46 The table below provides a summary of the estimated reduction in children in poverty on the BHC50 measure for different combinations of options, compared with the status quo.

Option	Reduction in child poverty compared to status quo			
	2019/20	2020/21	2021/22	2022/23
s 9(2)(f)(iv) [redacted]				
Wage indexation of benefits	0	0	0	-5,000
s 9(2)(f)(iv) [redacted]				

47 Modelling is not currently available on the AHC50 or material hardship measure, which significantly constrains our ability to compare the impact of different options. [redacted] s 9(2)(f)(iv) [redacted]

48 s 9(2)(f)(iv) [redacted]

4. Key Considerations with Indexation

Wage indexation may make it more costly for Government to shift underlying policy settings

49 In recent decades, successive Governments have often used income support packages to ‘catch up’ levels of financial support and adjust the underlying policy settings at the same time. Wage indexation would make it more expensive for the Government to adjust real relativities between different parts of the social assistance system.

50 A related disadvantage of wage indexation is that other factors are also relevant to setting social assistance thresholds. In particular, benefit-wage relativities are important both in maintaining financial incentives to work and, over the longer term, in determining equitable standards of living for beneficiaries compared with other groups in society.

s 9(2)(f)(iv) [redacted]

51 s 9(2)(f)(iv) [redacted]

Compared to the status quo, indexation will carry a significant fiscal cost

52 Officials have costed a series of indexation options, including both the budget forecast period and over a 10 year time horizon. As this shows, over time the difference between wage growth and inflation accumulates, and means that the fiscal costs will grow significantly outside of the budget forecast period.

53 The table below shows the fiscal costs for various options over the budget forecast period, assuming an implementation date of 1 April 2020. These are provisional estimates only and would likely change as the costs are refined.

	Fiscal Cost (per year)			
Option	2020/21	2021/22	2022/23	2028/29
1: Wage indexation of working age benefits	$50m	$100m	$130m	$0.7b

s 9(2)(f)(iv) [redacted]

54 s 9(2)(f)(iv) [redacted]

s 9(2)(f)(iv) [redacted]

55 s 9(2)(f)(iv) [redacted]

- [redacted]
- [redacted]

56 s 9(2)(f)(iv) [redacted]

s 9(2)(f)(iv) [redacted]

A note on the reliability of TAWA modelling in this report

57 This advice uses the Treasury's TAWA Model to estimate both fiscal costs and the impact on poverty on before-housing-cost measures. The Treasury considers:

- the fiscal costs to have medium reliability and moderate risk.
- the low-income poverty estimates to have low reliability and moderate risk.

58 Access to the anonymised data used in this advice was provided by Statistics NZ in accordance with security and confidentiality provisions of the Statistics Act 1975 and secrecy provisions of the Tax Administration Act 1994. Statistics NZ confidentiality protocols were applied to the data sourced from MSD. The results in this paper have been confidentialised to protect individual persons, households, businesses and organisations from identification. The results presented in this study are the work of the Treasury, not Statistics NZ.

Next steps

59 As noted earlier, the WEAG has recommended that the Government index all income support payments and thresholds annually to movements in average wages and that AS maxima are indexed to movements in housing costs.

60 Please indicate if you would like to submit a late Budget bid now for indexation of any current payments which are not proposed for major redesign by the WEAG. s 9(2)(f)(iv) [redacted]

- wage indexation of main benefit rates and/or
- s 9(2)(f)(iv) [redacted]
- [redacted]

61 If you wish to proceed with a late bid, we can provide a joint report with advice on implications of such changes - this would seek agreement from the Ministers responsible for the relevant payments, as well as provide a draft letter to the Minister of Finance informing him of the late bid.

62 s 9(2)(f)(iv) [redacted]

Appendix One: Summary of Indexation Settings

63 It is useful to consider indexation settings in the context of the three tiers of social assistance for beneficiaries.

- a first tier of working age benefits intended to provide an income to meet the general cost of living;
- a second tier of additional assistance for specific on-going costs, such as accommodation, disability and children; and
- a third tier of targeted assistance that is generally provided in relation to presenting hardship, and available only for costs considered 'essential'.

First tier of assistance

64 Rates of main benefits have a legislative requirement to be adjusted annually on 1 April by the rate of upwards movement in the CPI. The CPI measures the change in price of goods and services acquired by New Zealand households. The inflation adjustment has occurred every year since the early 1990s.

Second tier of assistance

65 Second tier assistance refers to additional assistance to people for specific on-going costs, such as accommodation, disability and the direct costs of children. A number of supplementary payment rates are adjusted each year according to movements in the CPI (this is mostly done by convention, as there is no legislative requirement). This includes payment rates of Disability Allowance and Childcare Assistance.

66 There are some notable exceptions in indexation settings of payment rates of second tier assistance:

- While the level of rent is part of the formula used to determine the amount provided, maximum rates of AS are not indexed regularly. The maxima were updated using 2016 rental costs on 1 April 2018 as part of the Families Package.
- The Family Tax Credit and Best Start payment rates have a legislative requirement to be adjusted when the cumulative CPI increase is 5 percent or more. With recent low inflation, the Family Tax Credit has not met the cumulative 5 percent threshold since 2012. Instead, an ad-hoc increase was made to rates as part of the Families Package.
- The newly introduced Winter Energy Payment is not inflation adjusted. As part of the Families Package, Ministers agreed not to index the Winter Energy Payment and to consider its indexation arrangements as part of a wider review of indexation settings.

67 There are two Working for Families payments that are for families with children who do not receive a main benefit and who work a minimum number of hours a week (20 hours for sole parents and 30 hours for couples).

- The IWTC is not indexed to the CPI and is required by legislation to be reviewed every three years. The rate was last increased (from $60 a week to $72.50 a week) in Budget 2015 as part of the Child Material Hardship package.
- The MFTC is not explicitly indexed, but as the MFTC ensures paid employment remains financially more attractive than being on a benefit – the payment rates tends to increase as benefits are indexed to inflation.

Third tier of assistance

68 Third tier assistance is tightly income and cash asset tested. It is generally provided to people in financial hardship, and available only for costs considered essential. While Temporary Additional Support payment is comprehensively inflation indexed, one-off hardship payment amounts are not.

69 One-off hardship payments generally have a maximum amount depending on the costs claimed. These maximums can be exceeded, but generally only in exceptional

circumstances. These cost categories (e.g. food, bedding) are not indexed, and have not been increased for some time.

Income and asset thresholds

70 Across the various tiers of assistance in the welfare system, there are various thresholds and limits that relate to income and assets. While most are regularly indexed for inflation by convention, some are not, including:

- AS cash asset levels (last adjusted 1988)
- Emergency Benefit/Hardship Benefits cash asset levels (last adjusted 1990)
- Abatement thresholds for main benefits (Jobseeker Support was last adjusted in 1996, while other abatement thresholds were increased in 2010)
- Childcare Assistance income thresholds (in 2010 Cabinet agreed that these thresholds would no longer be adjusted by movements in the CPI [CAB Min (10) 7/8 refers])
- Working for Families abatement thresholds (an ad-hoc adjustment was made on 1 July 2018 as part of the Families Package). As part of the Families Package, Ministers noted that the indexation of Working for Families abatement parameters would be considered as part of a wider review of the indexation of social assistance payments.

Appendix Two: The Household Living-Costs Price Index (HLPIs)

71 The Household Living-Costs Price Indexes (HLPIs) were introduced by Stats NZ in October 2016, with a historical series created going back to 2008. The HLPIs are an alternate inflation measure to the CPI that could be used to index social assistance payments and thresholds. The HLPIs provide greater insight into inflation experienced by the following household groups.

- beneficiaries
- superannuitants
- Māori
- income quintiles (five groups)
- expenditure quintiles (five groups)
- all households.

72 In addition to measuring inflation experienced by different household groups, the conceptual design of the HLPIs differs from the CPI in two important ways. The HLPIs:

- include interest payments (this includes interest payments on all consumer debt such as mortgage debt, car loans and credit cards)
- better reflect inflation experienced by a typical household.

73 The inclusion of interest payments on consumer debt better aligns with the inflation experiences of households, in particular owner-occupied households. The CPI excludes interest payments because of the CPI's principal purpose to inform monetary policy. Including interest payments in the CPI would introduce an unintended circular flow (i.e. increasing the Official Cash Rate would generally result in higher interest payments and therefore flow through to a higher CPI).

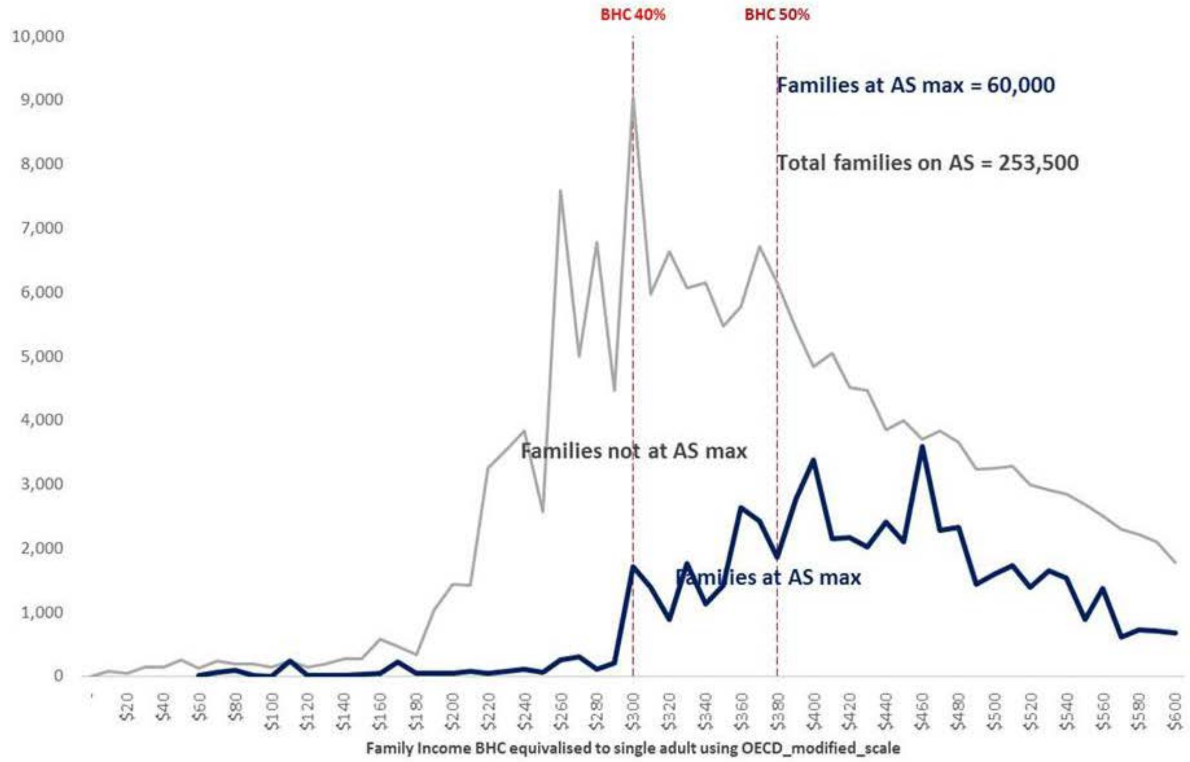
74 By treating each household equally, in terms of their influence on the expenditure items included, the HLPIs are more appropriate than the CPI for understanding inflation experienced by typical household groups. The CPI calculates inflation based on households overall (i.e. all New Zealand households are treated as one super household) and therefore higher spending households have a greater influence on the expenditure items. The approach used for the CPI is more suitable for informing monetary policy.

75 The HLPIs are more appropriate to use to index payments and thresholds as the methodology used to derive the HLPIs has been designed for indexation purposes. Adjustments would also more accurately reflect actual cost pressures faced by different household groups. For example, benefit rates could be indexed by the 'beneficiary HLPI', while NZS/VP payment rates could be indexed by the 'superannuitant HLPI' (although this is not likely to impact rates of NZS due to the wage adjustment requirement). The 'all households' HLPI could be used to adjust payments received by household groups not specifically covered by the HLPIs, such as Working for Families and Student Allowances.

76 While the HLPIs may more appropriately reflect changes in the cost of living for low-income households, their use for indexation purposes are unlikely to significantly affect the living standards of low-income households.

Appendix Three: income distribution for all families vs families at maxima

Before-housing-cost income distribution for MSD clients receiving AS



After-housing-cost income distribution for MSD clients receiving AS