MINISTRY OF HOUSING
AND URBAN DEVELOPMENT

Briefing

First home buyer support			
Date:	10 May 2019	**Security level:**	In Confidence
Priority:	High	**Report number:**	BRF18/19050252

Action sought		
	Action sought	**Deadline**
Hon Twyford **Minister of Housing and Urban Development**	**Agree** to the recommendations	20 May 2019
	Discuss with officials at the HUD Policy, Strategy and Governance Officials meeting on Monday 13 May.	13 May 2019
Hon Jenny Salesa **Associate Minister of Housing and Urban Development**	For information only	N/A
Hon Nania Mahuta **Associate Minister of Housing and Urban Development**	For inflation only	N/A

Contact for discussion				
Name	**Position**	**Telephone**		**1st contact**
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Other agencies consulted
Treasury, IRD and MSD have provided comments on capitalising Working for Families. Treasury has been consulted on using the HomeStart underspend. DPMC has been informed.

Minister's office to complete

- ☐ Noted
- ☐ Seen
- ☐ Approved
- ☐ Needs change
- ☐ Not seen by Minister
- ☐ Overtaken by events
- ☐ Declined
- ☐ Referred to (specify)

Comments

Date returned to MHUD:

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Briefing

First home buyer support

For:	Minister Twyford, Minister of Housing and Urban Development		
Date:	10 May 2019	**Security level:**	In Confidence
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Purpose

1. This briefing responds to your request for initial advice on first home buyer support, including capitalising Working for Families tax credits and changing the HomeStart and Welcome Home Loan settings. We understand that the policy objective is to support mid to low income households into homes built as part of the Government Build Programme, with a focus on families.

Executive summary

2. First home buyer support can be a useful way of supporting households around the median income in urban areas (incomes of around $70,000 to $100,000) into homeownership. Lower income households can also be helped in regional areas with low house prices, or with significant funding.

3. Support can help with two main barriers: accumulating a deposit and servicing the mortgage (alongside other ongoing costs, such as rates, maintenance and body corporate fees).

4. Support can be provided in a range of ways. Deposit support has the advantages of being simple to administer, requiring minimal capital funding, and targeting the deposit barrier. The deposit barrier appears to be the most common barrier for first home buyers with median and higher incomes.

5. Other forms of support – such as progressive home ownership - can work better for households with somewhat lower incomes, but can be complex and expensive for the government to provide. If implemented, the Affordable Housing Fund will increase the availability of progressive home ownership schemes, making use of the expertise, co-funding and land of community housing providers, Māori organisations and local authorities.

6. Households will be able to combine together several forms of support to afford a home. These include the existing products of HomeStart grants, Welcome Home Loans and KiwiSaver withdrawals, along with progressive homeownership schemes provided by housing providers, and any other forms of support that are made available. For example, the deposit required with shared equity schemes can be below 5%, so the entire deposit could come from HomeStart grant and KiwiSaver withdrawal where a household has an adequate income to make use of the scheme.

7. You have asked how the HomeStart grant underspend could be used. Spending on HomeStart grants is around $20m below its forecast appropriation of $106m. Officials are looking further at the limits on how this funding can be used. HomeStart is a demand-driven benefit or related expense (BORE) appropriation.The level of the appropriation is set as a high-end forecast of the funding needed under current policy settings. At the end of the financial year any underspend is expected to be returned to the centre, and the forecast revised to more accurately reflect demand, rather than policy settings being adjusted to make

full use of the appropriation. In effect the forecast reflects the policy settings, and changes to the policy settings would change the forecast. The fact that it is a BORE also means surplus funding cannot be transferred to a different appropriation through a fiscally neutral adjustment.

8. However, previous decisions have been inconsistent, and changes to HomeStart settings have been made in the past to make fuller use of the appropriation, such as increasing the house price caps in 2016 and 2018. The HomeStart grant settings may be able to be adjusted to provide greater support to particular first home buyers, and we are further investigating this with Treasury.

9. You have asked for further advice on capitalising a portion of Working for Families (WFF), or using the WFF eligibility criteria to determine the amount of a new deposit subsidy. Capitalising would involve paying out an estimate of the present value of future payments over a certain period of time (say, five years) as a lump sum rather than making the payments over time. Officials have looked further at both options in consultation with MSD, IRD and Treasury. Officials would instead recommend investigating reducing the deposit requirement on Welcome Home Loans from 10% to 5%, or creating a new deposit subsidy for families with regional targeting.

10. Capitalising a portion of WFF could be made to work but would have significant downsides, including:

    a. WFF is means tested, making it more difficult to capitalise than the historical family benefit, which was universal. Families' incomes and makeup change a lot over time, meaning that capitalising WFF would result in some families missing out on much needed income later on, and other families capitalising more than they would have been entitled to over time. Those that are underpaid would be at high risk of hardship, resulting in increased child poverty, particularly since the costs of owning a home (mortgage, rates, insurance, maintenance etc.) tend to add up to being higher than renting.

    b. The WFF settings are the same nationwide. Given the settings, there would be households who both receive working for families and could afford a home outside of Auckland, but very few of these households would be in Auckland.

    c. A capitalisation scheme would be complex to develop and administer, including likely requiring legislative change, so would take over a year to develop.

    d. A capitalisation scheme would bring forward spending, impacting on the budget balance and net core Crown debt.

    e. Capitalising WFF may not increase a household's borrowing power much as it would reduce their debt servicing capacity. In effect, mortgages already capitalise WFF tax credits in a prudent way as banks would take them into account in lending decisions.

11. Increasing access to high-LVR mortgages by modifying the Welcome Home Loan and HomeStart settings would provide an indirect way of helping households to capitalise their benefit, as it would allow them to borrow against future income (including WFF) without needing a large deposit. We can also further test with the banking sector as to whether they fully take into account WFF in their lending calculators.

12. Creating a new deposit subsidy possibly based on the WFF eligibility criteria could work. This may be able to be done as an extension of HomeStart or as a separate scheme. However, we would recommend developing eligibility criteria for the scheme that vary across regions so the scheme can be used in Auckland, rather than using the WFF eligibility criteria entirely.

13. Funding and resourcing would be needed for both options. Modifying HomeStart and Welcome Home Loans may be able to be done within a matter of months, depending on the availability of funding within the existing appropriations. Developing a new deposit subsidy or capitalising WFF may require funding from Budget 2020 and would take significant time and resourcing to design and implement.

14. We recommend delaying the announcement of any major new support schemes until they are near to being implemented. A long gap between announcement and implementation will incentivise people to delay buying a home until the scheme is available, making it more difficult to sell Government Build Programme homes.

Recommended actions

15. It is recommended that you:

1.	**Note** that there are restrictions around using the HomeStart underspend, and officials are investigating how the underspend can be used.	*Noted*
2.	**Note** that capitalising working for families would have a number of significant challenges, including potentially raising child poverty, overpaying or underpaying people, being difficult to use in Auckland, being highly complex, may not greatly increase borrowing power, and would take more than a year to develop as it would require significant policy work and legislative change.	*Noted*
3.	**Note** that using the Working for Families eligibility criteria as the basis for a new deposit subsidy – either as an extension of HomeStart or as an independent subsidy - could work if funding were available, although the criteria would need to be modified to work in Auckland.	*Noted*
4.	**Note** that reducing the deposit requirement of the existing products would allow first home buyers to borrow more against their future incomes, including Working for Families tax credits.	*Noted*
5.	**Note** that the Affordable Housing Fund will increase the availability of progressive home ownership schemes.	*Noted*
6.	**Agree** that officials investigate making changes to the existing homeownership products to help first home buyers with their deposit. This could include reducing the deposit threshold on HomeStart grants and Welcome Home Loans, making HomeStart available to groups of three or more buyers.	*Agree/Disagree*
7.	**Agree** that officials further investigate what the HomeStart underspend can be used for.	*Agree/Disagree*
8.	**Agree** that officials further investigate targeting homeownership support by family composition and region, either as an extension of HomeStart or as a separate scheme.	*Agree/Disagree*
9.	**Agree** that officials confirm the extent to which banks account for Working for Families payments in determining lending amounts (ie. how much they effectively capitalise it through mortgages).	*Agree/Disagree*
10.	**Discuss** with officials at the HUD Policy, Strategy and Governance Officials meeting on Monday 13 May.	*Agree/Disagree*

Fiona Ryan
Acting Manager, Housing System Performance
10 / 5 / 19

Hon Twyford
Minister of Housing and Urban Development
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Background

1. You have requested advice on additional support that could be provided to buyers of Government Build Programme homes, including:
    a. Extending deposit assistance for Government Build Programme homes,
    b. Increasing uptake of HomeStart and Welcome Home Loans, and
    c. Capitalising Working for Families for the purchase of a first home.
2. These options are being explored as part of the KiwiBuild reset.
3. We understand that the policy objective is to support low- to mid-income households into homes built as part of the Government Build Programme, with a focus on families.

Background on first home buyer support

4. First home buyer support can help mid-income households achieve homeownership. These households would typically have incomes around $70,000-$100,000 in urban areas. In some cases lower income households can also be helped, such as in regional areas with lower house prices or with significant amounts of funding.
5. There are two barriers that first home buyer support can help with are the deposit barrier (accumulating a deposit) and the serviceability barrier (paying the mortgage, along with other costs of homeownership like rates, insurance, maintenance and body corporate fees). First home buyers also need to have an adequate credit history, have the knowledge to navigate the home purchase process, and be able to find a suitable home in their area.
6. Support can be delivered in a range of ways, including as deposit subsidies, loan underwrites, progressive home ownership schemes (eg. shared equity schemes and rent-to-buy schemes), mortgage subsidies and low interest loans. These all help with the the deposit barrier, the serviceability barrier, or both, to varying degrees.
7. Support that helps first home buyers with their deposit tends to have the advantages of being simple to administer, require little capital from the government, and directly targeting the deposit barrier. Deposit support works best for households with median level incomes and higher. Both the deposit and serviceability barriers are important for first home buyers, but feedback from banks and first home buyer representatives suggests that the deposit barrier is the most common barrier. Around 60% of the 4200 people on the KiwiBuild register who responded to the survey question about their deposit reported not yet having an adequate deposit. In addition, separate HUD analysis suggests that 19% of renting, employed households in Auckland had enough income to service a mortgage but did not have a deposit, whereas only 11% had a deposit but not enough income to service a mortgage. A further 20% had both an adequate deposit and enough income. However, this HUD analysis is sensitive to the assumptions used.[1]
8. The current homeownership products all help first home buyers with the deposit barrier. The products are:
    a. **KiwiSaver withdrawals.** People may withdraw all of their savings – including the government contributions – aside from $1000. No income or house price caps apply.
    b. **KiwiSaver HomeStart grants.** These provide grants of up to $5000 to KiwiSaver members buying a first home. Groups of two or more buyers can receive up to two grants, and the grant amount is doubled if buying a new build. Income caps apply of

[1] An adequate income is assumed to be $110,000, and an adequate deposit is assumed to be $120,000 (20% of a $600,000 home).

$85,000 for sole buyers and $130,000 for groups of buyers, and regional house price caps apply. The house price caps are equal to or higher than with the KiwiBuild price caps depending on the region.[2]

c. **Welcome Home Loans.** These are government-underwritten mortgages up to 90% LVR for people who do not meet banks' normal lending criteria for high-LVR mortgages. The same income and house price criteria apply as for HomeStart grants. The government underwrite costs 2.2% of the loan value, of which 1.2% is paid by the government and 1% by the household.

9. Uptake of HomeStart and Welcome Home Loans is low in urban areas, especially Auckland. This is because there are few homes available below the house price caps and fewer households below the income caps who could afford a home.

10. Deposit subsidies only reach a certain distance down the income scale. To make use of a deposit subsidy, households will need to have enough or nearly enough income to service a mortgage. For example, for a family of four to service a Welcome Home Loan on a $600,000 home, they would need an income of at least $90,000 (figure 1).

11. Households that are some distance from homeownership would require very large deposit subsidies to afford a home (eg. over $50,000). Very large deposit subsidies may be seen as unfair, particularly given that a household's situation can change over time. A household with a moderate income at the time of purchasing a home may have a high income in a few years time.

12. For households who can afford 60-90% of a home, a combination of a deposit subsidy and serviceability support is needed. These households would typically have incomes below that required to afford full ownership – for example, an income of $70,000-$90,000 for a family of four buying a $600,000 home. The subsidy could take the form of an ongoing payment or a progressive home ownership scheme. The cost of ongoing support can accumulate to a significant amount over time. Many options also require the government providing the capital as well. Containing the cost relies on the buyer's income rising over time so that they can progress to full ownership.

13. The Affordable Housing Fund will increase the availability of ongoing support through increasing the availability of progressive home ownership schemes. Along with the existing home ownership products and potential new subsidies, this will create options for households who cannot afford to buy a home immediately. The affordable housing fund offers good value for money by using co-investment and the expertise of existing housing providers.

14. Homeownership is not a realistic prospect for low income households in urban areas (those with incomes below $60,000) unless they have significant other savings. The amount of support needed would be very large. In addition, research suggests that low income households may not benefit from homeownership as much as mid to high income households. This can happen if they can only afford to buy a home of very low quality, cannot afford to maintain it, or are unable to sustain homeownership in the long run. A secure tenure rental will often be the best option for these households.

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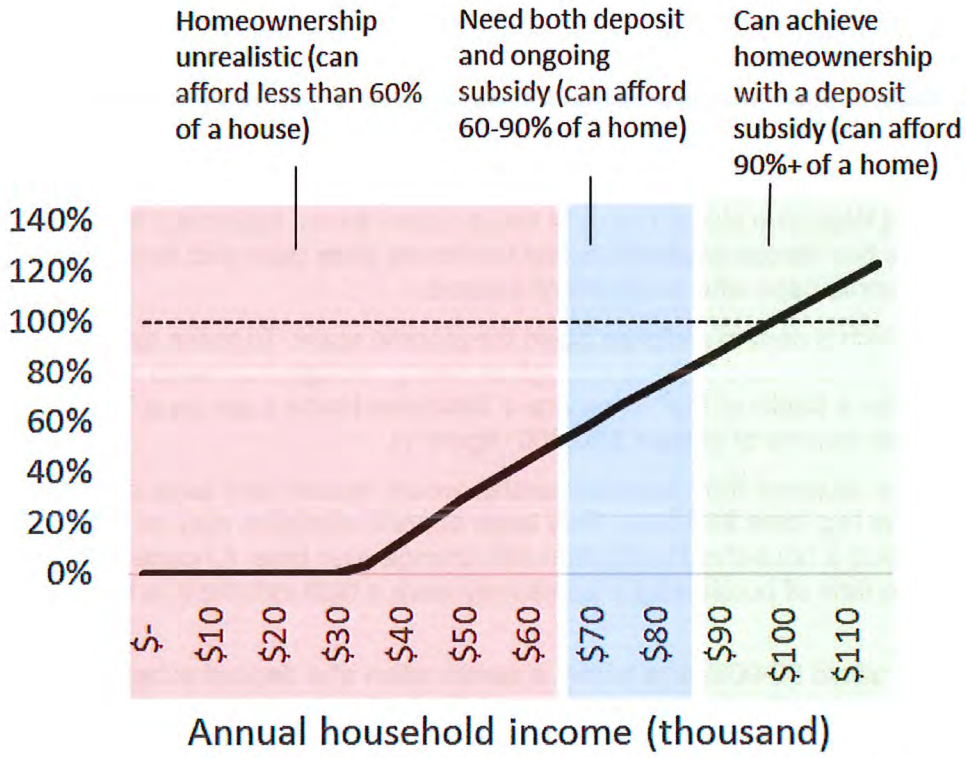
[2] The HomeStart and KiwiBuild price caps differ in Wellington, Tauranga, Hamilton and Chrischurch, where the KiwiBuild price cap is $500,000 and the HomeStart cap is $550,000.

Figure 1: Example of the proportion of a $600,000 house that a household could afford under the Welcome Home Loan servicability criteria



Note: Shows the proportion of a $600,000 house that a household with two adults and two children could afford, assuming they had a 10% deposit. The assumed interest rate is 5.8% and the mortgage term is 30 years.

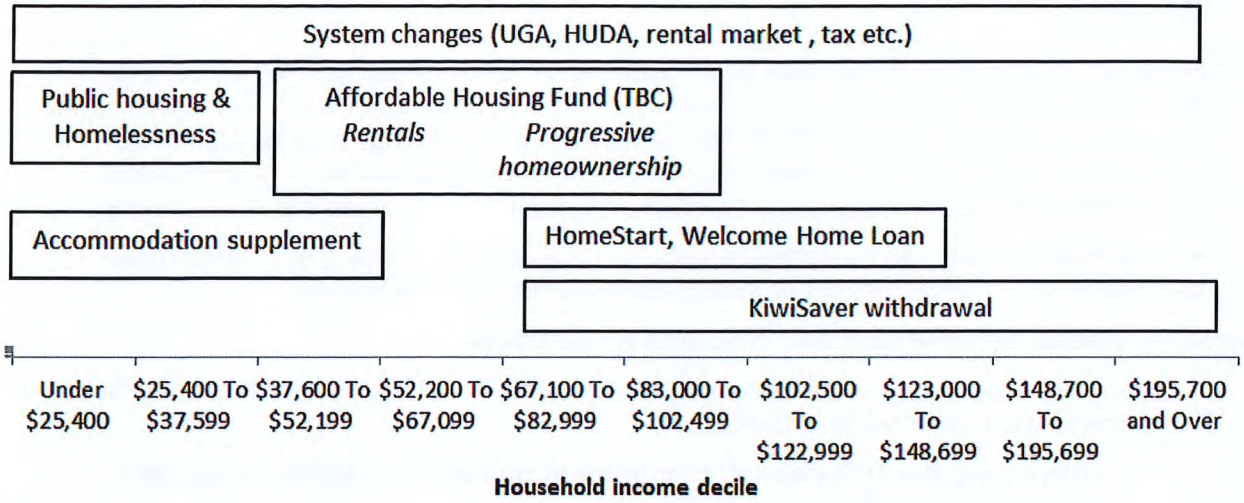
15. There are some downsides to homeownership subsidies that need to be managed.

    a. **Homeownership subsidies can be very expensive on a per household basis**. This downside can be managed by keeping the subsidy tightly targeted.

    b. **Homeownership subsidies risk inflating house prices**. This risk can be mitigated by keeping the subsidies small and targeted, reducing the extent to which the subsidy increases housing demand. The risk can also be mitigated by targeted subsidies towards new builds. However, targeting new builds is not a complete solution to the risk of inflating house prices unless it actually *induces* more supply (i.e. to what degree does deposit support increase developer confidence to develop). More demand would generally induce more supply, although this would depend on the specifics of the market and the design of the subsidy. If the subsidy does not induce more supply, it will draw more demand into the market for the same finite number of homes.

16. Figure 2 shows the typical income deciles some the government's interventions would operate at. The cost per household of supporting low income households into homeownership means that homeownership subsidies tend not to reach far below the median income. This downside can be managed by ensuring that there are other forms of support for households across the housing continuum, including for rentals, and making system changes that will make housing affordable in the long run. There would be some regional variation in this, with interventions reaching further down the income distribution in lower priced areas.

Figure 2: The typical income deciles the government's interventions will assist



Stacking support

17. As shown in figure 2, households surrounding the median income ($70,000-$100,000) will be able to combine together a range of support mechanisms to achieve homeownership. In an extreme case, a household could combine all of the following: KiwiSaver withdrawal, HomeStart grant, Welcome Home Loan, and a progressive home ownership scheme.

18. Combinations of products can be quite effective. For example:

    a. Shared equity schemes sometimes only require very low deposits of below 5%, as the equity partner's share contributes towards bank lending requirements. Households with an adequate credit record and income could use their HomeStart and KiwiSaver withdrawals to reach the deposit requirement.

    b. A household who has been saving regularly into KiwiSaver could get a significant deposit from withdrawing their KiwiSaver funds and receiving a HomeStart grant. They would only need a limited amount of additional savings to reach the 10% deposit required for the Welcome Home Loan.

19. As more support is stacked together, it becomes important for the administrative processes to be aligned to make it easy for first home buyers to navigate them.

HomeStart grants and Welcome Home Loans

The HomeStart and Welcome Home Loan underspends

20. The HomeStart grant spend has been $20m below the appropriation for the past two years (20% of the appropriation). Likewise, the Welcome Home Loan appropriation was underspent by $1.6m (19% of the appropriation) in the year ended June 2018.[3] We have focussed on the HomeStart underspend here as this is the much larger underspend.

21. You have asked how the HomeStart grant underspend could be used. Officials are looking further at the limits on how this funding can be used. HomeStart is a demand-driven benefit appropriation, and the level of the appropriation is set as a high-end forecast of the funding needed under current policy settings. At the end of the financial year any underspend is expected to be returned to the centre, and the forecast revised to more accurately reflect demand, rather than policy settings being adjusted to make full use of the appropriation. In effect the forecast reflects the policy settings, and changes to the policy settings would

[3] Welcome Home Loans are funded out of the HNZC Housing Support Services appropriation. $8.7m of funding is available, of which $7.1m was used.

change the forecast. This also means surplus funding cannot be transferred to a different appropriation through a fiscally neutral adjustment. Underspends do not accumulate up from year to year.

22. However, previous decisions have been inconsistent, and changes to HomeStart settings have been made in the past to make fuller use of the appropriation, such as increasing the house price caps in 2016 and 2018. The HomeStart grant settings may be able to be adjusted to provide greater support to particular first home buyers, and we are further investigating this with Treasury. Some initial possibilities for changes are noted below.

23. If insufficient funding can be obtained from the underspends, funding may need to be sourced from a new budget bid or making cost savings from elsewhere.

Increasing uptake of HomeStart and Welcome Home Loans

24. If funding were available, some beneficial changes that could be made to the HomeStart and Welcome Home Loan criteria could be:

    a. **Revisiting the 10% deposit requirement on Welcome Home Loans and HomeStart grants.**
    Officials could investigate the advantages and costs of reducing the deposit requirement on Welcome Home Loans from 10% to 5%. This would more closely align the Welcome Home Loan policy with the rest of the market. Welcome Home Loans required no deposit when they were first introduced in the mid-2000s, and the deposit requirement has varied over the past decade.

    HomeStart grants also require the buyer to have a 10% deposit made up of their own savings (ie. excluding the value of the grant). This requirement is of little value for two reasons. First, it works against the intention of HomeStart to help first home buyers into home ownership who struggle to save a deposit. Second, buyers who do not have a 10% deposit have in cases found a way to create the impression that they have a deposit, such as by presenting gift certificates that are not subsequently drawn, so very few applicants are declined based on this criteria.

    We would need to assess the cost of doing this and identify a funding source. A lower deposit requirement would increase the risk of the loan, and require additional funding for the government underwrite. However, the cost would likely be modest (perhaps a few million dollars per year). We would also need to further consider the risk that reducing the deposit requirement would pose for the borrowers, the government and the wider financial system.

    b. **Allowing HomeStart grants to be paid to all buyers where there are three or more buyers**.
    Currently only a maximum of two buyers per household can be paid a HomeStart grant. This disadvantages groups of buyers, such as multigenerational households, including many Pacific households. Officials could investigate the cost of allowing all buyers in groups of three or more buyers to be paid HomeStart grants. However, the cost would likely be no more than a few million dollars per year as only 0.6% of homes bought with the help of a HomeStart grant have three or more buyers.

    c. **Regionalising the income caps**.
    The income caps are currently the same across the country, which makes it more difficult to use HomeStart grants and Welcome Home Loans in high priced areas than low priced areas. Officials could investigate regionalising the income caps, such as by increasing the Auckland income cap to above $85,000/$130,000. However, this could be expensive and may deliver support to people who are not in great need.

    d. **Investigating the potential to increase the size of grants for new builds, potentially for mid income earners and families**.

Depending on the limits there are to using the HomeStart underspend, more significant changes like these may be able to be made, such as introducing grants that scale with family size.

25. Further work would need to be done to understand the impacts and costs of making these changes.

Capitalising working for families

26. Officials have given more in-depth consideration to capitalising working for families (WFF) to support families into ownership, in consultation with MSD, IRD and Treasury.

27. We have considered two options:

    a. Capitalising WFF (or a portion of it) so that the household becomes ineligible for ongoing payments.

    b. Using the WFF criteria as the eligibility criteria for a new deposit subsidy.

Capitalising WFF (or a portion of it) so that the household becomes ineligible for ongoing payments.

28. There are some significant differences between working for families and the historic family tax credit meaning a similar approach to capitalising a households entitlement would be challenging. Capitalising a portion of

The historical family tax was a universal payment for defined period

29. The family tax credit was a universal benefit paid for every child regardless of their parent's income. This benefit was guaranteed from the time a child was born until they were 16, and it could be continued until the age of 18 if in full time education.

30. People could apply to capitalise their benefit for the purchase of a new home and certain other circumstances as long as their child was under the age of 16. The capitalised amount was the net present value of expected future payments, with a 25% discount to account for mortality risk. As the payment was fixed and universal it was easy to calculate. The capitalisation scheme ran from 1958 until 1991.

31. Working for families is means tested, with entitlement dependent on a range of factors including income level, income source, hours worked, number of children and shared care arrangements. Analysis by IRD indicates that only around 10% of families received working for families or its predecessor, the family benefit, continuously for 18 years between 2000 and 2017. The entitlement amount of these families also varies a lot over time. This means that capitalising WFF would result in some families missing out on much needed income later on, or being overpaid. For example:

    a. A change in care arrangements resulting in the child moving out of the home after capitalising the payment would mean that the homeowner had capitalised benefits they would not have received as ongoing payments.

    b. Households whose incomes decline, but with income exceeding the $42,500 abatement threshold, would have capitalised a smaller amount than they would have received as ongoing payments.

32. Historically capitalisation of Family Benefit occurred when households were more nuclear and stable, which is no longer the case. This fluidity in family household composition over short periods of time means that any capitalisation would need to manage this risk.

33. While provisions could be designed to claw back or top up under or over payments or to capitalise a proportion of future credits only, these are likely to be complex. Rather than develop processes to estimate future entitlement, monitor and manage changes that might affect accuracy of the capitalised amount (both prospective and retrospective) and debt recovery, it would be preferable to base any capitalisation on current entitlements.

Capitalising future entitlements risks raising child poverty and may not affect borrowing capacity

34. Capitalising working for families to support families into home ownership could undermine the policy objective of reducing child poverty. A 2010 evaluation of WFF found that it had reduced child poverty by 8 percentage points (from 26 percent to 18 percent of children). Some families who capitalise their benefit for the purchase of a first home will be better off if they sustain homeownership. However, it is highly likely that some families who encounter financial difficulty after capitalising their benefit would experience severe hardship without having ongoing access to Working for Families credits, and this would increase child poverty. The cash flow demands of homeownership tend to be higher than the cash flow demands of renting once mortgage payments, rates, insurance, maintenance, body corporate and other expenses are taken into account. This would also put pressure on households who experience financial difficulties.

35. While capitalising future payments can help families to secure a deposit, their ability to service a mortgage will be reduced. It is highly likely that banks will take account of a family's reduced disposable income from capitalising the WFF credits and reduce their assessment of a family's mortgage servicing capacity. This would suggest that capitalising WFF would work best for households who could service a mortgage for a home, but lack the necessary deposit.

36. There is also a risk that capitalisation of WFF would affect incentives to work, although this is a less significant risk given the strong incentive to maintain mortgage payments and retain homeownership. The greater risk is that households fall into material hardship and do not have the WFF credits to rely on. This is mitigated at higher levels of income where entitlements are lower, but also means the value of any capitalised payments is also low.

The Working for Families payments and thresholds are not calibrated for home ownership across regions

37. WFF eligibility criteria do not vary across regions. Given the levels of income required to service a mortgage, few households in Auckland who could service a mortgage would be receiving WFF tax credits. Some indicative scenarios include:

    a. A family of four in Auckland would require around an income of $90,000-$100,000 to service a mortgage on a $600,000 home with a 10% deposit. At an income of 95,000, the current WFF entitlement is around $1300 per annum. Capitalising five years of this would give around $5000. This would only make a modest contribution to the deposit on an Auckland home.

    b. In contrast, a family of four in Wellington would require an income of around 80,000-85,000 to service a 500,000 mortgage with a 10% deposit. At an income of 80,000 the current WFF entitlement is around $5k per annum. Capitalising five years of this would give around $20,000 – a significant contribution towards a deposit.

    c. Families with more children would be entitled to higher WFF payments, but they would also likely be purchasing larger homes that would be higher than the entry level price points for Government Build Programme homes.

38. IRD figures indicate that around 5% of Auckland households receiving WFF have incomes over $90k, suggesting that few WFF recipients could afford a mortgage. 10% of WFF recipients outside of Auckland have an income above $80k, suggesting that there would be more scope for use outside of Auckland. Further work would be needed to determine whether these households could afford a home appropriate for their household size.

39. As the existing homeownership products are difficult to use in Auckland, it would be desirable for additional schemes to be accessible in Auckland.

Fiscal cost

40. The fiscal cost would also need to be taken into account. Capitalising payments would mean that rather than recognising payments on an annual basis, the full value of the payment would be recognised upfront. In theory, this policy would be cost neutral over the long term as it would be offset by small annual savings in WFF payments. However, the immediate expense to the crown of the full capitalised payment would flow through to the operating

balance and net debt. If demand were high, this could impact on the Government's ability to meet their Budget Responsibility rules.

Any work on capitalisation of WFF would need to take account of the wider welfare work programme.

41. Any work on capitalisation would need to be sequenced with other reforms. The Welfare Expert Advisory Group report discussed WFF and income adequacy. If you wish to progress capitalising WFF, we recommend you discuss the proposal with the Ministers of Social Development and Revenue.

Capitalising WFF would be administratively complex

42. It is likely that it would be extremely complex to administer. Aside from the existing WFF administration activities there would need to be processes developed to estimate future entitlement, methods to monitor and manage changes that might affect accuracy of the capitalised amount (both prospective and retrospective) and debt recovery.

Capitalising a portion of WFF

43. Capitalising only a portion of WFF could involve either capitalising a fraction of it, or only one component (such as Best Start or the In Work Tax Credit). Capitalising only a portion of WFF would reduce, but not eliminate some of the downsides of full capitalisation. For example, it would reduce the risk of poverty for households that make use of capitalisation. However, many of the other limitations would be unchanged, such as the ability to use it in Auckland and the administrative complexity.

Using the WFF criteria as the eligibility criteria for a new deposit subsidy

44. An alternative to capitalising would be to use the Working for Families eligibility criteria to develop a new deposit subsidy for first home buyers. This could potentially be done as an extension of HomeStart, or a subsidy that is administratively independent of both HomeStart and WFF.

45. This would be an option if funding were available. Eligibility criteria could vary by income, region, and household type. The criteria could be modelled off the Working for Families and accommodation supplement criteria, but would need to have different thresholds to these to target households able to afford a first home in a fair way across regions.

Recommended option: Investigate reducing the Welcome Home Loan and HomeStart deposit requirements

46. Reducing the deposit requirement on Welcome Home Loans to 5%, and eliminating the 10% deposit requirement on HomeStart grants would open similar opportunities to families as capitalising working for families. Loans allow households to borrow against future income, and this would include the benefit they can expect to receive from WFF. Officials recommend exploring this as a quick and low cost way of reducing the deposit barrier for first home buyers.

47. We will also further investigate the extent to which banks take into account Working for Families tax credits in their lending criteria, to ensure that they are taking it adequately into account.

Making additional support available for only Government Build programme versus other homes

48. The homes that additional support could be used on could include Government Build Programme homes, all new builds below price thresholds, or existing homes below price thresholds.

49. Officials' initial advice is that it would be best to make any support available for all new builds below a price threshold, whether or not they are part of the Government's Build Programme. Only making the support available for homes provided under the Government Build Programme would distort the development market, such as by incentivising developers to

access the Government Build Programme underwrite so that buyers can access the grant. It could have a chilling effect on private sector construction if first home buyers stop buying homes aside from those provided under the Government Build Programme, undermining the Government's objective of encouraging the private sector to deliver more affordable homes.

50. There could be a case to make some changes available for existing homes as well. Making support unavailable for existing homes would make it difficult to use in regional areas where few new homes are built. However, these areas are already well served by HomeStart and Welcome Home Loans. We can provide further advice on the case to include existing homes as you narrow down your preferred approach.

The scope and timeline for of any potential changes

Timelines

51. Funding and resourcing would be needed for any expansion of homeownership subsidies. Modest changes to HomeStart and Welcome Home Loans, such as adjusting the deposit threshold, may be able to be done within a matter of months, depending on the availability of funding within the existing appropriations.

52. More extensive changes, such as increasing the amount of the deposit subsidy for new builds using the eligibility criteria for Working for Families as a starting point, would require more time to develop and potentially funding from Budget 2020. The length of time to develop it would depend on where it sits against other priorities and the available funding, but could be a matter of several months or longer.

53. Developing a scheme capitalising Working for Families would take significant time and resourcing and may require funding from Budget 2020. It would likely also require legislative change to the Income Tax Act 2007. Therefore it would likely take at least a year to develop the policy and implement it.

Avoiding disrupting demand for homes

54. We recommend delaying the announcement of any major new support schemes until they are near to being implemented. A gap between announcement and implementation will incentivise people to delay buying a home until the scheme is available, making it more difficult to sell Government Build Programme homes.

Recommended approach

55. If you wish to support first home buyers, officials recommend:

    a. Implementing the affordable housing fund to make progressive home ownership schemes more widely available.

    b. Investigating changes to the HomeStart and Welcome Home Loan settings to make them better work for first home buyers. As a starting point, this could involve reconsidering the deposit requirement and the issue of having multiple borrowers. Reducing the deposit requirement on Welcome Home Loans could provide a relatively quick and low cost way of providing further assistance with the deposit barrier. This would effectively allow households to borrow more against their future income, including Working for Families benefits.

    c. Officials further investigate options to provide an additional deposit subsidy to mid-income families, either as an extension of HomeStart or as a new scheme, and what the HomeStart underspend can be used for.

Consultation

56. MSD, IRD and Treasury have provided input into capitalising Working for Families.

57. Treasury has provided input into the limitations on using the HomeStart underspend.

Next steps

58. We will discuss this paper with you at the officials meeting on Monday 13 May.

Annexes

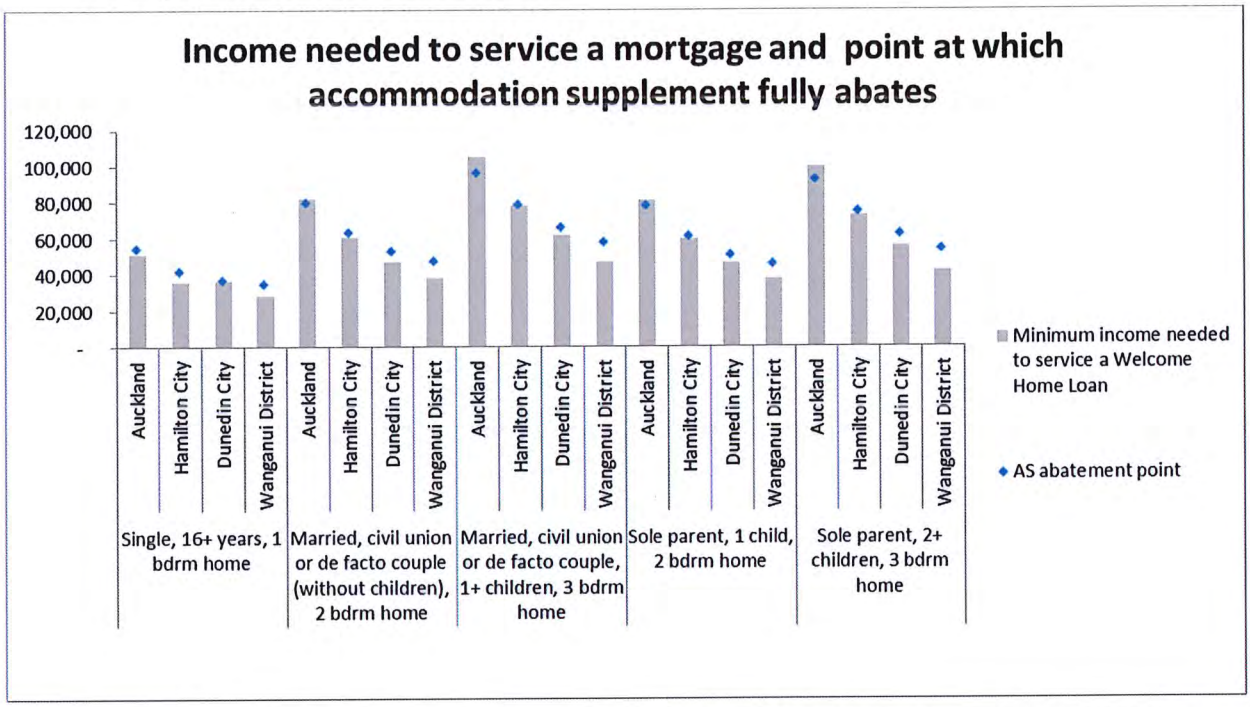
59. Annex A: Capitalising the Accommodation Supplement

Annex A: Capitalising accommodation supplement

60. We briefly cover capitalising the accommodation supplement (AS) for the purchase of a first home here for completeness.

61. Capitalising the accommodation supplement has many of the same challenges as capitalising working for families, including creating a risk of families later falling into poverty, the high risk of overpayment or underpayment, and administrative complexity.

62. However, capitalising AS is even more challenging than capitalising WFF because the income abatement points for the AS are lower and vary by region. There are very few households who have enough income to service a mortgage but receive AS, because by its nature it is targeted towards people who would struggle to pay their housing costs. The chart below illustrates this across family types in four cities. In addition, the cash asset thresholds mean households who save more than $8100 (single people) or $16200 (couples) towards are deposit will lose eligibility for AS.



Note: Assumes the family buys a lower quartile home with a 90% LVR mortgage on a 30 year term with a 5.8% interest rate.