remaining in the tax year (up until 1 April 2021) would be maintained.</p> <p>However, any increase delivered by a lump sum at the end of the tax year (to cover April to December 2020) cannot incentivise families to move off benefit after the fact.</p>	<p style="text-align: center;">-</p> <p>The MFTC threshold would not have met its policy intent of making low-income families better off working and receiving the MFTC than working and receiving a benefit.</p>
Equity	<p style="text-align: center;">+</p> <p>Fully aligning the threshold will mean MFTC recipients would be not be disadvantaged compared to working families receiving a benefit.</p> <p>Given the income assistance provided to those on benefit was increased on 1 April 2020 and the MFTC is set relative to the amount of income a beneficiary can receive, MFTC recipients should also be compensated for the increase in assistance to beneficiaries.</p>	<p style="text-align: center;">- -</p> <p>Not aligning the threshold will mean MFTC recipients would be disadvantaged compared to working families receiving a benefit.</p>
Future reform	<p style="text-align: center;">-</p> <p>Increasing the MFTC threshold may make future WFF reform more complex and costly, ^{s 9(2)(f)(iv)} particularly if there is a desire to avoid people being financially disadvantaged.</p>	<p style="text-align: center;">+</p> <p>Not increasing the MFTC threshold would make future WFF reform less complex and costly than Option One.</p>
Overall assessment	<p style="text-align: center;">0</p>	<p style="text-align: center;">-</p>

Adjustment to the Minimum Family Tax Credit - prospective

	Option One - Full alignment of the 2021/22 MFTC threshold to reflect abatement threshold increases (status quo)	Option Two - Partial alignment of the 2021/22 MFTC threshold	Option Three - No adjustment to the MFTC threshold
Work incentives	<p style="text-align: center;">+</p> <p>This option would maintain the original MFTC policy intent of providing low-income families (both sole parent and two-parent families) with a financial incentive to increase work and move off benefit.</p> <p>However, this option would extend the range of income over which families receive the MFTC, thereby reducing the financial incentive for those families to work more hours than the minimum required for the MFTC or earn more income.</p>	<p style="text-align: center;">+</p> <p>This option would maintain the original policy intent of providing low-income families a financial incentive to work and move off benefit. It would be for a slightly smaller group than Option One as only sole parents (who account for approximately 90% of MFTC recipients) would be better off on the MFTC.</p> <p>This would also extend the range of income over which families receive the MFTC, thereby reducing the financial incentive for those families to work more hours than the minimum required for the MFTC or earn more income. However, this would be less than Option One.</p>	<p style="text-align: center;">- -</p> <p>This option would significantly diminish the original MFTC policy intent of providing low-income families a financial incentive to increase work and move off benefit.</p>
Equity	<p style="text-align: center;">+</p> <p>Fully aligning the threshold will mean MFTC recipients (both sole parent and two-parent families) would be not be disadvantaged compared to working families receiving a benefit.</p>	<p style="text-align: center;">+</p> <p>Sole parents, who account for approximately 90% of MFTC recipients, would remain better off on the MFTC.</p> <p>However, some of the remaining 10% families receiving the MFTC may be financially better off working and receiving a benefit than working and receiving the MFTC.</p>	<p style="text-align: center;">- -</p> <p>Not aligning the threshold will mean some MFTC recipients would be better off working and receiving a benefit than working and receiving the MFTC. An important goal of the welfare system is to enable people to fully support themselves through paid work where this is appropriate.</p>
Future reform	<p style="text-align: center;">-</p> <p>Increasing the MFTC threshold may make future WFF reform more complex and costly, particularly if there is a desire to</p>	<p style="text-align: center;">-</p> <p>Partially increasing the MFTC threshold may make future WFF reform complex and costly; a partial alignment means families would gain around \$85 a week moving from working and</p>	<p style="text-align: center;">+</p> <p>With no alignment (ie, 2020/21 threshold of \$29,432 maintained for 2021/22), families would gain around \$60 a week moving from working and receiving a benefit, to working and receiving</p>

	<p>avoid people being financially disadvantaged. A full alignment means families would gain around \$125 a week moving from working and receiving a benefit, to working and receiving the MFTC. § 9(2)(f)(iv)</p>	<p>receiving a benefit, to working and receiving the MFTC. § 9(2)(f)(iv)</p> <p>However, this would be less costly and complex than Option One.</p>	<p>the MFTC. Therefore, non-alignment of the MFTC threshold is likely to make future WFF reforms less complex and costly than Options One and Two.</p>
Overall assessment	+	+	-

Key:

- ++ much better than doing nothing/the status quo
- + better than doing nothing/the status quo
- 0 about the same as doing nothing/the status quo
- worse than doing nothing/the status quo
- much worse than doing nothing/the status quo

Section 5: Conclusions

5.1 What option, or combination of options is likely to best address the problem, meet the policy objectives and deliver the highest net benefits?

Option One is the preferred option for abatement threshold increases

The proposed option for abatement threshold increase is Option One as it means the thresholds will better align with the original abatement settings (as well as WEAG’s recommendation), which enabled beneficiaries to work for longer hours before abatement occurred. This option will allow working beneficiaries to keep a greater proportion of their earnings before their benefit is affected, thereby improving income adequacy and financial incentives to work part-time while on a benefit.

This option may reduce the financial incentive for beneficiaries working part time to move into full time work. However, better incentivising beneficiaries to enter the labour market and maintain work, even if part-time work, is important. This is particularly so for those already disadvantaged in the labour market prior to COVID-19, such as sole parents and people with health conditions, injury or disability, for whom suitable work may only be part-time work.

Paid work can not only lift incomes and living standards, it can also enable people to experience better self-assessed health, life satisfaction and social connectedness. Part-time work can also provide a pathway to full-time work by providing opportunities to connect with the labour market, gain work experience and become familiar with the demands that can come with employment. Also, given the economic impacts of COVID-19 and many people facing reduced hours, this option ensures that those on low incomes with reduced hours can access financial assistance while still being attached to their job.

No consultation (beyond other Government agencies) has taken place as this change is a Manifesto commitment (and the Government’s consideration of it is Budget Sensitive).

Option One is the preferred option by IR for retrospectively adjusting the Minimum Family Tax Credit

Option One is the preferred option by IR, and is the proposed option in the Cabinet paper. MSD does not have a preferred option. Note that Cabinet agreed to adjust the 2020/21 MFTC threshold as per Option One on 30 November 2020 [CAB-20-MIN-0490].

This option means the financial incentive provided by the MFTC for families with children to move off benefit and into greater amounts of work would be maintained for the remainder of the 2020/21 tax year. While the increase cannot incentivise families with children to move off benefit for the period of the 2020/21 tax year that has already passed (April to December 2020), it addresses the potential equity issues, whereby those families who remained off benefit and in work during April to December 2020 are financially disadvantaged relative to those who were on benefit.

MSD and IR have different preferred options for prospectively adjusting the Minimum Family Tax Credit

Option Two is the preferred option by MSD, and is the proposed option in the Cabinet paper.

This option ensures that around 90% of MFTC recipients (ie, sole parents) would remain better off working and receiving the MFTC than working and receiving a benefit. While a partial increase would extend the income range over which the MFTC is available, resulting in reduced financial incentives to work greater hours for sole parents on low-incomes, the impact would be smaller than Option One. MSD considers fully aligning the MFTC threshold would increase the cost and complexity of any future WFF review s 9(2)(f)(iv) particularly if there is a desire to avoid people being financially disadvantaged. However, these effects will be less under Option One than Option Two.

IR's preferred option is Option One. While the fiscal cost of full alignment are greater than under other options, this option maintains the work incentives provided by the MFTC by ensuring low-income families with children (both sole parents and two-parent families) are better off working and receiving the MFTC than working and receiving a benefit.

IR does not consider the potential effects of aligning the MFTC threshold on any future WFF review to be a significant enough issue to warrant removing the work incentives currently provided by the MFTC.

IR considers that there is a potential equity issue if the MFTC threshold is not fully aligned. Less than full alignment potentially disadvantages those families who remain in work and off benefit, relative to those in work and receiving a benefit. If benefit settings are intended to reflect a minimum level of income for beneficiaries, then implicitly, the guaranteed minimum income provided to working and off-benefit families (via the MFTC) should be at least the same.

In advice to Ministers, the Treasury recommended the no prospective alignment option due to the tight fiscal environment. The Treasury also did not consider that the policy decision [to align the MFTC threshold with benefit rates] meets the threshold to be progressed as a Budget pre-commitment. While the Treasury acknowledged that it was likely to introduce greater complexity for clients, the Treasury did not agree that these adverse effects were sufficient to justify funding the initiative ahead of the Budget process given the tight fiscal environment. s 9(2)(f)(iv)

5.2 Summary table of costs and benefits of the preferred approach

Affected parties (identify)	Comment: nature of cost or benefit (eg, ongoing, one-off), evidence and assumption (eg, compliance rates), risks	Impact \$m present value where appropriate, for monetised impacts; high, medium or low for non-monetised impacts	Evidence certainty (High, medium or low)
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Abatement threshold increases

Additional costs of proposed approach compared to taking no action

Monetised cost to Crown	Increase in Benefit or Related Expenses from increasing	\$387.496 million over five years.	High
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	abatement thresholds to \$160 and \$250 per week on 1 April 2021 (one-off increase, no further increases in subsequent years).		
	Cost of MSD implementing the abatement threshold increases (IT, additional staff, training, communications etc).	\$6.4 million (one-off cost).	High
Low-income working individuals and families receiving main benefits	Reduction in financial incentive to work full-time.	Low to moderate impact: Increasing abatement thresholds will reduce the Effective Marginal Tax Rate (EMTR) for those below it, but will extend the range of incomes above it that experience high EMTRs (ie, low financial incentive to work).	Medium
	Some may be financially disadvantaged as a result of the abatement threshold increases: <ul style="list-style-type: none"> - Some people will lose their TAS disability exception as they move off the TAS upper limit and become ineligible for the DA exception - Some may face a reduction in the hourly Childcare Assistance subsidy rate as a result of abatement threshold increases if they become newly eligible for AS or their AS payment increases. 	Low to moderate impact: Around 79 individuals and families are expected to lose an average of \$19 a week.	Medium
Total Monetised Cost	Implementation and alterations to the operating model and the ongoing increase in benefit payments due to higher abatement thresholds.	\$393.896 million over five years.	

Non-monetised costs	<p>Following adjustment to the new abatement thresholds, there will be:</p> <ul style="list-style-type: none"> - a small number of people financially disadvantaged - a reduction in financial incentive to work full-time - additional work for case workers as more people become eligible for main benefits or AS. 	Moderate impact.	
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Abatement threshold increases

Expected benefits of proposed approach compared to taking no action

<p>Low-income working individuals and families receiving main benefits, non-beneficiaries receiving the AS, people newly eligible for benefits as a result of the changes</p>	<p>Incomes will increase as a result of changes to abatement thresholds.</p> <p>*This may, as a result, make housing more affordable for some (low to moderate impact).</p>	<p>Moderate to high impact:</p> <p>Around 82,900 individuals and families are expected to benefit by on average \$18 per week. Of these, around 15,500 are Māori families and 5,100 are Pacific families.</p> <p>Around 50,300 non-beneficiaries receiving AS are expected to benefit with an average gain of \$12*.</p> <p>Around 7,000 newly eligible people could take up a main benefit, while around 4,000 people could take up AS as a result of the changes.</p>	Medium
<p>Low-income working individuals and families</p>	<p>Improved financial incentives to work, particularly part-time which will increase incomes.</p>	<p>Moderate impact:</p> <p>Around 29,500 individuals and families currently receiving a main</p>	Medium

receiving main benefits		benefit are expected to benefit with an average weekly gain of \$29. Around 3,100 individuals and families receiving NZS are expected to benefit with an average weekly gain of \$21.	
Clients with children, including SPS recipients	Reductions in child poverty as families with children are able to work more hours before their benefits are abated.	Low to moderate impact: Around 50,200 families with children will benefit. It is estimated that the abatement thresholds will reduce child poverty by around 6,000 (+/- 3,000) on the AHC50 fixed line measure and 2,000 (+/- 3,000) on the BHC50 measure in 2021/22.	Medium
Total Monetised Benefit	No costings of monetised benefits.	N/A	
Non-monetised benefits	Improves financial incentive to work part-time and income adequacy for low-income individuals and families.	Moderate impact.	

Adjustment to the Minimum Family Tax Credit – retrospective (full alignment)

Additional costs of proposed approach

Monetised cost to Crown	Cost of adjusting the 2020/21 MFTC threshold (retrospective).	\$4.6 million in the 2020/21 tax year, \$24.1 million over	High
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		the forecast period. ¹⁶	
Low-income working individuals and families receiving the MFTC	<p>Some families may not gain as much when they receive a lump sum payment for the 2020/21 tax year that has already past (April to December 2020):</p> <ul style="list-style-type: none"> - A lump sum payment could lead to debts for some people as the MFTC is chargeable income for some types of financial assistance paid under the Social Security Act 2018 - The MFTC is assessable income for Public Housing purposes, for assessing eligibility and calculating the rate of Income Related Rent. 	Low impact.	Medium
Total Monetised Cost		\$4.6 million in the 2020/21 tax year, \$24.1 million over the forecast period.	
Non-monetised costs	Some families may be financially disadvantaged due to a lump sum payment for the retrospective increase.	Moderate impact.	

Adjustment to the Minimum Family Tax Credit – retrospective (full alignment)

Expected benefits of proposed approach

Low-income working individuals and families receiving the MFTC, and newly eligible	<p>Incomes will increase as a result of retrospective increase.</p> <p>Improved financial incentives to work and receive the MFTC compared to working and receiving a benefit.</p>	Moderate impact: Around 3,200 families receiving the MFTC in the 2020/21 tax year would gain an additional \$32 for each week they	Medium
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¹⁶ The fiscal cost is ongoing as the MFTC rate will also account for the April 2020 main benefit rate increase in prospective changes.

		<p>received the MFTC.</p> <p>The maximum possible increase for the year would be \$1,664 with an estimated average MFTC increase of \$1,280 per family.¹⁷</p> <p>Around 400 additional families would become newly eligible for the MFTC in the 2020/21 tax year.</p>	
Total Monetised Benefit	No costings of monetised benefits.	N/A	
Non-monetised benefits	Improves financial incentive to work part-time and improves income adequacy for low-income individuals and families.	Moderate impact.	

Adjustment to the Minimum Family Tax Credit – prospective (partial alignment)

Additional costs of proposed approach

Monetised cost to Crown	Cost of adjusting the 2021/22 MFTC threshold (prospective).	<p>\$17 million over the forecast period (assuming retrospective adjustment goes ahead).</p> <p>(This is \$34 million less than Option One).</p>	High
Two-parent families on the MFTC	Reduced incentive to be in work and on the MFTC than working and receiving a benefit as some two-parent families may be financially better off working and receiving benefit.	<p>Low impact:</p> <p>Around 10 percent of MFTC recipients are two-parent families.</p>	Medium

¹⁷ The newly eligible customers have incomes above the current threshold so the average gain for these customers will be less than \$32 dollars a week.

Sole-parent families on the MFTC	Reduced incentive for sole-parent families to work more hours than the minimum required to qualify for the MFTC.	Moderate impact.	Medium
Total Monetised Cost		\$17 million over the forecast period (assuming retrospective adjustment goes ahead).	
Non-monetised costs	For some families there may be reduced incentives to: <ul style="list-style-type: none"> - be working and receiving the MFTC than working and receiving a benefit - work greater hours than the minimum required. 	Moderate impact.	

Adjustment to the Minimum Family Tax Credit – prospective (partial alignment)

Expected benefits of proposed approach

Low-income families on the MFTC	<p>Incomes will increase as a result of partial increase.</p> <p>Improved financial incentives to work and receive the MFTC compared to working and receiving a benefit.</p>	<p>Moderate impact:</p> <p>Around 4,000 families are expected to receive the MFTC in the 2021/22 tax year. Of these, around 400 families would be newly eligible to the MFTC.</p> <p>These families would gain an additional \$22 for each week they receive the MFTC.</p> <p>This would be a maximum annual MFTC increase of \$1,144 per family.¹⁸</p>	Medium
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¹⁸ The gain would be less for families that do not receive the MFTC for the full year.

Total Monetised Benefit	No costings of the total monetised benefits.	N/A	
Non-monetised benefits	Improves financial incentive to work and receive the MFTC and improves income adequacy for low-income individuals and families.	Moderate impact.	

5.3 What other impacts is this approach likely to have?

Better incentivising beneficiaries to engage in work through abatement threshold increases could also lead to positive impact on broader wellbeing, as being in suitable work is good for people's health and wellbeing (provided the work is safe, stable, suits people's circumstances and financially beneficial).

The expected benefits described in section 5.2 will depend on the interaction between different assistance types, the extent to which people undertake further work and the subsequent impact on their earned incomes. Also, there is a risk that the gains will be lost over time if abatement thresholds do not increase in future years.

Section 6: Implementation and operation

6.1 How will the new arrangements work in practice?

The Manifesto commitment specified an implementation date of 1 April 2021 for abatement threshold increases.

Legislative vehicle

Changes to abatement thresholds require an Order in Council and regulation amendment. Abatement thresholds for main benefits and New Zealand Superannuation Non-Qualifying Partner are set out in Schedule 2 of the Social Security Act 2018. An Order in Council under section 452(2)(c) of the Social Security Act 2018 is required to make the abatement threshold increases for main benefits and NZS for April 2021.

Abatement thresholds for Veteran's Pension Non-Qualifying Partner and Veteran's Pension (under 65) are set out separately in regulation 42A of the Veterans' Support Regulations 2014, which will also require amendment.

Changes to the MFTC threshold can be made by an Order in Council as set out in sections ME 1(4) and MF 7(1)(d) of the Income Tax Act 2007. However, an Order in Council is required by 1 December for changes to apply from 1 April the following year.

Therefore, adjustments to the 2020/21 and 2021/22 MFTC thresholds would need to be made via amendments to the Income Tax 2007.

Communication

A communications plan will be developed to ensure the changes are communicated to staff and the public in advance of implementation.

Transitional arrangements

A Transitional Assistance Payment (TAP), which is a temporary non-taxable payment, could be considered for the small number of people (around 79 people) who may be financially disadvantaged by the proposed abatement threshold increases on 1 April 2021.

6.2 What are the implementation risks?

Minimal implementation risks with the abatement threshold increases

Implementation risks for abatement thresholds are minimal. The changes will use existing administrative structures and will not require any new service design.

There is a potential for public confusion around the proposed increases, as this proposal overrides the four-year adjustments to the abatement thresholds secured through Budget 2019. A communications plan will be developed to ensure sufficient information is provided to both staff and the public through various platforms, including MSD's website.

Some implementation risks with the adjustments to Minimum Family Tax Credit

A partial increase to the 2021/22 MFTC threshold may cause confusion with some people as to which option they would be better off under. Some two-parent families may be better off working and receiving benefit than working and receiving the MFTC, but for one reason

or another remain on the MFTC and receive less than what they may be entitled to. Material will be developed to ensure sufficient information about the MFTC adjustments are available to both staff and the public through various platforms, including IR's website.

Section 7: Monitoring, evaluation and review

7.1 How will the impact of the new arrangements be monitored?

Behavioural changes arising from abatement threshold increases can be monitored using administrative data

MSD will be able to use administrative data to monitor the trends in declared income before and after changes to abatement thresholds, including the trends for different subgroups (eg, Māori, Pacific people, sole parents, people with a health condition or disability).

An expected trend following the abatement threshold changes would be an increase in the level of income that clients declare to MSD, as a result of clients taking up extra work in response to the changes. There may also be a signalling effect (ie, changed behaviour) ahead of the changes.

Behavioural changes arising from adjustments to the Minimum Family Tax Credit can be monitored using administrative data

The effects of the MFTC threshold alignments can be monitored using data IR currently collects as part of administering the MFTC. This includes the number of MFTC recipients, the nature of those families, the amount of MFTC payments made, and MFTC recipient movement between the MFTC and the benefit. This administrative data will show what effect the MFTC alignment changes have on the up take of the credit, and the actual fiscal cost to the Government of the chosen settings.

7.2 When and how will the new arrangements be reviewed?

As part of the Welfare Overhaul work programme, MSD is working on developing a measure of a client's total income, and regularly reporting on this measure. Progression of this work will allow for reporting on this measure past 2021. The measure will allow MSD to analyse the longer term impact of this policy on client outcomes.

In December 2020, officials intend to provide advice to joint Ministers on a potential scope for a work programme to review WFF, which includes the MFTC. ^{s 9(2)(f)(iv)}

The WFF review is part of the broader welfare overhaul work programme and is expected to take at least 12 months. Any changes to WFF through legislative amendment would take even longer to implement.

It is noted that, subject to any change in Government policy on the alignment of the MFTC threshold to future changes to benefit rates or abatement settings, further reviews of the MFTC threshold will be required annually.