The impact of changes to Working for Families in the 2011 budget

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Child Poverty Action Group (Inc) (CPAG) is a non-profit group formed in 1994, and made up of academics, researchers, practitioners and supporters. CPAG has a strong education and research role which enables it to contribute to better informed social policy to support children in Aotearoa New Zealand, specifically children who live in poverty. CPAG believes that our 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 are not already supporting CPAG and you would like to make a donation to assist with ongoing work, please contact us at the address below or through our website:** www.cpag.org.nz.

This is part of Child Poverty Action Group's series of background papers.

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Introduction

Working for Families (WFF) is an important programme of redistribution to families. The changes announced in the 2011 budget, while subtle and masked with soothing words about 'gradual change', move New Zealand in a disturbing direction.

In the run up to the 2011 budget, WFF was portrayed in the media by business commentators variously as middle-class welfare; a subsidy to employers; something 'nice to have'; and an ill thought out 'election bribe' that Labour had used to win the 2005 election. Yet, when compared to other countries', WFF has never been generous, and it is not nearly as generous, well-designed or inclusive as the equivalent Australian programme for families.

While the immediate changes from the budget may appear minor, working families on low incomes will have a very significant reduction in social assistance by 2018 and New Zealand will fall even further behind Australia.

Working for families today

The current (2011) level of the two major WFF tax credits, the Family Tax Credit (FTC) and the In Work Tax Credit (IWTC) are set out in Table 1. To be eligible for the IWTC the family must not be drawing an income-tested benefit, and must meet hours of paid work requirements of 20 hours for a sole parent and 30 hours for a couple.

Table 1: WFF weekly child payments from 1 April 2011- children under 13*

	Weekly Support*
Family Tax Credit, first child	$88
Family Tax Credit, each additional child	$61
In Work Tax Credit One- three children	$60
Plus $15 for each additional child	
Threshold, joint income	$36,827
Rate of abatement	20%

*Higher rates apply for older children. In 2011, the rates for a first child if 16 or over is $101, a subsequent child if 13-15 is $69, and a subsequent child 16 or over is $91. See www.ird.govt.nz

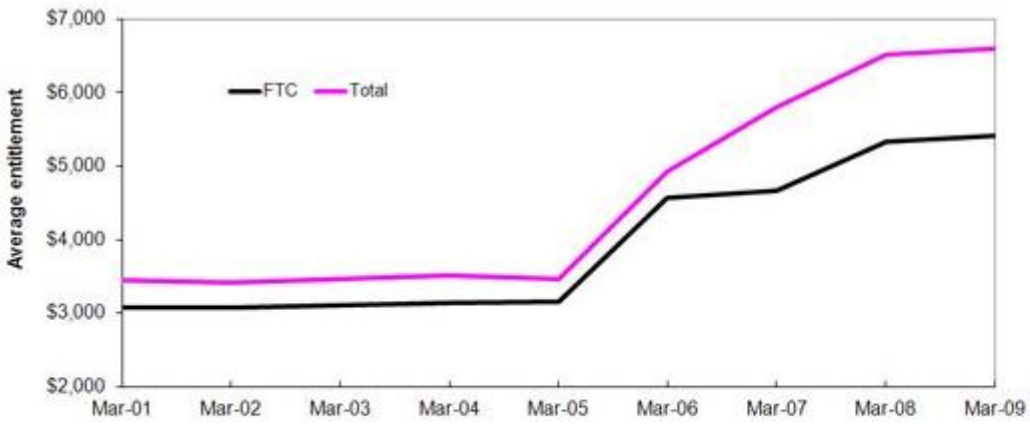
Adjustments for inflation for all parts, except the IWTC, occur when cumulative inflation exceeds 5%. The FTC abates from a family income of $36,827 at a rate of 20 cents for each extra dollar of income until it is all gone. If the family is also entitled to the IWTC, it starts to abate after the FTC, also at a rate of 20%. So, for example a family with 5 children can still access some part of the IWTC up to an income of $145,042.[1]

In 2008 CPAG estimated that approximately 185,000 children were in families not eligible for the IWTC (because their caregivers were on a benefit or did not meet the work requirements) and about 150,000 of these children were in severe and significant hardship. For this group there has been little relief, only exhortations for their parent or parents to get a

[1] See IRD http://www.ird.govt.nz/wff-tax-credits/entitlement/.

job, regardless of how inappropriate or difficult that might be. Yet it is possible for a caregiver in a 5-child, high-income family to be receiving the IWTC of up to $90 a week without any paid work requirement from the caregiver. The average difference in the treatment of those who are entitled to only the FTC is illustrated in Figure 1.

Figure 1: Working for Families Tax credits- Average per annum with and without the In Work Tax Credit



*Note: Other minor work related tax credits are included in total. Prior to the introduction of the IWTC in 2006, the Child Tax credit was paid, but only to those independent from the state, accounting for the difference up to 2006. **Source:** IRD website

2008 also marked the end of New Zealand's seven-year period of sustained economic growth and the beginning of the world-wide financial crisis and a protracted recession. In the difficult times of 2011 there are now around 230,000 children in families supported by a benefit. In the past, when low-wage parents needed state assistance for whatever reason, their Family Support could be expected to increase to compensate for their lower income. Now, because the IWTC is tied to paid work, family assistance for low-income families fails to provide this cushion. The caregiver loses $60 a week, or more for bigger families, just at the time when their children require more assistance, not less, to help avoid the economic and social exclusion that often accompanies joblessness.

The IWTC has proved hard to administer, and the take-up and compliance for low-income families is complex. As jobs are lost in the on-going recession, and in the aftermath of the Christchurch earthquake, family assistance no longer moderates the effects on children. New Zealand's remodelled welfare state increasingly provides a minimal subsistence safety net rather than a social security safeguard.

2011 Budget changes

As noted, in the lead-up to the 2011 budget, WFF was repeatedly painted in the media as too generous and in need of cutting in order to reduce the growth of the government's budget deficit. For example:

> *Dropping Working for Families, interest-free student loans and "free" early childcare would be the fastest way to reduce the budget deficit.* (Bernard Hickey, Sunday Herald 3rd April)

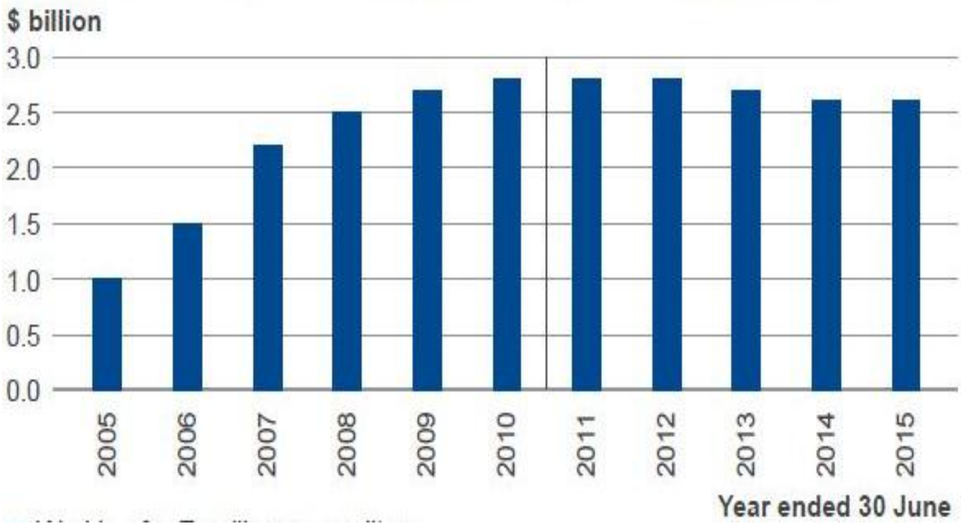
The Minister of Finance claimed:

> *The cost of Working for Families has roughly doubled from about $1.5 billion in 2005/06 to about $2.8 billion this year. That kind of growth is no longer sustainable and without changes the scheme would quite quickly become unaffordable*. (Bill English, Beehive news release, 19th May)

Is Working for Families unsustainable?

The data from the budget (Figure 2) tell a different story. The growth shown to 2009 was a result of WFF being phased in from 2005. WFF was in large part a catch up programme as family assistance had fallen far behind in real terms, and far behind comparable countries such as Australia.

Figure 2: Working for Families expenditure



Source: 2011 Budget

Far from showing rapid growth, nominal expenditure on WFF slowed markedly between 2009 and 2010 and was static between 2010 and 2011 and again between 2011 and this financial year 2012. This is surprising as one might have expected a growth in nominal expenditure given the GST inflation adjustments to WFF in 2010 and lower family incomes in the recession. The lack of expenditure growth may reflect in part that the threshold was frozen in 2010 and the IWTC is not indexed, but is likely also to reflect that as WFF is currently designed, the government actually saves money when low-income families lose work as they lose entitlement to the IWTC at the same time. A properly designed family assistance programme would provide a cushion in a recession and protect children.

In addition, under the 2011 budget, the WFF abatement threshold is to be reduced, from $36,827 in 2011 to $35,000 by 2018. The rate of loss of the WFF payments is to rise from 20% to 25% over the same period. The budget data shown in Figure 2 show an apparent modest decline until 2015 from these measures, but expenditures are in nominal dollars and do not show the full effect to 2018. Expenditure in 2018 looks on track to be about $2.25 billion.

There are no winners

The changes immediately post budget were claimed by the media to create 'winners and losers', with various business commentators approving of the changes, if not somewhat disappointed that they were not more drastic. For example, Simon Collins wrote in the NZ Herald that a low income 4-child family was to gain around $14 in 2012/13 while a top income family lost only around $8. This analysis was quite simplistic but added to the reassurance from the Government that the sacrifice required was minimal and manageable. Collins even found a family on a high income with multiple children proclaiming: 'Cut in tax credits good move' (NZ Herald 20th May).

Digging deeper into the figures reveals that, unfortunately, these changes signal a harsh change of direction, especially as the government has promised that there will be no further changes (presuming continuous election) until 2018.

A cumulative 21.6% inflation is expected based on budget forecasts out to 2018. If WFF had been fully indexed from 2011, roughly speaking by 2018 expenditure should be $3.4 billion. Thus, the expected spend of $2.25 billion represents a real cut of one third.

There are no winners even in 2012, despite some families getting a partial inflation adjustment. Beehive press releases gave the examples of how in 2012, a 3-child (10, 13, and 16 years old) family on $40,000 would get an increase of $4.12 a week. But, if their WFF had been inflation-adjusted they would have received $14. So they were losers, not winners. The official analysis goes no further than 2012.

Table 2 contrasts New Zealand's policy direction with that in Australia. The figures are illustrative only, using the example of a 1-child (under 15) family sitting at the current threshold of $36,827. The 2011 New Zealand budget projected a cumulative 5% 2-yearly inflation, that would lead to adjustment in 2012, 2014, 2016, and 2018, and the same method has been used to adjust Australia and New Zealand figures. There is no attempt in these figures to allow for the exchange rate which is currently very much in Australia's favour at around NZD$1.00 to AUD$0.76.

By 2018, the family on $36,827 is assumed to have its gross income increase only with the expected inflation. Table 2 shows that by 2018 this illustrative New Zealand low-income family is getting only $120 a week as compared to $180 with full indexation (or $167 if the IWTC remains unindexed). Using the budget's inflation forecast, the threshold of $35,000 in 2018 is the equivalent of $29,000 in 2011 dollars, only slightly over the current minimum wage.

One way to see how this impacts on our illustrative family is to ask, once the full changes have been implemented, what the family would be entitled to in 2011 dollars. Compared to the $148 they get now, they would get only $98 or a one third reduction. In other words, working families on low incomes can expect a very significant reduction in social assistance by 2018.

The contrast with Australia was already stark in 2011. A family in Australia gets the maximum of their tax credits in 2011 up to their higher threshold of AUD$45,114 whether or not the family is supported by a benefit. In 2018, the maximum per weekly payment will be AUD$206 per week and the full entitlement would be received up to AUD$55,000.

The 2011 New Zealand threshold is already only 81% of the Australian threshold or 61% if compared in New Zealand dollars. By the time we get to 2018 the New Zealand unadjusted threshold is 64% of the Australian threshold.

Table 2: Comparing New Zealand and Australia: 1 child family at current threshold

Year ended March	2,011	2012	2014	2016	2018
Threshold if indexed New Zealand	$36,827	$38,668	$40,602	$42,632	$44,763
Threshold as per 2011 Budget	$36,827	$36,377	$35,927	$35,477	$35,027
Rate of abatement	20%	21.25%	22.5%	23.75%	25%
Effect of inflation on wages	$36,827	$38,668	$40,602	$42,632	$44,763
1 child<15 if benefit paid	$88	$92	$97	$102	$107
1 child <15 full WFF if fully indexed	$148	$155	$163	$171	$180
Pre-budget indexation FTC only	$88	$92	$97	$102	$107
Pre budget FTC + unindexed IWTC	$148	$152	$157	$162	$167
Family on $36,827 WFF post budget, no indexation	$148	$143	$137	$130	$120
If new born and no PPL but PTC is paid*	$171.08	$166	$160	$153	$143
Australia					
Threshold annually indexed	$45,114	$47,368	$49,736	$52,223	$54,834
Rate of abatement	20%	20%	20%	20%	20%
Effect of inflation on wages	$45,112	$47,368	$49,736	$52,223	$54,834
Full tax credits 1 child (under 5)	$170	$178	$187	$196	$206
if child is new born and no PPL	$270	$283	$292	$301	$311

*PPL is Paid Parental Leave. The Parental Tax Credit (PTC) is up to $150 a week, depending on earned income, and is payable for up to eight weeks when a new baby is born. Like the IWTC, the PTC is not adjusted for inflation and is only paid if the family is not on a benefit.

The contrast is even more stark if the child is a newborn. For that first year of the child's life, a New Zealand family who today sits at the current threshold, by 2018 gets $143 per week or only $107 a week if they are on a benefit. The Australian family with a newborn, whether supported by a benefit or not, gets AUD$311 per week for that year.

Compounding this gap is the tax payable on low incomes, which is much lower in Australia. In addition, the after tax dollar buys more because their GST rate is still 10% compared to 15% in New Zealand. There are a range of other benefits for families, and over all, the Australian system is far more generous to middle and higher income families as well as to low income families, and to sole parents. Even recent budget changes in Australia have only impacted minimally, and largely focused on freezing the upper income threshold of AUD$150,000 as the cut out point for some payments. CPAG's 2011 update of *Left Behind,* 2008, gives more detail of Australia's policies and how they have evolved in the opposite direction to those in New Zealand.

Summary

Working for Families ‘reform’ is predicted by the Minister of Finance to save $448m to 2015 and clearly will save more by 2018. The saving however needs to be measured against what would have been the case if WFF had been fully indexed. If WFF was fully adjusted for inflation it should cost around $3.4 billion by 2018. The projection of around $2.25 billion by 2018 represents a substantial cut and takes New Zealand in the opposite direction to that of Australia, further undercutting the living standards of low and middle income families.

The official information about how individual families are affected are all for the 2012/13 financial year, and the figures are not inflation indexed, so that any negative effects are made to appear minimal. For this reason, political opposition is muted. If the same Government is in power for two more terms the incremental changes will be automatically implemented without the need for further parliamentary approval and it may be hard to reverse this unfortunate direction.

More worryingly, there has been no commitment from either major party to addressing the very low support of children in beneficiary families in New Zealand, nor the poor support for new-borns whose parents do not qualify for even the minimal Parental Tax Credit. The overwhelming complexity and design problems with WFF remain unexamined. The outlook for New Zealand’s poorest families and their children is bleak indeed.