

# **Welfare isn't working**

## **Child Poverty**

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**REFORM**  
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## **Welfare isn't working**

This is the second in a series of reports – written by Frank Field and supporting authors – which will investigate the Government's record on welfare since 1997. The first report looked at the New Deal for Young People, whilst subsequent reports will cover Tax Credits, the Child Support Agency, Sure Start, pension reform, the New Deal for Work, and the National Minimum Wage.

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## Executive summary

- In 1999, Tony Blair announced an historic mission to abolish child poverty within 20 years
- To achieve this aim, three targets were set:
  - to reduce child poverty by a quarter between 1998-99 and 2004-05;
  - to halve it by 2010-11; and
  - to eradicate it by 2020.
- By 2009, the Government will be spending £13 billion a year extra, the equivalent of a 4p tax cut, on increased benefits and tax credits for families with children.
- But, despite this huge expenditure, the Government missed the 2004-05 target and, in 2005-06, child poverty on the Government's preferred measure actually increased.
- On other measures the record looks weaker still:
  - there has been no change since 1997 in the numbers of children in severe poverty; and
  - one in five children living in households in poverty remain persistently poor.
- The current anti-poverty strategy is biased:
  - the risk of poverty for children has hardly changed for children in two parent families;
  - despite the Government's assertion that work is the best route out of poverty, half of all children in poverty remain in working households; and
  - there has been no reduction in the numbers of children in working poor households since 1995.
- Tax credits are badly designed:
  - despite the huge costs, only a quarter of children in poor working households receiving tax credits are taken out of poverty because of them. Over 700,000 children in poor working households are not receiving tax credits;
  - a further result of the poor design of the tax credits system is that two parent households need far greater earnings than a lone parent to move past the poverty line. In 2004-05, two parents with two children had to earn £240 a week to have a net income of £295, to lift themselves above the poverty line. By contrast, a lone parent with the same number of children needed to earn just £76 a week to gain a net income of £230, £5 above the poverty line; and
  - with tax credits not making allowance for the second adult in the

household, two parent families needed to work far longer to achieve the same level of income. In 2006, a lone parent with 2 children under 11, working 16 hours a week on the minimum wage, gained a total net income of £487 a week, largely due to tax credits. In order to attain the same weekly income, an equivalent two parent household needed to work 116 hours a week; an extraordinary 100 hours more than the single parent.

- Even though the Government has shifted the goal posts for the 2010-11 target – re-defining 1 million children out of poverty – it is still expected to miss this target by a significant margin. Government policies have to register a fall in the number of poor children which is eight times the rate achieved over the last five years to meet the 2010-11 goal.
- A new strategy is urgently needed which:
  - ceases discriminating against two parent working families;
  - as a result, ceases discriminating against single parents who re-partner and thereby encourages single parents to declare their existing partnerships;
  - increases incentives to work for potential second earners;
  - improves education outcomes at the bottom end to prevent intergenerational poverty; and
  - makes effective the child support system.

## 1. The story so far

In his 1999 Beveridge lecture, Tony Blair made an unprecedented pledge to eradicate child poverty in Britain, saying:

“Our historic aim will be for ours to be the first generation to end child poverty, and it will take a generation. It is a 20 year mission but I believe it can be done.”<sup>1</sup>

No Government has ever set itself such an audacious objective and no praise can be adequate in complementing it on such a noble aspiration. But how much progress has been made since this speech and what remains undone?

### The targets

To measure progress, this pledge was formalised into a Public Service Agreement (PSA) target.<sup>2</sup> This required a reduction by a quarter (from its 1998-99 level) in the percentage of children living in households below 60 per cent of median income by 2004-05. (Unless otherwise stated, this 60 per cent definition of poverty will be used throughout). This initial goal was a staging post towards the broader target of halving child poverty by 2010-11 and eradicating it by 2020.

### Increased spending

In order to meet the above targets, the Government has directed huge resources at families with children. Although it maintains that it is unable to give an estimate of how much it has already spent on programmes aimed at reducing child poverty, it calculates that as a result of tax and benefit changes since 1997, it will be spending an extra £13 billion a year on families with children by 2009. This is equivalent to a 4p cut in the standard rate of tax.<sup>3</sup>

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<sup>1</sup> Blair, T. (1999), *Beveridge lecture*, Toynbee Hall, 18 March.

<sup>2</sup> Department for Work and Pensions and HM Treasury (2002), *Public service agreement: technical note for the Department of Work and Pensions*.

<sup>3</sup> House of Commons, *Hansard*, 19 April 2007, col. 779-80.

## 2. 2004-05 target missed

There was general agreement that the first stage in achieving the overall objective of abolishing child poverty would be the easiest, i.e. moving above the poverty line those families whose income was nearest to that level of income. And this has proved to be the case, although not to the extent the Government had planned. Despite a significant reduction in child poverty against the Government's preferred measure of 60 per cent of median income, the 2004-05 target was missed (see Table 1).

On a Before Housing Costs (BHC) basis, relative child poverty fell from 3.1 million to 2.4 million between 1998-99 and 2004-05. But another 100,000 reduction was required to hit the 2.3 million target.

On an After Housing Cost (AHC) basis, the short fall was greater. Again, although child poverty fell from 4.1 million to 3.4 million, an additional fall of 300,000 was required to meet the initial target.

**Table 1: Relative Child Poverty, 1996-97 to 2005-06**

<b>Children in households below 60 per cent of contemporary median income, % and millions</b>				
	<b>Before Housing Costs (BHC)</b>		<b>After Housing Costs (AHC)</b>	
<b>Year</b>	<b>%</b>	<b>millions</b>	<b>%</b>	<b>millions</b>
1996-7	25.0	3.2	33	4.2
1997-8	25.0	3.1	32	4.1
<b>1998-99 (baseline)</b>	<b>24.5</b>	<b>3.1</b>	<b>32.5</b>	<b>4.1</b>
1999-00	23.4	3.0	31.9	4.1
2000-01	21.0	2.7	30.3	3.8
2001-02	20.7	2.6	29.6	3.7
2002-03	20.6	2.6	28.3	3.6
2003-04	20.5	2.6	27.9	3.5
<b>2004-05</b>	<b>19.6</b>	<b>2.4</b>	<b>27.3</b>	<b>3.4</b>
2005-06	20.5	2.5	28.6	3.5
<b>2004-05 target</b>		<b>2.3</b>		<b>3.1</b>
<i>Difference from target</i>		<i>0.1</i>		<i>0.3</i>
<i>1998-99 – 2004-05 change</i>		<i>-0.7</i>		<i>-0.7</i>
<i>2001-02 - 2005-06 change</i>		<i>-0.1</i>		<i>-0.2</i>

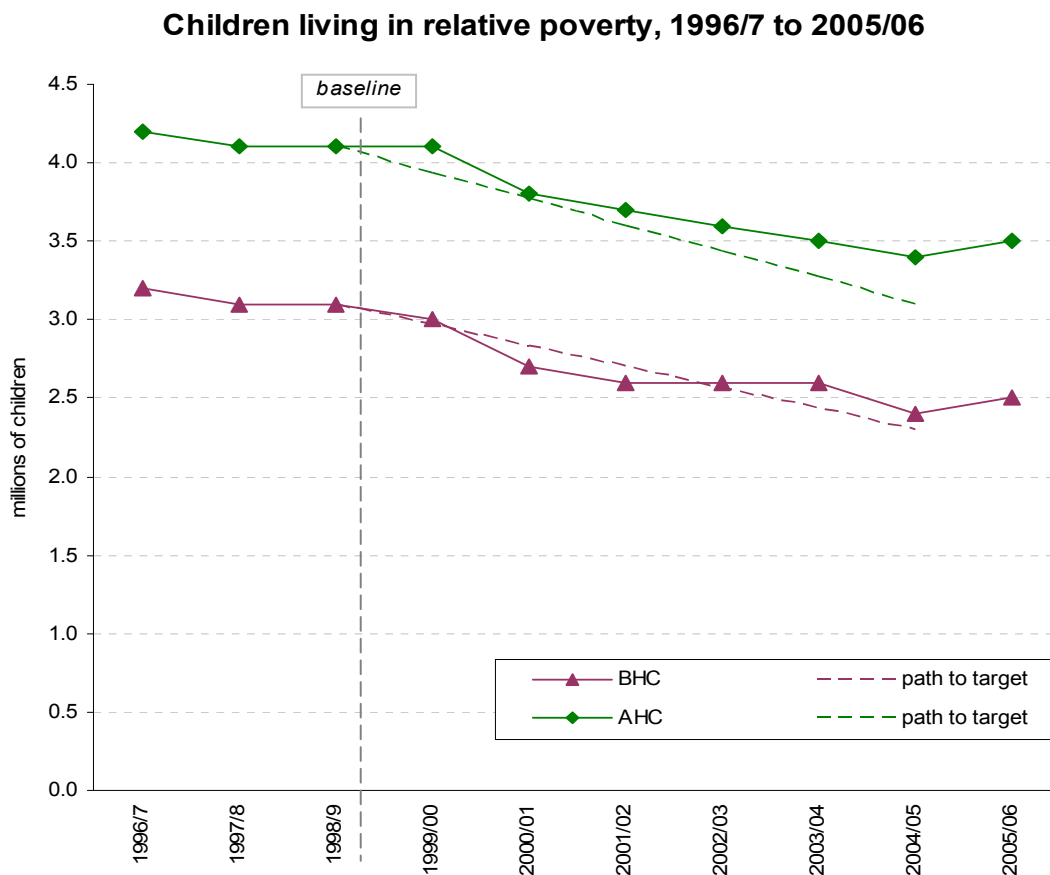
Source: House of Commons library

## Losing more ground

The latest data illustrate how difficult it is to merely maintain the important advance that has undoubtedly been made. The official figures for 2005-06 show that, instead of catching up in the last year, so to meet the first target, the position has deteriorated. An *additional* 100,000 children BHC, and 200,000 children AHC, were calculated to be in poverty last year (see Chart 1 below).<sup>4</sup>

What is also clear from the latest statistics is that most of the Government's progress in tackling child poverty took place in the first three years of the target being set, between 1998-99 and 2000-01. During this period, 400,000 children were taken out of poverty on a BHC basis and 300,000 on an AHC basis. Since then, progress has more or less stalled: child poverty has fallen annually, on average, by only around 20,000 BHC, or 40,000 AHC, over the five year period between 2001-02 and 2005-06. Important as this success is for each of the children affected, the change, in percentage terms, has been minimal.

**Chart 1**



Source: House of Commons Library

<sup>4</sup> Figures based on Government's original target measure using the McClement's equivalence scale. The increase is mirrored using the modified OECD scales.

### 3. Other poverty measures

A cut-off point of 60 per cent of median income measure allows us to see how many children are living in households below this threshold, but it tells us nothing about the changing number of children facing severe poverty. Nor does it tell us anything about the persistence of poverty. On these measures, the Government's record looks weaker still.

#### Severe poverty is unchanged

If we take a lower income target – 40 per cent of median income – the results are worse than if we take the higher 60 per cent cut-off point. The number and percentage of children living in households below 40 per cent of median income Before Housing Costs has not changed whatsoever since 1997.

700,000 children continue to live in severe poverty and the percentage of all children living below this line has remained the same at 5.5 per cent since 1997-98.

On an AHC basis the story is not that different. Although there has been a slight decline in numbers since 1997 (from 1.4 to 1.3 million), the rate is virtually unchanged with one in ten children still living in severe poverty.

**Table 2: Severe child poverty since 1997**

	Children in households below 40 per cent of median income			
	BHC		AHC	
	millions	%	millions	%
<b>1997-98</b>	0.7	5.5	1.4	11.0
<b>2005-06</b>	0.7	5.5	1.3	10.4

*Source: Institute for Fiscal Studies*

#### Persistent poverty remains high

Equally important is the length of time that children spend in poor households. The persistence of poverty is crucial to a child's long term prospects.

Persistence of low income is defined by the Government as spending three or more years out of any four year period in a household below 60 per cent of median income.

On this count, there has been a reduction in the percentage of children living persistently below the poverty threshold from 17 per cent, for the period 1997-2000, to 13 per cent between 2001-04, BHC, and from 22 per cent to 17 per cent over the same period, AHC. However, nearly one in six children in poverty remain persistently poor.

At the bottom 20 and 30 per cent of the income range there has been hardly

any progress since 1997. Around one in five children in the bottom 20 per cent of the income range are persistently poor on this measure, rising to nearly one in three of those in the bottom 30 per cent.

<b>Table 3: Persistence of child poverty</b>						
Percentage of group below threshold in at least three out of the last four years						
	BHC			AHC		
	Below 60 per cent of median	In bottom 20 per cent	In bottom 30 per cent	Below 60 per cent of median	In bottom 20 per cent	In bottom 30 per cent
<b>1991-94</b>	20	22	33	25	23	34
<b>1992-95</b>	18	21	32	23	22	34
<b>1993-96</b>	17	20	33	23	22	34
<b>1994-97</b>	17	20	32	24	23	34
<b>1995-98</b>	17	20	32	24	22	34
<b>1996-99</b>	16	20	32	23	22	32
<b>1997-00</b>	17	20	32	22	21	32
<b>1998-01</b>	17	21	31	22	22	34
<b>1999-02</b>	17	20	31	21	21	34
<b>2000-03</b>	15	19	30	19	20	33
<b>2001-04</b>	13	18	30	17	19	32

*Source: DWP, Households below average income 2005-06*

### **Child poverty measured by expenditure has increased**

The Institute for Fiscal Studies argues that, in many respects, expenditure is a better base from which to measure poverty. While income levels can be temporary (changing with employment status, sickness and age), spending patterns are usually more consistent, as people save and-or borrow to smooth the effects of these “income shocks”. The IFS argue that measuring household expenditure may give us a more reliable indicator of living standards and poverty.<sup>5</sup>

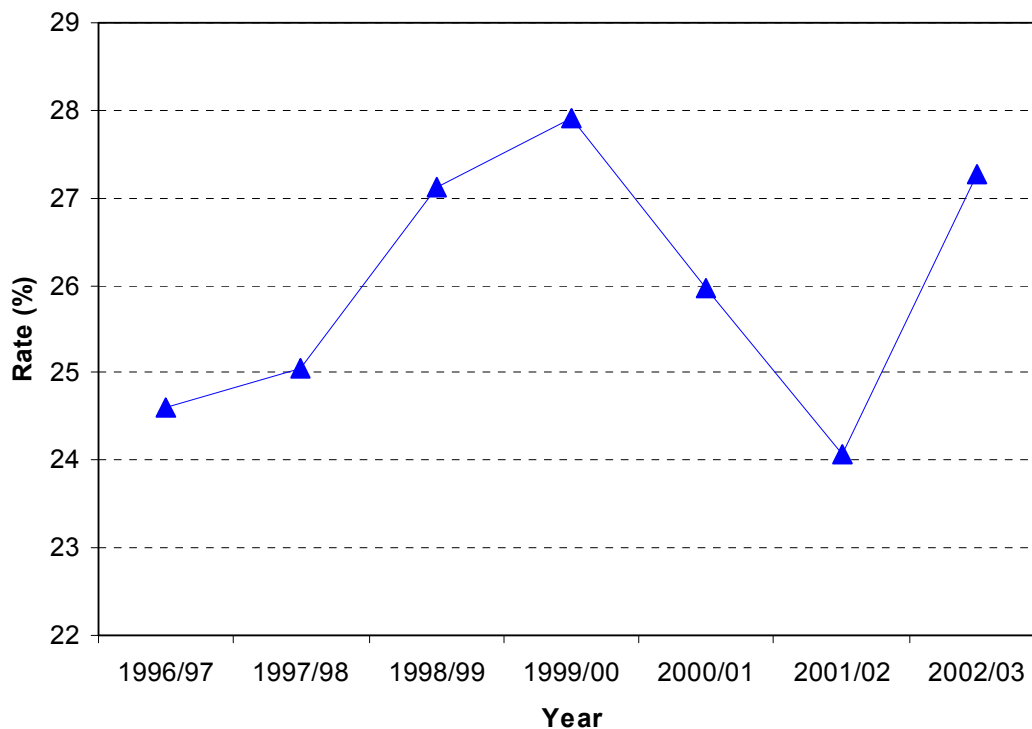
Chart 2 shows that in 1996-97, 24.6 per cent of children were in poverty on an

<sup>5</sup> Brewer, M., Goodman, A. and Leicester, A. (2006), *Household Spending in Britain: what can it teach us about poverty?*, Institute for Fiscal Studies.

expenditure basis. By 1999-00 it had peaked at 27.9 per cent before falling slightly in the next two years. The latest available data for 2002-03 show that it was back up to 27.3 per cent, nearly three percentage points above its 1997 level. The most optimistic interpretation that can be put on these data is that the 2002-03 figure is a blip. We will know whether this is so when the next set of expenditure data is compiled by the IFS. The Government should finance the IFS to produce these data.

**Chart 2**

**Expenditure Child Poverty Rates 1996/97-2002/03**



Source: Brewer, M., Goodman, A. and Leicester, A. (2006), *Household Spending in Britain: what can it teach us about poverty?*, Institute for Fiscal Studies. Expenditure measure is 60 per cent of median earnings BHC.

## 4. The future targets: 2010-11 and 2020

Despite extra spending on families with children, the Government missed its 2004-05 poverty target and has lost further ground in the last year. One in ten children live in severe poverty and persistent poverty remains disturbingly high.

The 2004-05 target was only the first of three targets set by the Government. By 2010-11 it aims to halve child poverty from its 1998-99 level and, by 2020, “to effectively eradicate” it (*sic*). After failing to achieve the first and easiest target, the Government has redefined the subsequent ones.

### Redefining 1 million children out of poverty

There was no consultation within Government, let alone with anyone else, when the original poverty targets were set. Even though one of the authors of this report was Minister for Welfare Reform at the time, he only learned of the targets by reading the newspapers. Had there been some discussion the Government might not have committed itself to the almost-impossible goal of abolishing child poverty by 2020.<sup>6</sup> It was therefore a welcome development that a consultation process was started in April 2002 and reported at the end of 2003. But, changing the targets to more rational ones, only after failure to meet the original targets, puts the Government in an unnecessarily weak position.

The result of this consultation was that the DWP changed the way it chose to measure the Government’s performance against its poverty targets.<sup>7</sup> The new child poverty target was to be measured by three different indicators:

- Relative low income indicator: keeping the 2004-05 target of 60 per cent of contemporary median income but on a BHC basis only.
- Absolute low income indicator: the number of children below 60 per cent of median income on the 1998-99 baseline and adjusted for price inflation only.
- Material deprivation and low income indicator: the number of children lacking “particular necessities” (undefined as yet) and living below 70 per cent of contemporary median income.

The most significant contrast with the 2004-05 target is that the new 60 per cent of contemporary median income indicator will only be judged on a BHC basis. The Government argued that this measurement was adopted to aid European Union comparisons.<sup>8</sup>

The change has provoked criticism that the Government is deliberately

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<sup>6</sup> The goal would only be achieved by reshaping the distribution of income to a degree never achieved in this country. The goal of abolition as an inspiration is difficult to praise adequately.

<sup>7</sup> Department for Work and Pensions (2003), *Measuring child poverty consultation*.

<sup>8</sup> *Ibid.*

shifting the goal posts to make it easier to meet its targets. The change has the effect of reducing the number of children in poverty by 1 million. Whereas, in 2005-06, relative child poverty was 3.8 million AHC it was only 2.8 million BHC.<sup>9</sup>

Commenting on the change, the IFS notes:

“By moving to a relative child poverty measure based solely on BHC incomes, fewer children have to be moved out of poverty for the Government’s targets to be met. This may make achieving the targets less expensive than had the focus on incomes measured AHC been maintained.”<sup>10</sup>

### **A new equivalence scale**

Whilst the Government has redefined a million children out of poverty by using only BHC, it has also made a further change which makes eliminating child poverty more difficult.

The new measure will also be using different equivalence scales – the device used to adjust household income to take account of family size and composition. Up until this change the targets were based on the McClements scale for equivalising incomes. From 2005-06 the Household Below Average Income survey on which child poverty figures are based, will use the Modified OECD equivalence scales, so as to bring them in line with international practice. The effect of this change is to increase the number of children in poverty by 300,000 (see Table 4) – thus partially compensating for the redefinition of 1 million children out of poverty, as discussed above.

**Table 4: Child poverty under the McClements and OECD equivalence scales**

	Number of children in poverty, million, BHC basis	
	McClements	OECD
<b>1998-99</b>	3.1	3.4
<b>2004-05</b>	2.4	2.7
<b>2005-06</b>	2.5	2.8

*Source: Brewer et al. (2007), Poverty and Inequality in the UK 2007, IFS*

### **What does “eradication” by 2020 really mean?**

The consultation on the new child poverty measure attempted to define what “eradication” by 2020 should mean. It commented that it could be defined as having a “material deprivation child poverty rate that approached zero and being amongst the best in Europe on relative low incomes”.<sup>11</sup> It was

<sup>9</sup> Note: this is using the new OECD equivalence scales for 2005-06 and not McClements scales as previously. Figures from Institute for Fiscal Studies (2007), *Poverty and Inequality in the UK*.

<sup>10</sup> Institute for Fiscal Studies (2004), *Poverty & Inequality in Britain*, IFS Commentary 96.

<sup>11</sup> Department for Work and Pensions (2003), *Measuring Child Poverty*

suggested that “best in Europe” could be defined as a relative rate no higher than the average of the best three European countries, or being within 2 per cent age points of the average of the best three: a rate of child poverty comparable to Sweden and Denmark.

The Child Poverty Action Group has pointed out that this would, in effect, still leave a considerable number of children in poverty. The “goal of ‘eradicating child poverty’ now appears not to mean removing every child from poverty at all”.<sup>12</sup>

### **2010-11 relative poverty target will be missed on current plans**

It has been argued elsewhere that the relative poverty target of halving child poverty by 2010-11 on a 60 per cent of median income basis, BHC, using the modified OECD equivalence scales, will be the “most binding” of the three new indicators.<sup>13</sup>

The fact that the Government missed the 2004-05 target, and that poverty on the 60 per cent of median income measure actually rose by 100,000 last year, will make it even more difficult to meet the 2010-11 target and eventually the 2020 target, however defined.

With child poverty falling by only 600,000 from its 1998-99 baseline, the number of children in poverty now needs to fall by a further 1.1 million by 2010-11 – to reach 1.7 million (BHC, using the new OECD scales). This requires a reduction of more than 200,000 over each of the next five years: *ten times* the rate achieved on average over the last five years, BHC (at around 20,000 a year).

The IFS forecast, before the 2007 budget, that on current tax and benefit policies there would be hardly any change in the number of children in poverty by 2010-11 and that the Government would miss the 2010-11 target by 1 million. Since the Budget in March, when the Government announced changes to tax credits which are expected to lift a further 200,000 children out of poverty, this forecast has been revised to 800,000.<sup>14</sup> On this basis, the fall in child poverty over the next five years needs now to be eight times the rate achieved over the last five (at 160,000 a year).

### **Cost of meeting targets**

Work undertaken by the IFS for the Joseph Rowntree Foundation has calculated what it would cost the Government to meet the 2010-11 and 2020 target using existing policy levers. Before Budget 2007, the Institute estimated that for the next target to be met, by 2010-11, the Government would need to be spending £4.3 billion more than is currently planned through increased tax

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<sup>12</sup> Doman, P. (2004), *Defining income poverty out of existence?*, Child Poverty Action Group.

<sup>13</sup> Institute for Fiscal Studies (2007), *Poverty and inequality in the UK*.

<sup>14</sup> Budget 2007 announced from April 2008 to 1) increase the income threshold at which working tax credit is received in full by £1,200 to £6,420 a year, 2) increase the child element of child tax credit by £150 a year above earnings indexation.

credits and benefits – nearly 1.5 pence off the standard rate of tax.<sup>15</sup>

This sum has been re-calculated following changes in the last Budget. The IFS now estimate that to have only a 50:50 chance of meeting the next target (i.e. a reduction of 800,000), there will need to be additional spending of £3.8 billion a year by 2010-11.<sup>16</sup> In 2020, the Government would need to be spending an extra £30 billion a year in order to abolish child poverty.<sup>17</sup> No one believes that anything like this sum will be forthcoming.

Future spending commitments are going to be much tighter than they have been previously. The 2007 Budget announced that growth in public spending would fall from an average of 4 per cent a year over the past nine years to 2 per cent a year between April 2008 and March 2011.<sup>18</sup> With financial resources decreasing, it is clear that the Government needs radically to re-think its anti-poverty strategy. Before we move to such a discussion it is important to look at the different risks children face in becoming poor.

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<sup>15</sup> A 1p change on the basic rate of income tax raises £3,150 million in 2007-08 (HMRC).

<sup>16</sup> Treasury Committee evidence, *Budget 2007*.

<sup>17</sup> Hirsch, D. (2006), *What will it take to end child poverty?*, Joseph Rowntree Foundation.

<sup>18</sup> Institute for Fiscal Studies (2007), *Green Budget*.

## 5. The risk of child poverty

An analysis of which children are most at risk of poverty suggests how the Government needs to reshape the whole of its anti-poverty strategy. The result of changes to the tax and benefit system since 1997 has been to reduce greatly the risk of poverty for children in lone parent households. In 1997-98, two out of three children in lone parent families were poor. By 2005-06, this had fallen to one in two (See Table 5).

**Table 5: Children's risk of living in households below 60 per cent of median income (AHC) since 1997-98, by family type and work status, %**

	1997-98	1998-99	1999-00	2001-02	2002-03	2003-04	2004-05	2005-06
<b>Lone parent, of which:</b>	<b>64</b>	<b>64</b>	<b>61</b>	<b>58</b>	<b>55</b>	<b>52</b>	<b>52</b>	<b>50</b>
in FT work	14	16	16	13	18	10	15	14
in PT work	42	50	41	40	36	30	32	30
not working	84	83	84	81	80	78	76	75
<b>Couple with children, of which:</b>	<b>25</b>	<b>25</b>	<b>24</b>	<b>22</b>	<b>22</b>	<b>21</b>	<b>21</b>	<b>23</b>
one or more FT self employed	30	31	29	29	25	26	28	33
both in FT work	2	1	2	1	3	3	2	3
one in FT work, one in PT work	6	7	6	7	6	5	6	7
one in FT work, one not working	27	30	28	23	25	22	23	26
one or more in PT work	64	58	65	61	59	57	48	53
both not in work	82	83	79	81	80	77	74	74

*Source: DWP, Households below average income 2005-06, supplementary table E3*

However, there has been no real change in the risk of poverty for children in two parent households. Children in these families have around a one in four chance of being in poverty; a similar level to that in 1997. In fact, in the last year there has actually been a rise, from 21 to 23 per cent, in the poverty risk

for children in two parent families.

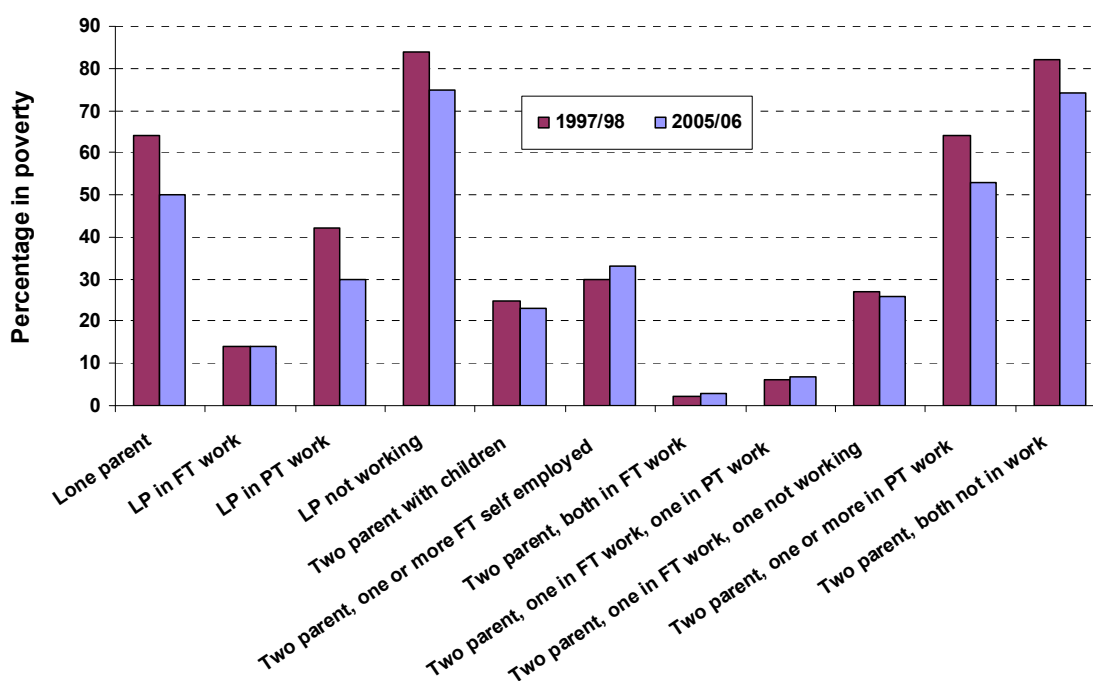
The reason why the risk of poverty for children in lone parent households has generally fallen so much is quite simple - there has been a drop in the poverty rate for workless lone parent households, which make up the majority of lone parent families in poverty, from 84 to 75 per cent. And for those in part time work, the risk has fallen from 42 to 30 per cent.

There has also been a decline in the risk of poverty for children in workless two parent households (82 to 74 per cent) and for two parent families where at least one parent is in part time work (from 64 per cent to 50 per cent).

Tax and benefit expenditure since 1997 has been most effective at helping lone parents and two parent families who are out of work (thereby reducing the risk of child poverty significantly in these households). But tax and benefit expenditure has not been nearly as effective at helping two parent households in work.

**Chart 3**

**Comparing the risk of child poverty by household type and work status, 1997/98 and 2005/06**

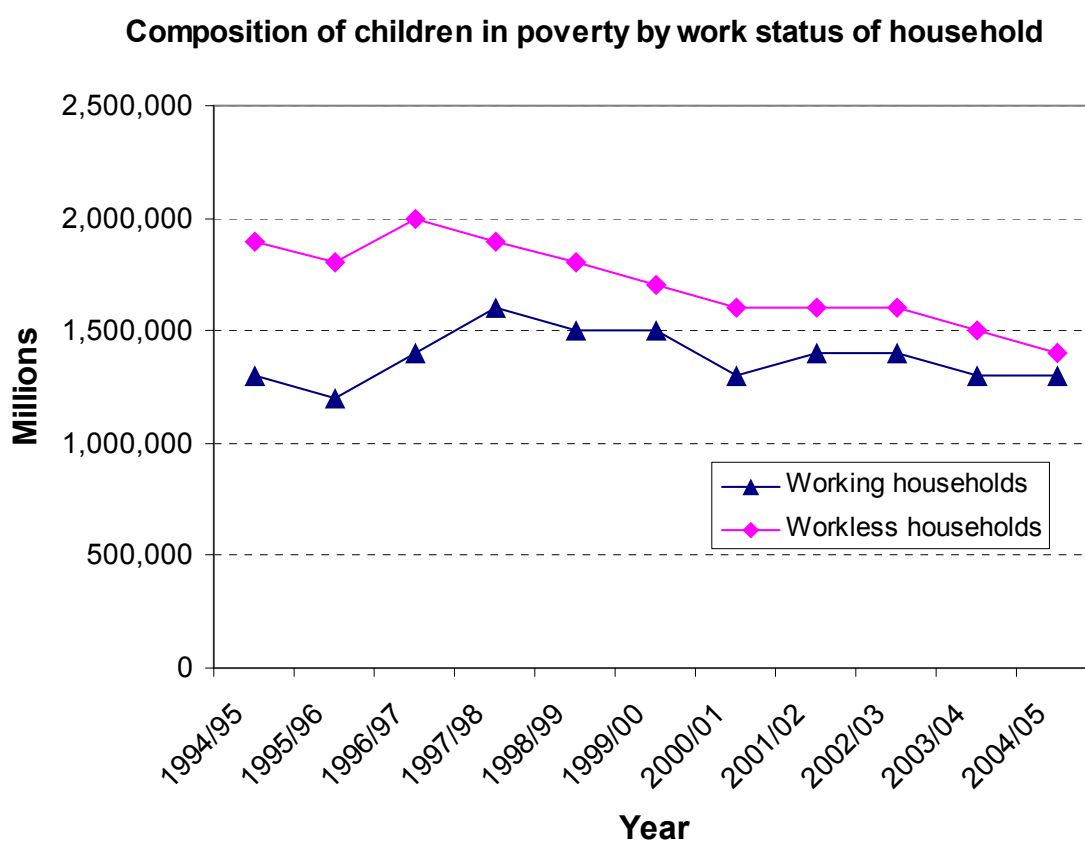


## 6. The composition of child poverty

Around 20 per cent of children in working families are poor. But because of the sheer size of the working household group, half of all children in poverty are now in working families.

This is largely attributable to the fact that, since 1997, there has been a convergence in the numbers of children in working and workless poor households. The number of children in workless households in poverty has fallen by 500,000 since 1994-95, but the number of children in poor working households was the same in 2004-05 as in 1994-95, at 1.3 million (BHC).<sup>19</sup>

**Chart 4**



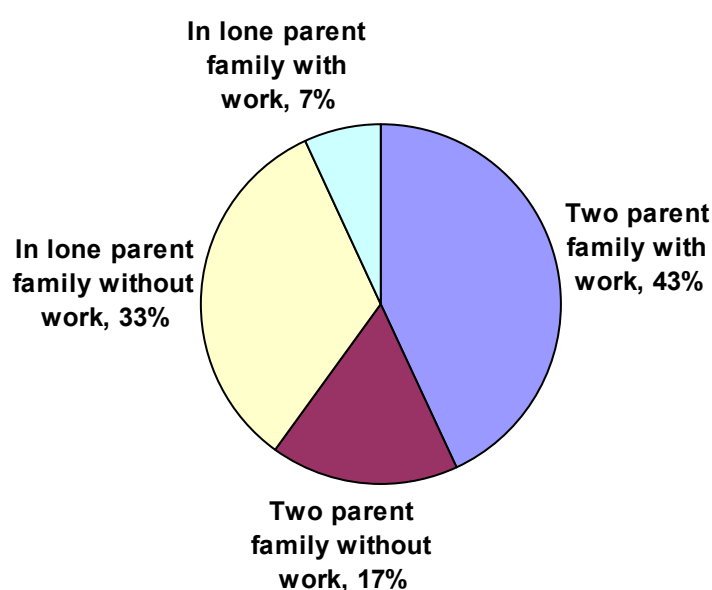
<sup>19</sup> Figures for children in poor working and workless households taken from Parliamentary Answer 133943, 25 April 2007.

## Two-fifths of poor children live in two parent families in work

Although the risk of poverty is lower in two parent households, their greater number overall means they represent a larger proportion of all children in poverty: 60 per cent of children in poverty live in two parent families; as compared to 40 per cent in lone parent families. In fact, two parent families in work account for the largest single group of poor children (see Chart 5):

**Chart 5**

### Composition of child poverty by household type and work status, 2005/06

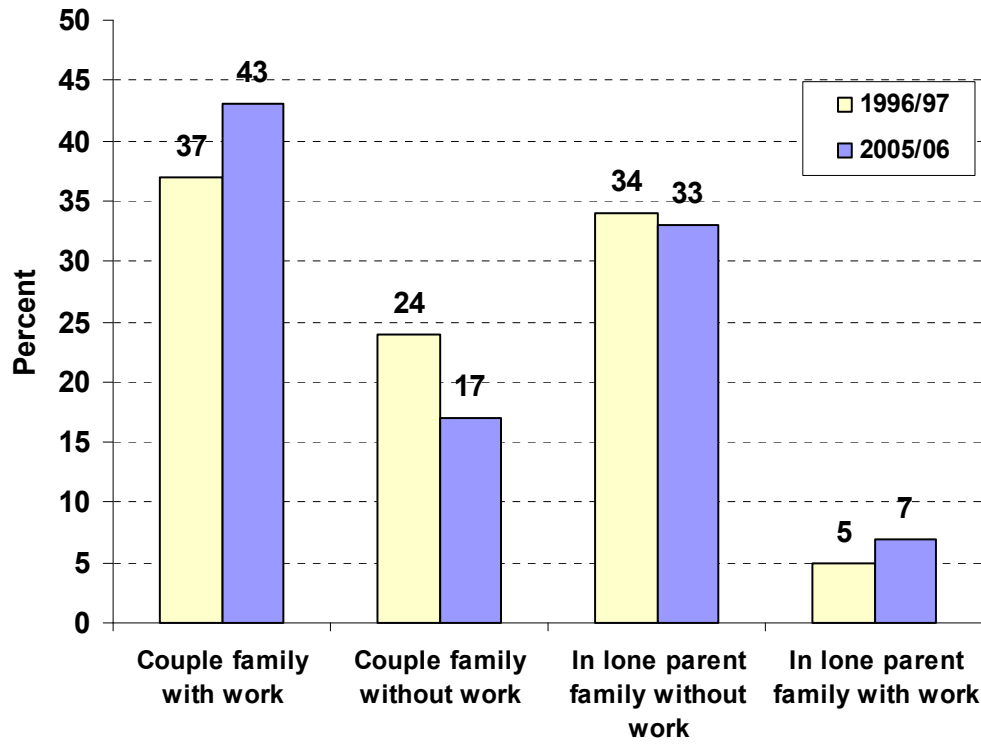


*Source: Department for Work and Pensions (2007), Households below average income 2005-06. supplementary table E5*

Since 1997, there has been an increase in the proportion of poor children in working two parent families; up from 37 per cent to 43 per cent, whilst there has been a drop from 24 to 17 per cent in the proportion of poor children in two parent families without work. There has been little change in the proportion of children in working and workless lone parent households. In other words, the tax and benefit changes have least helped working two parent families:

**Chart 6**

**Comparing the composition of child poverty by household types and family status, 1996-97 and 2005-06**



*Source: Department for Work and Pensions (2007), Households below average income 2005-06. supplementary table E5*

## **7. Two major design faults in the tax credit system**

### **Brutally discriminates against two parent households**

A significant reason behind the changing risk and composition of child poverty for different households is the Government's tax credit system. Children in working two parent households in poverty are brutally discriminated against.

While it is estimated that two parent households with two children need 30 per cent more income than lone parents to achieve the same standard of living<sup>20</sup> (resulting in a poverty line in 2004-05 for couples with two children of £294 a week, compared with £225 a week for a single parent with two children<sup>21</sup>) the tax credit system does not reflect this. It pays the same amount to a lone parent as to a two parent family (when they have the same number of children and the same gross income).

The result is that two parent households need far greater earnings than a lone parent to move past the poverty line. In 2004-05, two parents with two children had to earn £240 a week to have a net income of £295, to lift themselves above the poverty line. By contrast, a lone parent with the same number of children needed to earn just £76 a week to gain a net income of £230, £5 above the poverty line.<sup>22</sup>

And with tax credits not making allowance for the second adult in the household, two parent families needed to work far longer to achieve the same level of income. In 2006, a lone parent with 2 children under 11, working 16 hours a week on the minimum wage, gained a total net income of £487 a week, largely due to tax credits. In order to attain the same weekly income, an equivalent two parent household needed to work 116 hours a week; an extraordinary 100 hours more than the single parent.<sup>23</sup>

### **Not focused on children in poverty**

4.2 million children in working families in 2004-05 received tax credits over and above the family element. Of these, only one in four were lifted out of poverty as a result of these payments. But half of children in families claiming tax credit payments are not deemed poor. And around one in four received tax credit entitlement but remained in poverty (AHC), falling to nearly one in six BHC<sup>24</sup> (Chart 7). The results of tax credit payments do not square up with the Government's claim that selective policies are the means by which to help poor families most.

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<sup>20</sup> In technical terms this is called equalising income for household size and composition. The Government now uses the modified OECD scales to adjust incomes.

<sup>21</sup> Brewer, M. (2007), *Supporting couple with children through the tax credit system*, Green Budget 2007, Institute for Fiscal Studies. Using 60 per cent of median income BHC and OECD equivalence scales.

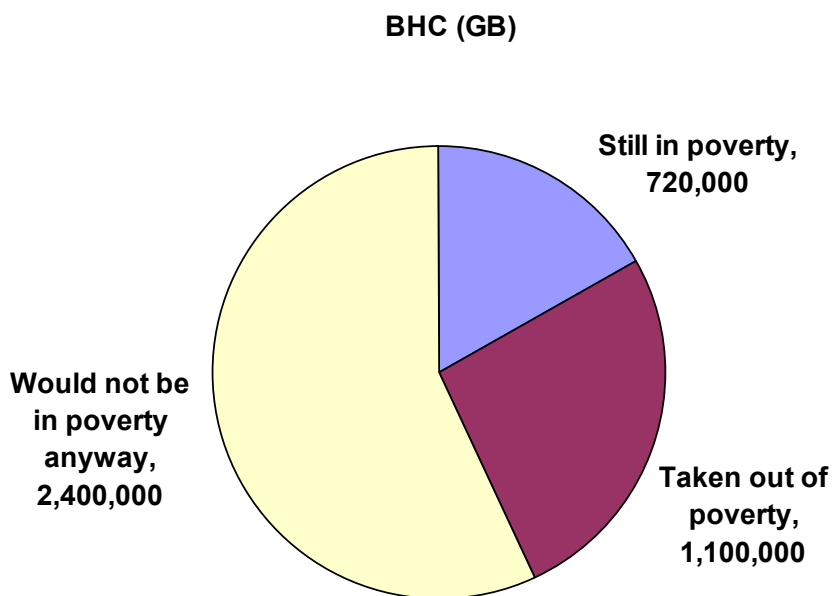
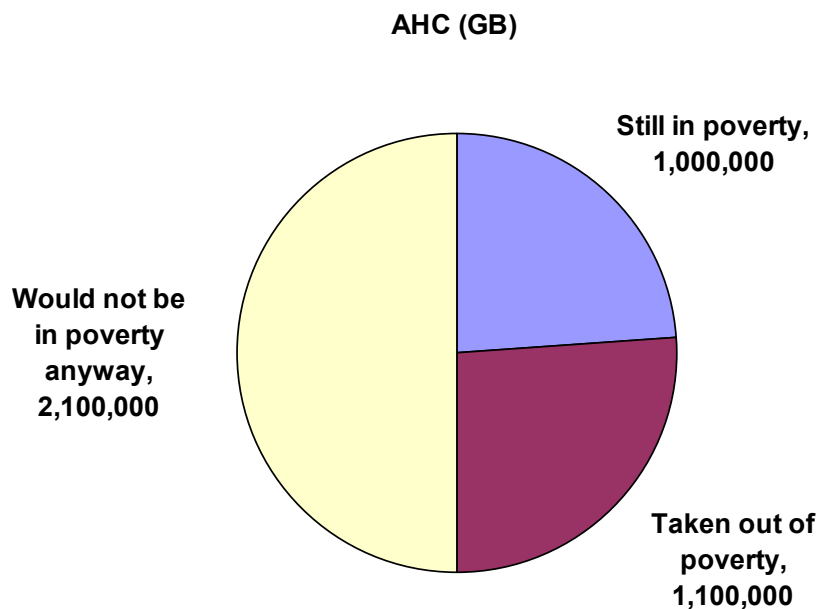
<sup>22</sup> Argument and figures taken from Institute for Fiscal Studies (2007), *Green Budget* (with corrections by Mike Brewer).

<sup>23</sup> House of Commons library note, 16 May 2007 (Net income is measured BHC).

<sup>24</sup> New Policy Institute, *The Poverty Site* website.

**Chart 7**

**Children in working households in receipt of tax credits above the family element, 2004-05**



*Source:: Figures provided by the New Policy Institute*

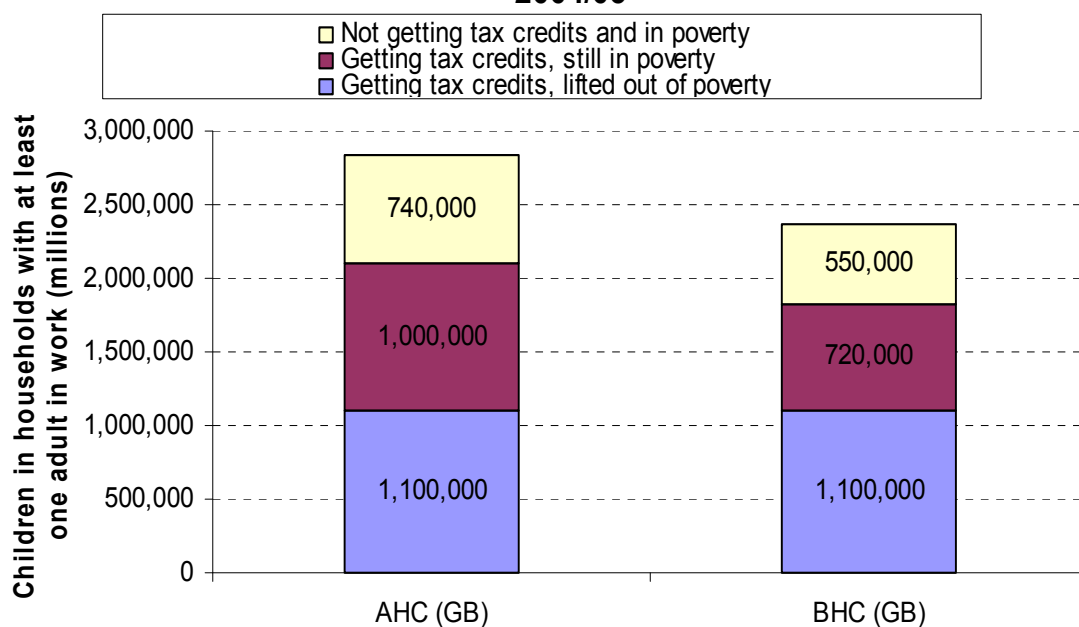
There were 2.8 million children in working poor households *excluding* tax credits in 2004-05 AHC, and 2.4 BHC.

On an AHC basis, 1.1 million were lifted out of poverty after tax credits were received, but 1 million were still in poverty with tax credits. Importantly, as many as 740,000 children were in poverty and not receiving tax credits.<sup>25</sup>

On a BHC basis, 1.1 million were lifted out of poverty by tax credits, while 720,000 were still in poverty with tax credits and 550,000 were in poverty without getting tax credits.

**Chart 8**

**Children in working poor households before tax credits,  
2004/05**



Source: New Policy Institute

<sup>25</sup> New Policy Institute, *The Poverty Site* website. Not receiving is a mixture of ineligible and not claiming.

## 8. Policy options

The Government has so far used two strategies to reduce both the risk and incidence of child poverty amongst families:

- increasing employment rates (particularly among lone parents), and;
- increasing benefits-tax credits.

In the early years, between 1997 and 2001, improvements in employment had driven the falls in child poverty.<sup>26</sup> But recent research by the IFS has shown the growing importance of increases in benefit and tax credits in achieving this goal.<sup>27</sup>

Given the reduced scope for large scale increases in benefits and tax credits due to reductions in expected increases in public spending, it is now important to re-focus the employment and tax credit strategy. It is also imperative that the Government start to address other important policies like child maintenance and education as agents in its anti-poverty strategy.

### Freud isn't the answer

While there has been a good deal of success in getting parents back to work, particularly lone parents (employment rates have improved from 47 per cent in 1997 to 56 per cent), this has stalled over the last year.<sup>28</sup> It is not clear, anyway, how much effect Government initiatives have had on this improvement (research has shown that policy reforms only accounted for about five percentage points of this increase, with the rest due to macro changes in employment).<sup>29</sup>

Yet one option, proposed in the Freud review, would be to increase conditionality on lone parents by time limiting benefit so that income support stops when the youngest child is 12, and not 16 as is the case currently.<sup>30</sup> However – as half of lone parents now on income support have at least one child under 5 and 80 per cent at least one child under 11 – time limiting benefit for single parents would not lead to a significant increase in the employment rate.<sup>31</sup> Time limiting benefit also ignores the other major route out of poverty for single parents: re-partnering.

There is a case for reviewing conditionality rules right across benefits. But this particular reform would have little effect. One neglected route out of poverty is for the non-working partner in a couple to get part time employment: this would reduce the risk of child poverty from 26 per cent to 7 per cent. But the deep bias in the tax credit system against two parent

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<sup>26</sup> Piachaud, D., Sutherland, H., & Sefton, T. (2003), *Poverty in Britain: the impact of government policy since 1997*, Joseph Rowntree Foundation.

<sup>27</sup> Institute for Fiscal Studies (2006), *Poverty and inequality in Britain*.

<sup>28</sup> Office for National Statistics.

<sup>29</sup> Institute for Fiscal Studies (2006), *Welfare to work policies and child poverty*.

<sup>30</sup> Freud, D. (2007), *Reducing dependency, increasing opportunity: options for the future of welfare to work*, Department for Work and Pensions.

<sup>31</sup> Hirsch, D. (2006), *What will it take to end child poverty?*, Joseph Rowntree Foundation.

families makes this an increasingly unlikely option.

### **Cease discriminating against two parent families**

Given that half of children in poverty are now in working households and 80 per cent of these are headed by couples, it is imperative that the tax credit system is re-balanced to take account of two parents and to encourage potential second earners in these families to work.

As it stands, although couples with children are expected to require greater income than lone parents to live above the poverty line, the tax credit system does not reflect this.

At the same time, Working Tax Credits increase the incentives to work for first earners in a couple while decreasing the incentives to work for the second potential earner. This comes about because Working Tax Credit is only available to households with at least one earner but is then means tested against the income of both adults. Hence, if the second adult were to get work too, payments would be reduced. According to IFS evaluations of the impact of the former working families tax credit (which was structured similarly to WTC), on the employment patterns of couples, showed that it increased employment amongst parents whose partner did not work and reduced it for parents where the other partner did work.<sup>32</sup>

One way of reducing child poverty would be to remove the bias against two parent families by re-weighting the tax credit system to take account of both the extra costs of two parent households and to encourage work of both parents in those households.

### **Cease discriminating against single parents who re-partner**

There is conflicting information on how important re-partnering is as an escape from welfare dependency for single parents. Data relevant to the period before 1997 show re-partnering as almost as important an exit as gaining work. The latest information, however, shows that while re-partnering's importance has fallen, it still accounts for over one in four exits of lone parents from welfare.<sup>33</sup> This fall is to be expected given the huge financial penalty in the tax credit system for families with two adults.

Even so these exits data are remarkable. One in four of single parents leaving the welfare rolls amounts to 70,000 each year.<sup>34</sup> Each of these single parents have found a partner where the household income from tax credits will not be increased whatsoever as a result of a second adult becoming part of the household. What might the exit rate might be if a reformed tax credit system took proper account of the second adult in a working household? Imagine also what the "exit rate" from welfare would be for couples who are illicitly

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<sup>32</sup> Argument taken from Institute for Fiscal Studies (2005), *Supporting couples with children through the tax system*.

<sup>33</sup> Department for Work and Pensions (2004), *Destination of benefit leavers*.

<sup>34</sup> House of Commons library figures show that for the latest data for the year to Feb 2005 around 270,000 lone parents left Income Support.

living together, while the mother claims for benefit purposes that she is a single parent family. There are, after all, 200,000 more single parents claiming tax credits that actually exist.<sup>35</sup> Ceasing to discriminate against two parent families would encourage a very significant number of single parents who are dishonestly claiming benefit as a single parent to cease to do so.

### **Child maintenance**

Given the fact that 40 per cent of children in poverty live in lone parent families, child support should be an integral part of lifting these children out of poverty. Currently only 22 per cent of lone parents and 4 per cent of couples are receiving maintenance payments. And child maintenance payments lift around 14 per cent of children in lone parents out of poverty and 3 per cent of those in two parent households.

Comparative data show what a more effective child maintenance system could achieve in decreasing child poverty. 25 per cent of poor children are lifted out of poverty by child maintenance in Australia, 24 per cent in Switzerland and 18 per cent in Sweden. By contrast, the figure for the UK is just 2.9 per cent.<sup>36</sup> We will return to the issue of child maintenance in a future report.

### **Education**

The best way to tackle future child poverty is to make sure that the children of today are equipped with the skills necessary to find well paid jobs tomorrow. For people leaving school at the minimum age, each extra year of schooling appears to boost earnings in mid-life by about 15 per cent.<sup>37</sup>

But one-in-ten 16 year olds still obtain fewer than five GCSEs; the same proportion as in 1999-2000. Again, this topic will be dealt with in a future report.

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<sup>35</sup> Brewer, M. & Shaw, J. (2006), *How many lone parents are receiving tax credits?*, IFS Briefing Note 70, Institute for Fiscal Studies.

<sup>36</sup> Harker, L. (2006), *Delivering on child poverty: what would it take?*, Joseph Rowntree Foundation.

<sup>37</sup> Hirsch, D. (2006), *What will it take to end child poverty?*, Joseph Rowntree Foundation.

## 9. Conclusions

The announcement by Tony Blair in 1999 that his Government would be the first to explicitly attempt to abolish child poverty was a noble objective and this Government deserves unreserved praise for putting child poverty at the top of its agenda.

But 10 years on and the record looks patchy. Although a great deal was achieved in its first term on its preferred relative poverty measure, it failed to meet its first target in 2004-05 and is set to miss all the future targets. Worse still, severe child poverty has been untouched and persistent poverty remains high.

To come anywhere near hitting the target for 2010-11 the Government would need to spend an additional £4 billion a year. But does anybody think this is a realistic option? A radical re-structuring of the Government's anti-poverty strategy is needed.

The clearest failing of its approach so far has been its treatment of two parent households in work. Although children in single parent families have the greatest risk of poverty, in absolute terms, children in working two parent households represent the largest single group of poor children.

To date, the tax and benefit system has been skewed towards lone parents by discriminating against two parents in work. In the last year there has been an actual increase in the percentage of children in working two parent households that are poor.

There is a single immediate step the Government should take. Any new money for the tax credit system should be used to lessen and then abolish the system's discrimination against two parent households. This would target help towards the largest group of poor children. It would also cease discriminating against single parents when re-partnering. Such a move would now be a more effective weapon against child poverty. It would increase the number of two parent families in work, make re-partnering of single parents an even more important exit from poverty and is likely to encourage significant numbers of single parents to regularise their partnering arrangements.

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