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The persistence of debt to government

Where debt to MSD, MoJ, and IR lasts beyond four years

**SOCIAL
WELLBEING
AGENCY**

TOI HAU
TĀNGATA



Te Kāwanatanga o Aotearoa
New Zealand Government

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Debt to government shows significant persistence

Debt is an important feature of many countries' financial systems and plays a role in smoothing household expenditure. Government debt also has the purpose of enforcing social obligations (for example, child support debt collected by Inland Revenue ensures the costs of raising a child are borne by both parents; fines are imposed by the courts as a penalty for illegal activities and become a debt held by the Ministry of Justice).

In early 2022 we published our initial analysis of debt to government. This initial analysis focused on how often people owe debt to more than one government agency, and patterns of debt owed across three agencies: the Ministry of Social Development (MSD), the Ministry of Justice (MoJ), and Inland Revenue (IR). It found that:

- A total of 762,460 New Zealand residents owe \$4.68 billion of combined debt to MSD, MoJ, and IR.
- Of these people, more than a quarter (28%) owe debt to two or more agencies, and 6 percent owe debt to all three.
- More than half of the debt owed to MSD, MoJ, and IR is owed by people with debt to more than one agency. The 6 percent of people with debt to all three agencies, owe 17 percent of the total debt.
- The distribution of debt is skewed: 47 percent of debtors owe less than \$1,000 and only 13 percent owe more than \$10,000.
- There are overlaps between different types of debt:
 - Benefit overpayment and recoverable assistance debt to MSD overlaps with child support and Working for Families (WFF) overpayment debt to IR, and fines debt to MoJ.
 - Fines debt to MoJ overlaps with debt to MSD, and child support and WFF overpayment debt to IR.
 - Income tax debt to IR overlaps with child support debt to IR.
- There are significant differences in the demographic characteristics of people with different types of debt.
 - Males are over-represented among people with income tax debt and liable parent child support debt to IR, and among people with fines debt to MoJ.
 - Females are over-represented among people with benefit overpayment and recoverable assistance debt to MSD, and among people with WFF overpayment debt to IR.
- Several debt types show evidence of persistence, with upwards of 70 percent of debtors being in debt for more than twelve months.

Following this initial work, conversations with the Department of the Prime Minister and Cabinet and with the cross-agency working group on debt identified the persistence of debt and its impact as an area needing further investigation.

This report examines debt persistence, by considering the 713,000 New Zealand residents who owed debt to MSD, MoJ, or IR in 2020 and examining debt records back nine years to 2012. This research also provides further insights on individuals and families who experience prolonged or persistent debt. We found that:

- More than 85 percent of people who owe debt to government have owed debt for at least one year. More than 45 percent have owed debt for at least four years.
- More than two-fifths (40 percent) of people with debt to MSD, fines debt to MoJ, or child support debt to IR had at least one debt that had lasted for more than four years.
- There are significant differences in how debt types are managed. The WFF and income tax debt types have a significant decrease in persistence after two years that the other debt types do not have.
- For people who owe more than one type of debt, close to half of their debt is owed to IR, but only 20 percent of repayments are made to IR. This means that the division of their repayments across debt types may not match the mixture of debt that they owe.
- Repayments are not keeping up with the creation of new debt. In 2020, repayments were about three-quarters of new debt created.
- Debt persistence disproportionately affects people with low income, people receiving main benefits, and people who owe debt to more than one government agency.
- New Zealand residents show different patterns from those non-residents who owe debt to government.

Results from this analysis are not intended to aid debt recovery, but to fill gaps in understanding about the causes and characteristics of persistent debt and debtors.

Overview of debt types and debtors

Table 1 sets out the range of debt types people owe to government, grouped by four broad causes. Data on only a subset of debt types was available for, and included in, our analysis. Those debt types in italics are excluded from this analysis.

Table 1: Debt types grouped by broad cause

Overpayment	Unmet Obligation	Loan	Punitive
<ul style="list-style-type: none"> • Benefit overpayment • Working for Families • <i>Receiving Carer – Child Support</i> 	<ul style="list-style-type: none"> • Income Tax • Liable Parent – Child Support • Overdue Student Loan • Family Court Contribution Orders 	<ul style="list-style-type: none"> • Recoverable Grants • <i>Student loan</i> • <i>Legal aid</i> 	<ul style="list-style-type: none"> • Fines • <i>Reparations to victims of crime</i>

Table 2 sets out the number of people who owe debt to government that has persisted for at least one, four, or eight years. It shows that:

- A significant number of people in New Zealand owe persistent debt to government (for example, more than 10% of adults have debt to MSD that has lasted at least one year).
- Debt has significant persistence. Of those people who have debt with 1+ years of persistence approximately half have debt with 4+ years of persistence.

Table 2: Debtors with persistent debt

Debt Type	1+ Years	4+ Years	8+ Years
Benefit debt (MSD)	373,635	225,075	133,113
Fines debt (MoJ)	180,315	108,801	58,176
Liable Parent – Child support (IR)	57,867	30,738	17,541
Working for Families (IR)	30,633	5,385	1,557
Income tax (IR)	130,593	13,236	4,851
Overdue student loan (IR)	25,947 ¹	11,349	4,857

Several dynamics contribute to persistence

The persistence of debt to government is caused by a range of factors. In addition to factors that are particular to the individual and their circumstances (such as, ability to repay, income, and other debts), there are a range of factors that are the result of government agencies' policies and practices. Our research has identified three dynamics that are likely to have significant effect on the persistence of debt:

- Differences in how agencies manage debt means that debt persistence varies between agencies.
- Repayment arrangements do not align to where debt is owed.
- Repayments are inadequate to address debt owed, and many debtors take on new debt.

There are differences in how agencies manage debt

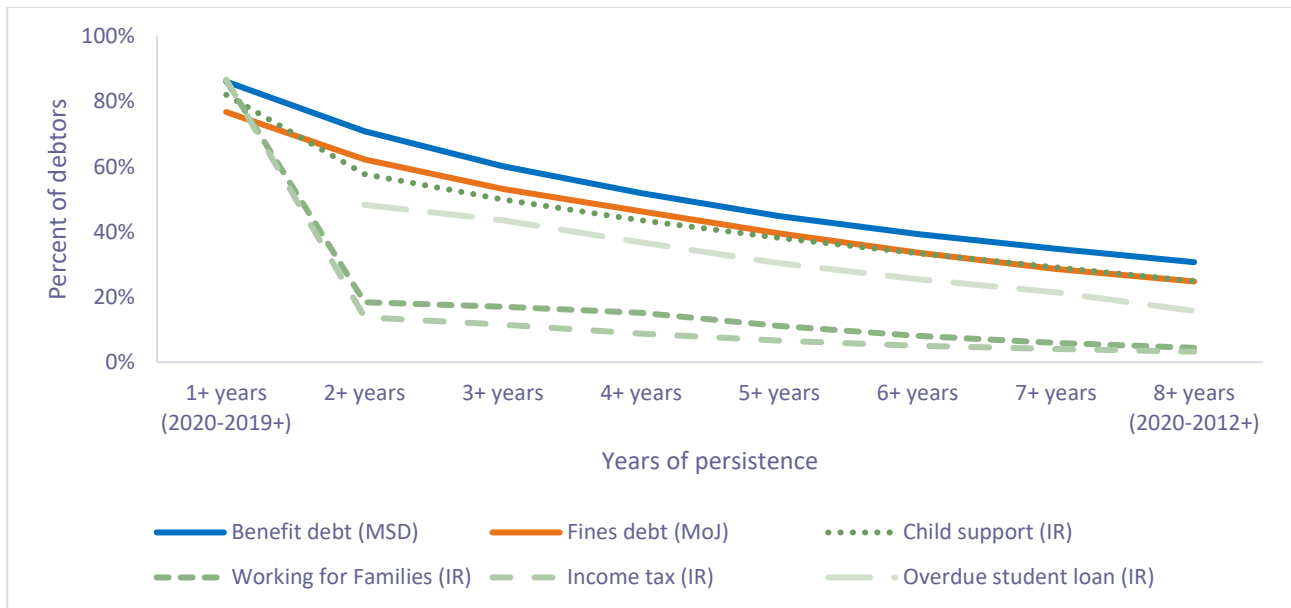
Once debt has been created, agencies' debt management practices determine how debt is recovered and when it can be written off. Operational practices around debt are often determined by a mixture of legislation, policy, practice, and available technology.

Figure 1 shows how the distribution of debt persistence varies between the different types of debt. It shows two broad patterns for debt types: persistence for benefit, fine, and child support

¹ Persistence of overdue student loan debt at 2+ years has been estimated. Exact numbers were not available due to a change in data storage environment at IR.

debts decreases smoothly over time. In contrast, persistence for income tax and WFF shows a sharp decrease after two years.

Figure 1: Percent of resident debtors with persistent debt in 2020 by type



Conversations with subject matter experts at MSD, MoJ, and IR highlights that some of this will be driven by differences in IR’s debt management policies. MSD is required to collect everything and has limited write off powers, while IR’s debt management policies allow it to write off debt that is not economical to collect.

Another factor driving this pattern is that several types of debt (including benefit, fines, and child support debt) disproportionately fall on people with limited incomes who make fixed repayments. This has been a deliberate choice by government to reduce the extent to which repayments cause undue financial hardship on debtors.

Figure 1 should not be interpreted as suggesting that more widespread write-off of debt to government would be desirable. Considering Figure 1 and Table 2 together, it is important to note that the three debt types with significant reductions in persistence are also the less common debt types. This means that the costs of applying a similar write-off policy to benefit, fine, and child support debt would be much more than the costs of the current write off practices.

It is also important to consider that these different debt types arise for different purposes, and that debt write-offs can create incentives and behaviours that are not aligned with the original purpose of the debt.

Repayments do not align to balances owing

More than a quarter (26 percent) of people with debt to MSD, MoJ, and IR owe debt to more than one agency. Figure 2 shows the distribution of people by the agency or agencies they owe debt to.

Figure 2: Debtors with debt to multiple agencies

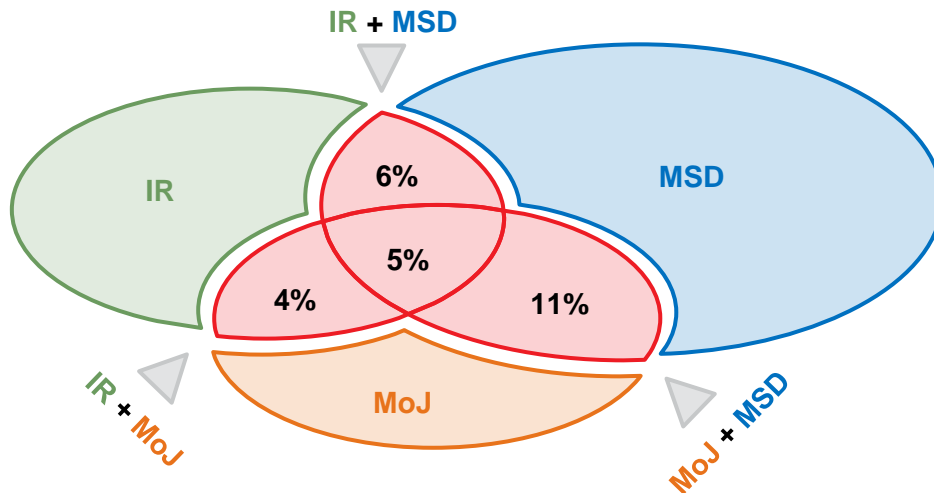
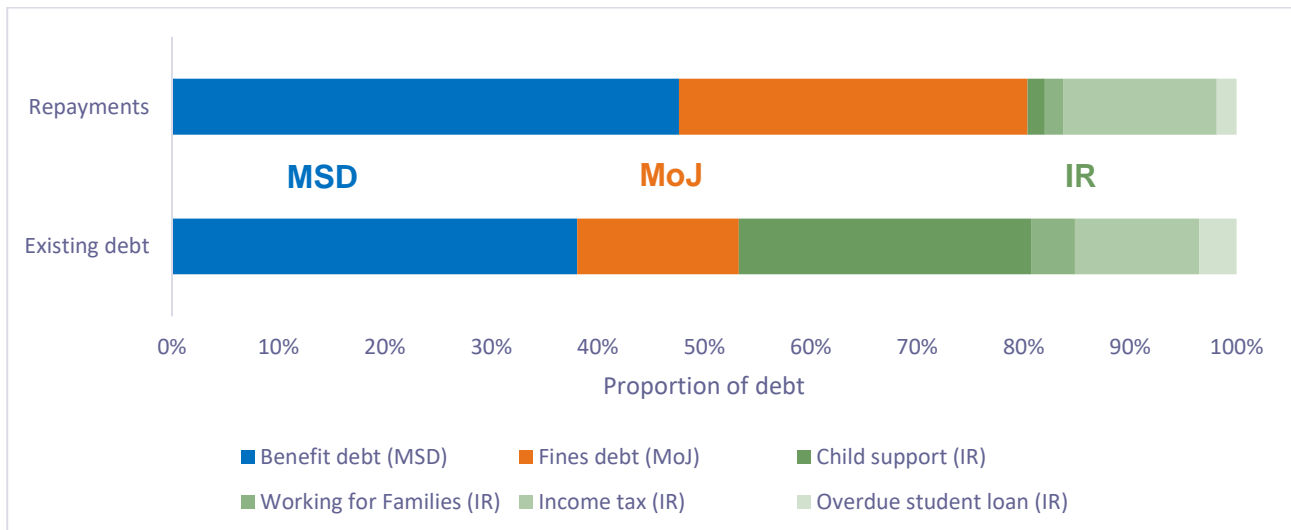


Figure 3 gives the distribution of existing debt and the distribution of repayments for those people with debt to more than one agency. It shows that almost half of debt owed by this group is due to IR, but 80% of repayments are made to MSD and MoJ.

Figure 3: Debt distribution for existing debt and repayments



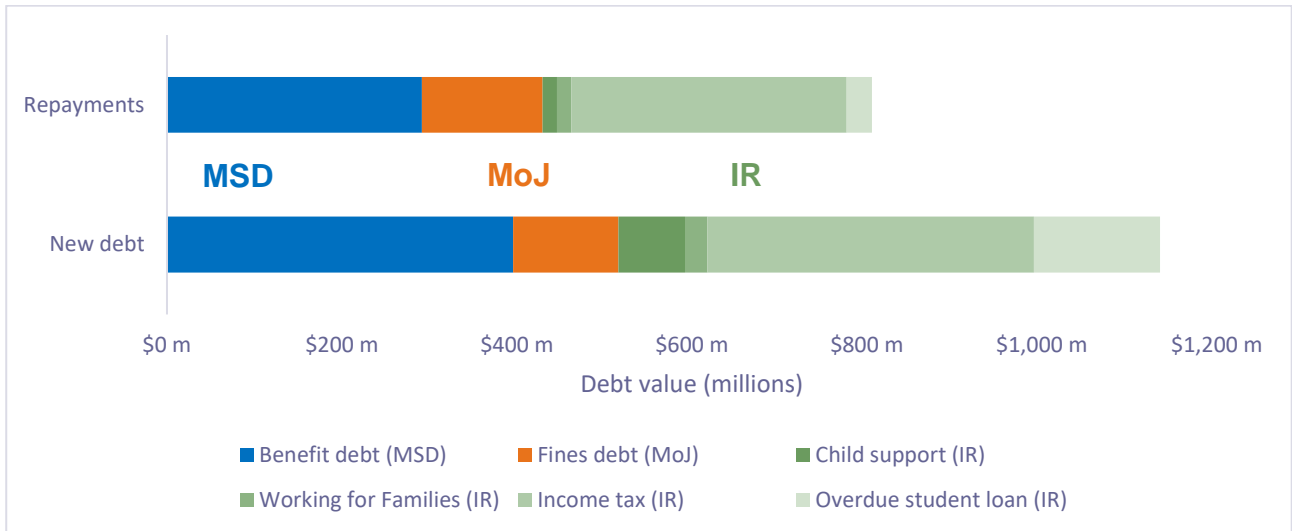
The consistency of repayments to MSD and MoJ is likely to be driven by repayments made by beneficiaries. This is because for people receiving a main benefit, repayments to MSD and payments of fines can be automatically deducted from the benefit prior to payment to the recipient.

However, interest and penalties are charged on debt to IR (where minimal repayments are made) while debt to MSD and fines debt attracts neither interest nor penalties. This unequal distribution of repayments may therefore result in debtors making greater overall repayments.

Repayments are inadequate

For a significant group of debtors, their repayments are not sufficient to address their debt in a timely manner. Figure 4 gives the distribution of borrowing and repayment in 2020 by agency and debt type. It shows that repayments in 2020 were about three-quarters of the new debt created.

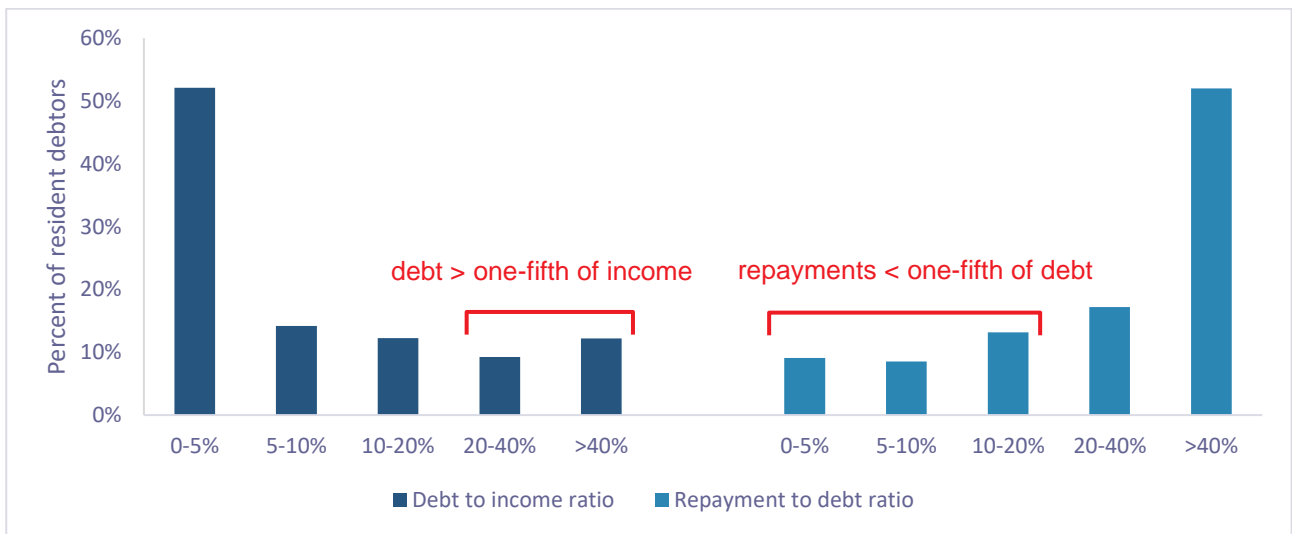
Figure 4 Debt distribution for repayment and new debt



Investigation of each debt type shows that only fines debt had repayments similar to new debt created in 2020. For all other debt types repayments are less than 84 percent of new debt created (and for child support and overdue student loans repayments were close to 20 percent of new debt created).

Another way to consider the adequacy of repayments is to consider the ratio of repayments, debt, and income. Figure 5 gives the distribution of debtors by these ratios.

Figure 5: Ratios between repayments, debt, and income



As we might hope, the majority of debtors have debts that are small compared to their income (far left bar, debt is 0-5% of income) and also the majority of debtors repay much of their debt each year (far right bar, repayments are at least 40% of debt balance owed).

However, for a significant percent of debtors the experience is very different. More than 20% of debtors owe debt that is at least one-fifth of their income. These debtors are unlikely to be able to afford the repayments necessary to clear their debt in a timely way. In addition, more than 30% of debtors repaid less than a fifth of their debt in 2020. At this rate these debtors will take at least five years to become debt free.

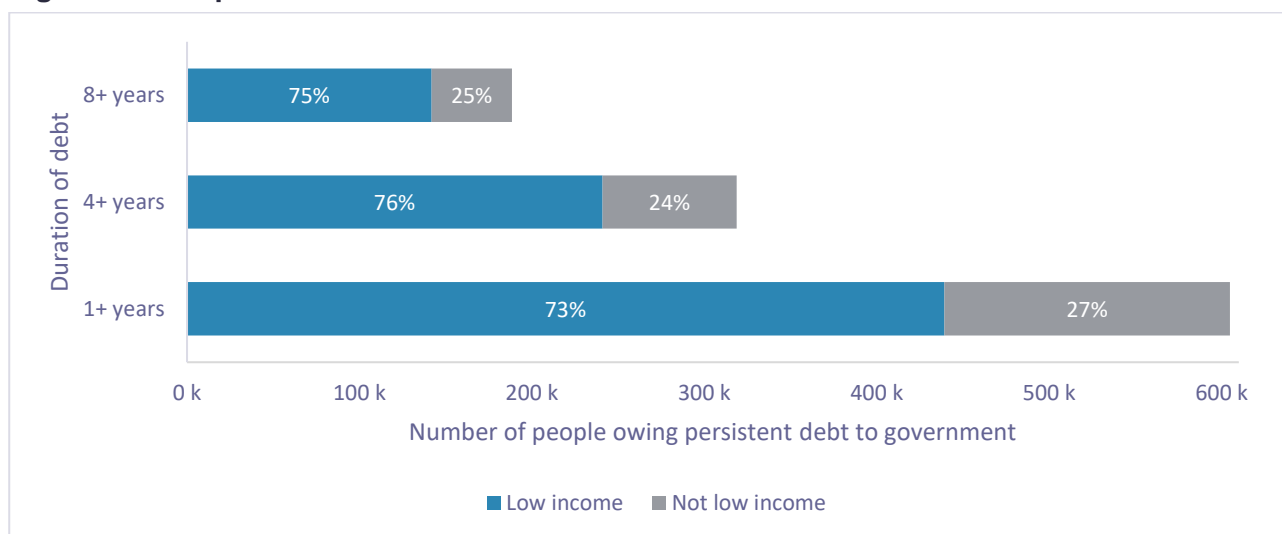
Persistent debt to government is a greater concern for specific groups

Persistent debt to government will likely be a greater concern where debtors also experience additional challenges or vulnerabilities. We examine debt persistence for three subgroups of debtors.

Three-quarters of those with persistent debt have low incomes

Income is an important first consideration because it determines the affordability of debt repayments. Figure 6 gives the number of people with one, four, and eight years of persistent debt to government by income. For this figure, we label people with an annual individual income less than \$45,000 as having low income.² It shows that three-quarters of those with persistent debt have low incomes and that this pattern applies whether we consider one, four, or eight years of persistence.

Figure 6: Debt persistence for low-income debtors



Persistent debt disproportionately affects those receiving government income support

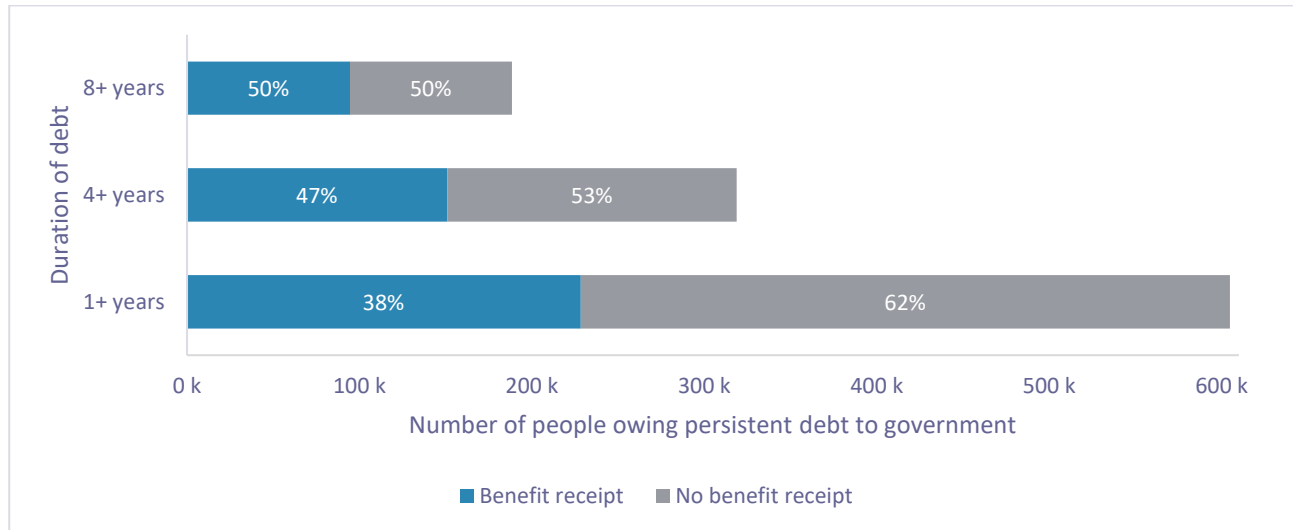
Benefit debt to MSD is the single largest category of debt. This debt is strongly associated with receipt of income support from MSD. About a third (35%) of people with debt to government in 2020 received a benefit for at least half of the year.³

² \$45,000 was calculated as the equivalent full-time, living wage in 2020 (\$22.10 per hour x 40 hours per week x 52 weeks per year).

³ This category overlaps with the low income category considered above. Most (90%) of people receiving a benefit also had low income. However, less than half (45%) of people with low income also received a benefit for more than half of 2020.

Figure 7 gives the number of people with one, four, and eight years of persistent debt to government by whether they received a main benefit for at least half of 2020. It shows that people receiving income support are more likely to have persistent debt, and are more likely to have debt that persists longer than four or eight years.

Figure 7: Debt persistence by receipt of income support

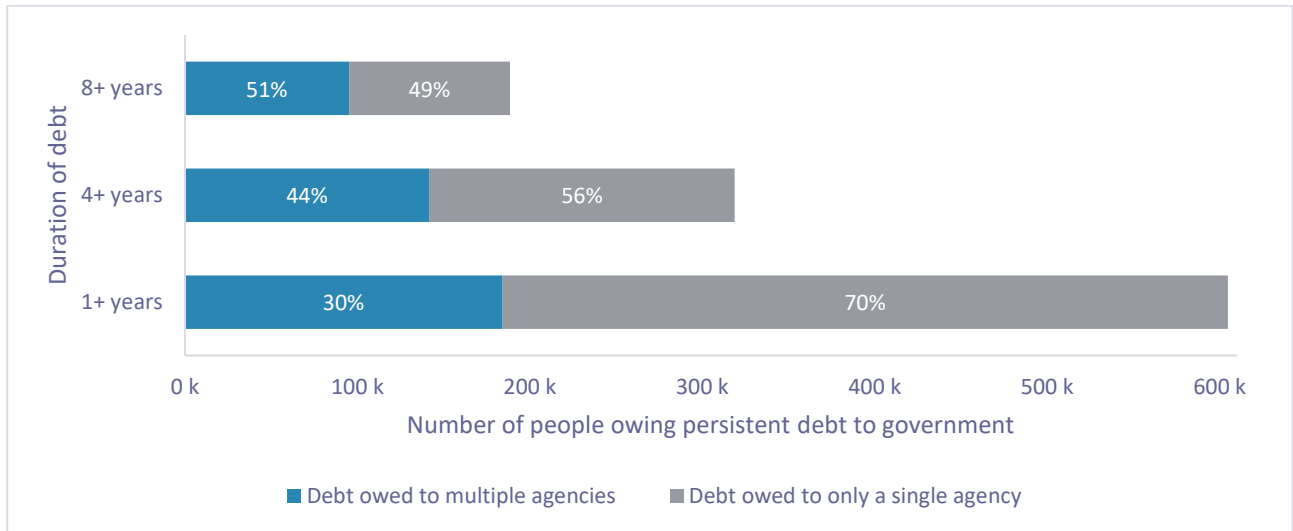


Persistence is a concern for people with debt to multiple agencies

Our previous research has shown that owing debt to more than one agency is associated with larger debt balances. Recall from Figure 2 that 26 percent of debtors owe debt to more than one agency. Where debt management is not coordinated between agencies, people who owe debt to more than one agency may be more likely to have persistent debt. For example, slow repayments to two agencies at the same time may be more costly than repaying each agency one after the other, especially where interest or penalties are charged.

Figure 8 gives the number of people with one, four, and eight years of persistent debt to government by whether they owe debt to multiple government agencies or only a single agency. It shows that people with debt to more than one agency are more likely to have persistent debt, and are more likely to have debt that persists longer than four or eight years. This affect is about twice as strong as the pattern we observe for benefit receipt.

Figure 8: Debt persistence by the number of agencies debt is owed to

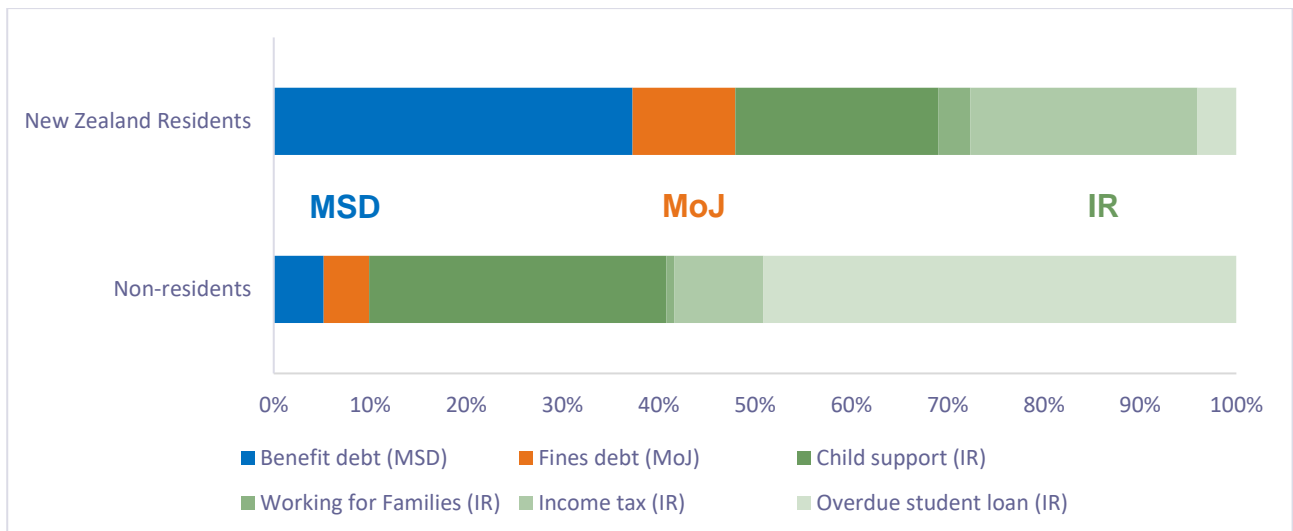


Non-residents are more likely to owe persistent debt

While the above results are all focused on New Zealand residents, our data also includes information on people who owe debt to government but are not resident in New Zealand.

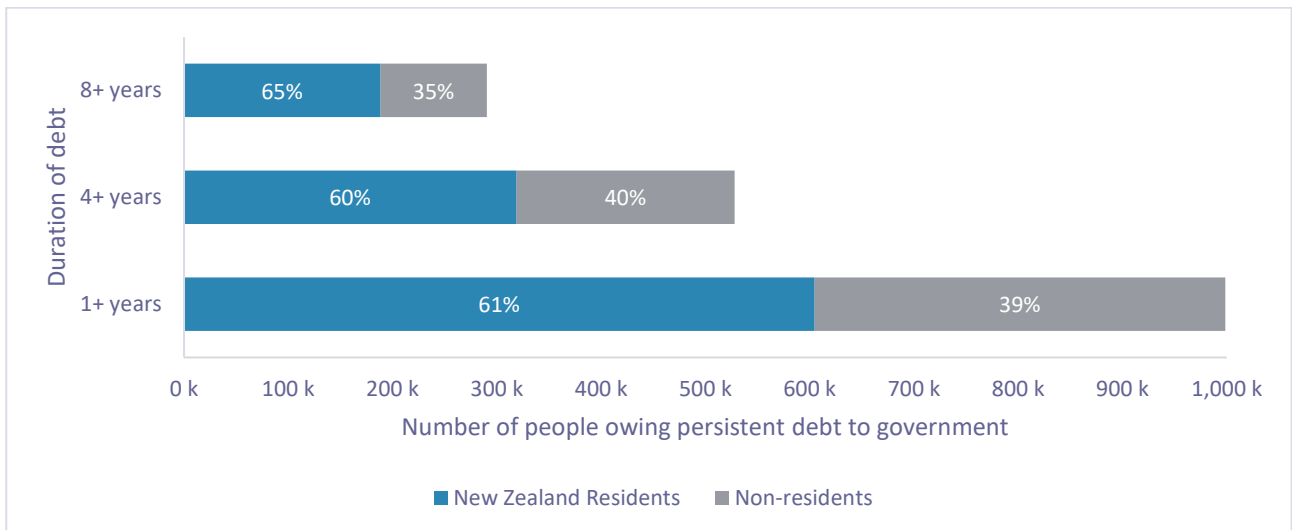
Figure 9 gives the distribution of the six debt types we consider by whether the debtor was resident in New Zealand during 2020. The bar for New Zealand residents is identical to the bar for existing debt in Figure 3. The figure shows that while debts to MSD and MoJ make up a significant percent of debt owed to government by New Zealand residents, the vast majority of debt owed by non-residents is child support and overdue student loans owed to IR.

Figure 9: Debt type distribution by New Zealand residence



We also observe significant persistence of debt by people who are not resident in New Zealand. Figure 10 gives the number of people with one, four, and eight years of persistent debt to government by whether they were resident in New Zealand during 2020. It shows that more a third of people with persistent debt to government are not residents in New Zealand.

Figure 10: Debt persistence for non-residents



Note that when considering non-residents, it is difficult for us to observe information like their income or whether they have dependent children. For New Zealand residents, persistence of debt can point to financial hardship or areas that debt management can be improved. However, for non-residents, persistence of debt may only indicate additional barriers to contacting non-residents and arranging repayments.

Appendix

Table 3 gives a short description of each of the debt types we consider in detail for our analysis.

Table 3 Debt type description

Agency	Debt Type	Description
MSD	Benefit debt Includes both overpayment of benefits and recoverable grants	Overpayment occurs when people receiving financial assistance from MSD receive payments they were not entitled to, or more of a payment they were entitled to, most often because of changes in circumstances (such as starting work, changes to hours worked, or changes in living arrangements). Recoverable grants occurs when people receive one-off grants to cover immediate, essential, or emergency expenses (such as car repairs or emergency medical treatment). Also includes advance payment of benefits to cover such costs.
Moj	Fines	This covers both infringement and court fines. Infringement fines come from issuing authorities such as local councils and the police. They become fines if they are not paid on time. Court fines arises when a judge or Justice of the Peace assigns then after a person has been found guilty of an offence.
IR	Liable Parent – Child Support debt	Occurs when a parent or carer applies to IR to collect child support payments from a child’s parent(s) and these payments are not made in full or on time.
IR	Working for Families (WFF) overpayment	Occurs when people receive more Working for Families (WFF) tax credits during the year than an end-of-year calculation shows they were entitled to.
IR	Income Tax debt	Occurs when people do not meet their obligations to pay income tax by the due date in the corresponding year.
IR	Overdue component of the Student Loan	Occurs when people do not meet their contracted obligation payments towards their student loan. This is determined by their income, when NZ based, or their student loan balance, when overseas based.

Debt to MSD and to IR can be further classified into fraud and non-fraud debt depending on whether the person intentionally mislead MSD or IR. Fraud debts are included in our analysis but are not separated out.