CHiLD POVERTY ACTION GROUP

# CPAG Submission

## Working for Families Tax Credits Review[1]

**17th APRIL 2022**

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## Summary

CPAG calls on the government to urgently reform Working for Families (WFF). The unaddressed flaws since the inception of WFF have contributed to the high rates of severe child poverty in New Zealand. CPAG asks for the following changes:

1. **Rename WFF and redefine goals to be about the needs of children, not paid work.**

2. **Make WFF child-centric and decouple from all paid work requirements and the source of parental income. This entails extending the equivalent of the In-Work Tax Credit to all low-income children, whether their parents are on-benefit or not[2] and acknowledges the valuable unpaid work of parenting.**

3. **Index all WFF payments to wages annually (and to inflation when it exceeds wage growth) as is the case for NZ super.[3] Increase WFF thresholds from which WFF starts to reduce to restore the real value last set in 2018, and index annually. In 2022, it should be at least $47,000.**

4. **Make work pay by a range of alternative measures**

    a. **Decrease the WFF abatement rate to 20% to lower the effective marginal tax rates on low income 'working' families and improve the returns from work.**
    b. **Increase the threshold for abatement of benefits to 10 hours at the minimum wage—would be $212 in 2022**
    c. **Abandon the suggestion of WEAG to create another work incentive and explore other more targeted ways to help with the costs of paid work.**

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[1] Public Consultation on Working for Families Tax Credits - Ministry of Social Development (msd.govt.nz)

[2] **The cost of extending the inflation-adjusted IWTC ($82 per week) to all low income families is estimated to be between $480m and $600m depending on the numbers who currently miss out because they are on benefits or have no paid work or do not know about it (maybe 120-150,000 families) and the numbers who are entitled to extra because they have more than three children.**

[3] NZS is CPI indexed until the wage floor is reached and then rises with average wages ( the case for many years now) . When inflation exceeds wage growth cpi indexation increases the % of the net average wage but this rise is limited to 72.5% ( thereafter wage indexation would occur).

## 1. The renaming of WFF

The official documents released recently show that there is little understanding of the primacy role of WFF in prevention of child poverty. Thus, the consultative material [4], the basis for this submission, begins

> *"Working for Families tax credits are paid to low and middle-income families to help them raise their family and stay in work."*

There is no acknowledgement here of the vital role that WFF should play in the prevention of child poverty. The focus is lost because of the dual and conflicting objectives in WFF. These were set out in the 2021 summary document of the first stage of the WFF review[5] :

*WFF combines dual objectives of income adequacy and work incentives …*

2. WFF has two objectives:
   - to support income adequacy and reduce child poverty
   - to improve financial incentives for low-income earners to participate in the labour market.

*WFF has achieved its key objectives for some groups, but has resulted in mixed effectiveness for others*

3. WFF improved income adequacy in working households, increased the labour force participation of sole parents, but reduced it for secondary earners:
   - the introduction of WFF reduced child poverty in working households, though not in 'non-working' households
   - however, subsequent increases to the FTC in the Families Package in 2018 are estimated to have further significantly reduced poverty across working *and* 'non-working' households with children
   - WFF had relatively modest impacts on labour supply, with some evidence that it increased the labour force participation of predominantly low-income sole parents, and reduced the labour force participation of relatively higher-income secondary earners in couples with children.

CPAG strongly suggests that the review first discusses around the objectives of WFF. Fundamentally WFF is a tool to *prevent* child poverty and assist family income adequacy. It should be renamed so that it is not seen to be about 'working' where working is assumed to be one kind of work only, ie paid work. The work of parenting is vital (especially critical in an aging society) and can preclude significant attachment to the paid workforce.

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[4] working-for-families-tax-credits-consultation-guidance-material.pdf (msd.govt.nz)

[5] Working for Families Review update and options for Budget 2022 (msd.govt.nz)

The goals are conflicting: If WFF is supposed to address child poverty then withholding part of it to incentivise paid work and get off a benefit in logic must leave those who do not get this payment further behind in poverty. The tool, poverty itself, becomes the work incentive. But many poor families, who need a benefit are not in a position to respond to such an incentive through illness, sole parenthood, pandemics, disability, restructurings, natural disasters and therefore endure deeper poverty that makes their situation even more difficult. Those who can come off benefits will do so when they are ready.

To reflect its true purpose, we strongly advocate renaming WFF, and that this be part of the review consultation. We ask for more care is taken with the visuals in public discussion documents on WFF. The colour photos in the consultation material provided for this appear to be only Māori, Pacific, India or Asian. However, the vast majority of child recipients are Pākehā. This programme must be portrayed as inclusive of all New Zealand children (on an income tested basis).

## 2. Make WFF child-centric

The consultative material document (CM) [6]says

> *"The [In Work Tax Credit] is paid to families who are working to help them with raising a family and to help make sure families are better off working than if they were not working."*

We note that that may have been the intention, but not the reality of how the IWTC works on many levels.

- First it assumes that looking after children is not 'work'.
- Second, many beneficiaries are in some paid work but they are excluded because they get a part benefit.
- Third, caregivers not in 'paid work' of any kind, may get the IWTC based on some attachment to the paid work of the other parent.

In a muddle of changes over time, ACC claimants over 3 months or more duration can get the IWTC, but it will be denied to those on the proposed social insurance[7]. It is also paid to those getting the MFTC, which is surely like a replacement part welfare benefit. Workers who benefited from the wage subsidy during covid could get the IWTC but those on COVID payments could not (unless their partner had earned income). The IWTC is designed as an incentive to be off a benefit, rather than an incentive to work an extra hour. Its incentive effects if any rely on perpetuating poverty in beneficiary families. There are many better ways to make paid work 'pay'.

### The Family Tax Credit FTC

The FTC should be the only tax credit, incorporating the IWTC.

### In Work Tax Credit (IWTC)

[6] Working for Families Review update and options for Budget 2022 (msd.govt.nz)
[7] See CPAG submission on social insurance CPAG-SUI-Submission_Final-April2022.pdf

*"The IWTC pays $72.50 a week for families with 1 to 3 children (with an extra $15 a week for each fourth and following child)".*

The IWTC is not automatically indexed. It has not been adjusted since 2016. An Inflation adjustment suggests it should be $82 a week in 2022 and $17 each for the 4th and additional children

*"In-Work Tax Credit payments begin to reduce once a family's Family Tax Credit payments have reduced to zero. In-Work Tax Credit payments also reduce at the same rate of 27 cents for every dollar of income. In-Work Tax Credit is paid to 188,500 families in work."*

We note that some are on relatively high incomes because the IWTC abates last - so that the IWTC is not a payment targeted to the transition to full time paid work. The irony is that a full-time carer in a high-income family may be receiving the IWTC for her children when she has no attachment to the paid workforce. For such families the IWTC has nothing to do with providing work incentives. By supporting her with the IWTC she has more incentive not to work because the family can afford for her to be at home.

## The Minimum Family Tax Credit

*"The Minimum Family Tax Credit is an additional top-up for low-income working families with children, and makes sure their income is at least $632 a week after tax."*

We note that these families get the FTC and the IWTC on top of the MFTC. The MFTC is paid when families are working 20 or 30 hours a week and do not get a main benefit. As it is a top-up to a certain level of income, when a family's income increases by a dollar the Minimum Family Tax Credit reduces by a dollar ie 100% effective tax is applied.

The Minimum Family Tax Credit is a complex unnecessary add-on to WFF paid to only 3,900 low-income working families. It fosters the pretence that somehow the family is 'off benefit' when the MFTC has all the characteristics of a tightly targeted welfare benefit. It is past time for this clumsy mechanism to be abandoned in favour of allowing people to retain a part-benefit where appropriate.

## Best Start

*"The Best Start Tax Credit pays $65.15 a week to all families for the first year of a newborn's life. You cannot get Best Start and Paid Parental Leave for the same child at the same time. Generally, a family's Best Start payments for a child starts once any Paid Parental Leave finishes. For families with children aged 1 and 2 years Best Start payments start to reduce once a family's income is higher than $79,000 a year. For every dollar of income above this amount, Best Start payments reduce by 21 cents."*

Best Start adds further complications because it abates separately and overlaps other WFF abatements for some families. That extra dollar above $79,000, already taxed at 33% is further reduced by 27cents of WFF tax credits and maybe a student loan repayment 12%.

With Best Start abatement of 21 % the effective marginal tax rate is 93%. **If Best Start is part of WFF then it should be joined up and not abated separately.**

## 3. Index WFF to wages annually as is the case for NZ super.

The current arrangement where only part of the WFF is indexed and only once cumulative inflation is 5% is unfair and damaging. By 2022, families had had no adjustment since 2018.

All parts of WFF should be wage indexed annually 'like' core benefits and NZS. In NZS there is also protection for the unusual case where inflation exceeds wages.

Thus NZS is CPI indexed until the wage floor of 66% is reached and then rises with average wages (the case for many years now) . When inflation exceeds wage growth, CPI indexation increases the % of the net average wage but this rise is limited to 72.5% ( thereafter wage indexation would occur). A similar approach should be taken to WFF indexation.

The WFF thresholds from which WFF starts to reduce to restore the real value last set in 2018, and index annually. In 2022, it should be at least $47,000 or more if wage indexed. The IWTC has not been adjusted since 2016 and should be $82 per week at least and an extra $17 per child for the 4th and additional children.

## 4. Make work pay by a range of alternative measures,

The IWTC and the MFTC are very poor and ineffective work incentives as inferred by the review to date[8].

> *WFF has achieved its key objectives for some groups, but has resulted in mixed effectiveness for others*
>
> 3. WFF improved income adequacy in working households, increased the labour force participation of sole parents, but reduced it for secondary earners:
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>    - the introduction of WFF reduced child poverty in working households, though not in 'non-working' households
>    - however, subsequent increases to the FTC in the Families Package in 2018 are estimated to have further significantly reduced poverty across working *and* 'non-working' households with children
>    - WFF had relatively modest impacts on labour supply, with some evidence that it increased the labour force participation of predominantly low-income sole parents, and reduced the labour force participation of relatively higher-income secondary earners in couples with children.

There are far better and effective ways to make working for an extra dollar worthwhile. These could include: reducing public transport costs; increasing subsidies for childcare; and reducing school costs. Reducing effective marginal tax rates is also critical.

[8] Working for Families Review update and options for Budget 2022 (msd.govt.nz)

There are changes to WFF and to the abatement of benefits that would improve incentives. CPAG suggests

a. Decrease the WFF abatement rate to 20% to lower the effective marginal tax rates on low income ‘working’ families and improve the returns from work.
b. Increase the threshold for abatement of benefits to 10 hours at the minimum wage—would be $212 in 2022.

CPAG cautions against the WEAG suggestion to create another work incentive (the Earned income Tax Credit)[9] and can expand on this if it is indeed under consideration.

[9] 8. Honorary Associate Professor Susan St John • Child Poverty Action Group (cpag.org.nz)