

# The Treasury

## Budget 2021 Information Release

### August 2021

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**MINISTRY OF EDUCATION**  
TE TĀHUHU O TE MĀTAURANGA



**Inland Revenue**  
Te Tari Taake



**TE TAI ŌHANGA  
THE TREASURY**

# Report

**Date:** 19 March 2021

**To:** Hon Grant Robertson, Minister of Finance  
Hon Chris Hipkins, Minister of Education  
Hon Carmel Sepuloni, Minister for Social Development and Employment  
Hon David Parker, Minister of Revenue

**CC:** Rt Hon Jacinda Ardern, Prime Minister, Minister for Child Poverty Reduction

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## **Further advice on the Budget 2021 proposal to increase main benefits following ministerial discussion**

### **Purpose of the report**

- 1 This report seeks confirmation of the:
  - 1.1 inclusion of an increase to student living support from 1 April 2022
  - 1.2 increase to the Minimum Family Tax Credit (MFTC) threshold following the benefit increase, and
  - 1.3 parameters of the Budget 2021 proposal to improve Childcare Assistance.

### **Executive summary**

*Ministers met to discuss income support proposals for Budget 2021...*

- 2 Income support Ministers met on 9 March 2021 to discuss the advice provided on increases to main benefits through Budget 2021 [REP/21/3/175 refers], as well as other income support proposals for Budget 2021.

*... and provisionally agreed the parameters for the bid to increase main benefits*

- 3 Officials understand there was provisional agreement in this meeting that the Budget 2021 proposal to increase main benefits be a \$50 increase in two stages (\$25 per adult per week from 1 July 2021 and a further \$25 per adult per week from 1 April 2022).
- 4 As outlined in previous advice [REP/21/3/175 refers], this staggered increase would mean that from 1 April 2022, main benefits would be roughly \$25 higher than equivalent rates of student living support which could have negative impacts on study incentives. Given this, Ministers also indicated that a \$25 per adult per week increase to student living support from 1 April 2022 be included in the proposal to increase main benefits through Budget 2021. A \$25 increase to student living support from 1 April 2022 would have an operating cost of \$318 million over the forecast period (if charged against the Budget 2022 allowance). The total cost of the proposal is **\$4.04**

**billion** over the forecast period<sup>1</sup>. There is an additional capital expenditure of \$455 million over the 10-year forecast period to account for the increases to student loan living costs. These costs are shown in detail in Appendix One.

*Ministers requested further advice on options for increases to the MFTC threshold following a benefit increase...*

- 5 The Budget 2021 proposal to increase main benefits also includes a partial increase to the MFTC threshold to ensure sole-parent families working at least 20 hours per week (but not necessarily two-parent families) will be financially better off receiving the MFTC rather than receiving a benefit. Sole parents comprise around 90 percent of MFTC recipients (around 4,000 families). This partial alignment approach was agreed by Ministers for the upcoming increases to main benefit abatement thresholds, as it balanced the trade-offs between policy intent, financial incentives to work, fiscal cost and impacts on the Working for Families review that is currently underway.
- 6 The fiscal cost of partial alignment in the event of a two-stage benefit increase is \$52 million. Ministers asked officials to provide advice on alternative options to partial alignment to the MFTC threshold for the main benefit Budget proposal.

*... an alternate option has a lower cost but results in drops in income for families and is more administratively complex*

- 7 Currently the MFTC formula assumes that the Winter Energy Payment (WEP) is paid over 12 months (rather than just from May to October when it is paid) and the MFTC stays at that higher rate for the full year. An alternative approach would be to calculate the MFTC to have a lower threshold in the non-WEP period, and a higher MFTC threshold in the WEP period. This option preserves the policy intent of the MFTC, to be better off receiving MFTC than a benefit (for sole parents), at lower fiscal cost. This "reduced WEP" option is estimated to have a fiscal cost of \$23 million over the forecast period, \$29 million less than that of the partial alignment option.
- 8 However, this option means that recipients would face a \$42 per week drop in income at the end of the winter period. This is a significant drop in income for low-income families. This would mean that, on an annual basis, MFTC recipients would be approximately \$1,250 worse off per year, compared to a partial alignment approach.
- 9 Officials recommend that the MFTC threshold continues to be partially aligned if the proposed benefit increase is progressed so that the MFTC works at least partly as intended and provides a better outcome for families. The variability of the MFTC (and therefore of families' incomes) may also impact on the accuracy of families' entitlements, makes planning and budgeting difficult, and increases confusion.

*Ministers indicated the Budget 2021 proposal to improve Childcare Assistance should introduce indexation only*

- 10 Officials understand that Ministers are interested in pursuing an alternative option for the Budget 2021 bid on Childcare Assistance – introducing indexation of income thresholds to average wage growth (with the current income thresholds frozen since 2010). Officials note that implementing this option only will not have any immediate effects on parents, but a gradual impact over time by allowing parents to work and retain their existing entitlement to Childcare Assistance, preventing any further weakening of financial incentives to work.

11 [33]

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<sup>1</sup> Note that the overall cost will increase by approximately \$560 million if the second \$25 is charged against the Budget 2022 allowance because it includes an additional year in the forecast period.

## Recommended actions

It is recommended that you:

*Budget 2021 proposal to increase main benefits and student support*

- 1 **note** that the proposal to increase main benefits by \$25 per adult per week on 1 July 2021 and increase both main benefits and student living support by \$25 per adult per week on 1 April 2022 (including the complementary income support changes and the partial increase to the Minimum Family Tax Credit) will cost \$4.04 billion over the forecast period
- 2 **note** there is an additional capital expenditure of \$455 million over the 10-year forecast period to account for the increases to student loan living costs
- 3 **note** that a \$25 per adult per week increase to student living support from 1 April 2022 will mean main benefits and student support are roughly the same level. However, indexation of main benefits to wages will mean that benefits increase at a faster rate than student support so will still be slightly higher than equivalent student support rates
- 4 **note** that officials will provide further advice on the indexation of student support to average wages for consideration as part of Budget 2022

*Decisions on the Minimum Family Tax threshold (MFTC) following increases to main benefits*

For the Ministers of Finance, Social Development and Employment and Revenue:

- 5 **note** that there is an alternative option in addition to a partial increase (which ensures sole-parent families working at least 20 hours per week will be financially better off receiving the MFTC rather than remaining on the benefit) that is less costly but results in significant drops in income for MFTC customers and is more administratively complex
- 6 **agree**

### EITHER

- 6.1 that the proposal continue to include a partial increase to the MFTC threshold to \$32,656 from 1 July 2021, and \$34,684 from 1 April 2022, at a fiscal cost of \$52 million over the forecast period (**recommended**)

Yes/No	Yes/No	Yes/No
Minister of Finance	Minister for Social Development and Employment	Minister of Revenue

**OR**

- 6.2 change the proposal to include the “reduced WEP” partial increase of the MFTC, at a fiscal cost of \$23 million over the forecast period (**not recommended**)

<b>Yes/No</b>	<b>Yes/No</b>	<b>Yes/No</b>
Minister of Finance	Minister for Social Development and Employment	Minister of Revenue

- 7 **note** the increase to the MFTC threshold will have to be progressed through Budget night legislation and progressed under urgency in order to meet the 1 July 2021 implementation date

*Budget 2021 proposal to improve Childcare Assistance*

For the Ministers of Finance and Social Development and Employment:

- 8 **confirm** that the Childcare Assistance proposal for Budget 2021 is to introduce indexation of income thresholds for Childcare Assistance to average wage growth

<b>Yes/No</b>	<b>Yes/No</b>
Minister of Finance	Minister for Social Development and Employment

- 9 **note** that should this be funded through Budget 2021, changes to regulations will be required

[33]

[33]

10 [33]

11

<b>Yes/No</b>	<b>Yes/No</b>	<b>Yes/No</b>	<b>Yes/No</b>
Minister of Finance	Minister of Education	Minister for Social Development and Employment	Minister of Revenue
<hr/>	<hr/>	<hr/>	<hr/>
Keiran Kennedy Manager The Treasury	Katrina Sutich Group Manager, Tertiary Ministry of Education	Polly Vowles Policy Manager Ministry of Social Development	Maraina Hak Policy Lead Inland Revenue
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Hon Grant Robertson Minister of Finance	Hon Chris Hipkins Minister of Education	Hon Carmel Sepuloni Minister for Social Development and Employment	Hon David Parker Minister of Revenue

## **Ministers recently met to discuss income support proposals for Budget 2021, including main benefit increases**

- 12 Income support Ministers met on 9 March 2021 to discuss the advice provided on increases to main benefits through Budget 2021 [REP/21/3/175 refers], as well as other income support proposals for Budget 2021.
- 13 Officials understand there was provisional agreement in this meeting that:
  - the Budget 2021 proposal to increase main benefits be a \$50 main benefit increase in two stages: \$25 per adult per week on 1 July 2021 and a further \$25 per adult per week on 1 April 2022
  - an increase to student living support rates of \$25 per adult per week from 1 April 2022 be included in the proposal to keep main benefits and student living support at relatively the same level
  - the Budget 2021 proposal to improve Childcare Assistance be introducing indexation of income thresholds for Childcare Assistance to average wage growth.
- 14 Officials were also asked to provide further advice on options for alternative increases to the MFTC threshold following any benefit increase.
- 15 This report provides updated modelling and seeks confirmation of the provisional decisions made to inform Budget 2021 decisions, as well as further advice on the MFTC threshold.
- 16 Officials understand there was also interest in further advice on the interactions between benefit increases and Special Needs Grants. This advice is being provided to the Minister for Social Development and Employment following this report [REP/21/3/264 refers].
- 17 Further advice has been provided to the Minister for Social Development and Employment on:
  - [33]
  - the Budget 2021 proposal on changes to improve the medical certificate process [REP/21/3/237 refers]<sup>2</sup>.

## **Increasing main benefits by \$50 per adult per week in two stages over 2021 and 2022 through Budget 2021**

- 18 The total cost of a \$50 per adult per week main benefit increase in two stages over 2021 and 2022 is \$3.8 billion over the forecast period.
- 19 This cost includes:
  - complementary changes to the definition of income for Childcare Assistance (to exclude supplementary assistance as income) and,
  - the Temporary Additional Support (TAS) formula (so that the TAS disability exception better reflects disability costs) [REP/21/1/019 refers]<sup>3</sup>

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<sup>2</sup> Further advice is also being provided on time-limited funding for the Training Incentive Allowance [REP/21/3/267 refers].

<sup>3</sup> The complementary changes to Childcare Assistance and TAS will require amendments to regulations by 1 July 2021.



- a Transitional Assistance Payment (TAP) for the benefit increase on 1 July 2021 to ensure that people are not unintentionally financially disadvantaged by this change<sup>4</sup>, and
  - a partial increase to the MFTC threshold.
- 20 These changes are estimated to reduce the number of children living in poverty in 2021/22 by:
- 9,000 ( $\pm 5,000$ ), increasing to 18,000 ( $\pm 8,000$ ) in 2022/2023 on the before-housing-costs primary measure (BHC50) and
  - 14,000 ( $\pm 5,000$ ), increasing to 25,000 ( $\pm 6,000$ ) in 2022/2023 on the fixed line after-housing-costs (AHC) measure.
- 21 Approximately 430,000 individuals and families are expected to benefit from the policy (this includes 36,000 non-beneficiaries), with an average gain of \$23 per week from 1 July 2021, increasing to an average gain of \$46 per week from 1 April 2022 (when factoring in flow-ons to other assistance).
- 22 Like other major reforms, such as Budget 2019 changes, there is a group of non-beneficiaries receiving the Accommodation Supplement (AS) who will be disadvantaged due to the flow-on impacts of increasing main benefits<sup>5</sup>. Around 20,000 individuals and families would face a reduction of their AS of around \$5 per week from 1 July 2021 increasing to 22,000 individuals and families facing a reduction of around \$11 per week from 1 April 2022. This group will not be covered by the TAP described above, as these reductions reflect the intended targeting of payments. This approach is also consistent with other recent income support packages.

### **Increasing student living support by \$25 per adult per week from 1 April 2022 would keep benefit and student living support levels broadly aligned**

- 23 As outlined in the advice on a \$50 per week increase to main benefits [REP/21/3/175 refers], the \$25 per adult per week increase to main benefits from 1 July 2021 would roughly align main benefits and base student living support (this includes the student allowances rates and the student loan living cost maximum)<sup>6</sup>. However, with the further increase of \$25 per adult per week from 1 April 2022, main benefits would be roughly \$25 per week higher than equivalent rates of student living support.
- 24 Having a higher main benefit rate compared to student support may incentivise people to not study and remain on (or apply for) a main benefit when this may not be what they want or in their longer-term interest. This incentive increases when considering the additional assistance available to beneficiaries but not students, such as WEP and the higher rates of accommodation support through AS<sup>7</sup>. Given this, Ministers indicated that a \$25 per adult per week increase to student living support

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<sup>4</sup> The Minister for Social Development and Employment will need to establish a Welfare Programme to enable the provision of a TAP by 1 July 2021.

<sup>5</sup> Increases to main benefits increase the entry threshold for AS meaning that non-beneficiaries are required to use more of their income to cover their accommodation costs.

<sup>6</sup> Until 2018, equivalent student allowance and main benefit rates were broadly the same. As a result of recent policy changes made to both the student support and income support systems, main benefit rates are currently around \$25 per week lower.

<sup>7</sup> The proposal to reinstate the Training Incentive Allowance may also incentivise movement onto benefit to undertake study. This is because additional assistance for employment-related training would be provided to certain beneficiaries.

from 1 April 2022 also be included in the Budget 2021 proposal to increase main benefits<sup>8</sup>.

- 25 A \$25 per adult per week increase to student allowances from 1 April 2022<sup>9</sup> would cost \$318 million over the forecast period (if charged against the Budget 2022 allowance). There is capital expenditure of \$455 million over the 10-year forecast period to account for the increases to student loan living costs.
- 26 Alongside broadly aligning main benefits and student living support, a \$25 per adult per week increase to student support will help to mitigate some of the affordability challenges faced by students. Student groups have consistently emphasised ongoing affordability challenges in engagement during COVID-19 and the Education Conversation/Kōrero Mātauranga.
- 27 As noted above, this increase would mean benefits and student living support would be roughly the same rate. The key difference in rates following this increase would be the indexation of rates, as main benefits are indexed to average wage growth whereas student living support is indexed to CPI (inflation). This difference means main benefits are likely to increase at a faster rate than student support going forward.
- 28 <sup>[33]</sup>

*The costs of the second \$25 per week increase may be charged against the Budget 2022 allowance*

- 29 The total cost of the Budget 2021 proposal to increase main benefits (and complementary changes, including to the MFTC and student living support) would be **\$4.04 billion** over the forecast period. There is an additional \$455 million over the 10-year forecast period to account for the increases to student loan living costs.
- 30 We understand that one option under consideration is to charge the second \$25 increase (and associated student support changes) against the Budget 2022 allowance. This decision will be taken by Budget Ministers throughout the Budget process.
- 31 The total cost of the proposal (including complementary income support changes and a partial increase to the MFTC) would increase under this approach to:
- \$2.2 billion charged against the Budget 2021 allowance (1 July 2021 increase); and
  - \$2.4 billion charged against the Budget 2022 allowance (1 April 2022 increase)
- 32 A breakdown of these costs is provided in Appendix One.

### **Increasing main benefits requires decisions around subsequent increases to the Minimum Family Tax Credit threshold**

- 33 The Budget 2021 proposal to increase main benefits also includes a partial increase to the MFTC threshold to ensure sole-parent families working at least 20 hours per

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<sup>8</sup> An increase per adult means that a couple who are on student allowance dependent partner rates would receive an extra \$50 net per week (\$25 each).

<sup>9</sup> Increases to student support are usually made from 1 January, as April is partway through most learners' programmes of study. However, effectively promoting the increase should mitigate any potential impact of an April increase on learners' decisions about starting study in January to March 2022.

week (but not necessarily two-parent families) will be financially better off receiving the MFTC rather than remaining on the benefit<sup>10</sup>.

- 34 A partial increase means that the MFTC threshold would increase from \$30,576 to \$32,656 on 1 July 2021, and to \$34,684 on 1 April 2022. The fiscal cost of partial alignment for a two-stage benefit increase is \$52 million. This partial alignment approach was agreed by Ministers for the upcoming increases to main benefit abatement thresholds, as it balanced the trade-offs between policy intent, financial incentives to work, fiscal cost and impacts on the Working for Families review that is currently underway.
- 35 At the 9 March meeting, Ministers considered the question of the consequential MFTC alignment with the proposed benefit increase. While Ministers agreed that the current “partial alignment” approach should be the starting point, Ministers also asked for further advice on what other less costly MFTC alignment options are available.

*The MFTC formula could be changed to reduce costs while ensuring sole parents remain marginally better off in work by changing how the Winter Energy Payment is treated*

- 36 In November 2017, when the WEP was introduced for beneficiaries and super annuitants, Ministers agreed that MFTC recipients should be guaranteed to receive more from being in full-time work than they would on benefit at any point during the year, regardless of whether WEP was being paid at the time or not. It was decided that the MFTC formula would assume that WEP is paid throughout the year, not just between 1 May and 30 September.
- 37 Therefore, under the current MFTC formula:
- between 1 May and 30 September, when beneficiaries receive the WEP, MFTC recipients are marginally better off than they would be on benefit
  - between 1 October and 30 April, when the WEP is not paid, MFTC recipients are financially better off than they could be on the benefit by an amount roughly equivalent to the weekly amount of WEP.

Figure one: Partial alignment of the MFTC threshold

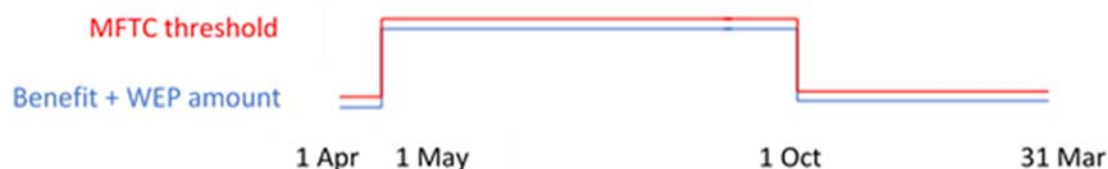


- 38 This formula results in a slightly inflated MFTC threshold in order to smooth income for recipients as shown in Figure one above.
- 39 Officials have considered alternative options for providing a lower-cost MFTC threshold that would still maintain the key policy intent of the MFTC. Out of those, there is only one option, which would alter the way the WEP is treated in the MFTC formula.
- 40 The MFTC would have a lower threshold in the non-WEP period, and a higher MFTC threshold in the WEP period (a two-rate “reduced WEP” option). Under this method, the MFTC threshold would mirror the increase and decrease of benefit income received during the year. This is illustrated in Figure two below.

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<sup>10</sup> Sole parent families represent approximately 90 percent of MFTC recipients.

Figure two: Reduced WEP option – Two-rate MFTC threshold



- 41 From 1 July 2021 the MFTC threshold would change from \$30,576 (at 1 April 2021) to \$32,656. However, from 1 October 2021 to 31 March 2022, the MFTC threshold would decrease to \$30,472, which is below the threshold at the start of this tax year. This option has a fiscal cost of \$23 million over the forecast period, which is \$29 million less than that of the partial alignment option.
- 42 The advantage of a two-rate MFTC threshold is that it would reduce the fiscal cost of MFTC, while ensuring that MFTC recipients would be marginally better off in work and receiving MFTC than being on benefit regardless of when, and for how long, during the year that they receive the MFTC.
- 43 However, this option means that recipients would face a \$42 per week drop in income at the end of the winter period. This drop is more than the drop in income beneficiaries receive when WEP ends by approximately \$10 per week<sup>11</sup>.
- 44 \$42 per week is a significant drop in income for low-income families and would mean this income would not be available to offset their costs related to working, such as transport or childcare. This would mean that, on an annual basis, MFTC recipients would be approximately \$1,250 worse off per year, compared to a partial alignment approach. On average, this equates to a \$24 per week reduction over the year.
- 45 The variation in the MFTC thresholds may also impact on the accuracy in calculating families' MFTC entitlements, which could mean less timely support (under-payments) or debt (over-payments). This would increase confusion for families and administrative complexity. To illustrate the extent of this, the MFTC threshold would change seven times over the next two fiscal years with this option. Variability of income also makes planning and budgeting difficult for families.
- 46 The fiscal savings of \$29 million forecast under the reduced WEP option is modest in the context of a total Budget bid of \$4.04 billion.
- 47 For these reasons, officials do not recommend this option, and instead recommend that the partial alignment approach be implemented.

*Regardless of the MFTC option preferred by Ministers, legislative change will be required*

- 48 Regardless of whether Ministers choose to proceed with a partial alignment approach or a two-rate reduced WEP approach, the change in MFTC thresholds would need to be made via Budget night legislation and progressed under urgency.

## **The Budget 2021 proposal to improve Childcare Assistance**

*Introducing indexation of income thresholds for Childcare Assistance to average wage growth*

- 49 The Minister for Social Development and Employment was invited to submit a Budget 2021 bid on improving Childcare Assistance. <sup>[33]</sup>

The income thresholds

<sup>11</sup> It is anticipated low-income families will see a drop in energy costs at the time in which WEP ends.

for Childcare Assistance have been frozen since 2010, so have reduced considerably relative to wages. We understand that Ministers are interested in this bid being an alternative option of introducing indexation of income thresholds to average wage growth. The costs for this initiative are outlined below.

<b>Option</b>	<b>2021/22</b>	<b>2022/23</b>	<b>2023/24</b>	<b>2024/25 and outyears</b>
Introducing indexation of Childcare Assistance income thresholds to average wage growth	\$1.298m	\$2.099m	\$3.812m	\$6.089m

50 This option would be implemented on 1 April 2022, and income thresholds would be rounded up to the nearest dollar. This option will require amendments to regulations by 1 April 2022.

51 Officials note that this option alone will not have any immediate effects, but rather a cumulative effect over time. Indexing the income thresholds for Childcare Assistance to average wage growth will allow parents to work and retain their existing entitlement to Childcare Assistance, preventing any further weakening of financial incentives to work. Compared with the status quo of no indexation, the number of parents who are eligible for Childcare Assistance will gradually increase over time.

[33]

52 [33]

- [33]

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53 [33]

54

## **Next steps**

55 Officials understand the outcome of these decisions will be considered as part of the Budget 2021 process.

56 Should these options be progressed through Budget 2021, officials will provide further advice on the legislative changes required for the complementary income support changes, MFTC and indexation of Childcare Assistance income thresholds.

57 [33]

## Appendix One: Detailed costings for the policy changes

**1 July 2021** – first \$25 increase to main benefits and complementary changes – includes 'partial alignment MFTC'

<b>Operating</b>	2021/22	2022/23	2023/24	2024/25 & out years	Total
Main benefits	\$542.717m	\$539.186m	\$533.525m	\$530.575m	\$2,146m
MFTC	\$8.025m	\$8.000m	\$8.000m	\$7.000m	\$31m
<b>Total</b>	\$550.742m	\$547.186m	\$541.525m	\$537.575m	\$2,177m

**1 April 2022** – second \$25 increase to main benefits and associated \$25 increase to student support – includes 'partial alignment MFTC'

<b>Operating</b>	2021/22	2022/23	2023/24	2024/25	2025/26 & out years	Total
Main benefits	\$126.152m	\$497.508m	\$491.713m	\$484.379m	\$484.379m	\$2,084m
MFTC	-	\$8.000m	\$7.000m	\$6.000m	\$6.000m	\$27m
Student allowance	\$23.103m	\$71.574m	\$73.564m	\$74.927m	\$74.927m	\$318m
<b>Total</b>	\$149.255m	\$577.082m	\$572.277m	\$565.306m	\$565.306m	\$2,429m

<b>Capital</b>	21/22	22/23	23/24	24/25	25/26	26/27	27/28	28/29	29/30	30/31	Total
Student loans	\$16.4m	\$51.2m	\$51.1m	\$50.5m	\$51.0m	\$49.8m	\$48.6m	\$46.9m	\$44.9m	\$44.9m	\$455m