

The Treasury

Budget 2015 Information Release

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Reference: T2014/2197

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Date: 12 December 2014

To: Minister of Finance (Hon Bill English)

Deadline: 15 December 2014

Points for meeting on children in material hardship

You are meeting with the Prime Minister and Ministers Tolley, Bennett and Joyce on Monday 15 December to discuss the children in material hardship package for Budget 2015. This aide memoire has been written to accompany the report that you have received from the Department of Prime Minister and Cabinet (DPMC) for this meeting.

We have been involved in the preparation of the report and we agree with the options presented, and the general advice provided.

We would specifically highlight the following points for your discussion on Monday:

- **Targeting the Family Tax Credit (FTC) to younger children:** Our first-best advice for the centrepiece of the package is to target the FTC to younger children (aged 0-2 years), given the importance of these early years for cognitive development (which severe material hardship may affect) and the consistency with work obligations in the benefit system. However, we agree that if this is not a feasible option because of concerns about the lack of coverage of the families in material hardship, and the drop in income once a child turns 3, then this option should be dropped from further work.
- **Framing and centrepiece:** The decisions around the content of the package, and particularly around the centrepiece, are finely balanced, and fundamentally depend on the weighting of the two key objectives to reduce severe material hardship and preserve work incentives. Options to preserve work incentives will necessarily involve greater 'spill over' to families who are less likely to be in severe material hardship.
- **Benefit and In-Work Tax Credit centrepiece – Package 1:** The benefit increase would be relatively targeted to families in severe material hardship. The increase to the In-Work Tax Credit (IWTC) is much less targeted. If this option is chosen as the centrepiece of the package, we would be keen to explore options within this that would increase the targeting of the IWTC, consider its interaction with the Minimum Family Tax Credit (MFTC) and potentially address some of the problems with the MFTC. This package, with both the IWTC and a childcare

option focused on low to middle income earners, is more weighted towards working families. This has good coverage of the families in material hardship, but 'spill over' to families not in material hardship.

- **Accommodation supplement centrepiece – Package 2:** On balance, we slightly prefer this option as a centrepiece. This is driven by the evidence that there are increasing levels of housing stress and low residual incomes, particularly among beneficiaries, and the better targeting of this option to families in material hardship. If the cost of the package needs to be reduced, we recommend prioritising AS increases targeted to families with children over regional increases that also provide greater support to households without children.
- We recognise that there are risks with this option overall, particularly around landlord capture. However we believe that the risk will be smaller for options that are targeted at a narrower range of households (i.e. families with children), than if additional AS is provided on the basis of location. The smaller size of this centrepiece, particularly if the regional AS components are not included, mean that a larger childcare option could fit within the package.
- **Benefits and smaller accommodation supplement centrepiece – Package 3:** This package is the most weighted towards beneficiary families. If the cost of the package needs to be reduced, a lower increase in benefit could be considered (\$20 per week rather than the current \$25 per week increase). Or a lower increase in benefit could be traded-off for a more substantial package on childcare, to balance the impact of the benefit increase on work incentives.
- **Other options for the package and interaction with the centrepiece:** We recommend that childcare and other costs options are included as part of the package. Both of these work-streams contain scalable options, so their interaction with the centrepiece and their relative priority are important. On childcare, we recommend increasing support for both working families and those on a benefit, with some of the cost offset by reducing eligibility for higher-income households.
- Substantially increasing support for other costs (hardship assistance) could be detrimental to work incentives given the 'cliff-face' of assistance disappearing at very low incomes. We recommend continuing to consider increases in assistance for families with newborns and school-aged children, and accommodation costs. We do not recommend continuation of work on increased assistance for transport or dental costs, particularly given their high costs (totalling around \$25 million per year) relative to options with, in our view, higher priority (childcare and smaller AS options).
- **Budget 2015 context and caveat on costs estimates:** As you know, Budget 2015 will be challenging, and decisions here will impact on other areas where there are significant pressures. It is important to note that the current cost

estimates do not include departmental costs for IT and staffing, or any estimate of increased take-up, which depending on the package of options chosen could be more or less significant. Officials will provide operational costs, and estimates of increased take-up rates, for consideration as part of the next phase of work. This package, proposing immediate additional income support to families in severe material hardship, is part of a broader work programme to improve social outcomes for disadvantaged families, including the social investment budget.

[9]

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