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GROUP

Child Poverty Action Group

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Finance and Expenditure Select Committee

Parliament Buildings

Wellington

Submission:

Taxation (Income-sharing Tax Credit) Bill

This submission is made on behalf of CPAG.

Child Poverty Action Group (Inc) (CPAG) is a non-profit group formed in 1994, and made up of academics, activists, 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. http://www.cpag.org.nz/

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We wish to speak to this submission

Introduction

CPAG agrees that recognising the costs involved in raising children, and assisting single income families, and/or making it easier for one parent to remain at home, are worthwhile aims. However, ***income splitting*** is not an appropriate policy response. We outline our reasons for this below. First we wish to highlight some points from the Regulatory Impact Statement (RIS) issued by Inland Revenue in June this year.[1]

The RIS notes that for couples the decision about whether or not to stay home and care for children often comes down to finances. It states that one aim of the Bill is to "give families with children additional financial support" (p. 4), but then goes on to say that it does not focus on ensuring income adequacy for families from week to week. This suggests that the Bill's provisions are designed reward for a lifestyle choice rather than provide financial support to New Zealand families who need it the most. The RIS

[1] Available http://www.treasury.govt.nz/publications/informationreleases/ris/pdfs/ris-ird-istc-aug10.pdf.

also notes that the biggest benefits of this fiscally expensive ($450 million for children up to 18 years of age, plus annual operating costs of $3-4 million) tax break would go to higher single income households, while low-income households would get the least, and sole parent households – the group most likely to live in poverty – would get nothing (p. 4). We would add in the case of dual earner low-income households the benefits would be almost non-existent, as highlighted by the table in appendix of the RIS. We would also like to highlight the Treasury comment on income-splitting cited in the RIS.

> *The Treasury considers that the credit is poorly targeted and has negative distributional impacts, as 78 percent of the benefits are expected to accrue to families earning over $70,000 per annum. In addition, the fiscal cost of the proposal, estimated to be $502 million per annum by the end of the Budget 2011 forecast period, will be more than 45% of new spending in Budget 2011 if progressed. Given the substantial fiscal cost, and the minor economic benefits, Treasury does not recommend introducing an income-sharing tax credit.*

Along with Treasury, we are concerned about the negative distributional impacts, that is to say this measure will further contribute to New Zealand's already high levels of socioeconomic inequality.

We are also concerned that this is yet another Bill that may potentially breach New Zealand's human rights legislation.

We now outline our general concerns about the Bill.

1. ***Income splitting should not be a priority for scarce resources***. It is anticipated that income splitting will cost $450m, and as much as 43%, or $194 million of that cost is expected to go to households with incomes over $120,000 (Inland Revenue Department, 2008). If there is more money to be found for families, the urgent and critical problem is the meagre child-related support given to families on benefits and other low-income families. We also note that $450 million is equivalent to cuts to early childhood education announced in the 2010 budget. It seems perverse that the government is requiring some sole parent beneficiaries to seek work while it is cutting back on ECE funding, while an equivalent amount is essentially as a tax break to high-income families.

   Income splitting does not help low-income struggling families. It offers little or no assistance to low-income families, and none at all to sole parent families.

   Income splitting will have no effect on child poverty. The MSD's 2008 report on living standards shows that one in five New Zealand children are experiencing 'serious hardship' and 'unacceptably severe restrictions on their living standards' (Perry, 2009). $50 million could go a long way to alleviating this unacceptable level of child poverty.

2. ***Income splitting is not a recognition of the worth of the stay at home parent. The income splitting proposal is not actual income splitting and it reinforces stereotypes that do not help women.***[2]

   Under progressive taxation on an individual basis, there is an incentive to actual income splitting (putting assets in her name as the lower paid taxpayer, encouraging her to work part-time to assist in his business where appropriate). Under notional income splitting proposed in this Bill, there is no incentive for actual redistribution of household resources so that she has income and assets in her own right. Instead, there is an end of year calculation that results in a rebate. While it is good that this is paid to the caregiver (rather than as a tax offset to the primary earner's tax liability), the rebate cannot be taken as recognising the value of her care-giving. The higher his income the greater the value of her work on this measure.

   In this modern world, it is clear that women need to maintain some attachment to the workforce. Notional income splitting provides a clear disincentive for her to work part-time (and thus retain her skills) because she is taxed at the joint rate; and it provides an incentive for him to work more (usually higher paid) hours. The stereotypes that did not work well for women in past times are reinforced. This may be ultimately bad for both partners, and could result in a less productive workforce.

3. ***The problem has been mis-specified**.* There is said to be an inequity between the single earner and dual earner households on the same income. But like may not be compared to like here. For example: take two couples, with children, each on a total annual income of $100,000. In the first couple, there is is a single earner working 40 hours; and in the second, both parents work 40 hours. The second family thus has 40 hours of childcare to pay for while the first obtains those services on a tax-free basis from the stay at home parent. They are not in the same horizontal situation and should not be taxed the same.

4. ***Current arrangements provide an incentive for sharing of work and care**.* In the example above, suppose the second family shares work and care, so each parent works 20 hours and each cares for the children for 20 hours. The incentive to share on this basis while children are young may be healthy for society, and more in tune with the realities of the 21st century. It is illogical to argue, as in 1.2, that income splitting gives parents 'greater choice'. When faced with the choice of whether he works an extra 10 hours overtime a week or she does some work part-time (in a less skilled position often), the clear

[2] This section assumes for simplicity that 'he' is the breadwinner – obviously the roles can be reversed.

message is that it is better for him to work. This does not promote 'work-life balance'.

5. ***Working for families is the mechanism for transferring taxes paid by workers to caregivers.*** The income splitting proposal has not been thought through for those who get Working for Families as well.

6. ***Income splitting provides perverse incentives to claim partnership***. In contrast to the welfare system where it is disadvantageous to defined to be in a 'couple', this proposal offers an incentive for parents to be classified as in a partnership of some kind. Given the remarkable diversity and fluidity of families in New Zealand (see for example Families Commission, 2008), this policy may be very hard to administer (as is the current welfare system) . What happens for example when parents separate?

7. ***Income splitting is optional.*** Whose option will this be:- his or hers?

CPAG urges the government not to proceed with this costly and inequitable proposal. In 2001, the McLeod Tax Review (The Treasury, 2001, p. 98) concluded:

> *Income splitting creates as many problems as it solves. Also, it is not well targeted. Income splitting favours any couple with one income. Traditional families with an 'empty nest' and a well-paid principal earner would benefit; working sole parents with dependent children would not.*

References

Families Commission. (2008). the Kiwi Nest [Electronic Version] from http://www.nzfamilies.co.nz/sites/default/files/downloads/kiwi-nest.pdf.

Inland Revenue Department. (2008). *Income Splitting for Families with Children: A Government Tax Policy Discussion Document*. Wellington: Inland Revenue, available at: http://www.taxpolicy.ird.govt.nz/publications/files/incomesplittingdd.pdf.

Perry, B. (2009). *Non-income measures of material wellbeing and hardship:first results from the 2008 New Zealand Living Standards Survey, with international comparisons*. Wellington: Ministry of Social Development.

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