

# The Treasury

## Budget 2017 Information Release

### Release Document July 2017

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[38]	to enable the Crown to negotiate without disadvantage or prejudice	9(2)(j)
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[40]	Not in scope	

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## Treasury Report: Final decisions - Family Incomes Package and Budget Package

<b>Date:</b>	28 April 2017	<b>Report No:</b>	T2017/1120
		<b>File Number:</b>	SH-13-5-2-3

### Action Sought

	Action Sought	Deadline
Prime Minister (Rt Hon Bill English)	<b>Note</b> the contents <b>Agree</b> to the recommendations	Monday, 1 May 2017
Minister of Finance (Hon Steven Joyce)	<b>Note</b> the contents <b>Agree</b> to the recommendations	Monday, 1 May 2017
Associate Minister of Finance (Hon Simon Bridges)	<b>Note</b> the contents <b>Agree</b> to the recommendations	Monday, 1 May 2017
Associate Minister of Finance (Hon Amy Adams)	<b>Note</b> the contents <b>Agree</b> to the recommendations	Monday, 1 May 2017

### Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
[34]	Analyst, Tax Strategy	[39]	[23]
Dr Eina Wong	Senior Analyst, Tax Strategy	[39]	[23]
Kamlesh Patel	Team Leader, Budget Coordination	[39]	[23]

### Actions for the Minister's Office Staff (if required)

**Return** the signed report to Treasury.

Note any feedback on the quality of the report

**Enclosure:** No

## Treasury Report: Final decisions - Family Incomes Package and Budget Package

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### Executive Summary

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This report seeks your agreement on final decisions for the Budget 2017 packages:

- an adjustment to the Family Incomes Package by increasing the Accommodation Benefit for students.
- [33]
- an increase to EQC levy rates.

Each decision has a fiscal impact. Fiscal impacts can be incorporated in the final fiscal forecasts if a decision is made by Monday, 1 May 2017.

#### ***Accommodation Benefit***

We have previously reported on options for changes to the Accommodation Benefit (T2017/1091 refers). We understand the preference is for Option B: increasing the maximum payment by \$20 per week to \$60.

[33]

[33]

#### ***EQC levy***

Cabinet are likely to make decisions on increasing EQC levy rates in late May. The Minister of Finance and the Treasury recommend that EQC's current premiums levied from residential property owners are increased to ensure that the EQC scheme remains financially viable and that premiums charged should reflect the cost of the perils EQC covers, including the cost of administering the scheme and arranging reinsurance.

According to detailed research by the EQC, the "break-even" premium for EQC is estimated at 23 cents per \$100 of cover, compared to the current rate of 15 cents per \$100 of cover. The increase equates to a \$2.12 per week increase for most home owners. The previous increase on 1 February 2012 equated to a \$2.65 per week increase for most home owners.

## Recommended Action

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We recommend that you:

### **Accommodation Benefit**

- a **agree** to increase the maximum weekly Accommodation Benefit by \$20 per week from 1 April 2018;

<i>Agree/disagree</i> Prime Minister	<i>Agree/disagree</i> Minister of Finance	<i>Agree/disagree</i> Associate Minister of Finance (Hon Bridges)	<i>Agree/disagree</i> Associate Minister of Finance (Hon Adams)
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- b **approve** the following changes to appropriations to give effect to the decision in recommendation a above, with a corresponding impact on the operating balance;

Vote Social Development Minister for Social Development	\$m – increase/(decrease)			
	2017/18	2018/19	2019/20	2020/21 & outyears
Benefit or Related Expense: Student Allowances	6.3	19.5	19.5	19.8

<i>Approve</i> Prime Minister	<i>Approve</i> Minister of Finance	<i>Approve</i> Associate Minister of Finance (Hon Bridges)	<i>Approve</i> Associate Minister of Finance (Hon Adams)
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- c **direct** the Ministry of Social Development to draft the Order in Council required to change Schedule 3 of the Student Allowances Regulations 1998;

<i>Directed</i> Prime Minister	<i>Directed</i> Minister of Finance	<i>Directed</i> Associate Minister of Finance (Hon Bridges)	<i>Directed</i> Associate Minister of Finance (Hon Adams)
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[33]

**EQC levy**

n **agree** to in principle to increase EQC levy rates to 23 cents per \$100 of cover;

<i>Agree/disagree</i>	<i>Agree/disagree</i>	<i>Agree/disagree</i>	<i>Agree/disagree</i>
Prime Minister	Minister of Finance	Associate Minister of Finance (Hon Bridges)	Associate Minister of Finance (Hon Adams)

o **note** the fiscal impacts of recommendation k above will be reflected in the final fiscal forecasts for Budget 2017 due to be completed on 3 May 2017;

p **note** that the proposed increase in EQC levy rates are expected to have the following impact on the operating balance; and

	<b>\$m – increase/(decrease)</b>				
	<b>2016/17</b>	<b>2017/18</b>	<b>2018/19</b>	<b>2019/20</b>	<b>2020/21</b>
Operating Balance	-	43.000	147.000	148.000	150.000

q **note** Cabinet are likely to make final decisions on levy rates in late May and the intention is to announce the increase at Budget or shortly after.

Dr Eina Wong  
**Senior Analyst**  
**Tax Strategy**

Kamlesh Patel  
**Team Leader**  
**Budget Coordination**

Rt Hon Bill English  
**Prime Minister**

Steven Joyce  
**Minister of Finance**

Hon Simon Bridges  
**Associate Minister of Finance**

Hon Amy Adams  
**Associate Minister of Finance**

## Treasury Report: Final decisions - Family Incomes Package and Budget Package

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### Purpose of Report

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1. This report seeks your agreement on final decisions for the Budget 2017 packages:
  - an adjustment to the Family Incomes Package by increasing the Accommodation Benefit for students.
  - [33]
  - an increase to EQC levy changes.
2. Each decision has a fiscal impact. Fiscal impacts can be incorporated in the final fiscal forecasts if a decision is made by Monday, 1 May 2017.

### Family Incomes Package – Accommodation benefit

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#### Background

3. On Tuesday 18 April 2017, Cabinet authorised Budget Ministers, in consultation with the Minister for Social Development, to investigate an adjustment to the Family Incomes Package for students with high accommodation costs, to be included in the final fiscal forecasts (CAB-17-MIN-0184 refers).

#### Structure of housing subsidies for students

4. The Accommodation Benefit (AB) is paid as a supplement to student allowance recipients. A student allowance recipient is entitled to a flat payment that varies by the region in which they live.
5. Students who do not meet the financial criteria for the student allowance – and so are ineligible for AB – are also ineligible for the Accommodation Supplement (AS). However, students who do not qualify for the student allowance for non-financial reasons may qualify for AS. Non-financial reasons include postgraduate study and exceeding the maximum number of weeks in receipt of the allowance.
6. Sole parent students receive the AB at a rate equivalent to the AS and will benefit from the AS component of the Family Incomes Package. For other students, AB subsidises 50 per cent of the average room rent in the region above \$40 up to a maximum of \$40.<sup>1</sup> For example, in a region where the average room rent is \$100, the AB rate in that region is \$30. In contrast, AS subsidises 70 per cent of the recipient's total accommodation costs above the entry threshold, up to the applicable maxima for the area.
7. In 2015, around 51,000 students received AB, and around 12,000 received AS. Around 170,000 students eligible to receive a student loan do not receive either AB or AS.

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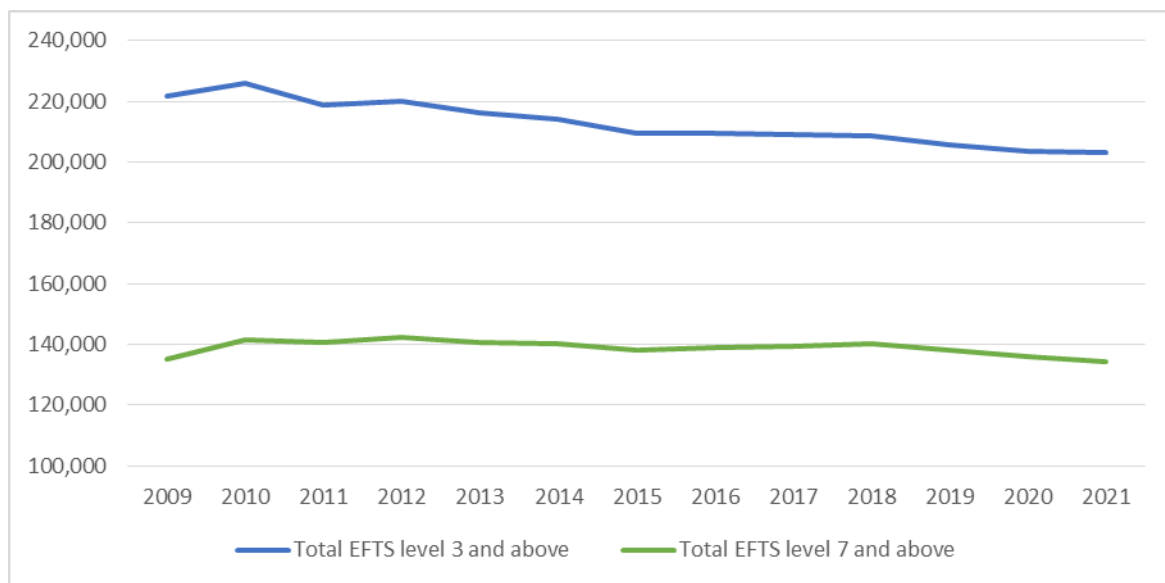
<sup>1</sup> The formula for calculating the AB rate is: (regional average room rental - \$40)/2, up to a maximum of \$40. In our previous report, the formula was incorrectly specified (T2017/1091 refers).

These students are unlikely to gain from the Family Incomes Package (assuming they have no income above \$14,000).

### Trends in student support

8. Enrolments at level 7 and above (for example, bachelor's degrees or above) have been relatively static since 2009, and enrolments at level 3 and above (for example, certificates or diplomas) have declined slightly from 2009. Both are projected to decline slightly to 2021. Macroeconomic conditions (employment and incomes) have also improved in recent years, meaning that fewer students are eligible for targeted income support through Student Allowance.
9. All else equal, the volume of students accessing housing subsidies could be expected to decline over the medium term. However, increases in housing costs may see increases in the average subsidy per student. Figure 1 below shows total EFTS since 2009 and forecast EFTS to 2021, while Figure 2 shows the annual percentage change.

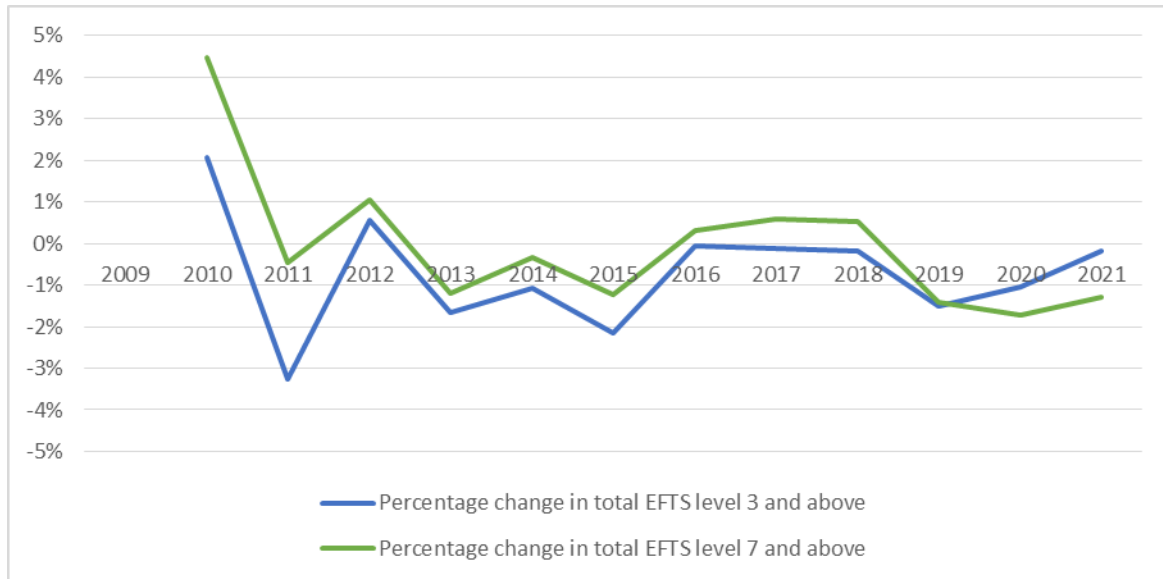
Figure 1: Total EFTS 2009 - 2021



Source: Ministry of Education



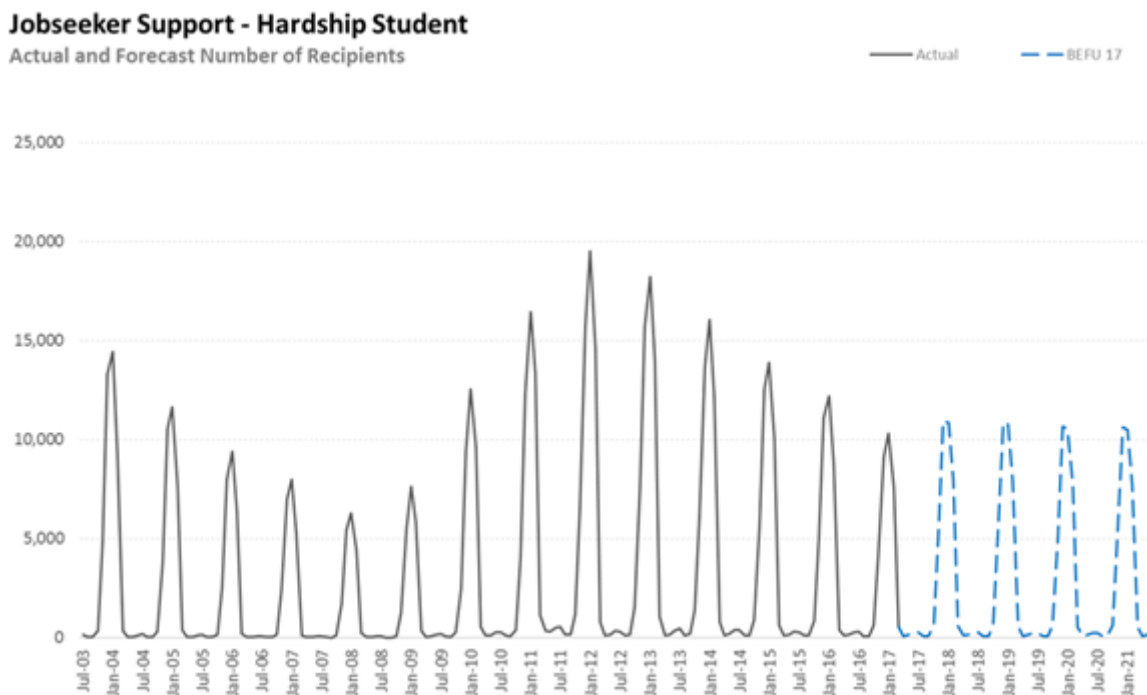
Figure 2: Percentage change in total EFTS 2009-2021



Source: Ministry of Education

10. Reliable data about student hardship during the year are not available. However, students in financial hardship during study breaks can access Jobseeker Support Student Hardship. This provides a weekly payment to help with living costs during study breaks of more than three weeks.
11. Jobseeker Support Student Hardship grants are highly seasonal and predominantly accessed over the summer period. The number of grants will most closely reflect the number of students eligible for the student allowance and labour market conditions, but may provide a loose proxy for hardship during the year. Figure 3 below provides the number of recipients.

Figure 3: Trends in Jobseeker Support – Student Hardship 2003 - 2021



Source: Ministry of Social Development

## Options

12. We have previously reported on options for changes to the Accommodation Benefit (T2017/1091 refers). We understand the preference is for Option B: increasing the maximum payment by \$20 per week to \$60 from 1 April 2018. This would benefit around 45,000 students.
13. Table 1 below shows AB rates based on 2017 rents. AB rates are calculated based on average rents, and increases in average rents for areas not at the maxima will flow through to the payment rates.

Table 1: Accommodation Benefit rates based on 2017 rents

Region	Current Rates (\$) based on 2017 rents	Proposed Option B (\$)
Auckland	40.00	60.00
Wellington	40.00	60.00
Christchurch	40.00	60.00
Dunedin	40.00	51.00
Hamilton	40.00	49.50
New Plymouth	40.00	52.50
Napier	40.00	46.50
Nelson	40.00	51.50
Whangarei	40.00	43.50
Palmerston North	40.00	40.50
Whanganui	27.00	27.00
Invercargill	26.50	26.50
Rotorua	39.50	39.50
Gisborne	40.00	40.00
Greymouth	40.00	42.00

14. The fiscal cost of this option is presented in Table 2 below.

Table 2: Fiscal cost of increasing Accommodation Benefit maximum by \$20 per week

Vote Social Development Minister for Social Development	\$m – increase/(decrease)			
	2017/18	2018/19	2019/20	2020/21 & outyears
Benefit or Related Expense: Student Allowances	6.3	19.5	19.5	19.8

[33]



## EQC levy increase

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### Key reasons for the proposal to increase the EQC levy

28. Cabinet are likely to make decisions on increasing EQC levy rates in late May. The Minister of Finance and the Treasury recommend that EQC's current premiums levied from residential property owners are increased to ensure that the EQC scheme remains financially viable and that premiums charged should reflect the cost of the perils EQC covers, including the cost of administering the scheme and arranging reinsurance.
29. Prior to the Canterbury earthquakes, more than \$6b in funds had accumulated within the Natural Disaster Fund (NDF), complementing EQC's reinsurance programme by providing capital for EQC to meet its obligations, including its reinsurance deductible. The Canterbury earthquakes are expected to substantially exhaust the NDF, reducing EQC's financial resilience and effectively placing the Crown on risk for supporting EQC.
30. Based at current premium settings, EQC's current financial forecasts suggest that even in the absence of any significant natural hazard event such as the recent Kaikoura earthquake, it will take more than three decades before the NDF reaches EQC's current reinsurance deductible of \$1.75b. This is because the current EQC premium is below the "break-even" point for the expected costs of the hazards covered by the EQC Act and the cost of administering the scheme, including the cost of EQC's reinsurance programme.
31. According to detailed research by the EQC, the "break-even" premium for EQC is estimated at 23 cents per \$100 of cover, compared to the current rate of 15 cents per \$100 of cover. In addition, analysis of New Zealand and international evidence commissioned by EQC in 2016, suggests that modest increases in residential insurance prices such as the "break-even" premium for EQC would result in relatively small decreases (less than 1%) in the demand for residential insurance.
32. Pricing EQC premiums at the "break-even" rate would, in the absence of any significant natural hazard events, mean that the NDF would reach EQC's current reinsurance deductible of \$1.75b in around 10 years.

33. The increase equates to a \$2.12 per week increase for most home owners. The previous increase on 1 February 2012 equated to a \$2.65 per week increase for most home owners.
34. Accordingly it is recommended that the current EQC levy be increased to 23 cents per \$100 of cover.

### **Proposed timing and expected financial impact**

35. The Minister of Finance and the Treasury recommend the proposed increase is announced as part of Budget 2017 or shortly after with an effective date of 1 November 2017. The previous increase was announced on 11 October 2011 and was effective from 1 February 2012.
36. The expected financial impact of the proposed increase is reflected in Table 4.

Table 4: Expected financial impact of EQC levy increase

<b>Financial impact on</b>	<b>Fiscal Year 2017/18</b>	<b>Fiscal Year 2018/19</b>	<b>Fiscal Year 2019/20</b>	<b>Fiscal Year 2020/21</b>
Operating Balance	+\$43m	+\$147m	+\$148m	+\$150
Total Crown cash flows	+\$70m	+\$160m	+\$162m	+\$163m
Core Crown net debt	No impact	No impact	No impact	No impact

37. The table above assumes no significant natural disaster events.
38. The cash flow impact is higher than the operating balance impact as EQC's customers normally prepay insurance premiums (via annual contracts).
39. There is no direct impact on core Crown net debt as the extra levy revenue is assumed to be used to rebuild the NDF. This would in effect mean that the EQC can rebuild assets to be used to fund current claims and any future disaster before requiring future support from the Crown. Therefore the additional cash received by EQC would reduce the probability or the amount of a call on Crown guarantee facility.

### **Issues impacting on future EQC levy rates**

40. The proposed EQC levy increase to 23 cents does not specifically take into account any cover cap changes (from the current cap of \$100,000 for buildings and \$20,000 for contents) or other changes that may arise from the EQC Act Review process. The new/amended EQC Act if enacted will only become operative in 2020 and the final outcome is still uncertain at this stage. In addition, the Treasury's view is that the EQC levy should be reviewed regularly and thus a levy review once the EQC Act has been amended would be a normal course of action. It is also worth considering that in 2020 expected natural hazard risks as well as reinsurance industry conditions could be very different from today and this may also impact on the adequacy of the levy setting.
41. The Treasury is engaging with the EQC on an integrated Risk Financing Framework which incorporates the Crown's risk appetite, levy settings and reinsurance cover. This integrated Risk Financing Framework will be implemented as part of the EQC fiscal 2018/19 reinsurance programme and will be a factor in future levy reviews.

## Next steps

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### ***Accommodation Benefit***

42. Changes to the AB rates in Schedule 3 of the Student Allowances Regulations 1998 can be implemented by Order in Council. This can be drafted for Ministers' consideration alongside the Accommodation Supplement changes.

### ***EQC levy increase***

43. The Treasury will be providing a paper for EGI in May seeking Cabinet agreement to the future design of EQC land and building cover.