

Working for Families under attack

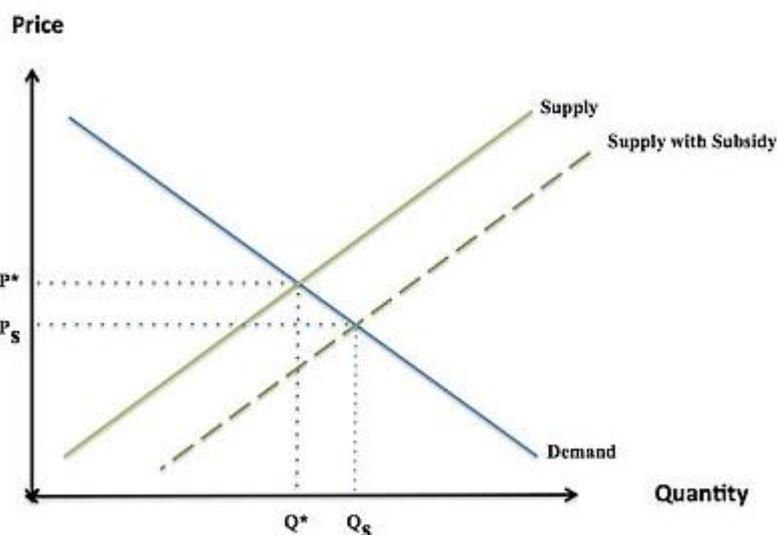
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The [debate about WFF](#), including Matthew Hooton's extreme view that WFF is [communism by stealth](#) is full of sound, fury and little substance. Eric Crampton now weighs in with a more academic approach to support the view that [Working for Families is an employer subsidy](#).

The essence of his argument is, yes, it is an employer subsidy, but that is no bad thing. He even prefers a subsidy to minimum wage legislation:

Wage subsidies place the burden of supporting the employment of those with lower productivity on the tax base in general. Minimum wages place that burden on those who would employ those workers, their customers, and on workers disemployed in the process. The former seems to me both more efficient and more equitable.

His argument is that "Labour markets are generally competitive - employers have to compete for workers, and workers have to compete for jobs." So, it seems, we can draw standard demand and supply curves.



Having assumed it is a "competitive market" he then bases his analysis on thinking that WFF is like any standard tax or subsidy. As any stage one student of economics knows, who gets the advantage depends on the slope (elasticity) of the curves. In the extreme:

'If the demand for labour were perfectly inelastic (and labour supply were other than perfectly inelastic), a government wage subsidy would only benefit employers. They would employ the same amount of labour at a lower cost (to them), with workers taking home the exact same amount as before. The supply of labour depends on the after-tax-and-transfer salary on offer, and take-home pay would not change''.

In essence, Crampton says neither demand nor supply will be perfectly inelastic, and therefore some of the benefit- maybe the bigger share, will go to the worker.

But does this reflect how WFF actually works? Unlike demand and supply in a competitive market for, say, fresh fish, the labour market is based on rules and regulations of which the minimum wage is a good example. But even if the labour market were like the market for fish, the **simple diagram above works only if WFF is an hourly subsidy not a lump sum.**

WFF is quite different to the Earned Income Tax Credit in the US. WFF does not subsidise the hourly rate. Let's take a low wage, one-full time earner family, with children on the living wage rate of \$20.20 per hour or \$42,000 per annum. First, WFF is a payment *for the children*, going to the caregiver not to the worker. The caregiver gets the same WFF of \$9646 for the one child family (more for additional children) whether their partner works 20 hours, 30 hours or 40 hours, and so it does not shift the labour supply of the worker.

A plausible way WFF can affect this very low income labour market is through something called an 'income effect'. The idea here is that the lumpsum might make the family feel wealthier and so can 'afford' to work less. However, the family qualifies for the lumpsum WFF only *if there is a child*. The extra mouth to feed is likely even, after WFF, to make them feel, **and be**, poorer not wealthier.

So what if income for this family is more than \$42,700. The problem for the 'WFF is an employer subsidy' argument is that the exact reverse is true. Extra income is effectively taxed because an extra dollar earned reduces WFF by 25 cents. That additional tax, if shared between employer and employee in a competitive market, would mean the employer might actually *raise* the wage rate somewhat. The opposite of a subsidy in fact.

Crampton notes that "At least some of the point of Working for Families was to increase the benefit of being in work relative to being on benefit for people like single parents." The part he refers to is the 'In Work Tax Credit' (IWTC) that can be received only if the sole parent works 20 or more hours per week and is off the benefit. This is a clumsy discriminatory and ineffective part of WFF but again this is a lump sum not an hourly subsidy. The sole parent is a subset of the labour supply with a vertical supply curve at 20 hours. Thus a perverse effect might be that a sole parent working fewer than 20 hours could ask for her wage rate to be reduced on the condition that the employer falsifies her hours to say she is working 20 hours.

There is a tiny, tiny, part of WFF that could be construed to be an employer subsidy. It is a nasty little twist called the Minimum Family Tax Credit that tops up family incomes to around \$26,000. There are only about 3000 families that access this tax credit. Sole parents have to work 20 hours to get it, and be off benefit. Any extra income from *any* source including child support reduces this tax credit dollar for dollar. In terms of the diagram, the labour supply is vertical at 20 hours. If you twist yourself into knots, it is conceivable that a sole parent might forego a wage rate increase the employer is giving to others as it won't actually help them. This pernicious tax credit is an insignificant part of the WFF cost and **does not mean** WFF in total can be described a wage subsidy.

The [treasury modelling](#) Crampton refers to showed “the introduction of the new policy [WFF] increases labour supply of sole parents by an average of 0.62 hours per week, but decreases labour supply of married men and women by 0.10 and 0.50 hours per week, respectively”. But there are more married people than sole parents. If the aim was to increase overall work effort it was a miserable failure because Treasury’s figures imply that overall hours of work must have *declined*.

Forgotten in the ‘WFF is a subsidy to employers’ debate is the understanding that WFF is a payment for children. Indeed, I can’t recall children getting a mention in any of the recent attacks on WFF. They are invisible in Crampton’s analysis.

Labour made a huge mistake in calling family payments for children paid to the caregiver ‘Working for Families’. There has been confusion ever since. We need to delink WFF from any fixed hours of work requirement, rename it ‘Family Assistance’ or ‘Child Tax Credits’, make it more generous and more like the system they have in Australia. Over there they don’t seem confused about the purpose of their family assistance.

There is one more thing that is disturbing in Crampton’s analysis. To return to his conclusion quoted at the beginning of this commentary- he would prefer a wage subsidy to a minimum wage. The competitive market for low skilled workers might drive the wage down from the minimum or \$16.50 an hour to \$12 say. Will WFF kick in to save the day? Sadly no, it will be the same amount as before, so the only outcome will be increased family misery.

If Crampton wants to argue that WFF should be like the earned income tax credit in the US then he should say so and be prepared to explain why the US has one of the worst records on child poverty.