Child Tax & Welfare Benefits and Their Possible Effect on Population Growth

Prepared for Population Matters by Alan Castle January 2013

1. Introduction

Family Allowance started almost 70 years ago and, in its present form of Child Benefit and together with other significant tax and welfare benefits, is now an important part of many family incomes. At a time when UK population is substantially above what many be considered to be a sustainable level, and UK fertility remains well above the European average, is there a link between the value of tax and welfare benefits and larger families? If there is, how can the money used for these benefits be used to help families without encouraging them to have children for financial reasons?

Priority access to both social housing of any kind and larger properties are sometimes cited as a further incentive to childbearing. Detailed consideration of this has been omitted from this study for reasons of simplicity. However, this benefit will be restricted in some cases by the implementation of the proposed benefit cap.

2. Background

2.1 The Family Allowances Act 1945 came into operation from 6 August 1946, and was the first law to provide child benefit in the United Kingdom. In taxation, there had been a child allowance for some time but this did not benefit the unemployed or other families who paid no tax, and benefitted the taxpayer rather than the carer, raising a doubt about whether the money reached its intended target. Family allowances had been one of the items proposed by the Beveridge Report in 1942 in order to ameliorate child poverty. The Labour Party briefly debated pressing for allowances during the Second World War, but a party conference resolution to this end was opposed by the trades unions for fear that the amount paid would be taken into account in wage negotiations, leaving workers no better off.

As passed, the Act allowed payment of an allowance of five shillings per week for each child in a family, other than the eldest; later Acts increased this sum. One-child families received no benefit at all and the Family Allowance Act 1956 addressed this, extending the provision to all children whilst the child was of school age, up to the age of 18, if apprenticed or in full-time school education. Subsequently, for ease of administration, it was incorporated into the tax system as an allowance against income tax, but, since the majority of taxpayers were fathers, it was suggested that it rarely reached its intended target, and did not help those who paid little or no tax. For that reason it became Child Benefit, effectively reverting to being a welfare allowance, but is anomalous in continuing to be administered by the tax authorities rather than the Department for Work & Pensions.

Table 1: Amounts payable from April 2011 and fixed for 3 years are:

<table>
<thead>
<tr>
<th>Who the allowance is for</th>
<th>Current weekly amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Eldest or only child</td>
<td>£20.30</td>
</tr>
<tr>
<td>Additional children - per child</td>
<td>£13.40</td>
</tr>
<tr>
<td>Guardian's Allowance - per child</td>
<td>£15.50**</td>
</tr>
</tbody>
</table>

**Guardian's Allowance is a tax-free payment for people who are bringing up children whose parents have died, and is paid in addition to the Child Benefit payment.

2.2 Child Tax Credit

Child Tax Credit was introduced in April 2003 and replaced the Children's Tax Credit and the child-related part of
the Working Families Tax Credit. It also replaced the child elements of Income Support and Jobseeker’s Allowance. It is paid either weekly or monthly, is in addition to Child Benefit and like Child Benefit is paid free of tax. Eligibility requirements are quite complicated and Child Tax Credit may be payable in conjunction with Working Tax Credit.

Table 2: This table shows how payments are made up:

<table>
<thead>
<tr>
<th>Element</th>
<th>Annual amount for 2012-13 (£)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Family element (one per family)</td>
<td>545</td>
</tr>
<tr>
<td>Child element (paid for each child/qualifying young person)</td>
<td>2,690</td>
</tr>
<tr>
<td>Disabled child element (paid in addition to the child element)</td>
<td>2,950</td>
</tr>
<tr>
<td>Severely disabled child element (paid in addition to the child and disability elements)</td>
<td>1,190</td>
</tr>
</tbody>
</table>

Table 3: The actual total amount payable is based on income. As a rough guide, an award of Child Tax Credit is made if there is one child and a household income of up to about £26,000 or two children and a household income of up to about £32,200.

Examples of Payments for Tax Year 2012/13 if the Individual is not Eligible for Working Tax Credit

<table>
<thead>
<tr>
<th>Annual income (£)</th>
<th>One child/ qualifying young person</th>
<th>Two children/ qualifying young persons</th>
<th>Three children/ qualifying young persons</th>
</tr>
</thead>
<tbody>
<tr>
<td>No income</td>
<td>3,240</td>
<td>5,930</td>
<td>8,620</td>
</tr>
<tr>
<td>5,000</td>
<td>3,240</td>
<td>5,930</td>
<td>8,620</td>
</tr>
<tr>
<td>8,000</td>
<td>3,240</td>
<td>5,930</td>
<td>8,620</td>
</tr>
<tr>
<td>10,000</td>
<td>3,240</td>
<td>5,930</td>
<td>8,620</td>
</tr>
<tr>
<td>15,000</td>
<td>3,240</td>
<td>5,930</td>
<td>8,620</td>
</tr>
<tr>
<td>20,000</td>
<td>1,545</td>
<td>4,235</td>
<td>6,925</td>
</tr>
<tr>
<td>25,000</td>
<td>0</td>
<td>2,185</td>
<td>4,875</td>
</tr>
<tr>
<td>30,000</td>
<td>0</td>
<td>135</td>
<td>2,825</td>
</tr>
<tr>
<td>35,000</td>
<td>0</td>
<td>0</td>
<td>775</td>
</tr>
<tr>
<td>40,000</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>45,000</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>

In addition Working Tax Credit may also be payable in respect of some childcare costs (see Para 3).

2.3 Planned Changes to Tax Credits

From 2013/14 Child and Working Tax Credit, as well as a raft of other benefits, will be replaced with Universal Tax Credit. Child Benefit however will continue to be paid in addition, although the basis will change with regard to families with higher rate taxpayers. While the new Tax Credit amounts have not been announced, the Government has made a commitment that no family will be worse off. Despite that commitment, from 15 April 2013 the Government is introducing a cap on the total amount of benefit that working-age people can receive.

The benefit cap will mean that working age people cannot receive more than a set amount in benefits, even if their full entitlement would otherwise be higher. The cap will be set at the average net earned income of working households. This is estimated currently to be £350 per week for a single adult with no children and £500 per week for a couple or lone parent, regardless of the number of children they have. It will apply in respect of Child Tax Credit and many other allowances and benefits paid currently, the main one being Housing Benefit, and subsequently Universal Credit as well as Child Benefit.

The cap will apply in England, Scotland and Wales. It will be phased in, with four London boroughs trialling it from April 2013. National rollout will be over the summer of 2013.
2.4 Tax & Benefits System & Social Behavior

There is a long history of using the tax and welfare system to modify social behavior, and fuel, tobacco, alcohol and vehicle excise duties are all examples of this. All use a financial disincentive to discourage a particular behavior. In the case of Vehicle excise Duty (VED) for example, this was originally the same amount for any car but is now designed to discourage the ownership of vehicles that have higher emissions. The higher are the emissions, the higher is the VED. It is therefore reasonable and logical to suspect that in some cases a tax or welfare benefit may be an incentive - after all bonus payments in industry are common and their effect very well documented. While such incentives may not be intended in respect of a particular tax or benefit, there are sometimes unintended and unenvisaged consequences, and it may be that growth in population in the immediate post war years discussed later could have been partly stimulated by a benign welfare structure. Welfare benefits are very easy to introduce but few Governments have the political courage to remove them and the longer they exist, the more embedded they become. As more time passes, the original purpose is often forgotten and sometimes ceases to be relevant, so a measure that may lead in part to increased population continues to have that effect at a time when Government should be seeking to achieve the opposite.

2.5 Fertility

In considering whether child benefit payments and other tax credits affect population growth, it is necessary to consider fertility. As a measure, "fertility rate" is the number of children born per couple, person or population. Human fertility depends on factors of such as nutrition, sexual behavior, culture, instinct, endocrinology, timing, economics, way of life, and emotions.

Table 4: The following table is taken from a European Commission Report using data as at October 2011, on total fertility rates in the 27 European states.
Sustainable Population Level

There is no starvation or mass homelessness in the UK, fuel is freely available, we have regular electricity & gas supplies and supermarket shelves are full, so presumably the current population of about 62 million people is sustainable. This surely is the popular perception and may explain in part why people in general seem relatively unconcerned about the challenge we face.

The question of what is a sustainable level for the population of the UK is discussed in a 2007 paper by Dr Martin Desvaux, a trustee of the Optimum Population Trust, in which it is suggested that the UK's sustainable population based on ecological footprinting data is between 17-27 million.

Other studies suggest that a reduction to that level will take too long to achieve to avoid major ecological and sustainability problems and that there are sound economic reasons why a reduction beyond 50 million is not achievable in any reasonable timescale (Adam Smith's report in 2010 entitled "Is it Feasible for the UK to Move Towards a Sustainable Population by 2050 While Supporting an Ageing Society?"). This is because a sharp downward correction at a time when the population is ageing overall will leave too few tax paying wealth creators supporting too many elderly dependents, and the tax burden on those tax payers simply too great. It seems clear however from both these papers that, notwithstanding the undeniable challenges faced in striving towards such a goal, Government should be intent on doing so by any reasonable means at its disposal. One of the conclusions reached by Dr Desvaux is the need for all countries to have a National Population Strategy but the UK Government, like many other governments, appears to continue to have no explicit strategy, and this is without doubt the main reason why the public inertia mentioned earlier continues. His final comment in the paper is:

"Failure of politicians to grasp this nettle and lead their nations to accept the necessity of and to provide the means to have smaller families will be to threaten the world at large with the worst population crash in the history of humankind. Is it to much to hope that, with all the knowledge and technology at the disposal of the planet's..."
According to Table 3 of the statistical bulletin issued by the Office for National Statistics in 2010 on Cohort Fertility in the UK, during the lifetime to date of women born in 1960, 20% have 3 children and 11% have 4 or more. Based on the tables in Paras 2.1 & 2.2 above, a family with 3 children and household income of £15,000 per year, for example, can receive £8,620 Child Tax Credit, and £2,449.20 in Child Benefit. These benefits are paid free of tax and are equivalent to an extra £13,837 in gross earned income. In addition, Working Tax Credit may also be payable in respect of some childcare costs but the system is very complicated and giving an accurate example is difficult.

Combined with housing benefit, which rises with family size, the unpaid income available to those with larger families is thus substantial when compared with other benefits available to those who are unemployed and with the income available from many jobs. In the past, the availability of these and a raft of other welfare benefits may have encouraged larger families but from April 2013 a new benefits cap and Universal Credit will limit the financial incentive and it will be interesting to see what effect this may have on fertility rates in coming years. This is seen as very much a step in the right direction and in its way is a means of limiting child benefit.

If, however, the family is not in receipt of other benefits, the impact of the cap on Child Benefit/Tax Credit payments alone will be minimal to non-existent. The problem is we cannot wait long to find out, and need an answer to these questions:

- When the UK population is already well above that suggested to be the sustainable level and fertility rates are higher than desirable, should the Government pay any incentive at all to families to have children?
- Would it be better to restrict or remove the incentive, and to use the annual saving to provide ring-fenced support directly for the benefit of children, and not paid to their carers?

There is little if any direct evidence that our tax and welfare benefit system as currently structured provides an incentive for larger families, so the assumption that it does is largely intuitive. However circumstantial evidence comes from the ONS statistics. For women born in 1930 and who therefore entered marriage/child bearing age at the end of World War Two there was a big jump in fertility from 2 children/woman for those born in 1920 to 2.35, and up to a peak of 2.42 for those born in 1935, since when fertility gradually fell to the 2000 level of 1.64 and then increased again to the current level of 1.94. Since this period of child bearing ages coincides with the introduction of Family Allowance, it is reasonable to assume that the Allowance may have acted as an incentive as argued earlier, although once again it cannot be claimed in isolation as the sole contributory factor. It is possibly coincidence that, since the introduction of Child Tax Credit, the rate has started to increase again. Can we deduce anything by comparing the supposed relationship between benefit payments and fertility rates in the UK with those in other European countries? A paper produced in 2003 by the Council on Contemporary Families, an American organisation ‘dedicated to providing the press and public with the latest research and best-practice findings about American families’, compared family policy in the US, Japan, Germany, Italy and France, including the payment of benefits and allowances.

With regard to Italy it noted: “Italy’s financial provisions for families are relatively low in the scheme of provisions of other European countries (Bettio and Prechal 47). The value of tax breaks and child benefits for a couple with two children is equal to about four percent of the average 1992 male wage, less than half the value of French benefits…….”

In the case of France: “The value of French child benefits for a couple with two children was equal to about 9.5 percent of the average 1992 male wage (Bettio and Plantenga). This is the highest benefit value of the countries discussed in this paper.”

As noted earlier Italy has had a low fertility rate compared to UK, while in France the rate was similar to our own, so the relative levels of benefits & allowances in the two countries seems to support the assumption we have been making about the UK. A more statistically sound and comprehensive study was carried out by the Department of Work & Pensions (DWP) in 2003 (DWP Research Report No. 174 ‘A Comparison of Child Benefit Packages in 22 Countries’). Chart 1 in the report shows the cash value in £sterling of the child benefit package after housing and services paid to a ‘representative’ sample of families. There is a clear correlation between the
fertility rates in Table 4 above and the benefit amounts in the chart in almost every case, other than two marked exceptions.

The first is Germany, which has a similar level of benefit payments to the UK but a much lower fertility rate, and Austria, which has one of the very lowest fertility rates in the EU but the best overall benefit level of all 22 countries in the study by a large margin. In the case of Germany the fertility and benefit data is unreliable because it is affected by reunification, which took place during the period. Austria however is more difficult to explain and there seems no obvious answer. However from these two documents the evidence would seem to support the suggestion that higher benefit levels result over time in higher fertility rates. As previously demonstrated, the amounts available through Child Benefit and Child Tax Credit can be substantial relative to other household income and it is reasonable to infer that they may act as an incentive to have a larger family. Some families, and in particular single parent families, have come to rely on Child Benefit and the other associated tax credits and benefits as part or indeed most of their household income and their lifestyle is set accordingly. Even for the ‘well off’ middle class earners who pay tax at higher rates the threat of removal of Child Benefit has brought claims of impending hardship, which although hardly credible are understandable - nobody likes to lose money.

Current Government actions to restrict benefit for higher rate tax payers address the problem of the unfairness of universal benefits, but ignore the wider issues discussed here and create other practical difficulties – the so called ‘cliff edge’. There are several alternative suggestions being discussed to avoid the ‘cliff edge’ issue but there appear to be no alternatives being aired with regard to restructuring the system as a whole, and no awareness of the possible negative impact of Child Benefit/Tax Credit on over-population problems. Any change should gradually remove any incentives to increase income through childbearing but at the same time protect the very poor, and ensure that the removal of benefit is seen not as a cost saving exercise but as a redirection of cash to provide alternative support that is of value to a family, not dependent on the number of children. Any such change will not by itself solve the over-population problem, but should be a part of the national strategy for population that we urgently need.

4. Policy Options

As originally envisaged by Beveridge, child payments were intended primarily to combat child poverty, but the money was paid to families as an allowance rather than used in some other way to benefit children directly. In spite of the changes that have taken place and the strong emphasis over recent years on ‘eradicating child poverty’ there is little evidence that child focused payments to parents are actually used in full for the benefit of children, and circumstantial evidence and logic suggests that higher fertility rates may continue to be driven by these payments. To change the system now in order to remove any incentive to have larger families means finding an alternative approach to that taken since the end of World War Two in spite of the fact that the majority, if not all, European governments currently follow a similar approach. Importantly, it must be acknowledged also that removing existing benefits in whole or in part would cause considerable hardship to a large number of families, and underlines the need to deal with such issues constructively and with due regard to the circumstances of those families. There are a number of alternative approaches and the following are just some examples.

4.1 Restricting Child related Benefits

In response to the Governments proposal to restrict Child Benefit payments to higher rate tax payers, Population Matters commented in May 2012 that this perhaps did not go far enough and suggested:

“…..an alternative approach, which is that child benefit should be paid only for the first two children in any household. However, it is important that child poverty is not worsened and, for those on low incomes, additional payments should be made to those with larger families to preserve their current level of benefits.

This would send out the much needed message that smaller families are in the interest of society as a whole in Europe’s most densely populated country, where continuing population growth is contributing to growing housing shortages and planning pressures, traffic and transport congestion, energy and water security issues and unwanted carbon emissions. Limiting the payment of child benefit to the first two children in any household would also mean that the majority of people with two or fewer children would not be subsidising those who choose to have larger families. Finally, it would also provide significant savings.”
While this would undoubtedly be a welcome step in the right direction, as seen from 2.1 & 2.2 above Child Benefit on its own is not necessarily the main issue, and is but part of the problem. Restricting the benefit and tax credit to a certain number of children, perhaps on a tapering basis while reducing it, still provides a financial incentive to have children and although restricting the benefits to, say, two children, may seem a simple solution, it has its difficulties. To achieve the aim of removing the larger family incentive it would need to be applied to the individual and not the family, to ensure that a woman who changes life partner does not simply reset eligibility for the benefits, and this will leave it open to political challenge on grounds of fairness & equality. Such a system would be administratively complex, clumsy and expensive to operate, making it open to dissatisfaction and criticism. We certainly do not need another Child Support Agency scandal. Despite these reservations, it is worthy of serious consideration to explore more closely what impact it might have and how best to operate it.

4.2 Removal of All Child related Benefit Payments

If the view that the current system incentivises larger families is correct then the most obvious answer is to remove all payments. This appears to be drastic and in order to do it in an acceptable manner the removal of tax and welfare benefits going to parents or guardians of children would need to be implemented gradually over several tax years, perhaps continuing the benefit to existing children until their normal non-qualification age, or to a reduced maximum age of say 12. It is unlikely in any event that such an established benefit can be weaned away quickly, but this makes it no less desirable in the medium to long term.

Obviously, financial support for families in real need must be safeguarded in some way so, as the existing benefits are removed, there should be the parallel establishment of a ring-fenced fund earmarked to benefit of children of poorer families. Funded by an annual payment from Government equivalent to what would have been paid in Child Benefit/Tax Credit, the Fund could be used to support children in ways that are likely to be seen as having financial value for the family. For example:

- The provision of universally free or heavily subsidised child-care and/or education facilities (including higher education). Free child-care would have a coincidental economic benefit of allowing women to go back to or to seek work, but that would be a matter of choice.
- The provision by Local Authorities of more after school facilities, children & youth groups, sports facilities etc.
- Free baby food vouchers and clothing for children on a means tested basis.

These few examples, of which there are no doubt many more, could be employed alone or together and phased in as funds allow. However, the extent to which the needs of the poorer families could be met easily, and whether they would see the value mentioned earlier is a difficult to judge. Such a major shift would take much longer to achieve than the previous option, the policy changes associated with it are fraught with complexity and the danger of creating even more unintended consequences likely.

4.3 Other Tax Changes

An even more radical idea is to introduce an increased Personal Tax Allowance for childless married women and/or those with no more than two children. This does not directly benefit children and is the exact reverse of where we are now. The idea is also not without challenges, the obvious ones being on the grounds of equality and cost. Why not men, and how difficult is it to administer? It could be considered, however, as part of any National Strategy on Population.

5. Conclusion

It seems that the Government through the review carried out by Ian Duncan-Smith has missed an important opportunity to create a child benefit system which suits today instead of 1945, and continues to tinker to save money without thought of any of the wider issues. Mr. Duncan-Smith has tried to tidy things up in a caring way, but it is clear from other recent announcements by, for example, the Housing Minister (28 November 2012), who
believes that we need ever more land on which to build more houses and that those who value a rural existence should be more public spirited and stop objecting, that the Government still does not understand the importance of reducing the UK's population. Indeed, as mentioned, earlier successive governments have failed to grasp the need for a proper National Population Strategy. This is exactly what is now needed urgently, and a part of that Strategy should be a change through evolution to gradually remove the incentive to increase income through childbearing. It is vital at the same time to protect the very poor, and ensure that the removal of benefit can be seen not as a cost saving exercise but redirection of cash to provide alternative support that is of value to a family, and not dependant on the number of children.

Note: This is a contribution to the current public debate rather than formal Population Matters policy.