

The Treasury

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[40]	Not in scope	

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Joint Report: Transitional Assistance Fund for Family Incomes Package

Date:	21 April 2017	Report No:	T2017/1092
		File Number:	SH-13-5-2-3

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Steven Joyce)	Note the contents Agree to the recommendations	Friday, 28 April 2017
Associate Minister of Finance (Hon Simon Bridges)	Note the contents	Friday, 28 April 2017
Associate Minister of Finance (Hon Amy Adams)	Note the contents	Friday, 28 April 2017
Minister for Social Development (Hon Anne Tolley)	Note the contents Agree to the recommendations	Friday, 28 April 2017

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
Dr Eina Wong	Senior Analyst, Tax Strategy, The Treasury	[39] [23]	✓
Simon MacPherson	Deputy Chief Executive, Policy, Ministry of Social Development	[39] N/A (mob)	

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

Joint Report: Transitional Assistance Fund for Family Incomes Package

Executive Summary

While the Family Incomes Package will provide significant benefits to more than 1.3 million New Zealand families, some individuals and families are likely to be financially disadvantaged by the package as a result of the interactions between different forms of assistance within the tax and transfer system.

Most recent estimates suggest that approximately 3,000 individuals or families across four distinct groups are likely to be financially disadvantaged by the package:

- Approximately 1,630 Ministry of Social Development (MSD) clients are expected to lose a maximum of \$3 per week from an increase to the Accommodation Supplement (AS) entry thresholds;
- Approximately 180 MSD clients are expected to lose less than \$1 per week from interactions between the AS and Temporary Additional Support (TAS);
- Approximately 75 MSD clients are expected to lose an average of \$7 per week across the package as a whole where these clients lose eligibility to the TAS disability allowance exception and benefits from other parts of the package do not outweigh these losses; and
- Approximately 1,120 Inland Revenue (IRD) clients are expected to lose an average of \$1.70 per week as a result of interactions between the Family Tax Credit (FTC) and the tax system with approximately 120 of these clients losing more than \$3 per week.

Every April, the Annual General Adjustment (AGA) results in changes to the amount of assistance many MSD clients receive. The 2018 AGA will take effect on 1 April 2018 and is likely to offset some of the small decreases people may see from this package (e.g., someone losing \$2 or \$3 per week from the package may end up being compensated for this through an increase to benefit or NZ Super rates from the AGA).

On 18 April 2017 Cabinet agreed that a Transitional Assistance fund be established to compensate those who are financially disadvantaged as an unidentified consequence of the net effects of the package.

Officials recommend that those eligible for the Transitional Assistance fund should include:

- Those MSD clients who lose eligibility to their TAS disability allowance exception and, as a result, are financially disadvantaged across the whole package (average payment of \$7 per week for 75 clients); and
- Individuals and families who are financially disadvantaged as a result of the package by more than \$3 per week but whose particular circumstances have not yet been identified.

Inland Revenue does not recommend providing compensation to the group that are financially disadvantaged from interactions between the FTC and the tax system given that the group losing more than \$3 per week is small (approximately 120 families), with relatively high household incomes of above \$76,000 per annum. The absolute maximum loss for a

single family would be \$15 per week and more than 40% of these losses would have occurred in 2019 in any case under the existing Working for Families legislative settings.

Subject to agreement to the recommendations in this paper, MSD will draft a Ministerial Welfare Programme for the Minister for Social Development to authorise to compensate those individuals and families who meet the agreed parameters of the Transitional Assistance Fund.

The estimated numbers of those financially disadvantaged in this paper will change as the implementation date approaches and the base data used for the estimates changes. It is also important to note that current estimates have been based on a comparison of 1 April 2018 under current policy settings with 1 April 2018 with the policy changes from the Family Incomes Package implemented. As we move forward, officials will model the expected change in income from 31 March 2017 to 1 April 2018 which will account for other changes expected to happen on 1 April 2018, such as the Annual General Adjustment as well as the Family Incomes Package policy changes.

Recommended Action

We recommend that you:

- a **Note** that on 18 April 2017, Cabinet agreed to a Family Incomes Package as part of Budget 2017 to provide better rewards for hard work, help lower income families with young children meet their living costs, simplify the tax system, and improve incomes for those with high housing costs.
- b **Note** that Cabinet agreed that a financial assistance payment should be made available to Ministry of Social Development clients who are financially disadvantaged as an unidentified consequence of the net effects of this package, and authorised the Minister of Finance and Minister for Social Development to agree the parameters of the financial assistance payment.
- c **Note** that approximately 3,000 families and individuals across four groups have been identified so far as being likely to be financially disadvantaged by the Family Incomes Package:
 - i. Approximately 1,630 Ministry of Social Development clients are expected to lose a maximum of \$3 per week from an increase to the Accommodation Supplement entry thresholds.
 - ii. Approximately 180 Ministry of Social Development clients are expected to lose less than \$1 per week from interactions between the Accommodation Supplement and Temporary Additional Support.
 - iii. Approximately 75 Ministry of Social Development clients are expected to lose an average of \$7 per week across the package as a whole where these clients lose eligibility to the TAS disability allowance exception and benefits from other parts of the package do not outweigh these losses.
 - iv. Approximately 1,120 IRD clients are expected to lose an average of \$1.70 per week as a result of interactions between the FTC and the tax system with approximately 120 of these clients losing more than \$3 per week.
- d **Agree** that the following groups should not be compensated:
 - i. Those who are expected to lose less than \$3 per week from an increase to the Accommodation Supplement entry thresholds or interactions between the Accommodation Supplement and Temporary Additional Support; and

Agreed/Not agreed

Minister of Finance

Agreed/Not agreed

Minister for Social Development

- ii. Those losing out solely from interactions between the FTC and the tax system.

Agreed/Not agreed

Minister of Finance

Agreed/Not agreed

Minister for Social Development

- e **Agree** that the following groups should be eligible for support from the Transitional Assistance Fund:
 - i. The estimated 75 clients who are expected to lose eligibility to the Temporary Additional Support disability allowance exception and as a consequence will be

financially disadvantaged across the whole package by an average of \$7 per week; and

Agreed/Not agreed

Minister of Finance

Agreed/Not agreed

Minister for Social Development

- ii. Individuals and families who are financially disadvantaged as a result of the package by more than \$3 per week but whose particular circumstances have not yet been identified.

Agreed/Not agreed

Minister of Finance

Agreed/Not agreed

Minister for Social Development

- f **Agree** that the Transitional Fund should provide assistance until the client notifies MSD of a change in circumstances that results in any change to the level of assistance they are eligible for or until a period of 24 months has elapsed.

Agreed/Not agreed

Minister of Finance

Agreed/Not agreed

Minister for Social Development

- g **Note** that, subject to agreement to recommendations 4, 5 and 6, the Ministry of Social Development will draft a Ministerial Welfare Programme for the Minister for Social Development to approve which will provide the authority and parameters for the Transitional Assistance Fund.
- h **Note** that the Ministry of Social Development, the Treasury and Inland Revenue will work together to provide regular updates to the Minister of Finance and the Minister for Social Development on the estimates of the number of individuals and families who are likely to be financially disadvantaged by the package.

- i [33]

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Joint Report: Transitional Assistance Fund for Family Incomes Package

Purpose

1. This report seeks agreement to the parameters of the Transitional Assistance Fund to be established to compensate those who are financially disadvantaged by the Budget 2017 Family Incomes Package.

Background

2. The Family Incomes package which was agreed by Cabinet on 18 April 2017:
 - a increases the \$14,000 income tax threshold to \$22,000, and the \$48,000 threshold to \$52,000;
 - b aligns the Family Tax Credit (FTC) rates for young children to those for children aged 16 to 18, increases the abatement rate to 25% and reduces the abatement threshold to \$35,000;
 - c removes the Independent Earner Tax Credit; and
 - d increases the Accommodation Supplement (AS) maxima to reflect 2016 rents, while re-allocating locations into different AS areas to reflect rental costs.
3. While more than 1.3 million New Zealand families will benefit financially from the package, interactions between different types of assistance means that a small number of families and individuals are likely to be financially disadvantaged.
4. On 18 April 2017 Cabinet agreed that a financial assistance payment should be made available for Ministry of Social Development clients who are financially disadvantaged as an unidentified consequence of the net effects of the package. Cabinet also authorised the Minister of Finance and Minister for Social Development to agree the parameters of the financial assistance payment.

Defining those who are financially disadvantaged by the package

Financially disadvantaged means those whose estimated income on 1 April 2018 is less than it was on 31 March 2018...

5. It is important to define the term 'financially disadvantaged' in the context of the Budget package. Consistent with the approach taken to compensating those who were financially disadvantaged by the Child Material Hardship package, officials propose to define financially disadvantaged as:

Those individuals or families whose estimated net income on 1 April 2018 (the day of implementation) is lower than their estimated net income on 31 March 2018 (the day before implementation).

6. Estimating the impacts of the package is difficult because of the different types of assistance included (for example, tax credits are generally calculated on an annual basis and are only confirmed at the end of the financial year while AS is paid on a

weekly basis throughout the year). Officials considered using an estimate of individual or family income over the entire year (1 April 2018 to 1 April 2019) to calculate the impact of the package. However, this approach would introduce significant additional uncertainty and complexity (e.g. many individuals and families undergo changes in circumstances throughout the year which would be difficult to estimate accurately).

7. Another alternative would be to conduct a retrospective calculation at the end of the financial year once the annual income for the individual and family was known and any tax credits had been paid. This approach was discounted because of the time delay involved.
8. The recommended approach is to identify those individuals and families most likely to be negatively affected at the point of implementation of the package and make compensation available to those who meet the parameters of the transitional assistance fund.

...once all elements of the package have been considered.

9. Another consideration is whether the calculation of financial disadvantage should include all elements of the package across Inland Revenue (IRD) and the Ministry of Social Development (MSD) or whether the calculation should apply separately to assistance provided by each agency. For example, should somebody who sees a minor reduction in assistance from MSD (because of a small reduction to their AS resulting from a rise to the AS entry threshold) but sees a bigger reduction in income tax paid to IRD be considered to be financially disadvantaged by the package?
10. Officials recommend considering all elements of the package together so that people are only considered to be financially disadvantaged if they are worse off once all elements of the package (and any flow-ons) have been taken into account. Again this follows the approach taken in previous tax and transfer packages.
11. As officials recommend defining financially disadvantaged as those who are worse off at the time the package comes into effect on 1 April 2018, those who have losses solely due to the tax aspects of the package would not be considered as financially disadvantaged. Actual losses would not be known at that time and estimates of annual income will be speculative. However, when considering the losses arising from the AS changes, any estimated gains from the weekly increase in FTC or reduction in tax payable could be taken into account.

Overview of those likely to lose out from the package

12. Officials have modelled the expected impacts of the package and identified those who are most likely to be financially disadvantaged. It is important to note that these figures are only estimates which will change over time as the base data used to make them is updated. Final figures about those who will be financially disadvantaged will depend on a range of factors including the level of take-up of available assistance and the extent to which people provide full information to the relevant agency.
13. Four distinct groups comprising approximately 3,000 individuals and families have so far been identified as those who are most likely to be financially disadvantaged by the package once all of the changes have been considered. There are other individuals and families who may face a small loss in one particular form of assistance but where this loss is more than outweighed by other changes across the package.
14. The four groups who are expected to be financially disadvantaged across the whole package are:
 - a **Group One – AS entry threshold increase:** Approximately 1,630 MSD clients with children aged 16-18 are expected to lose a maximum of \$3 per week as a result of an increase to the AS entry threshold caused by the FTC changes. This group will

not benefit from the FTC changes because of the age of their children and any benefits from other parts of the package are not sufficient to outweigh the increase to the AS entry threshold.

- b **Group Two – Reduction in Temporary Additional Support (TAS):** Approximately 180 MSD clients are expected to lose a maximum of \$1 from a reduction in TAS that marginally outweighs their increased AS (caused by the fact that MSD does not pay TAS for amounts that are less than \$1).
- c **Group Three: Loss of TAS disability allowance exception:** Approximately 75 MSD clients are expected to lose their TAS disability allowance exception as a result of any increase to assessable income including AS, FTC, NZ Super and earnings after tax. The TAS disability allowance exception allows for 30% of total excess disability costs to be paid if the clients' disability costs exceed the TAS upper limit. These clients are expected to be financially disadvantaged because as they receive more in AS and other forms of assistance, they move off the TAS upper limit and therefore become ineligible for the TAS disability allowance exception. 75 of these clients are expected to be financially disadvantaged across the entire package while approximately a further 500 clients will lose their TAS disability allowance exception but will receive benefits from other parts of the package that more than offset this reduction. The average loss for the 75 clients who are likely to be financially disadvantaged across the entire package is approximately \$7 per week across the whole package.
- d **Group Four: Losses from interactions between the FTC and tax changes:** Approximately 1,120 IRD clients with children between the ages of 16 and 18, and no children below that age, are expected to be financially disadvantaged because the age of their children means they will not benefit from the FTC change and their reduced income tax payments are more than offset by the FTC abatement changes. These clients lose an average of \$1.70 per week with approximately 120 clients losing more than \$3 per week. Some of these clients' losses will be offset by changes to the AS maxima, but some losses will increase by about \$2 per week if the family is receiving AS below the maxima. Data in relation to this group has been drawn from Treasury's modelling – IRD are in the process of checking these results against their own administrative data but this data was not available in time for this report. IRD modelling (not using administrative data) shows that those being disadvantaged generally have household incomes above \$76,000 per annum. The actual amount of any loss will only be known once their taxable and family scheme income is known for the tax year 2018/19, around July 2019.

Officials recommend that those facing losses of less than \$3 per week should not be compensated...

- 15. Decisions are needed about which of the groups outlined above should be compensated for any losses they face as a result of the implementation of the package.
- 16. The losses faced by Groups One and Two are small with the maximum loss of \$3 per week only estimated to apply to approximately 70 of the 1,780 clients in Groups One and Two. The remaining 1,710 clients are estimated to lose less than \$2 per week. These losses may well be offset or even outweighed by other changes happening at the same time. For example, every April the Annual General Adjustment (AGA) results in changes to the amount of assistance many MSD clients receive. The 2018 AGA will take effect on 1 April 2018 and is likely to offset some of the small decreases people may see from this package (e.g. someone losing \$2 or \$3 per week from the package may end up being compensated for this through an increase to benefit or NZ Super rates from the AGA). Officials do not therefore recommend compensating clients in Groups One and Two.

...but compensation should be made available to those facing more significant losses

17. Officials consider that clients in Group Three who face losses across the whole package because they lose eligibility to the TAS disability allowance exception as a result of the package should be compensated. The average loss for these 75 clients is \$7 per week and compensating these clients by this much would mean that these 75 clients would be no worse off overall but would not benefit from the package.
18. There is a further group of approximately 500 MSD clients who will lose their TAS disability allowance exception but will receive benefits from other parts of the package that more than offset this reduction. Officials do not propose compensating these clients as they are not financially disadvantaged by the overall package.
19. There is a risk that these clients could consider themselves to be worse off from the reduction they would see in their assistance from MSD in relation to their disability costs (i.e. they may not make the connection between this reduction and the increase in income that would result from the changes to the tax system). MSD considers that this risk can be managed through communications about the interactions between different elements of the package.

Those who are likely to be financially disadvantaged from interactions between the FTC and tax changes are in materially different circumstances than those MSD clients losing their TAS disability allowance exception

20. Estimates suggest that approximately 1,120 clients are expected to be financially disadvantaged by the interaction between the FTC and tax changes. Of this group approximately 120 are expected to lose more than \$3 per week. The largest loss using prior years' administrative data is \$13 per week, ignoring any gains or losses from AS changes. A further AS loss of approximately \$2 per week is possible, meaning the total weekly loss for a family could be \$15 per week.
21. IRD has been consulted on this paper and does not recommend providing compensation to this group given that:
 - a the group is small (120 families);
 - b the largest loss using previous data seems to be, at an absolute maximum, \$15 per week for a single family. In this regard, the group has relatively high household incomes of above \$76,000 per annum;
 - c some of these losses would have occurred in 2019 under the existing legislation; and
 - d it is possible that, on a week-to-week basis, these families would not have a reduced cash flow. This might be the case if they (like many clients) wait till the end of the year before filing for their Working for Families entitlements.
 - e Inland Revenue does not have the operational systems or legislative authority to make small payments to compensate particular groups who may be financially disadvantaged, and clients in this group may not have an existing relationship with MSD.
 - f Previous schemes to compensate families have had 0% take up rates when relying on self-identification.
 - g The administration costs of such a scheme (e.g. designing a form, validating applications) are likely to be disproportionately large compared with the compensation, and could outweigh the total amount of compensation.

- h Data-matching to ensure that gains or losses from AS are taken into account will almost certainly provide incorrect information if a client's income changes throughout the year (given that Working for Families is based on yearly income), or their housing situation changes.
 - i Any loss will only be known about 16 months after the package comes into effect when income for the year is finalised.
22. If Ministers want to try to compensate those in this group, a proposed approach would be for information about the compensation offer to be made available by IRD. Clients who considered they met the threshold for compensation (i.e., were disadvantaged by more than \$3 per week) would complete an application form provided by IRD which would then be passed to MSD. MSD would then check the relevant information on its systems and with IRD before administering the payment.
 23. It would be impossible to identify all groups who would be disadvantaged in advance, as some clients wait until the end of the year before claiming Working for Families, and the remaining clients receive payments that are either overpayments or underpayments and must be squared up at the end of the year in any event. Given that it would be impossible to know which of these clients who claim WFF at the end of the year would be disadvantaged, officials suggest that any self-identification approach only applies to those who receive WFF weekly or fortnightly.
 24. The self-identification approach is based on one that was put in place for the Child Material Hardship package. Although this approach was put in place for the Child Material Hardship package it was not used in practice as no clients applied for support through this avenue.

Overview of proposed approach to compensation for groups estimated to be financially disadvantaged by the Family Incomes Package

25. The table below outlines the four groups who are likely to be financially disadvantaged by this package and the recommended approach to compensation for each group.

Table 1: Groups financially disadvantaged by the Family Incomes Package

No.	Issue	Estimated number of those disadvantaged	\$ amount of estimated loss	Eligible for Transitional Assistance fund?
1	<p>Group One - AS entry threshold increase</p> <p>Small reduction in AS because AS entry threshold rises (as a result of increase in the Family Tax Credit (FTC)) but family does not benefit from FTC increase (because they have children aged 16-18).</p>	1,630	<p>Maximum of \$3 per week:</p> <p>70 clients estimated to lose \$3 per week</p> <p>800 clients estimated to lose between \$2 and \$3 per week</p> <p>760 clients estimated to lose between \$1 and \$2 per week</p>	No
2	<p>Group Two – Reduction in Temporary Additional Support (TAS)</p> <p>Clients who lose more in Temporary Additional Support then they will gain from the increase to AS – this is caused by the fact that MSD does</p>	180	Maximum loss of \$1 per week	No

	not pay TAS for amounts that are less than \$1			
3	<p>Group Three: Loss of TAS disability allowance exception</p> <p>Clients who will lose their TAS disability allowance exception as a result of the increased AS. The TAS disability exception amount allows for 30% of a clients' total excess disability costs to be paid if a clients' disability costs exceed the upper limit for TAS. These clients will lose because as they receive more in AS and other assistance, they move off the TAS upper limit and therefore become ineligible for the TAS disability allowance exception</p>	75 expected to be financially disadvantaged across the whole package	75 clients expected to lose an average of \$7 per week across the whole package	Yes
4	<p>Group Four: Losses from interactions between the FTC and tax changes</p> <p>IRD clients with children between the ages of 16 and 18 may be financially disadvantaged because the age of their children means they will not benefit from the FTC change and reduced income tax payments may be more than offset by FTC abatement changes</p>	1,120 (120 with losses of more than \$3 per week)	<p>Less than \$1 per week – 640</p> <p>Between \$1 and \$2 per week - 290</p> <p>Between \$2 and \$3 per week - 70</p> <p>Between \$3 and \$4 per week - 60</p> <p>Between \$4 and \$5 per week - 40</p> <p>Between \$5 and \$6 per week – 10</p> <p>Between \$6 and \$15 per week – 10</p> <p>More than \$15 per week - 0</p>	No If Ministers wanted to compensate this group, officials suggest that this compensation offer be limited to the approximately 120 clients expected to lose more than \$3 per week.

Of those in Group Four, the mean family income is calculated by the weekly loss bands below in Table 2:

Table 2: Average weekly loss and mean family income

Bands	Count	Percentage of loss faced in 2019 anyway	Mean Family Income
More than \$6	10	46	74 000
Between \$5 and \$6	10	43	57 000
Between \$4 and \$5	40	44	64 000
Between \$3 and \$4	60	44	62 000
Between \$2 and \$3	70	43	60 000
Between \$1 and \$2	290	41	50 000
Less than \$1	640	40	48 000

MSD will manage and administer the Transitional Assistance fund

26. MSD will be responsible for managing and administering the Transitional Assistance Fund. The fund would be modelled on the fund used in the Child Material Hardship package. Those in scope for payments from this fund would be:
- a Those who lose eligibility to their TAS disability allowance exception and are financially disadvantaged across the whole package with an average loss of \$7 per week; and
 - b Individuals and families who are financially disadvantaged as a result of the package by more than \$3 per week but whose particular circumstances have not yet been identified.
27. We recommend that the payments should be provided for a maximum of 24 months or until the client notifies MSD of a change in circumstances that results in any change to the level of assistance they receive.

Under current estimates, sufficient funding is available in the Transitional Assistance fund to cover the cost of the proposed compensation payments

28. A total of \$2.2 million over four years was set aside for the Transitional Assistance payment in Budget 2017 as follows:

	\$m – increase/(decrease)			
Vote Social Development Minister for Social Development	2017/18	2018/19	2019/20	2020/21 & outyears
Benefits or related expenses: Transitional Assistance	1.063	0.50	0.40	0.250

29. Under current estimates this funding should be sufficient to cover the expected costs of the Transitional Assistance payment.

Estimates of the numbers of those who are financially disadvantaged by the package will fluctuate over time

30. All information about expected losers is based on estimates at a particular point in time. These estimates will change between now and the implementation date of 1 April 2018.
31. These estimates can be supplemented by increased data sharing between MSD and IRD. From July 2017 MSD and IRD will be able to share information more freely under the authority of an improved data sharing agreement between the two agencies. This will allow MSD and IRD to more accurately estimate the impacts of the package on individuals and families.

[33]

32. [33]

Next steps

33. Subject to agreement to the recommendations in this report MSD will develop a draft Ministerial Welfare Programme for the Minister for Social Development to approve which will provide the authority and parameters for the Transitional Fund.
34. MSD, Treasury and IRD will also work together to provide regular updates on the estimates of the number of individuals and families who are likely to be financially disadvantaged by the package.