
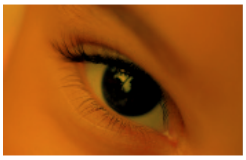

# Supporting family incomes in New Zealand and Australia

A background paper by
**Yun So and Susan St. John**
Child Poverty Action Group
2017

# About Child Poverty Action Group

Child Poverty Action Group (CPAG) is an independent charity working to eliminate child poverty in New Zealand through research, education and advocacy. CPAG believes that New Zealand's high rate of child poverty is not the result of economic necessity, but is due to policy neglect and a flawed ideological emphasis on economic incentives. Through research, CPAG highlights the position of tens of thousands of New Zealand children, and promotes public policies that address the underlying causes of the poverty they live in.

If you would like to support CPAG's work, please visit our website: www.cpag.org.nz

# About the authors

Yun So received her First Class Honour's degree in Economics and Bachelor's degree in Psychology and Sociology at the University of Auckland. She is interested in the areas of social policy and in exploring various dynamics in the labour market both at micro and macro level, in particular researching various impacts benefit systems can have on the labour market. Yun works as a researcher at CPAG, and as a research assistant at the  Retirement Policy and Research Centre.

Susan is co-editor of CPAG's flagship publication Our children, our choice: prioritites for policy (2014) and co-editor of Left Further Behind: How policies fail the poorest children in New Zealand (2011). Susan is co-author of the 2014 report The complexities of 'relationship' in the welfare system and the consequences for children and has recently led the CPAG campaign to "Fix Working for Families", authoring background papers relating to the failure of the Working for Families tax credit scheme.

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# Introduction

Both New Zealand and Australia assist families with children with a range of child-related tax credits that support family incomes.

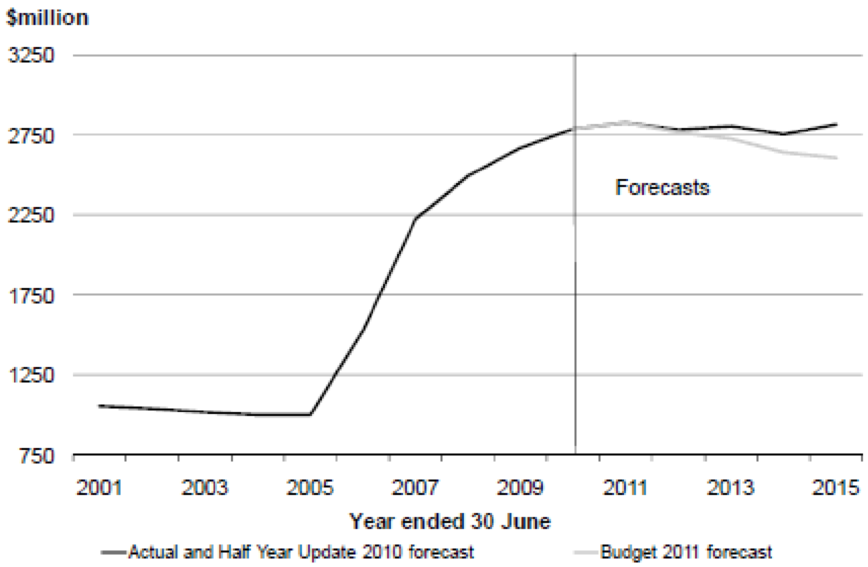
The New Zealand tax system is much less progressive than the system in Australia which taxes lower incomes much more generously; thus New Zealand has more reason for a sound and generous programme to support families with children. While there have been recent attempts in Australia to reduce their Family Tax Benefit programme by, for example, freezing rates and thresholds in 2016, it is still far more effective in supporting low income families than New Zealand's Working for Families tax credit package (WFF).

The introduction of WFF during 2005-2007 expanded spending compared to the former tax credits as Figure 1 shows. But that reflected the neglect of the system over many years, rising child poverty, and New Zealand falling well behind Australia. Much of the extra spending was merely an inflation catch-up.

Using Figure 1, in 2011 the New Zealand Government claimed the growth of expenditure from 2006 to 2011 was unsustainable, and justified some far reaching cuts to WFF:

"The cost of Working for Families has roughly doubled from about $1.5 billion in 2005/06 to about $2.8 billion this year [2011]. That kind of growth is no longer sustainable and without changes the scheme would quite quickly become unaffordable." [1]

**Figure 1. Cost of WFF from 2001- 2015**[2]




But WFF was not fully implemented until 2007/8. So the growth in spending was always going to be fast to start with, and then plateau. From 2008-10, nominal spending rises only with inflation and hence projections show a much slower, less alarming rate of growth.

In light of New Zealand's flat tax system and 15% GST on everything, a generous system to recognise the impact of family size on the capacity to pay tax is needed. Nevertheless in 2011, the Government cut WFF back, while sweetening the cuts with an inflation adjustment in 2012.

1 https://www.beehive.govt.nz/release/changes-better-target-working-families

2 http://www.treasury.govt.nz/budget/2011/execsumm/11.htm

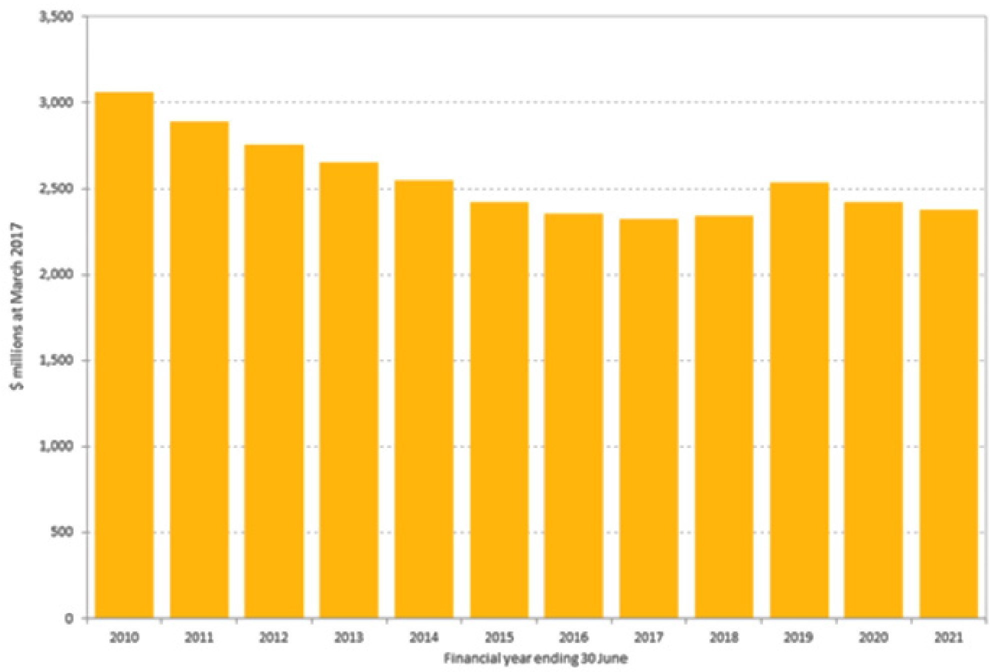
"Working for Families is a broad and generous scheme and that will remain the case. But these changes will better target payments towards lower income families, ensuring the scheme is sustainable into the future," (Hon Bill English as Minister of Finance, 2011).

"… the changes will better target Working for Families to those most in need. Lower income families and beneficiaries will be largely unaffected by these changes, and the majority of families currently receiving Working for Families will get an increase in their payments after 1 April 2012." (Hon Paula Bennett as Minister for Social Development, 2011)

Since 2012 there has been no inflation adjustment to any part of WFF. A fiscally neutral change was made in 2016 when the unindexed In-Work Tax Credit (IWTC) for working families was increased by $12.50 a week, but that was offset by an increase to the abatement rate to 22.5% and a reduction in the threshold to $36,350. The effect is to sharply increase the clawback of WFF as family income increases.

WFF has fallen sharply in real terms since 2010 as shown in Figure 2 and an additional $700 million per annum in 2017 is needed just to restore its 2010 original value. Another $500m is needed to remove the discrimination that denies at least $72.50 a week of the IWTC to the very worst-off families. Figure 2 shows a boost in year ended June 2019 from adjustments to the family tax credits from 1 April 2018 but that again erodes out to 2021.

**Figure 2. Real Expenditure on WFF from 2010-2021 (Budget 2017)**




Is New Zealand really too generous in the support of children and families? This background paper will investigate this question in greater depth using the real life case study of Sam and Maria to illustrate how families experience the system in New Zealand and how they might expect to be treated in Australia.

# A family's struggle

Maria and Sam have five children (aged 4, 7, 9, 12, and 14), and they live in a Housing New Zealand (HNZ) state house. Their house is very small for seven people but it has given them security for 10 years and, until recently, HNZ allowed them to pay an income related-rent of around $250 per week. Sam works 40 hours weekly for $16.80 per hour in a factory. Neither Maria or Sam drink, smoke or gamble, however, even with subsidised rent, they were struggling to feed their family. They were so desperate they took out loans with loan sharks just to pay for the basics. With hungry, active young boys, Sam and Maria were often at the Salvation Army for foodbank help.

Maria decided to go back to work five days a week at McDonalds for $15.80 an hour. This was far from easy for her with five young children. However, as Maria increased her working hours, their rent suddenly went up to $446 as her income meant they no longer qualified for an Income Related Rent (IRR). They lost $142 a week from their WFF and of course, Maria also had less time to care for her family, so everyone was under stress. Loans started mounting for the basics of school uniforms, stationery, school fees, food and childcare. Then, the family received a notice from HNZ that they needed to find a private rental since they were earning a higher rate. Stress mounted even more as Sam and Maria could see that a private rental would provide their family no security of tenure and disrupt their children's schooling.

Eventually, the family got behind in their rent payments.  Rent arrears of over $2000 accrued, and HNZ issued them with an eviction notice.  Maria's and Sam's working hours were also affected because so much time was spent at appointments with Work and Income New Zealand (WINZ), the community law office, the Ministsry of Social Development (MSD), HNZ and budgeting services. Eventually they were advised that Maria should stop work altogether because her income was the problem.

Maria has now cut work back to just one day a week to keep a foot in the door of employment, and to just keep their Income Related Rent. But that could be jeopardised if Sam ends up working overtime. They are paying less rent and get more WFF, but once again they cannot survive on such a low income. They have just pawned their wedding rings and are attempting to withdraw Sam's small KiwiSaver fund under hardship provisions.

After very time-consuming negotiations, HNZ agreed that the eviction would be waived and WINZ agreed to lend them the money to repay the arrears. They were not so lucky with their request for help with food.  A food grant that was approved three weeks ago was declined.  Why? Sam had just got a 20 cents per hour increase in income that disqualified them.

This brief paper unpicks the reasons why Sam and Maria[3] are struggling and shows how they would be treated in Australia.

3 This case study is found here http://thedailyblog.co.nz/2017/03/19/what-would-you-do-prime-minister-english/

# What happens if Maria works eight hours at the minimum wage?

## New Zealand

As shown in Table 1, if Maria works eight hours a week at $15.80 per hour and Sam works 40 hours at a rate of $16.80, they have a combined annual gross income of $41,517 and receive a net income of $35,691. This amount is clearly insufficient to provide for a family with five children.

Hence, for this family, WFF tax credits are of utmost importance. The maximum annual entitlement a family with five children earning less than $36,350, is $23,556. WFF payments start reducing (abating) at 22.5 cents for each dollar of a family's income over $36,350. Sam and Maria's gross income is above the threshold, their WFF reduced to $22,393. Total disposable income for Maria and Sam's family is $58,084.

If they pay an income-related rent to Housing NZ (now $299 a week, $15,548 annual), their remaining annual income is only $42,536. On a per person basis this is $6,000 pa.

## Australia

Had this family been living in Australia[4], the circumstances would have been a lot different. The minimum wage in Australia is AUD $17.70, an amount that is higher than Sam's rate in New Zealand. Hence, an assumption will be made in this example that both will earn this minimum wage. Maria would not be paying any income tax, since the tax rate is 0% for those who earn below $A18,200. Table 1 shows their combined total gross income is A$44,179 and net income is A$40,642. This is much higher than the net income from working Sam and Maria's family would receive in New Zealand.

Moreover, this family would also be eligible for the Family Tax Benefit Part A (FTBA), for each of their children and Family Tax Benefit Part B (FTBB) a family payment that varies depending on the age of the youngest child. If the family's adjusted taxable income is between A$51,904 and A$94,316, then a clawback of 20 cents in the dollar of income applies. In total, Sam and Maria's family would receive A$28,901 for their five children with no abatement.

In addition to this, this family would also be eligible to receive Family Tax Benefit Part B. In Australia, if the primary earner's income is at or below the limit of A$100,000, FTB Part B will be assessed based on the secondary earner's income. The secondary earner can earn up to a maximum of A$5,475 each year. However, this payment is reduced by 20 cents for each dollar of income earned over A$5,475. Overall, this family would be eligible to receive further financial assistance of A$4,031.56, which gives a total disposable income of A$73,574.42. Per person this is just over A$10,000 per annum.

The National Rental Affordability Scheme (NRAS) in Australia provides people on low to moderate incomes with an opportunity to rent homes at a rate that is at least 20 per cent below market value rent. Suppose Sam and Maria were living in Melbourne which has one of the highest rental prices. The median rent for four bedroom house in Melbourne is A$430. Since Sam and Maria are eligible to apply for NRAS, they would have to pay A$344 for their weekly rent, costing A$17,888 annually.

4 https://www.humanservices.gov.au/sites/default/files/2017/03/co029-1703.pdf

After paying rent, this family would have A$55,686.

Clearly, even with a rent rate that is higher than paid by Maria's and Sam's family to HNZ the total disposable income for this family would be markedly greater in Australia. This reflects the generosity of the Australian system to support families with children.

## Would the living wage rate help?

Suppose both Maria and Sam earn the 2017 living wage rate (LWR) of $20.20 in New Zealand. As shown in the table, they have a total gross of NZ$50,419 and a total net income of $43,164.

At this gross income, Maria and Sam get $20,390 WFF, after abatement is applied. This is a total loss of $2,003 (annual) of WFF. Sam and Maria's total disposable income after receiving WFF, is $63,554.

Since Sam works at a higher wage rate, the family will have to pay a higher rent of $442 per week to HNZ. The annual rent increases to $22,984.00, and the family's total after rent disposable income is $40,570. The final disposable income for Sam and Maria in this case, is significantly lower than the final amount explored in Case 1 ($42,536).

While the LWR would help many workers in New Zealand, Sam and Maria's case highlights how the tax credit system and housing support schemes can interact to a family's disadvantage.

**Postscript**: The Budget 2017 has promised that low-income working families especially with several young children will get a boost from 1 April 2018, reflected in increased spending on WFF in Chart 1 for 2018/19 and Table 2.

Large young families like Sam and Maria will gain, but they will find that they will lose their WFF more quickly than before, as the clawback is increased to 25% and the threshold is reduced to $35,000. If they qualify for an Accommodation Supplement (AS) and Sam has a student loan, they will face very high effective marginal tax rates over long income ranges.[5]

5 Tax (17.5%) ACC (1.2%) Accommodation supplement (25%), WFF (25%), student loan repayment (12%) KiwiSaver3% combine to give EMTRs of up to nearly 85%.

**Table 1: Total Disposable Income for a Family 2 Adults, Five Children**

| | Hourly Rate | Hours Per Week | Gross Per Week | Annual Gross | Tax Rate | Tax Amount | Net | Family Support | | Total Disposable (Annual) | Total Disposable After Paying Rent |
|---|---|---|---|---|---|---|---|---|---|---|---|
| ***New Zealand*** | | | | | | | | Working For Families Tax Credit | | $58,084.41 | $42,536.41 |
| Case 1. Min. wage | | | | | | | | | | | |
| Maria | $15.80 | 8 | $126.40 | $6,572.80 | *10.5% | $690.14 | $5,882.66 | $22,392.95 | | | |
| Sam | $16.80 | 40 | $672.00 | $34,944.00 | *10.5% & 17.5% | $5,135.20 | $29,808.80 | | | | |
| Total | $32.60 | 48 | $798.40 | $41,516.80 | | $5,825.34 | $35,691.46 | | | | |
| Case 2. Living wage rate | | | | | | | | Working For Families Tax Credit | | $63,553.97 | $40,569.97 |
| Maria | $20.20 | 8 | $161.60 | $8,403.20 | 10.50% | $882.34 | $7,520.86 | $20,389.91 | | | |
| Sam | $20.20 | 40 | $808.00 | $42,016.00 | 10.5% & 17.5% | $6,372.80 | $35,643.20 | | | | |
| Total | $40.40 | 48 | $969.60 | $50,419.20 | | $7,255.14 | $43,164.06 | | | | |
| ***Australia*** | | | | | | | | Family Benefit Part A | Family Benefit Part B | $73,574.42 | $55,686.42 |
| Maria | 17.7 | 8 | $141.60 | $7,363.20 | 0.00% | $0.00 | $7,363.20 | $28,900.70 | $4,031.56 | | |
| Sam | 17.7 | 40 | $708.00 | $36,816.00 | 19 cents for each $1 over $18,200 | $3,537.04 | $33,278.96 | | | | |
| Total | 35.4 | 48 | $849.60 | $44,179.20 | | $3,537.04 | $40,642.16 | $32,932.26 | | | |

**Table 2: Maximum Entitlements in New Zealand (Five Children) 2017/8**

| Age of Children | 14 years | 12 years | 9 years | 7 years | 4 years | Weekly Sum | Annual Sum |
|---|---|---|---|---|---|---|---|
| FTC (weekly) | $92.73 | $64.44 | $64.44 | $64.44 | $64.44 | $350.49 | $18,225.48 |
| IWTC (weekly) | | $72.50 | | $15.00 | $15.00 | $102.50 | $5,330.00 |
| Total (Max. Available) | | $294.11 | | $79.44 | $79.44 | $452.99 | $23,555.48 |
| **Maximum Entitlements 2018/19** | | | | | | | |
| Age of Children | 14 years | 12 years | 9 years | 7 years | 4 years | Weekly Sum | Annual Sum |
| FTC (weekly) | $102.00 | $91.25 | $91.25 | $91.25 | $91.25 | $467.00 | $24,284.00 |
| IWTC (weekly) | | $72.50 | | $15.00 | $15.00 | $102.50 | $5,330.00 |
| Total (Max. Available) | | $357.00 | | $106.25 | $106.25 | $569.50 | $29,614.00 |

**Table 3: Maximum Entitlements in Australia (Five Children)**

| Age of Children | 14 years | 12 years | 9 years | 7 years | 4 years | Weekly Sum | Annual Sum |
|---|---|---|---|---|---|---|---|
| Family Tax Benefit A | $133.23 | $105.64 | $105.64 | $105.64 | $105.64 | $555.78 | $28,900.70 |
| Family Tax Benefit B (depends on the age of the youngest child) | | | | | $84.79 | $84.79 | $4,409.20 |
| Total (Max. Available) | $133.23 | $105.64 | $105.64 | $105.64 | $190.43 | $640.57 | $33,309.89 |

# Glossary of terms

**Abatement rate:** The percentage of an extra earned gross dollar over the threshold that is 'clawed back'.The abatement rate for WFF in 2018 is 25% meaning that each extra dollar over the abatement threshold causes a loss of 25 cents of WFF.

**Effective Marginal Tax Rate (EMTR):** The effective marginal tax rate (EMTR) is the difference between an extra dollar of gross income and what is actually left in the hand after the combined effect of tax and other losses. For example, a dollar earned over the WFF threshold of $35,000 is not only taxed at 17.5% but 25% of that gross dollar is lost from WFF entitlements. This is like a marginal tax rate of 42.5% and hence is referred to as an effective marginal tax rate of 42.5%. If a parent also pays the minimum requirement for their student loan repayment and the minimum for KiwiSaver, and loses 25 cents for each extra dollar earned in accommodation supplement, then the EFTR becomes 17.5% + 3% + 25% + 25% + 12% = 83.5%. The value of a dollar earned over $35K is therefore only 16.5c. Loss of childcare subsidies and higher child support payments may also increase the EMTR still further for some parents.

**Family Tax Credit (FTC):** A per child per week amount that varies with age paid as the main part of Working for Families. In 2017 it is paid in full up to a total annual family gross income of $36,350,(reduced to $35,000 in 2018), then abated (reduced for extra earnings).

**In-Work Tax Credit (IWTC):** A part of Working for Families tax credits that is paid only to those who meet the minimum paid work requirements and are not on a benefit - a minimum of 30 hours per week for a couple; a minimum of 20 hours per week for a sole parent. The IWTC is currently paid at a maximum rate of $72.50 for one to three children (reduces over the maximum entitlement threshold). A family with more than three children receive a further $15 per child.

**Parental Tax Credit (PTC):** A part of Working for Families tax credits that is aimed at helping with the costs of a new baby for the first ten weeks after a baby's birth. Families can't receive both PTC and Paid Parental Leave. It is income-tested and paid up to a maximum of $220 per week, or payable as a lump sum.

**Minimum Family Tax Credit (MFTC):** A part of Working for Families tax credits that is paid only to those who meet the minimum paid work requirements and are not on a benefit, in order to bring family's net annual income to $23,764. The rate is variable and based on earnings and is not related to the number or ages of children. Paid work required - couple minimum 30 hours per week, single minimum 20 hours per week.

**Tax Credits:** A child-related tax "credit" is a payment made to eligible people who have dependent children in their care. The credits effectively reduce the amount of tax paid to recognise the costs of children. In some countries all families are helped by such payments, but in New Zealand, policy focuses on only low and middle income families, by abating or reducing child tax credits when total income exceeds a threshold.

**Working for Families (WFF):** New Zealand's system of child or family-related tax credits paid to low to middle income earners. WFF is made up of four separate kinds of tax credit.