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# Complex Family Payments: What it Costs the Village to Raise a Child

Trisha Jha

THE CENTRE FOR INDEPENDENT STUDIES

**National Library of Australia Cataloguing-in-Publication Data:**

Author: Jha, Trisha, author.

Title: Complex family payments: what it costs the village to raise a child / Trisha Jha .

ISBN: 9781922184344 (paperback)

Series: CIS policy monographs ; PM141.

Subjects: Family allowances--Australia.

Child care--Costs.

Taxation--Australia.

Australia--Economic policy.

Other Authors/Contributors:

Centre for Independent Studies (Australia), issuing body.

Dewey Number: 362.7130994

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PM141

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## ACKNOWLEDGEMENT

The author would like to thank two anonymous reviewers for comments on an earlier draft. The author would also like to acknowledge all of her colleagues for their guidance, particularly Dr Jennifer Buckingham, Dr Jeremy Sammut and Professor Peter Saunders. Any errors remain her own.

## Executive Summary

- The total federal government expenditure in 2013–14 on family payments was $32 billion, amounting to 7.7% of total federal expenditure in that year, and 22% of total federal spending on social security and welfare.
- It is broadly accepted that the tax and welfare systems should provide some support for parents with children, even if the why and how of it is contentious.
- Policy decisions made in the past few years on child care and paid parental leave suggest that the core principles for family payments are the principle of need (strong means-testing) and increasing female labour force participation.
- Family Tax Benefits (FTB) and child care fee assistance are the two areas in which spending is the most significant and, in the case of child care assistance, the most likely to grow rapidly if left unchecked.
- Family Tax Benefits in the form of Part A and Part B cost $14.8 billion and $4.7 billion, respectively, and are aimed at assisting families with the cost of children (Part A) and enabling choices about parenting and labour force participation (Part B).
- Every year, child care fee assistance in the form of the Child Care Benefit and the Child Care Rebate costs $2.4 billion and $2.2 billion, respectively, and is aimed at 'assisting low-income families with the cost of childcare' (Child Care Benefit) and 'helping eligible working parents with the cost of child care' (Child Care Rebate).
- Over time, governments have attempted to shape policies that are all things to all people instead of reforming with a clear, unified set of purposes.
- In an attempt to achieve all possible outcomes, from equity to neutrality, the way programs are designed and overlap leads to perverse incentives that have a negative impact on workforce participation.
- Withdrawal of Family Tax Benefits and the increase in personal income tax liability as someone earns more can conspire against families at certain income levels. When the significant cost of child care is added to this mix, some families—and women in particular—find themselves in circumstances where it pays for them to not work at capacity.
- The costs of these disincentives are both short and long term; there are significant consequences for women's income at retirement and their financial security more generally, especially in cases of divorce.
- Instead of proposing expensive new schemes to mitigate these problems, this report outlines possibilities to fix the existing schemes to facilitate workforce participation.
  - Family Tax Benefits ought to be reformed with the punitive effects of high effective marginal tax rates (EMTRs) in mind.
  - The income test for FTB Part A should be simplified.
  - The work tests for eligibility for both Child Care Rebate and Child Care Benefit should be better aligned to the amount of subsidised care for which a family can be eligible.
  - The government should frame child care as a workforce participation measure and consider reducing regulation to ease the pressure on costs for the budget and for families.

## Introduction

The $32 billion spent on family payments in 2013–14 amounted to 7.7% of total federal expenditure in that year, and 22% of total federal spending on social security and welfare.[1] Family Tax Benefits (FTB) is the third largest single federal government spending program, after transfers to the states and the Age Pension.[2] Together, FTB, child care fee assistance, and Parenting Payments constitute the majority of spending on the family payments system, and are significant areas of expenditure in the federal budget in their own right.

Current budget conditions—including an estimated $50 billion deficit for 2013–14, spending increases from large new programs, and reduced revenues[3]—necessitate spending cuts in the short term. Over the next few decades, however, there will be further strain caused by an ageing population, increasing health spending, and a shrinking tax base. The pressures the nation's finances are facing now and well into the future mean that policy analysis and reform are needed, not just some trimming. This also means it is imperative that policy reform be undertaken with a view to minimising the disincentives to work embedded within the system.

In 2013, the Abbott government appointed two committees to undertake significant reviews into government expenditure and transfer payment policy: the National Commission of Audit and the McClure welfare review. Both reviews to some extent involved tackling inefficient expenditure and perverse incentives. In its report released in March 2014, the Commission of Audit recognised many of the problems discussed in this report, but the McClure welfare review's interim report, released in June 2014, has not recognised the problems of payment overlap and payment withdrawal—and the consequences for work incentives.

Within that context, this report aims to examine the complexities of family payments and uncover some possibilities for reprioritising and better targeting the family payments system to reduce expenditure and disincentives to work over the long term.

The primary focus of this report is on FTB and child care fee assistance, as spending is the most significant in these two areas and, in the case of child care assistance, the most likely to grow rapidly if left unchecked (Figure 2). The current paid parental leave scheme is a relatively small payment, and recent changes to Parenting Payment mean that it is set to decline in terms of both expenditure and the number of recipients. However, the paid parental leave scheme proposed by the Abbott Coalition government will add another $2 billion–3 billion to family payment outlays.[4] Other payments are mentioned to provide a holistic view of the system but not examined in detail. This is followed by a description of the various payments, some details about how much they cost, and an analysis of the ways in which different programs interact with one other. Finally, the report discusses how the system as a whole creates undesirable outcomes through perverse incentives.

> Historical spending growth, and hence the size of the structural spending base, will make responding to the spending pressures of an ageing population more difficult. Early adjustments to the structural spending base now will limit the need for much larger adjustments to the ageing-sensitive spending categories of health, pensions and aged care in the long run … The largest pressure on the budget is projected to come from health, reflecting ageing pressures, increasing demand for health services and the funding of new technologies. Pressure also is expected to come from increased spending on age-related pensions and non-age-related income support payments. Within other income support, spending on the Disability Support Pension and family payments are projected to bring the largest annual pressure on future budgets.
>
> — *Intergenerational Report 2010*, 49

## The principles of family payments

The conceptual basis of family payments is the recognition that families with children have different needs to those without and, consequently, should be treated differently in the tax and welfare systems. The varied policy responses across different countries—and, indeed, throughout Australia's own history—flow from this core recognition.

Beyond this, there are a number of principles that can underpin policy in this area. Some of these principles complement and mutually reinforce one other to provide a sound set of assumptions upon which policy is based. Others, however, contradict one other. When policy is based upon contradicting principles, it is often fraught, and confused purposes are evident.

These principles are:

1. **Alleviating child poverty:** This entails providing family payments on a needs (that is, means-tested and targeted) basis[5]—a form of 'vertical equity.'
2. **Compensating parents for children on the basis that children confer social benefits:** This entails a non-means-tested per-child benefit.[6] The magnitude of this compensation would be informed by the extent to which children confer private benefits. Pro-natalism (the intention to increase the birth rate) is also a part of this.[7]
3. **Ensuring 'horizontal equity,' or recognising that the income required for a subsistence lifestyle is much higher for those with children than those without**: This most commonly entails the recognition of children by the tax system through concessions made to their parents' tax liability.[8]
4. **Enhancing gender equality on the basis that women disproportionately bear the economic inequities of giving birth to and raising children:** This entails a family payments system (including child care) that does not create disincentives to work.[9]
5. **Facilitating higher rates of workforce participation among parents, particularly mothers:** This entails a family payments system that actively creates incentives to work and enables access to child care services.[10]
6. **Maintaining 'neutrality,' or enabling families to make their own choices about work, children and home production:** This entails policies that do not confer extra financial benefits or incentives to a particular choice or combination of choices.[11]

Australia's family payments system is a patchwork of policies inspired by many of these principles. The first principle, alleviation of child poverty, is clearly evident in the majority of our programs being means-tested and providing more to those with the least. The third principle of horizontal equity, however, is what inspired the old non-means-tested system of tax concessions, and its closest contemporary analogue is FTB Part B. The fourth principle—gender equality—is invoked as a defence of the relatively recent policies of paid parental leave and increased subsidies for child care fees, and the fifth—facilitating female labour force participation—is a key motivating factor in these policies. The sixth principle—neutrality—contradicts principles 4 and 5.

There is also the question of whether it is an appropriate role for the government to provide incentives to work to mothers, and if it is right to do so by taxing a single-earner family to assist with child care subsidies. Furthermore, Principle 1 (poverty alleviation/vertical equity) and Principle 3 (horizontal equity) contradict each other. This contradiction is particularly salient to the Australian family payments system and will be discussed in depth later.

Table 1 illustrates which payments fulfil certain principles and which payments contradict a given principle.

**Table 1: Family payments policies and underpinning principles**

| | 1. Poverty alleviation | 2. Social benefits | 3. Horizontal equity | 4. Gender equality | 5. Workforce participation | 6. Policy neutrality |
|---|---|---|---|---|---|---|
| FTB Part A | ✓ | | ✓ | | | ✓ |
| FTB Part B | | ✓ | ✓ | | | ✓ |
| Child Care Fee Assistance | | | | ✓ | ✓ | × |
| Paid Parental Leave | | | | ✓ | ✓ | × |
| Baby Bonus/Newborn loading | | ✓ | | | | ✓ |
| Dad and Partner Pay* | | | | ✓ | | |
| Parenting Payments (income support for parents) | | ✓ | | | | |

* The current program of Dad and Partner Pay is available to the partners of birth mothers regardless of whether they are working mothers. By contrast, the Coalition's proposal, which rolls a partner entitlement into the mother's Paid Parental Leave entitlement, discriminates, by definition, against the partners of those who do not meet the work test.

To argue that successive governments have attempted to remake the entire system on one set of priorities understates the complexity of these competing issues of principle. It is not the case that governments of a particular ideological persuasion pull policy in one direction and governments of another pull policy in the opposite direction. It is precisely *because* governments have attempted to shape policies that are all things to all people instead of reforming for consistency that there is no clear, unified set of purposes for the system. Unfortunately, there is no consensus as to what these purposes should be, and policymakers have done little to clarify the goals and objectives of a family payments system in recent years. Over the last century, the family payments policies of successive governments have been developed both to reflect and shape the dominant social attitudes to families, particularly mothers. The refocus in priorities and principles over a time of substantial societal change have not been consistent or coherent, and so the system has become increasingly complex, with numerous competing and perverse incentives.

## Historical development

The first federal family payments policy was the Maternity Allowance, a cash payment announced in 1912 and designed to provide financial assistance to mothers and newborns for health purposes, in the absence of public provision of medical services.[12]

Other than the Maternity Allowance, the method of recognising the cost of children was a system of income tax deductions. This system of concessions was the way to ease the burden on families caused by costs incurred for things like health, education and general living expenses.[13] It was also, however, regressive—James Scullin, later prime minister, observed that it benefitted wealthier families more than poorer ones:[14] Wealthier families are able to afford more and, therefore, deduct more.

The next important addition was in 1941, after the Commonwealth Court of Conciliation and Arbitration justified the introduction of Child Endowment, to exist alongside the tax concession system. The Child Endowment scheme was financed through a payroll tax,[15] on the basis that the basic wage only provided sufficient living for a family of three. Therefore, the tax-free Child Endowment, initially for every child after the first, was intended to perform the task of a wage increase without the associated adverse effects of a real wage increase.[16] At the same time, high-income earners could no longer benefit from the tax concession system for those children who received the Child Endowment.

The system of tax concessions for families existed up until 1976, recognising that different circumstances (children) deserved different tax treatment.[17] The dual system of concessional rebate and cash payment at this time also went above and beyond merely *assisting* with the costs of children: In 1960, a family with an income 150% of average weekly earnings with three dependent children was a net beneficiary of the family payments system. Their post-tax and transfer income exceeded their pre-tax and transfer income by 3%.[18]

After 1976, the concessional tax system was abolished and the Child Endowment was renamed Family Allowance and increased. The payment remained universal.[19] The universal nature of the payment is important because it highlights that family payments were not intended to function as a 'top-up' only intended for those otherwise incapable of adequately providing for their children. Rather, these payments were made with respect to children regardless of their parents' circumstances, suggesting that any and all children conferred social benefits and that caring for them should be facilitated. It is also important to note that all of this occurred as public provision of in-kind services that benefit families, like health and education, expanded greatly.

During the Hawke-Keating years, family payments underwent a significant shift in focus. Means-testing was introduced for the Family Allowance, and a supplement for low-income families was added.[20] This was in response to then Prime Minister Bob Hawke's infamous pledge at the ALP campaign launch for the 1987 election: 'By 1990 no Australian child will be living in poverty.'[21] It was possibly also a way to placate the union movement, given that Hawke promoted the supplement on the basis that a tax-free cash payment would be more beneficial than a wage increase.[22] A system that had hitherto involved relatively even distribution of benefits across levels of income became distinctly bottom heavy in that more money went to those least well-off. Another change was the introduction of the Home Child Care Allowance for sole and stay-at-home parents—and the forerunner of FTB Part B.[23] In essence, Family Tax Benefits as we know them today had their genesis in the 1980s.

## Box 1: The shift from horizontal to vertical equity

Together, the universal system of Child Endowment/Family Allowance and the accompanying system of tax concessions demonstrated the salience of horizontal equity and compensating parents for children as the core foundational principles for family payments. Under the old system, the core rationale was clear: Family payments existed to recognise that children confer social benefits and there are differing circumstances, which mean parents of children have needs that those without do not. When the concessional system was abolished in favour of higher cash payments, the first blow was struck to the horizontal equity principle. These cash payments could then be reformed in a way that reinvented the foundational principle. This is precisely what happened when the Hawke-Keating governments reformed family payments. Universalism was removed by introducing means-testing, and a supplement for low-income earners meant that vertical equity—the principle of need—began to dominate. The shift, however, was not complete and the tension between the two forms of equity is embedded within the system to this day.

Assistance for child care costs was only added to the family payments program in a meaningful way in the Hawke and Keating years, and its position within the broader program of family payments has increased rapidly since. Labor's duration in power (1983–96) saw the expansion of the existing community child care centres, the facilitation of employer-provided and for-profit centres, and the provision of means-tested fee relief and a non-means tested Child Care Rebate to assist families with the costs involved. The core rationale was driven by economic and labour force-related concerns.[24] Many of the debates that characterise the issue today—such as the role of accreditation, the scope of means-testing, and the link to workforce participation—began in this period.

The Howard government attempted to achieve policy neutrality: The introduction of the Baby Bonus was a compromise response to growing demands for paid parental leave—which, by definition, discriminates between working and non-working women. However, the Howard government began to undermine policy neutrality with the reintroduction of the Child Care Rebate. The expansion of this program by the Rudd government, combined with the introduction of a paid parental leave scheme in the Labor government's first term, saw the balance begin to tip.

The 2014 Budget abandons the principle of neutrality. Among the measures announced were an expanded and much more generous paid parental leave scheme, as well as a significant reduction in the scope of FTB Part B. The budget papers also showed enormous growth in child care subsidies over the forward estimates. This, combined with the previous government's decision to greatly reduce the value of the Baby Bonus in the new Newborn Supplement, suggests that the government's main priority is reducing expenditure in the form of cash payments and investing in female workforce participation—that is, not treating all life choices the same way.

The way policy has developed shows priorities for family payments have changed over time. However, the core family benefit, FTB Part A, has remained more or less intact since its inception as the Child Endowment. There is still a clear link between family payments and the recognition of, and support for, the costs of children—both the costs of raising them and the costs of income and opportunities foregone in the process.

## Box 2: Neutrality

'Neutrality' in the context of family payments means a system of policies that do not create incentives for a parent and secondary earner in a household to go to work and use child care, to provide entirely home-based labour, or some combination of both. The social shift, driven in particular by increased female labour force participation, is what gave rise to the 'different but equal' logic of a benefit for home care, and a separate benefit for external child care in the 1980s. This can only be considered a form of neutrality if the entitlement levels and eligibility criteria are roughly the same. However, the chasm between a recognition of home care and assistance for child care fees has been growing. The most recent changes in the budget to FTB Part B further underscore the downgraded importance of policy neutrality.

## The recent fiscal state of family payments

In 1988–89, family allowances (the forerunner to the contemporary FTB) amounted to 0.5% of GDP. This was despite the Hawke government increasing family allowances for low-income families. In the first Howard budget in 1997, family allowances were increased to about 1.2% of GDP despite the spending cuts that accompanied that budget. Spending on family payments peaked at around 2.8% of GDP in 2004,[25] even as the economy was undergoing a period of rapid growth. According to the *Intergenerational Report 2010*, family payments—Family Tax Benefits, child care fees, parental and baby payments, and the Parenting Payment—amounted to 2.6% of GDP in 2009–10.[26]

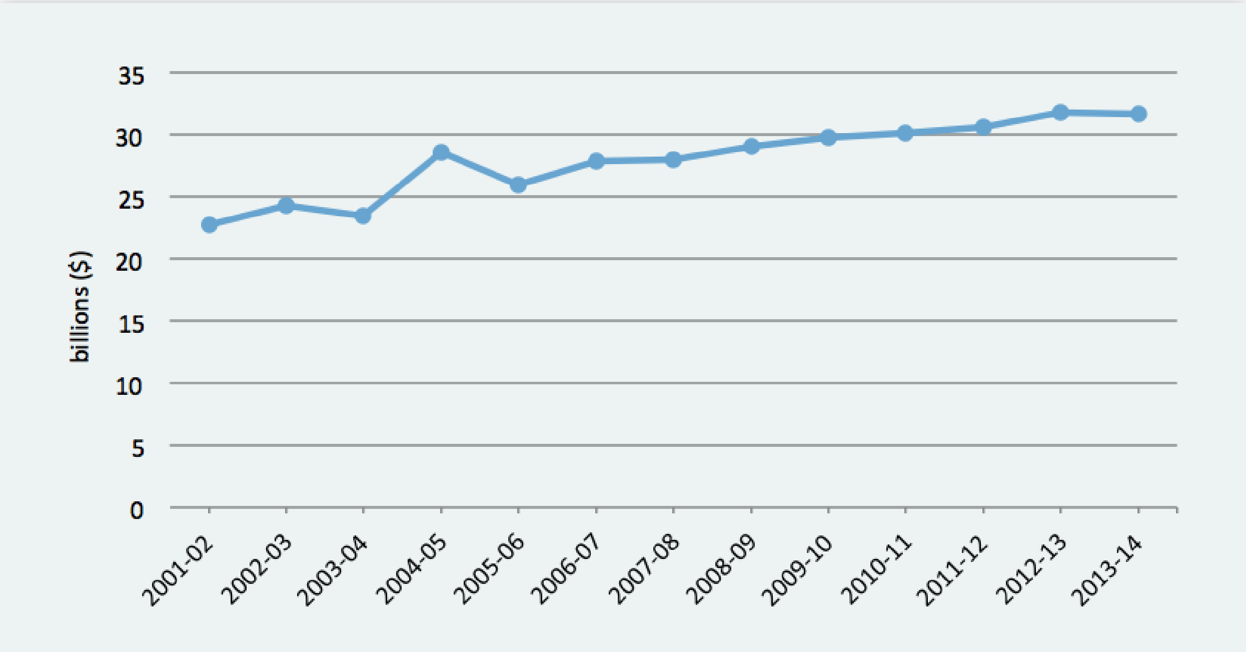
Spending as a percentage of GDP is an imperfect indicator of the real size and growth of family payments, as it is a relative measure. Growth in GDP can obscure growth in expenditure. Real expenditure figures (Figure 1) reveal a greater increase in family payments in the last decade than the GDP index suggests.

Australian Bureau of Statistics (ABS) data on the number of families and the total expenditure on family payments reveal that in real (inflation-adjusted) terms, family payments spending has gone from an average of $9,662 per family with dependent children in 2002–03 to $11,197 in 2009–10.[27] On a per-child basis, spending has increased from $5,239 to $5,982 in the same period.

While the Rudd-Gillard federal governments made some attempt to curtail spending in the family payments portfolio by altering the Baby Bonus and introducing more stringent means-testing for FTB Part B, spending grew overall, largely driven by increasing child care expenditure. Both the Rudd-Gillard government and the Abbott government have frozen the income thresholds used for means-testing and the indexation of the payments for FTB and child care fee assistance. Total spending, $32 billion in 2013–14, will fall from 2012–13 levels, and will continue to reduce as a result of changes to policy settings (most significantly to FTB).

However, the government's proposed Paid Parental Leave (PPL) scheme and increased child care expenditure (which grew by 9.9% in a single year[28]) suggest that the total envelope of family payments expenditure is expected to stay stable or even grow (exact figures for the proposed PPL scheme are as yet unknown) despite reductions in some program areas like FTB and Parenting Payments.

**Figure 1: Total expenditure on family payments, 2001–02 to 2013–14, real (adjusted) $billions**




**Source:** DSS (Department of Social Services) and DoE (Department of Education) and their antecedents, *Portfolio Budget Statements* (various years).

## Components of family payments

Table 2 does not include other in-kind support for families such as public provision of health and education or personal social services.

**Table 2: Current family payments at-a-glance***

| | Expenditure | | |
|---|---|---|---|
| | **2012–13** | **2013–14** | **2014–15** |
| **Family Tax Benefits** | | | |
| • FTB Part A (includes FTB Part A end-of-year supplement, Large Family Supplement, and Multiple Birth Allowance)<br>'To make payments to assist low- and medium-income families with the costs of raising dependent children.' | $14.3 billion | $14.8 billion | $14.6 billion |
| • Schoolkids Bonus (linked to eligibility for FTB Part A)<br>To assist with back-to-school related expenses, e.g. uniforms, books, extracurricular activities. However, there is no way to link the payment to these specific expenses—the relationship is notional only. | $1.4 billion | $684 million** | Nil |
| • FTB Part B (includes FTB Part B end-of-year supplement and Clean Energy Supplement)<br>'To make payments … to enable families to exercise choices to balance labour force participation and child care responsibilities.' | $4.5 billion | $4.7 billion | $4.6 billion |
| **Child Care** | | | |
| • Child Care Benefit<br>'To assist low income families with the cost of child care.' | $2.5 billion | $2.4 billion | $3.1 billion |
| • Child Care Rebate<br>'This assistance helps eligible working parents with the cost of child care, if they are using approved child care for work-related reasons.' | $2.1 billion | $2.2 billion | $3.2 billion |
| • Jobs, Education and Training Child Care Fee Assistance (JETCCFA) | $111 million | $88 million | $117 million |
| • Child Care services support<br>(not a cash family payment, but a subsidy to service providers) | $394 million | $317 million | $450 million |
| **Parental and Baby Payments** | | | |
| • Parental Leave Pay<br>'To help parents (usually birth mothers) spend time at home with a newborn or recently adopted child, and to help employers retain skilled staff.' | $1.4 billion | $1.7 billion | $1.8 billion |
| • Dad and Partner Pay (from 1/1/13)<br>'To help dads or partners … take time off work to bond with their newborn or recently adopted child.' | $35 million | $96 million | $97 million |
| • Baby Bonus<br>'To make payments to families to assist with the costs arising from the birth or adoption of a child.'<br>Replaced by the Newborn Supplement (a smaller loading on FTB Part A) and Newborn Upfront Payment from 1 March 2014 | $807 million | $389 million | N/A |
| **Welfare** | | | |
| • Parenting Payment (Partnered)<br>'Provides income support for the principal carer of a child aged under six years if the carer is partnered.' | $1 billion | $828 million | $1 billion |
| • Parenting Payment (Single)<br>'Provides income support for the principal carer of a child aged under eight years if the carer is single.' | $4.5 billion | $3.6 billion | $4.3 billion |
| **TOTAL** | **$33.2 billion** | **$32 billion** | **$33.3 billion** |

**Source:** DSS (Department of Social Services) and DoE (Department of Education), *Portfolio Budget Statements*, 2013–14 and 2014–15.

* All figures are in nominal terms and taken from Portfolio Budget Statements of the Department of Social Services and the Department of Education.

** This figure assumes that only the January 2014 instalment of the Schoolkids Bonus will be paid. It is contingent on the repeal of the legislation by the test date of 30 June 2014. As that has not happened, the expenditure will be closer to $1.3 billion.

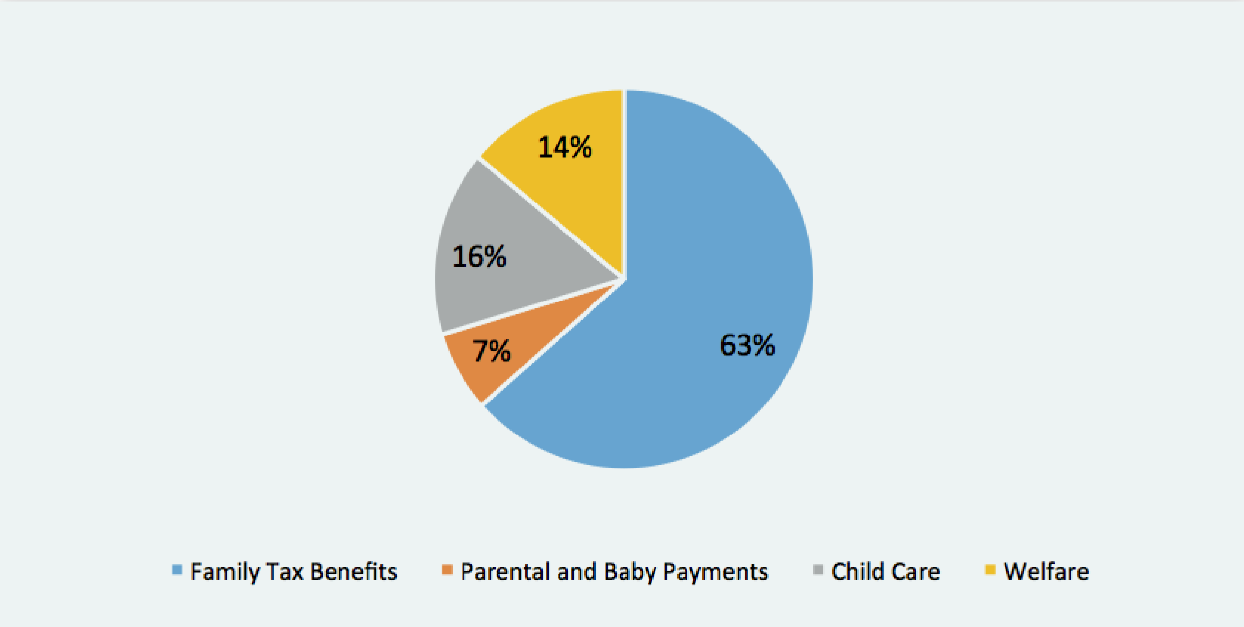
## Family tax benefits and child care subsidies

The two major components of the family payments system are Family Tax Benefits and Child Care subsidies. Figure 2 shows that together they comprise the majority (79%) of family payment costs, but they are also of major significance in terms of their impact on the choices families make about work—which is important given the future fiscal and demographic challenges posed by an ageing population.

This complex system is not only a large impost on taxpayers but it can also create disincentives to work, mostly for women. The costs exceed mere inefficient spending. There are consequences for women's income at retirement and financial security more generally, especially in cases of divorce. Such problems are acknowledged, and policymakers and commentators often propose various (often expensive) schemes to mitigate them. The Coalition's proposed Paid Parental Leave scheme, which includes superannuation, is one such example.

For these reasons, the remainder of this report will focus on detailing the intricacies of the design of family tax benefits and child care fee subsidies, including how the programs overlap and the cumulative impact the policies can have on families.

**Figure 2: Share of family payments spending by program type, 2013–14**




**Source:** DSS (Department of Social Services) and DoE (Department of Education), *Portfolio Budget Statements* 2013–14.

## Family tax benefits

FTB is the most significant family payments program for which the government is responsible, and it is the program with the longest and most complex history. It has two components—FTB Part A, which is a per child payment, and FTB Part B, which is a per family payment. As family payments have increased in real terms and the policy settings surrounding them have become more and more complex, unintended consequences have become evident.

### Family Tax Benefit Part A

FTB Part A is the staple family benefit. ABS data and Income Support Customers statistics show that 65% of families with children aged 18 and under received FTB Part A.[29] About 63% of children benefit from FTB Part A.[30] According to the Department of Social Services (DSS), the purpose of FTB Part A is:

> … to make payments to assist low- and medium-income families with the costs of raising dependent children. This supports better family functioning by improving the financial wellbeing of low- and medium-income families with children.[31]

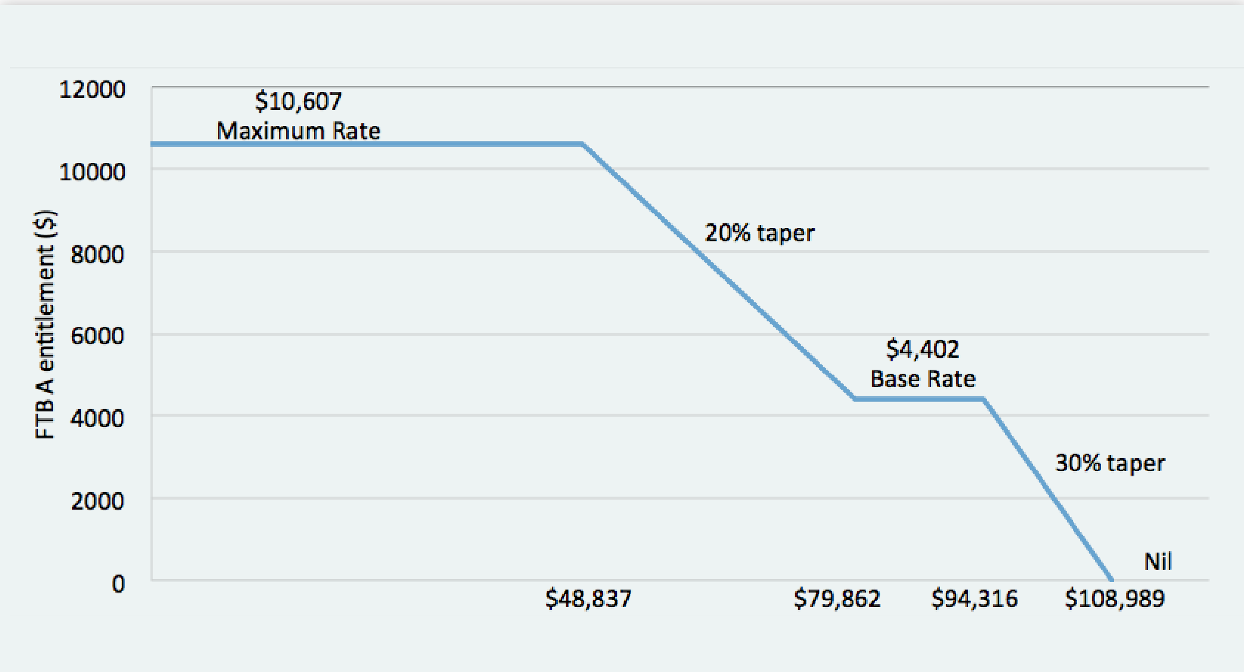
FTB Part A is the most complex aspect of the family payments system. It uses two different income tests to determine eligibility. One test applies a part rate—a reduced maximum rate—for incomes above $48,837, where the benefit is reduced at 20 cents in the dollar above that amount. The other test reduces the base rate by 30 cents in each dollar for incomes above $94,316. Whichever test provides the higher level of entitlement is the one that applies. The 2014 Budget eliminates the extra $3,796 threshold allowance for each FTB-eligible child after the first, though this change has yet to be legislated.[32]

FTB Part A has two payment brackets based on the ages of children. Under-13s are eligible for a maximum fortnightly payment of $172.20. Children aged 13 to 15 years, and 16- to 19-year-olds who are full-time secondary students, receive up to $224. The base rate for all children irrespective of their age is $55.16.[33]

There is also a supplement, worth up to $600 per child, per year, that is payable upon lodgement of tax returns and satisfaction of immunisation and health check requirements for young children.[34] Given that applying for family tax benefits requires households to estimate income in advance, the supplement can be used to offset any overpayments that may have occurred over the course of the financial year.[35] It was introduced in 2004 to reduce the administrative problem where families had underestimated their income and, therefore, overestimated their entitlement, and were consequently in debt to the government.[36]

FTB Part A, at the time of writing, also included the Schoolkids Bonus as an additional lump sum payment to those with FTB Part A eligibility.[37] The Baby Bonus, which was once a separate and higher payment, has been replaced by a loading on FTB Part A as of

**Figure 3: FTB Part A Income Test (family with two children under 13)**




Includes the FTB Part A supplement and the Energy Supplement

**Source:** Centrelink, *A Guide to Australian Government Payments* (January–March 2014).

1 March 2014.[38] The loading takes two different forms: the Newborn Supplement, either payable as a lump sum or as a loading over 13 weeks, and the Newborn Upfront Payment. Receipt of the latter is conditional upon receipt of the former and it is worth $500, though the total amount received under both payments cannot exceed $2001.50 for the first child and $1000.50 for second and subsequent children. Significantly, these two payments cannot be received by families accessing the Paid Parental Leave payment.

In addition, changes to Family Tax Benefits in the 2014 Budget mean that from 1 July 2015, sole parent families eligible for the maximum rate of FTB Part A can receive a $750 per-child supplement for children aged between 6 and 12.

## Family Tax Benefit Part B

FTB Part B is the component of the family payments system designed for families with only one main earner, be they single or partnered. According to ABS data and Income Support Customers statistics, the percentage of families with kids aged 18 and under who received FTB Part B is about 52%.[39] The number of children who benefited from FTB Part B as a percentage of total number of children aged 18 and under is also about 52%.[40]

FTB Part B is a per-family payment (as opposed to a per-child payment like FTB Part A) that is calculated on the age of the youngest child.[41] Like FTB Part A, there is an additional supplement (worth $300), which is used to offset overpayments.

FTB Part B is not as complex as FTB Part A. It is means-tested, primarily on the secondary earner's income, and eligibility is restricted to those whose partner does not earn above $100,000 (as of the 2014 Budget). Single parents automatically receive the maximum payment if their income is below $100,000.[42]

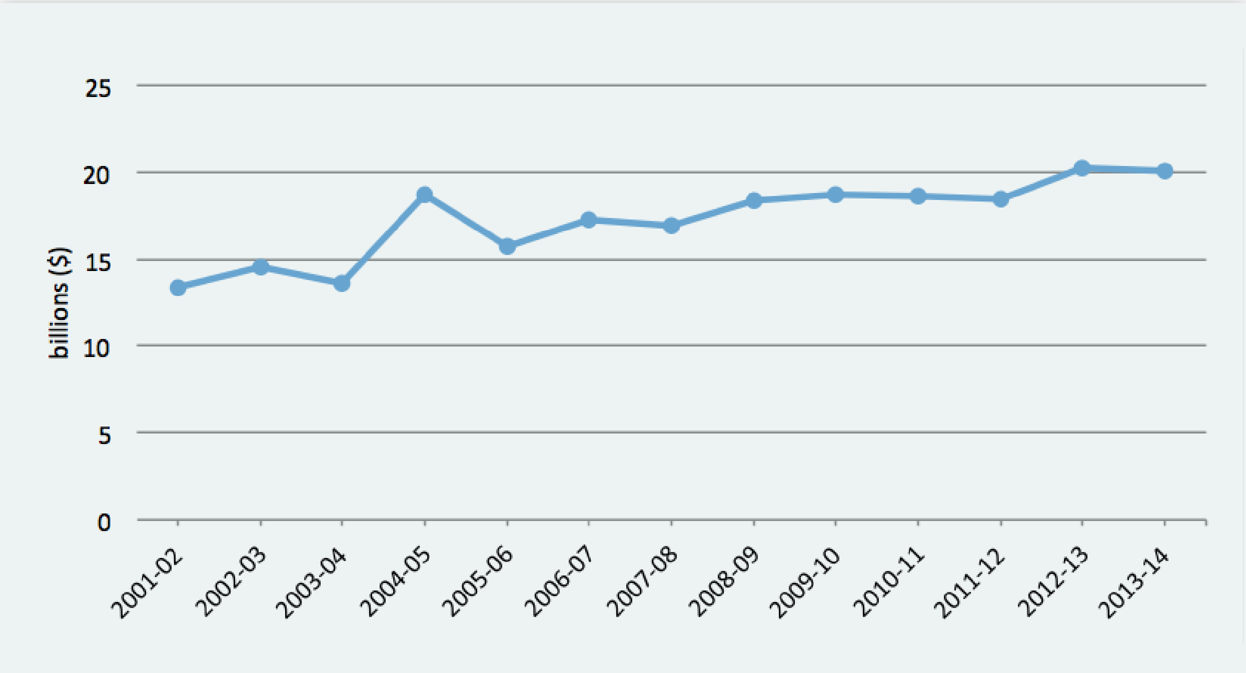
The payment structure is slightly less complex than that of FTB Part A—there are only two rates, maximum and part, and a higher payment applies to those families whose youngest child is below 5 than for families whose youngest child is 5 or older. Where the youngest child is below 5, the maximum fortnightly payment is $146.44; where the youngest is 5, the maximum payment is $102.20.[43] As announced in the 2014 Budget, from 1 July 2015, FTB Part B is no longer payable to families whose youngest child is aged 6 or over. This loss has been partially ameliorated for sole parent families with the addition of the aforementioned sole parent supplement attached to FTB Part A.

For two-parent families, secondary earners can earn up to $5,183 before their payment begins to be reduced by 20 cents in the dollar. If the youngest child is aged below five years, the secondary earner cannot earn more than $26,390 to be eligible for the part payment. If the youngest child is 5, this cut-off threshold is lowered to $20,532.[44]

## Expenditure

Figure 4 shows a large boost to Family Tax Benefits in 2004–05, and while spending fell back immediately after that, it has escalated further since. Moreover,

**Figure 4: Family Tax Benefits (FTB) expenditure, 2001–02 to 2013–14, real (adjusted) $billions**




**Source:** DSS (Department of Social Services) (and its antecedents), *Portfolio Budget Statements* (various years).

spending on family payments remained virtually unchanged during the Rudd-Gillard years even as spending cuts were made to reduce the budget deficit in the wake of the global financial crisis. The uptick in 2012–13 is explained by the introduction of the Schoolkids Bonus attached to FTB Part A (though only half of the increase is expenditure additional to the budget bottom line). The Schoolkids Bonus is essentially a reinvention of the Education Tax Refund—the key difference being the Schoolkids Bonus is an automatic payment rather than a rebate payable upon lodgement of receipts of education expenditure.

## Objectives

FTB Part A and Part B have different objectives. FTB Part A is the 'bread and butter' of the system. It is designed to provide a means-tested recognition of the costs of children on a per-child basis.

FTB Part B was devised to achieve horizontal equity for sole breadwinner couples—yet if horizontal equity means treating couples in the same circumstances equally, then there is inequity in the fact that a couple family where one person earns $70,000 is worse off in the tax system than a family where two people earn $35,000 each, as the latter has two tax-free thresholds.[45]

FTB Part B attempts to offset the tax burden of the family in the form of a (tax-free) cash benefit to the stay-at-home parent or secondary earner. As these tables show, it is not a perfect compensation—and these do not incorporate the value of child care subsidies, either.

Alongside tax equity, the role of FTB Part B is to provide some form of remuneration to recognise the unpaid labour a stay-at-home or secondary earner parent does inside the home. Its supporters claim FTB Part B also exists to make a system that invests so much in child care more neutral in terms of how it treats the work/life choices of individual families.[46] In other words, FTB Part B exists so government policy does not explicitly give preference to working parents over stay-at-home parents.

## Complexities

The objectives of FTB Part A and Part B seem clear, but there is a great deal of complexity underpinning this system. These complexities relate to features of individual programs as well as the system itself.

According to Helen Hodgson, associate professor of taxation at Curtin University, the complex state of FTB Part A can be traced directly to the Family Allowance and the Family Allowance Supplement during the 1980s and 1990s.[47]

The attempt to combine Family Allowance and Family Allowance Supplement has led to a situation where FTB Part A tries to ensure vertical and horizontal equity using two different mechanisms:

1. the payment amount is divided into four tiers as a result of two income tests applied at separate ends of the income scale, with more money going to those at the bottom and with the payment amount reducing with higher levels of income.
2. the amount of entitlement changes according to how many children there are, and the rate of payment changes according to the age of the child.[48]

In addition, there are numerous supplements such as the Energy Supplement, the Multiple Birth Allowance (for simultaneous births of three or more), the Large Family Supplement (for families with four or more dependent children), the Single Income Family Supplement, and the Low Income Family Supplement—all of which are linked to FTB eligibility. These supplements are usually small—a few dollars a fortnight, or $300 upon lodgement of a tax return in the case of the latter two.

**Table 3: Two parents in full-time work, two children aged 4 and 7**

| | Taxable income | Tax liability | FTB entitlement (Parts A and B) | Final post-tax-and-transfer position |
|---|---|---|---|---|
| Partner 1 | $35,000 | $2,747 | | |
| Partner 2 | $35,000 | $2,747 | | |
| Family total | $70,000 | $5,494 | $4,907 | $69,413 |

**Table 4: One parent in full-time work, two children aged 4 and 7**

| | Taxable income | Tax liability | FTB entitlement (Parts A and B) | Final post-tax-and-transfer position |
|---|---|---|---|---|
| Partner 1 | $70,000 | $14,297 | | |
| Partner 2 | $0 | $0 | | |
| Family total | $70,000 | $14,297 | $8783 | $64,486 |

**Source:** ATO (Australian Taxation Office), 'Comprehensive Tax Calculator' and Centrelink, 'Rate Estimator.'

There is also systemic complexity. Many of the families receiving FTB Part B are also entitled to FTB Part A—94% of FTB Part B recipients receive FTB Part A.[49] This means secondary earners in most FTB Part B families face high effective marginal tax rates (EMTRs) caused by the cumulative withdrawal of both payments at certain income levels.[50] But the potential work disincentives caused by EMTRs is secondary to the act of investigating how one's circumstances will change—not an easy task for most people. The EMTR issue is a significant part of the complexity embedded within the FTB program because it is symptomatic of confused purposes and unintended consequences.

## Impacts

Due to the significant overlap in FTB Part A and Part B recipients, we cannot treat both parts as completely separate policies that have discrete effects on the people who receive them. Recognising this, the Henry review recommended that FTB Part A and Part B be combined, and there be a uniform withdrawal rate to ease the pressure on EMTRs.[58]

An EMTR takes into account both the effect of a higher rate of personal income tax and the withdrawal of payment as someone moves up the income scale. The problem caused by high EMTRs is that there is often (subject to individual preferences) little financial gain to increasing work commitments, creating a work disincentive.

The withdrawal of benefits can essentially conspire against families at certain income levels so that there is little benefit for the secondary earner to work, or take on more hours.[59] A study undertaken by staff at the National Centre for Social and Economic Modelling (NATSEM) in 2009 suggested that around 11.4% of mothers and 20.5% of fathers among FTB Part A recipients faced high EMTRs of over 50%.[60]

This effect can be exacerbated by the lack of availability and expense of child care in some areas, even taking into account the available subsidies. Research

### Box 3: Tax/welfare churn

In 1975, *The Canberra Times* wrote on the topic of the government increasing family payments:

> The full equity aspects of the changes cannot be comprehended properly unless and until the continuing transfer of such a large proportion of personal incomes to the Government is recognised as the reverse of the rest of its total social-welfare program.[51]

That statement is as true today as it was almost 40 years ago. Taxing middle-class families with one hand only to give cash payments with the other is inefficient from an economic standpoint; it also obfuscates the reality of the relationship with the tax-transfer system. This obfuscation creates complexities for families, especially if they receive more than one kind of benefit—as most are.

### Box 4: Complexity for older children

The maximum rate of FTB Part A allows for older children (13–19) to be eligible for a higher payment. The rationale for this is based on the Henry tax review, which comments on evidence that the cost of children goes up the older they get—everything from clothing to school expenses to leisure activities is more expensive for a teenager than a primary school student.[52] This is also backed by research from the Australian Council of Social Service (ACOSS),[53] and supported by the interim report of the McClure welfare review.[54] The higher rate for older children only applies for those eligible for the maximum and part rates as the payment flattens out with regards to age in base rate and tapered base rate recipient families. The higher payment could also be interpreted as a way to keep in school teenagers who are old enough to legally leave school, when they might otherwise be tempted to drop out.[55]

However, providing extra payment for a child simply because they are a teenager is not a priority. The capacity for families to earn is much higher (given their caring responsibilities have reduced) and teenagers are old enough to participate in the labour force in their own right. Organisation for Economic Co-operation and Development (OECD) research suggests there is more benefit to reducing poverty in families through higher levels of benefits when children are younger as this has a flow-on effect, whereas the financial circumstances of families with older children aren't as malleable.[56] But it is still a matter for debate whether the explicit link between child costs and child payments is retained, or using cash benefits to insulate younger children from future poverty is a better strategy.

The higher payment is even more superfluous as teenagers aged at least 16 in the lowest income families are currently almost invariably eligible for Youth Allowance, the receipt of which cancels out that child's eligibility for FTB Part A. The payment rates are almost the same ($224/fortnight for FTB Part A vs $223/fortnight for the Youth Allowance), as are the parental income cut-offs for the maximum payment ($48,837 vs $47,815) and the taper rates—20 cents in the dollar for each dollar earned by the parents above the aforementioned thresholds.[57] The two could be better aligned, but overall the higher rate for older children adds to complexity and duplicates an existing program.

undertaken by the Grattan Institute, in conjunction with modelling from NATSEM, suggests that the cumulative effect of benefit withdrawal, higher tax rates, and child care costs is both significant and regressive. For example, a couple family where both parents earn $40,000 each and have one child in long day care only take home half of the second income if the second earner chooses to work full-time. A family with two children in long day care, where one person is earning $70,000 and the other has the capacity to earn the same, is in a situation where the net benefit is reduced to 20 cents in the dollar if the secondary earner works more than two days (16 hours) a week.[61] Even without child care costs, low-income earners can end up taking home less than 60 cents in the dollar.[62]

Data from the Longitudinal Study of Australian Children (LSAC) on families with one jobless (includes both not in the labour force and unemployed) member indicates that 11% of women and 5% of men said their joblessness was due to their partner earning enough, the cost of child care meaning it would not be worthwhile, or fearing the loss of benefits. [63] While this pales in comparison to the number who say they are jobless by choice (which is 82% of women and 21% of men), these statistics indicate there are people whose work choices are being distorted by the disincentives created by the family benefits system. It is also worth noting that this data only takes into account people who are jobless, and not those who wish to increase their work commitment but face these disincentives.

Structures of family payments that create disincentives for workforce participation do not just cause problems from the perspective of excessive or poorly targeted expenditure. Policies that keep secondary earners, mostly women, participating below their capacity have flow-on effects. These effects can include overall lower lifetime earnings, reduced financial independence (especially in cases of divorce and upon reaching retirement age), and the general social benefits of work.[64]

The upshot of the situation is that some people are in circumstances where it pays for them to not work at capacity. There are real consequences for having such a system. One is that the economic benefits and increased tax take that arise from having a higher participation rate and increased labour supply remain untapped;[65] another is that women disproportionately bear the brunt of the resulting inequities (which in some cases will be borne by the taxpayer at some point over the lifecycle). The current system involves inefficient spending but it needs to be reformed because it punishes those who wish to or need to work.

### Box 5: Are universal benefits a solution?

In the case of family payments, avoiding high EMTRs caused entirely by the system is impossible without implementing universality. Universal benefits are often promoted as a solution to the EMTR problem. To an extent, EMTRs in income brackets where families are moving away from benefits and into work are inevitable. Avoiding the work disincentive effect that accompanies high EMTRs is desirable, but not so desirable that it should come at the cost that a universal benefit entails.

The main argument against implementing universal cash benefits is they would be incredibly expensive, with little to show. In a study undertaken to model the effects of Norwegian-style universal family payments on the Australian population, it was revealed that universal benefits (and the corresponding lower EMTRs) would only have a small effect on labour participation of women. Not only that, it would considerably increase expenditure on family payments—by $9.5 billion in 2006–07 terms.[66] It would also undermine the Australian system’s strength in having fairly low levels of tax-welfare churn compared to other OECD nations.[67]

Universal payments would also contradict the principle of vertical equity that is embedded in the Australian payments system.[68] It would essentially amount to wealth redistribution from people without dependent children to those with. Some kind of wealth redistribution—funding programs through taxation revenue—is commonplace for something that is deemed to have sufficient social benefits, but the question becomes what is defined as a social benefit, and to what extent this needs to be supported by the government.

Children are sometimes said to confer social benefits. In spite of the panic over fertility that filled public commentary around the turn of the century, the birth rate has increased. However, even if fertility were once again to become the principle on which family payments policy is based, the evidence simply does not support the notion that pro-natalism in the form of cash transfers has the effect of increasing fertility.[69] In light of this, and the pragmatic argument that there simply isn’t money to spend on assisting families who are on incomes that can support children, universal cash payments should not be considered a solution to the problem of EMTRs.

## Child care

There are two main forms of child care subsidies for parents: Child Care Benefit and Child Care Rebate. A program of means-tested fee relief was introduced in the 1980s and then joined by an early version of the Child Care Rebate from 1994.[70] The two were then combined into the Child Care Benefit in the rationalisation of the family payments system that accompanied the first Howard budget.[71] The Child Care Rebate was re-introduced as the Child Care Tax Rebate in 2004. The logic of having two programs designed differently yet ostensibly for the same purpose has always been murky—for instance, today's system much more closely resembles that which existed 20 years ago despite the many changes to the system in the intervening period.

There are also two main forms of government-sanctioned care for which subsidies are available: 'registered' care and 'approved' care. Child Care Benefit is available for both forms of care, whereas Child Care Rebate is only available for approved care. 'Registered' care is usually an informal carer who has nevertheless registered with the government. 'Approved' care is a much more complex category that applies to formal care (long day care, family day care, and out-of-school hours care are the main categories). Approved care must also meet certain minimum standards set by the federal government. As will be explained below, the bulk of subsidies are only available for specific types of government-sanctioned care, which can create negative outcomes.

### Child Care Benefit

Child Care Benefit is a means-tested payment intended to offset the impost of child care fees for families. The rate of Child Care Benefit entitlement is calculated according to income—so that the lowest-income families get the most—type of care, and the number of children. The maximum rate of benefit for a non-school child is $3.99 an hour; the rate for school children is 85% of non-school children. The benefit can be paid to the provider or as a lump sum into a nominated account.[72]

The income threshold at which a family becomes ineligible for the benefit changes according to the number of children in care, but for families with one child in approved care the threshold is $145,642.[73] For registered care, there is no income test.

### Child Care Rebate

Child Care Rebate is also a cash benefit that subsidises the fees of child care for families to make it more affordable. It operates alongside Child Care Benefit and one must be eligible for Child Care Benefit to receive Child Care Rebate, even if they are not entitled to anything because their income is too high. The key difference between the two is that Child Care Benefit may be claimed for registered care, but Child Care Rebate can only be claimed for approved care services, and there is no limit on hours per week of approved care for which Child Care Rebate may be claimed. Child Care Rebate is not means-tested, meaning that all Child Care Benefit recipients are entitled to Child Care Rebate, but not all Child Care Rebate recipients receive Child Care Benefit. Child Care Rebate covers up to 50% of out-of-pocket expenses on child care fees and the rebate is capped at $7,500 per child, per year[74]—an amount not currently being indexed in line with inflation.

Child Care Rebate can be paid in a few ways: annual lump sum, quarterly lump sum, directly to the provider, or fortnightly into a nominated account. There is a policy advantage to having a rebate rather than have the subsidy go directly to the provider as this means customers are forced to pay upfront and are, therefore, at least somewhat sensitive to prices. Nevertheless, given the size and scope of the rebate's coverage, there is pressure on expenses in this area.

### The work/training/study test for child care fee assistance

Both parents, or a lone parent, must meet the work, training and study test to be eligible for both Child Care Benefit and Child Care Rebate.

However, the work test is not well aligned to the amount of subsidised care for which one is eligible. There is effectively no work test for families who claim Child Care Benefit for up to 24 hours a week of approved care, as well as up to 50 hours a week of registered care. To receive Child Care Benefit for up to 50 hours a week of approved care, a family must only meet 15 hours a week of work, study or training.

As the receipt of Child Care Rebate is contingent upon meeting the requirements for Child Care Benefit, the work test is similar for both payments. However, there is no minimum number of hours per week of participation to be eligible for Child Care Rebate—a family need only demonstrate that they are working, looking for work, in training/study, or upskilling through voluntary work at any time during the week for which Child Care Rebate is claimed.[75]

## Box 6: Poor alignment of work/study/training test and subsidy entitlement[76]

**Example 1:** Lisa is studying at university and is partway through her course. Though the semester ends in late November, and the following semester does not resume until March the following year, Lisa is still eligible to receive up to 24 hours a week of Child Care Benefit because she intends to resume her course in March, even though she is not actively studying over the end-of-the-year/Christmas break. She is also entitled to Child Care Rebate.

As the *Social Security Law Guide* points out:

- Vacations during the course of study are included.
- Lecture/tutorial times need not coincide with child care times.
- Both contact and non-contact study hours are included.
- Contact hours need not match child care hours.

**Example 2:** Jane and her husband, John, are unpaid volunteers for a charity for 10 hours per week, but this voluntary work does not improve their skills or employment prospects. Because of this, and as this totals fewer than 15 hours a week per person, their commitments do not satisfy the work/training/study test. However, if they increased their volunteering to at least 15 hours per week, this would satisfy the test. They are entitled to both Child Care Benefit and Child Care Rebate.

As the *Social Security Law Guide* points out:

- Voluntary work must either improve work skills or employment prospects, or total 15 or more hours in a week.
- Voluntary work hours need not coincide with child care hours.

According to the government's policies for Child Care Benefit and Child Care Rebate, this assistance is intended to help families put their children in child care while they are at work. A separate form of subsidy, called Jobs, Education and Training Child Care Fee Assistance (JETCCFA) is also available, particularly for families on income support.

The way the work/study/training test is designed means parents can do very little in terms of these three activities and still be eligible for a lot more assistance than they really require. A simple 1:1 subsidy (one hour of work/study/training means one hour of subsidised care) is obviously inappropriate as it does not take into account travel time, but it is quite clear from these examples that the amount of subsidy should better reflect the amount of time dedicated to these activities.

## Expenditure

As Figure 5 shows, expenditure on child care provision and fee subsidies remained mostly stable over the course of the Howard government (1996–2007). The significant increase came with the introduction of Child Care Rebate alongside Child Care Benefit. Under the Rudd government, the percentage of child care fees that could be offset with Child Care Rebate rose from its original 30% to 50%, and Figure 5 shows that increase taking effect.

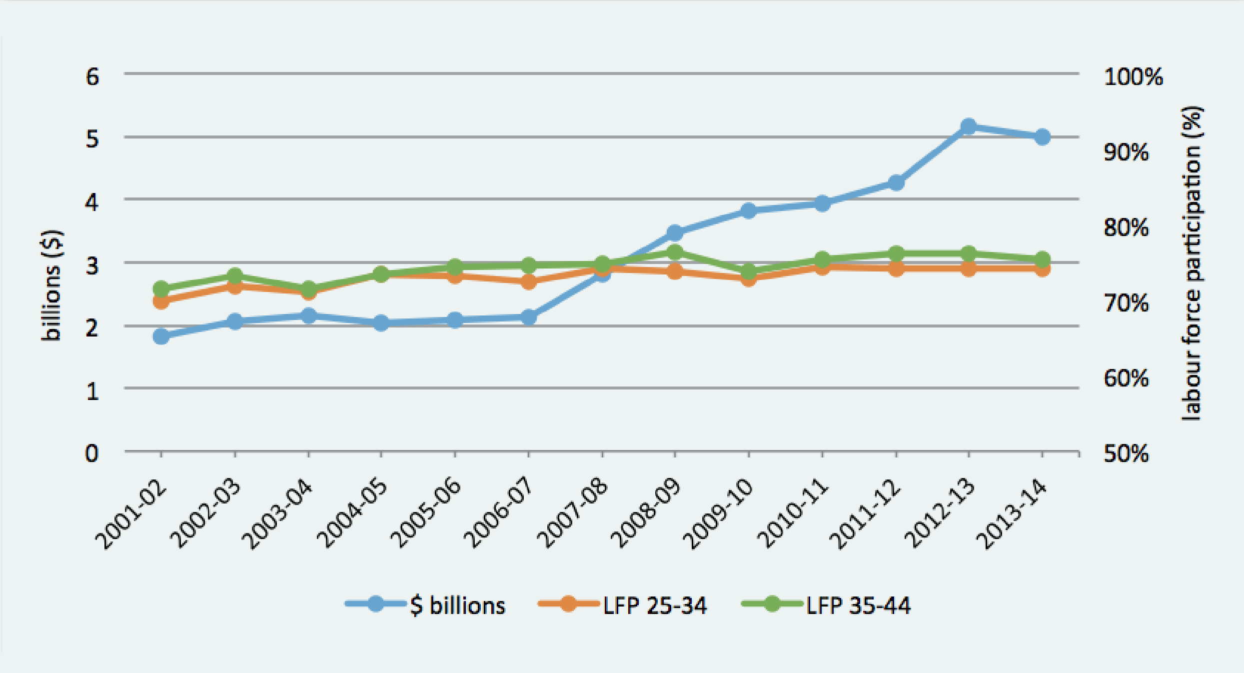
## Objectives

Child care concerns became part of the policy agenda under Hawke and Keating due to the recognition that child care is the cost of mothers participating in the workforce. As has been pointed out from various quarters—Prime Minister Tony Abbott included—it makes little sense to train women and have them attain tertiary degrees at a higher rate than men[77] and then make it financially difficult for them to both maintain a career and care for children unless their earning capacity is high.[78]

Despite men taking more responsibility for children than ever before—including working from home, teleworking, and using other flexible work options—women still undertake the majority of domestic work and child care, even if they are in paid employment.[79] This means the issue of non-parental child care and its interaction with other family payments cannot be abstracted away as only a question of family choices; it has to be understood in the context of the consequences for women's economic and financial lives because the outcomes are so disproportionate. This is especially so given that child care and family payments in general are so intimately linked for mothers of dependent children, as the earlier discussion on family tax benefits explained.

However, to acknowledge this reality is not to argue in favour of reckless expenditure and universal child care programs. The social benefits of child care relative to the costs of facilitating access to it do not exceed the bounds of workforce participation measures. Policy needs to recognise that some kind of government involvement in child care (there are numerous forms this involvement could take; increasing subsidies further is not realistic) is necessary to keep women

**Figure 5: Child care expenditure, 2001–02 to 2013–14, real (adjusted) $billions; rate of labour force participation for females aged 25–34 and 35–44**




**Source:** DoE (Department of Education) (and its antecedents), *Portfolio Budget Statements* (various years).

**Notes:** Inclusive of Child Care Benefit, Child Care Rebate, Child Care support assistance, and Jobs, Education and Training child care fee assistance (JETCCFA).

Not shown: Expenditure on the Child Care Tax Rebate from 2004–05.

* Child Care Rebate payable as cash through the Family Assistance Office.

† Rate of Child Care Rebate was increased from 30% to 50%.

in the workforce, but it is questionable whether it is appropriate for government to sideline parental care by subsidising child care that is not explicitly tied to workforce participation. This is especially important as families often choose to have one parent drop out of the workforce to care for children, and it is their taxes (as exemplified in tables 3 and 4) that fund these significant child care fee subsidies.

## Complexities

Child care fee assistance is complicated in three main ways:

- how it interacts with other family payments (discussed in the previous section on the impacts of family tax benefits)
- how the programs themselves are designed and how the design is informed by specific objectives
- how program design can have flow-on effects that affect the supply of child care services.

The complexity of Child Care Benefit lies in trying to calculate the amount of benefit one is entitled to. Rates for school children (e.g. those attending out-of-school hours care) are 85% of those for non-school children. The maximum rate of benefit for a non-school child is $3.99 an hour, but the benefit rate also depends on the type of care used by the family.[80] The different rates that apply to different types of care and families on different incomes are not made clear to families; this is established by a formula administered entirely by the relevant department.

The other key aspect of Child Care Benefit is that it can only be used to offset fees for services from ‘registered’ and ‘approved’ providers. A ‘registered’ provider is usually an informal carer, such as a relative or nanny, who is required to be registered with the Department of Human Services (DHS) to make families using their services eligible for Child Care Benefit. Other carers falling under the ‘registered’ category can include individuals providing care in what would otherwise be considered approved care services, and the same rules apply to them as to other kinds of registered carers.[81]

Being a registered provider means lodging an application with the DHS—filling out forms, providing receipts to customers, meeting any licensing requirements in the relevant state (such as a Working with Children check), and anything else required by the federal government.[82] The maximum Child Care Benefit parents can receive from this process with providers is $33.30 a week.[83]

### Box 7: Tax-deductible child care?

Child Care Rebate exists as a response to Australian taxation law. According to legislation on tax deductibility for work-related expenses, child care arises from personal circumstances and as such it is insufficiently work related.[90] Courts in other countries have deliberated over the proposition of tax-deductible child care, and proceedings reveal that it is a contentious issue elsewhere. Nevertheless, this has not been the case in Australia.[91] It is in recognition of this, as well as the fact that simple tax deductions do not benefit low-income earners very much, that the Howard government introduced Child Care Tax Rebate in 2004.[92] Therefore, the lack of means-testing Child Care Rebate should be seen as, in effect, an alternative to the tax deductibility of child care.

The *Inquiry into Balancing Work and Family* undertaken by the Family and Human Services Committee in the House of Representatives in 2006 found that this bureaucratic process was linked to those using in-home care and created a black economy with wages paid cash-in-hand, detrimental to both families and workers.[84]

'Approved care' is a more restricted category than 'registered care.' Care providers who fall into the category of 'approved care' make their customers eligible for Child Care Benefit and Child Care Rebate. The system of approved care provision includes long day care, family day care, outside school hours (OOSH) care, occasional care, and in-home care. Unlike those that fall under the 'registered' category, all these service providers have to meet the requirements of the National Quality Framework, the 40 pages of federal legislative extracts that set out minimum conditions, and whatever state and local government authority regulations apply.[85] Some such minimum standards relate to floor space, staff-to-child ratios, and participation in the relevant accreditation system.[86] The National Quality Framework, which is in the process of being phased in over a period of years, includes new requirements for staff qualifications. Increasing qualification standards and staff-to-child ratios is expensive for families and taxpayers, and the evidence base that purports this extra expense is an 'investment' is open to question.[87]

The complexity of the 'approved care' policy also lies in the outcomes that such a heavily regulated system creates. The *Inquiry into Balancing Work and Family* recognised that the approved category, dominated as it is by centre-based group care facilities, is the only type of care for which meaningful financial assistance is available, and this creates a 'one size fits all' approach that does not meet the needs of many families.[88] The inquiry also reported that given that the approved care category is dominated by the 8am–6pm model, this severely curtailed the working options of several parents—mostly mothers (partnered and single alike).[89]

## Problems with the system of family payments

The notion that taxpayers ought to provide some support for parents with children is broadly accepted, even if the why and how of it is a subject of much debate. In an attempt to achieve all possible outcomes, from equity to neutrality, the way programs are designed and the way they overlap leads to perverse incentives that have a negative impact on workforce participation. The contradictory objectives of different policies, as discussed earlier, lead to further complexity as well as inefficient expenditure. As the previous sections have shown, expenditure on family payments in general has increased in spite of strong GDP and wage growth.

Complexity also goes beyond whether policies contradict each other. From the perspective of the recipients of family payments, it is a difficult task to work out in advance the benefits for which you are eligible, and then whether you will be better or worse off if you work more or less. Even the simple guide published by Centrelink, 'A Guide to Australian Government Payments,' dedicates 12 pages to family payments. It is relatively easy to figure out if you can get the maximum rate of a particular payment or if your income is simply too high, but for those with mid-level incomes—the vast majority of benefits recipients—working out how much one's payment is reduced due to increased income is a significant task. The system is so incomprehensible that families are entirely beholden to the bureaucrats at the Family Assistance Office.[93] This is especially true for people in irregular work as they have difficulty accurately predicting their annual income and, thus, how much benefits they are entitled to.[94]

### Possibilities for family tax benefits reform

The Henry review limited its recommendations to the simplification of the existing transfer system for family payments by recommending that FTB Part A and Part B be combined into a single payment. Family tax benefits ought to be reformed with the punitive effects of high EMTRs in mind, and they should be altered to have a simpler income test. Simplifying the income test for FTB Part A would affect many families, considering that the number of recipients of FTB Part A as of June 2012 was 1.6 million.[95] The National Commission of Audit recommended far-reaching reforms to FTB Part A, the most significant of which is the removal of the base rate of payment—so the maximum rate of payment would simply taper to nil. Reforming the program to reduce the high levels of expenditure in this area has been done with the changes to FTB Part B in the 2014 Budget, and freezes to thresholds and indexation of the payments. However, the freezing provisions are a blunt instrument to reduce expenditure and recipient numbers over time, when policy reform could achieve both those things as well as reduce perverse incentives, and do so while keeping low-income families relatively insulated. Some changes to FTB Part B in the budget retain, and in some cases exacerbate, EMTRs. A key example of this is the FTB Part A supplement for sole parents, which is no longer payable over $48,837 rather than tapering out. This is referred to as 'sudden death.'

Though the interim report of the McClure welfare review was written before changes were announced in the budget and cannot be faulted for not acknowledging that specific problem, it is disappointing that the more general problem of FTB overlap and withdrawal were not investigated. This could be a result of a phenomenon of categorisation whereby bureaucratic and political language makes much effort to distinguish family payments from income support, with the consequence of ignoring how the two overlap. It does, however, mean that any examination of the income support system is only looking at half the picture if family payments are overlooked.

## Possibilities for child care fee assistance reform

Since the government has decided that child care access is a policy priority, the central objective should be to provide child care in such a way that allows more parents (mostly women) to participate in the workforce, and for society to reap the benefits from higher participation rates. These core principles, combined with the necessity of controlling expenses in this area, suggest that the work tests for eligibility for both Child Care Benefit and Child Care Rebate should be better aligned to the amount of subsidised care for which a family can be eligible. The Productivity Commission's review into child care is a welcome development, as the government must re-evaluate its priorities for child care. While the draft report touches on the unnecessary complexity of two separate subsidies, it fails to address some other problems with child care that are raised in this report.

## Some alternatives

Another option for reform is a tax credit scheme similar to the Howard government's 1997 Family Tax Initiative (FTI), which involved a $1,000 per-child increase to the tax-free threshold and an addition of $2,500 per sole parent family. Below the first marginal rate threshold, these benefits could be cashed out. There was a cap on the income at which a family would stop receiving the FTI benefit—an effective means-test.[96] However, in the case of a tax credit-based family payments system that is not universal, like the FTI, the EMTR problem still exists because of the tapering provisions. Furthermore, it would not provide extra assistance earmarked for use on child care fees, which appears contrary to the government's general goal of increasing female workforce participation through facilitating child care access.

A universal scheme along these lines is another option. It would be very expensive in terms of foregone revenue and would sit awkwardly alongside the heavily means-tested system of social security and welfare benefits more broadly. However, it would restore horizontal equity (Principle 3 on page 4) to the tax system by acknowledging that the income of people with dependent children has more demands on it than the income of people without dependent children. A more detailed formulation of how this would work in practice is outlined in Barry Maley and Peter Saunders' 2004 report, *Tax Reform to Make Work Pay*.[97]

# Conclusion

The family payments system has developed largely in an *ad hoc* manner and evolved in response to changes in contemporary political imperatives. The result is a system that is complex and characterised by confused purposes, and the costs of which will be difficult to maintain in the face of current and ongoing fiscal problems.

There is a significant gap between what programs are designed to achieve and the impacts they actually have on the people for whom they are intended. The first step is to clarify the purposes of the family payments system as a whole. As we have seen, different programs have clearly defined purposes, but when combined often overlap or contradict each other. The 2014 Budget made some changes that were hinted at as being on the basis of principle—the changes to FTB Part B are a perfect example of this. Treasurer Joe Hockey said in his budget speech, 'Staying at home should be a parent's choice but there are limits on how much support the taxpayer can give.' The core principles and priorities need to serve as a foundation for reforms to the system.

The priorities are clear. Reforming Family Tax Benefits with a view to simplifying the programs and reducing perverse incentives will make money go further through reprioritisation. In the same way, reassessing eligibility for child care fee assistance—including widening the category of approved carers to ease pressure on the system and tightening the work test for the recipients—will reduce the problems of complexities and cost.

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## About the Author

**Trisha Jha** is a Policy Analyst with the Social Foundations Program at The Centre for Independent Studies. She holds a Bachelor of Arts (International Relations) from the Australian National University. Trisha has contributed to CIS publications *Emergency Budget Repair Kit* and *Submission to the National Commission of Audit*.

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CIS Policy Monograph • PM141 • ISSN: 0158 1260 • ISBN: 978 1 922184 34 4 • AU$9.95
Published August 2014 by The Centre for Independent Studies Limited. Views expressed are those of the authors and do not necessarily reflect the views of the Centre's staff, advisors, directors or officers.

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PO Box 92, St Leonards, NSW 1590 Australia • **p:** +61 2 9438 4377 **f:** +61 2 9439 7310 **e:** cis@cis.org.au