

# The Treasury

## Budget 2011 Information Release

### Release Document

June 2011

[www.treasury.govt.nz/publications/informationreleases/budget/2011](http://www.treasury.govt.nz/publications/informationreleases/budget/2011)

Key to sections of the Official Information Act 1982 under which information has been withheld.

Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

- [1] 9(2)(a) - to protect the privacy of natural persons, including deceased people
- [2] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials
- [3] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions
- [4] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information or who is the subject of the information
- [5] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage
- [6] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice
- [7] 6(a) - to prevent prejudice to the security or defence of New Zealand or the international relations of the government
- [8] 9(2)(h) - to maintain legal professional privilege
- [9] 6(c) - to prevent prejudice to the maintenance of the law, including the prevention, investigation, and detection of offences, and the right to a fair trial
- [10] 9(2)(d) - to avoid prejudice to the substantial economic interests of New Zealand
- [11] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice.

Where information has been withheld, a numbered reference to the applicable section of the Official Information Act has been made, as listed above. For example, an [8] appearing where information has been withheld in a release document refers to section 9(2)(h).

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

Date: 31 January 2011

SH-3-2-4-6



**THE TREASURY**

Kaitohutohu Kaupapa Rawa

To: Minister of Finance

## **AIDE MEMOIRE: WORKING FOR FAMILIES - OPTIONS FOR BUDGET 2011**

This Aide Memoire briefs you in advance of your meeting with the Minister for Social Development and Employment and the Minister of Revenue on Wednesday 2 February at 8am to discuss options for reforming the Working for Families (WFF) scheme.

In November 2010 Treasury provided you advice on ways to de-index WFF without affecting lower income earners, and advice on the feasibility of making broader changes to the scheme [T2010/2353 refers]. Following feedback on that report and a subsequent meeting with you, we have further narrowed down the options in that paper.

The revised set of options are presented in a set of A3 sheets, which contain a high level description of each option and a summary of the analysis. They are structured in a similar way to those presented to you for the Budget 2010 tax package. Accompanying those A3s is a paper containing supporting analysis of the options.

A high level description of the five options (and the variations under each) is as follows:

### ***Option 1: Change the Indexation of the Family Tax Credit (FTC)***

- a) Remove automatic indexation of FTC rates with future decisions on an ad hoc basis by Ministers during the annual budget process.
- b) Continue to index the FTC but only for lower income earners shifting the abatement threshold to avoid a cliff-face.
- c) Remove the indexation of the FTC but pay beneficiaries a child allowance (paid weekly) to compensate them for their loss in purchasing power.

### ***Option 2: Increase the abatement rate***

- a) Increase the universal abatement rate from the current abatement threshold of \$36,827 to either: 22.5%, 25%, or 30%.
- b) Increase the abatement rate of the In-work Tax Credit only to either: 25% or 30%.

### ***Option 3: Simplify the Family Tax Credit payment schedule***

- This option simplifies the FTC payment schedule by removing the higher rates for teenagers (i.e. having one rate for the first child and one rate for subsequent children).

### ***Option 4: Change the In-work Tax Credit (IWTC) to individual child rates***

- a) Change the IWTC to \$15 per child per week.
- b) Change the IWTC to \$20 per child per week for the first three children, then \$15 per week thereafter.

### **Option 5: Lower the abatement threshold from \$36,827**

- a) Lower the abatement threshold from \$36,827 to \$30,000.
- b) Lower the abatement threshold from \$36,827 to \$25,000.

These options have been analysed using five criteria:

- **Fiscal cost** – Impact on the cost to the Crown;
- **Targeting considerations** – Whether the option alters the allocation of funding toward lower income earners;
- **Equity considerations** – Consideration of aggregate poverty measures and changes in disposable income (i.e. winner/loser analysis);
- **Affect on work incentives and efficiency** – Does each option alter incentives to enter paid employment and/or work more hours; and
- **Administrative simplicity and public compliance.**

These five criteria are described in further detail in the supporting materials paper.

### **Treasury Comment**

The options above present a range of ways to alter the scheme to generate fiscal savings, but that also seek to minimise impacts on low income and beneficiary families. With each option, however, there are trade-offs that need to be considered including: reducing incentives to work; decreasing both real and nominal disposable income; and increasing the administrative complexity of the scheme. The options are designed so that the targeting of the funding is either improved or is unchanged. Note that none of the options are expected to result in any measurable increase in income poverty or income inequality measures.

In Treasury's view removing the automatic indexation of the Family Tax Credit (Option 1A) would be a good way to generate fiscal savings without affecting incentives to work or reducing nominal disposable incomes. Ministers could then decide to increase the FTC rates during the annual budget process and assess future spending on the FTC against other priorities [3]

However, if rates were not increased periodically, over time this would impact on the income adequacy of lower income earners and child poverty rates could be expected to increase.

As Option 1A affects low income earners over time, Options 1B and 1C are designed to generate fiscal savings (up to \$183m and \$184m per annum respectively), but also compensate lower income earners for their loss of purchasing power. While they add complexity to the system, combining these options with simplifying the payment schedule (Option 3) would be one way to minimise any implementation and compliance costs.

If larger fiscal savings were desirable, then we would recommend increases in the abatement rate (Option 2), which generates fiscal savings ranging from \$90m to \$380m per annum. Option 2 also better targets the scheme to lower income earners removing assistance for those on the highest incomes and also avoids affecting anyone below

the abatement threshold. The main drawback with Option 2, however, is that every family above the abatement threshold will have their disposable income reduced.

Working for Families is a policy with significant fiscal cost (almost \$3 billion per annum), but one where there is little evidence of its cost effectiveness or value for money. It is still our view that more work, in addition to this process, is required to find out whether the substantial fiscal cost could be better spent on other policies that achieve that same objectives.

### **Process**

All these options could be announced at Budget 2011 with a likely implementation date of 1 April 2012. Note that an implementation date any earlier than this (e.g. 1 October 2011) would significantly increase implementation costs. At your meeting this week we will be seeking your feedback as to which options you would like us to develop further. We would then seek formal decisions from joint Ministers in mid March with decisions from Cabinet required in April when finalising the 2011 budget package.

[1] Analyst, Workforce Attachment and Skills, [1]  
**Simon MacPherson**, Manager, Workforce Attachment and Skills [1]