

ECONOMIC SURVEY OF NEW ZEALAND 2005:
RAISING FEMALE LABOUR FORCE PARTICIPATION

*This is an excerpt of the OECD Economic Survey of New Zealand, 2005,
from chapter 4*

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Broadening choices and options for families

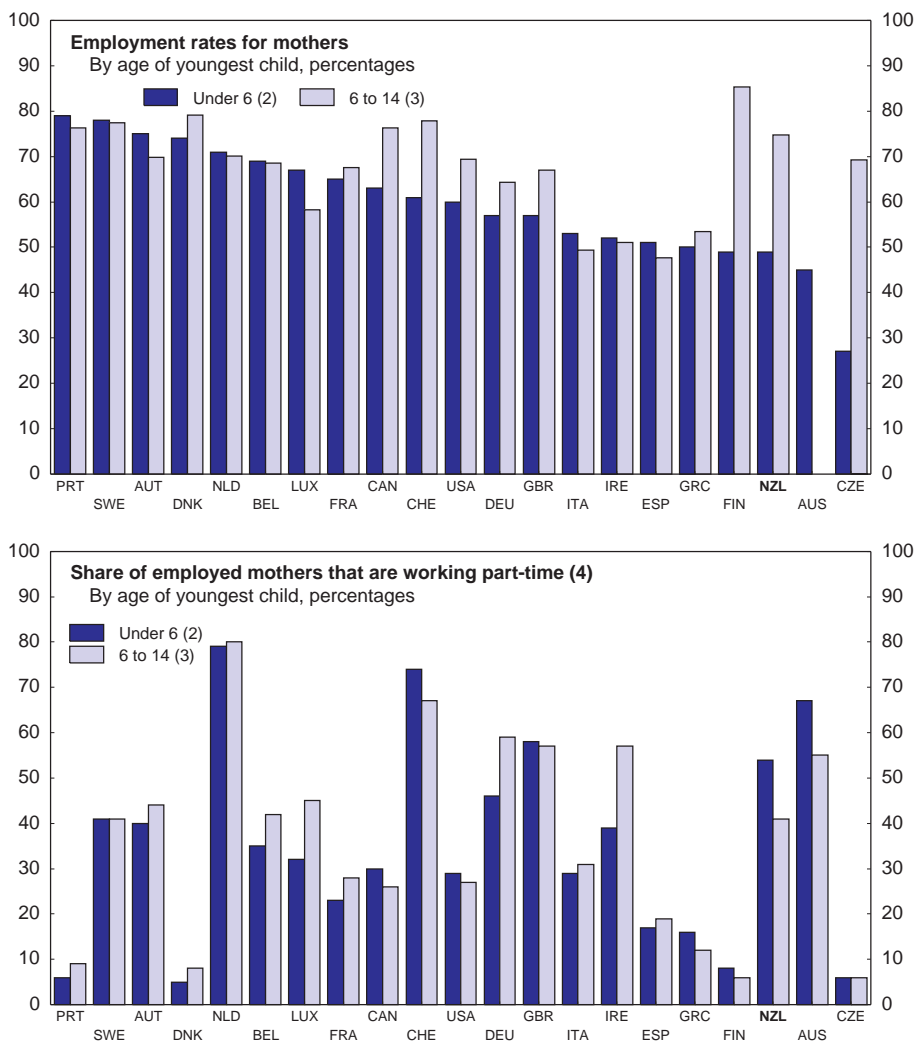
1. While New Zealand's overall female participation is comparatively high by international standards, it has one of the lowest rates of employment among mothers with children under the age of 6 years in the OECD. Employment rates rise sharply once children go to school (Figure 4.3). However, NZ mothers who are employed are more likely to work part-time compared with other OECD countries. To some extent, this may reflect a lifestyle preference among NZ families and a belief that mothers want to and/or should stay at home to care for their children in the early years,¹ although there is little hard evidence about what mothers' underlying preferences are.²

2. Significant economic disincentives discourage some mothers who might otherwise want to undertake paid work or extend their working hours, especially if the household is within the income brackets over which family assistance or the accommodation supplement is phased out and/or they are faced with having to find and pay for childcare (Roseveare, 2005). Some of these economic incentives persist once children go to school albeit to a reduced extent, which is reflected in high share of part-time work. Countries where distortions to the economic value of market work are less significant generally have higher participation rates amongst mothers with young children, and their women working part-time tend to work more hours (OECD, 2005c). This suggests that reducing such obstacles would allow NZ families to exercise a wider range of choices about how to reconcile paid work and family responsibilities.

3. Having access to good quality, affordable care for children is an important prerequisite for parents who want to undertake paid work. Although the move to providing 20 hours free education for all children is important in its own right, it will also help to reduce the financial cost faced by working parents. But the costs of care are still substantial for younger children, for supplementary hours for three and four year olds and for after-school care (Table 4.5). Overall, NZ households face significantly higher parental childcare costs than many OECD countries for a two-earner couple earning the average male and female wage (Bradshaw and Finch, 2002). Reducing the care costs faced by parents would impact on one important factor that makes paid work or increasing hours less attractive to second earners, in particular. Although the *Working for Families* package increased income-tested childcare subsidies, these are fully abated once

household income has reached just over 75% of the average household income for couples with dependent children.³

Figure 4.3. **Employment of mothers**
2002 or latest available year¹



1. 2001 for Canada, Denmark, Ireland, Japan, New Zealand, and United States; 2000 for Australia.
2. Under 5 years old in Australia; under 7 in Sweden.
3. 6 to 13 in the United States; 6 to 16 in Canada, Finland and Sweden; 6 to 17 in New Zealand.
4. Part-time work is less than 30 hours per week.

Source: OECD (2005), Society at a glance: OECD social indicators.

4. Cost is not the only obstacle that parents face; they also need to be able to find quality childcare and out-of-school-hours care, the supply of which is somewhat patchy in some areas. As a result, parents in areas where there is inadequate availability may have little choice but to forego work, unless they can

make informal arrangements, for example by resorting to relatives (Byrne 2002). In many other OECD

Table 4.5. **Childcare costs for couple households**

	Percentage		
Gross wage earnings, as percentage of APW earnings ¹			
Primary earner income	100	100	100
Secondary earner income	33	67	100
Fees paid by parents, as percentage of APW earnings			
Young children (two children, aged 1 and 4)			
Part-time childcare fees	23%	23%	23%
Full-time childcare fees	45%	45%	45%
School age children (two children aged 7 and 9)			
Out-of-school-hours care fees	14%	14%	14%
Average effective tax rates on second earners ²			
Without childcare fees	17%	19%	21%
With part-time childcare for two children	85%	53%	43%
With full-time childcare for two children ³	153%	87%	66%
Without out-of-school-hours care fees			
Without out-of-school-hours care for two children	17%	19%	21%
With out-of-school-hours care for two children	58%	40%	34%

1. Average Production Worker annual earnings in 2004 were NZD 41 778.

2. Average effective tax rates on second earners are calculated as the difference between the increase in gross earnings and the increase in net income when a second earner starts work, expressed as a proportion of the second earners' income.

3. Some of these situations are unlikely to occur in practice, for example, someone earning only 33% of the APW wage would probably not require full-time childcare.

Source: OECD (2004), "Babies and Bosses", Vol. 3.

countries, either the local authorities systematically provide collective care through early childhood centres, after-school and holiday programmes (usually with a parental fee and sometimes through sub-contracting arrangements) and/or parents make their own care arrangements but can claim back some of the cost against their taxes. Either way, parents in these countries can have reasonable confidence that if they wish to work, they will be able to obtain care. This suggests that if the authorities want to raise labour force participation amongst those mothers who wish to work, they might need to redesign the subsidy arrangements to ensure that they encourage sufficient supply to match work-related demand. Of course, some working parents might use an expansion of subsidised supply as an opportunity to switch from informal care provided by relatives, neighbours and friends, to formal care. However, this may actually provide better care for the children: one recent study in the United Kingdom found that informal, unpaid carers provided lower quality care on average than either paid home-based carers or care centres (Gregg *et al.*, 2005).

5. Considerable fiscal costs would be associated with a significant reduction in the outlays that parents face for care. Judging whether this public spending would be justified depends not only on the immediate impact it would have on labour supply, but also what benefits it would deliver to parents and to society over the longer term.⁴ If the labour supply elasticity for mothers is low in New Zealand, then the deadweight losses of additional subsidies would be high per additional hour of paid work induced. But such a weak response would be rather surprising, given the extent of reported under-employment among NZ women⁵ and that mothers in a range of other OECD countries generally want to work more hours than

they currently do (Jaumotte, 2003). Overseas experience also suggests that labour supply elasticities may be higher in the longer run than the short run, especially if it becomes easier for women to remain more closely attached to the workforce in the first place. In New Zealand, availability and affordability of child care and after-school care have been cited as important obstacles (Wylie *et al.*, 2001).

Strengthening the incentives to work for low- and middle-income families

6. The *Working for Families* package announced in the 2004 Budget will be phased in progressively by 2007 (see Box 4.3). However, while the package provides significantly larger income transfers to many families, it will be likely to encourage the labour supply of sole parents, and discourage the labour supply of secondary income earners (Nolan, 2004). For beneficiaries, the package has lowered EMTRs at two points in the income spectrum – for initial earnings (up to NZD 80 per week) and around the point where it becomes more attractive to take up the in-work payment than to stay on income assistance. Even so, once the abatement rates for the different components are aggregated, the effective marginal tax rates (EMTRs) faced by some single-income households are so high as to create a poverty trap – if they increase their hours worked they lose almost all the extra market income they would earn (Figure 4.4). For couples, the higher ranges of income over which the income-tested transfers are abated could have the effect of discouraging the potential second earner from working or the principal earner from earning additional income (Figure 4.5). In sum, the increase in levels of assistance and provision of the new In Work Payment come at the expense of much higher EMTRs for higher incomes.

7. There are several ways in which these negative incentives to work could be addressed. One approach would be to shift to family assistance that is targeted on other features rather than income, such as number and age of children.⁶ Such transfers have the strongest effect on incentives to work if paid in forms especially attractive to working parents, most notably through reducing the cost of childcare and after-school care. In contrast, the work incentives associated with universal childcare benefits are weaker because non-earned income reduces the amount of market income the family needs to earn to meet a given level of outgoings. Even without taking into account childcare costs, most OECD countries already structure their tax and transfer systems so as to provide a higher net income to families with dependent children than those without, for a given level of gross earnings (Figure 4.6). Indeed, New Zealand is unusual in providing virtually no income boost for families earning the annual average production worker wage or higher. The *Working for Families* package will provide larger income transfers when fully implemented but at the expense of higher EMTRs. The fiscal cost of a shift away from income-tested family assistance towards more universal transfers could be contained by targeting other forms of support most generously on very young children, given that once children are in school, parents could be expected to rely more heavily on market income if they wish to ease the household budget constraint.

Box 4.3. Family assistance and the Working for Families package

Present structure of income-tested family assistance

Income-tested family assistance is delivered through several channels.

- Several elements are paid through the tax system. Family Support is the main payment per child and is paid at a higher rate for older children. It is paid to all income-qualifying families, regardless of the source of their income. The Child Tax Credit is an additional payment available only to non-beneficiaries. The Family Tax Credit is paid to families on very low incomes where at least one parent is working and is designed to bring income up to a guaranteed minimum level for a family. The Parental Tax Credit is a payment for the first eight weeks after birth to help defray one-off costs.
- The Accommodation Supplement is a non-taxable benefit delivered through the Work and Income Department and provides assistance towards accommodation costs, depending on housing circumstances and location. It is available to both beneficiaries and non-beneficiary families.

- Childcare and Out of School Care and Recreation (OSCAR) subsidies are non-taxable and paid directly from Work and Income to the care provider. The childcare subsidy is available for children under five years old for up to 50 hours per week, while the OSCAR subsidy is available for up to 20 hours per week during term time and up to 50 hours per week during school holidays.

Working for Families package

The *Working for Families* package has three objectives: making work pay, improving income adequacy, and achieving a social assistance system that supports people into work. The reforms will be fully implemented by 1 April 2007, in the following sequence:

October 2004

- For beneficiaries, abatement of the accommodation supplement during the first NZD 80 of gross weekly earnings was eliminated, and, for non-beneficiary families, the thresholds for abatement of the accommodation supplement were raised.
- Childcare and OSCAR hourly subsidy rates were increased.

April 2005

- The maximum rates of the accommodation supplement were raised for some locations.
- Family Support rates were increased and the child component of core benefits was eliminated.

October 2005

- The Childcare and OSCAR subsidy rates will be further increased.

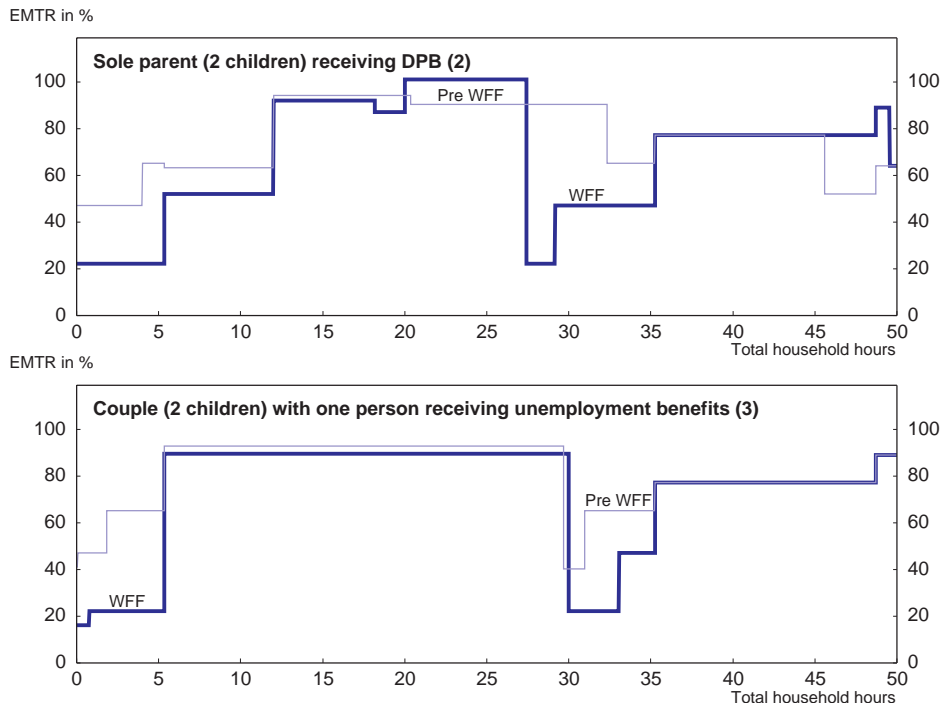
April 2006

- The NZD 15 per week per child Child Tax Credit will be replaced by an in-work payment of NZD 60 per week available to families not on benefits and working at least 30 hours per week for a couple or 20 hours per week for a sole parent.
- The thresholds for abatement of family assistance will be raised and the Family Tax Credit increased to provide a guaranteed minimum family net income of about NZD 17 000.

April 2007

- Family Support rates will increase by NZD 10 per child per week.

Figure 4.4. **EMTRs faced in moving from benefits to work (1)**
Before and after the Working for Families package

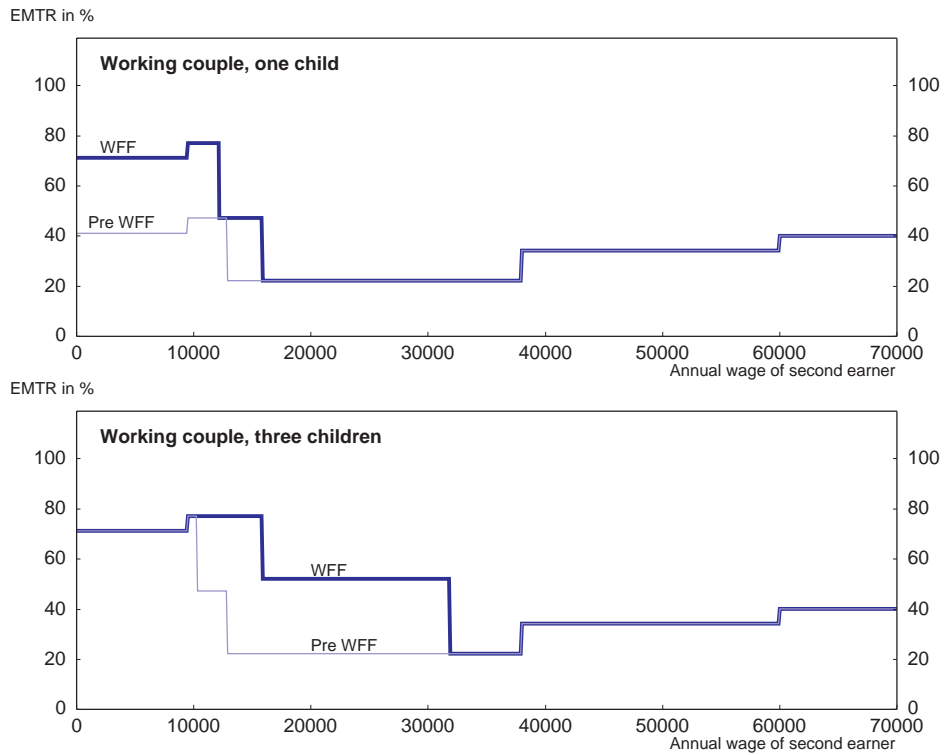


1. Two children (both under 16, one under 12), supplementary earnings at NZD 15 per hour.
 2. Annual rent of NZD 10 000.
 3. Annual rent of NZD 15 600.
- Source: New Zealand Treasury.

8. Another possible approach focuses more directly on couples with children who are particularly adversely affected by the increased EMTRs embodied in the *Working for Families* package. These households would get minimal additional disposable income from the second earner unless the additional hours lift the household's annual income above around NZD 60 000 (depending on the number of children, accommodation costs, and where in the country they live). Some 34% of couples with children earned household income less than this in the year to June 2004. But couples with one earner drawing on family assistance have the advantage of having extra hours available for unpaid household work or leisure. This bias against market participation would be mitigated if the definition of household income used to qualify for assistance were adjusted to include an imputed income for the potential second earner, set, for example, at the minimum wage. This would mean that fewer one-earner couples would qualify for family assistance in the first place, but couples that did would not face punishing EMTRs if the second person obtained market income up to the imputed income level. This approach would involve fiscal savings compared with the present arrangements and provide explicit recognition of the value of unpaid household work, thereby also improving horizontal equity.

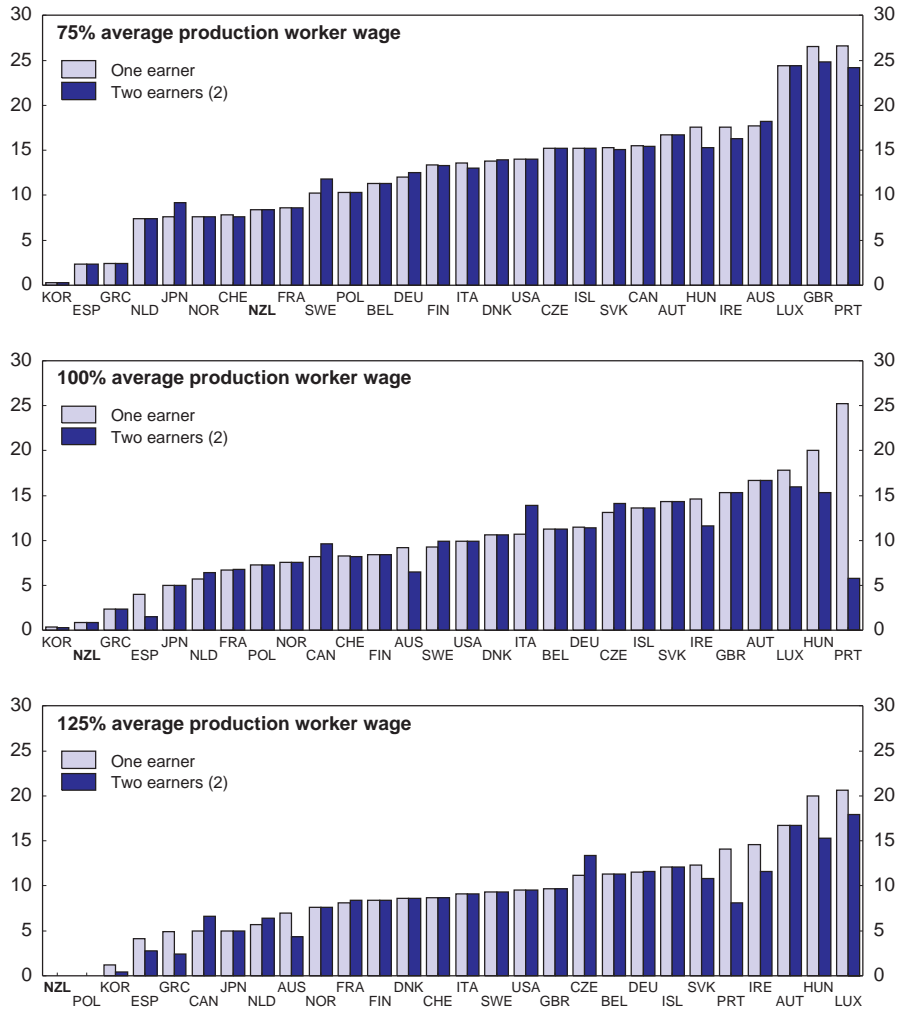
9. For sole parents, some of the damaging impact on work incentives arising from the abatement rates on mean-tested benefits could be reduced by strictly limiting the DPB only to those with young children, as many countries already do. Around half of those drawing the DPB have no children younger than 5 years old, and face very little pressure to find a job since the work test was removed in 2003. In contrast, people on unemployment benefit face clear employment expectations and effective active case management tools are available and being used⁷ (OECD, 2005b). In any case, the proposed shift to the single core benefit approach is expected to address this issue more directly.

Figure 4.5. **EMTRs faced by potential second earners (1)**
Before and after the Working for Families package



1. Assuming the working partner earns NZD 40 000 per year and the family pays rent of NZD 15600 per year in Auckland.
Source: New Zealand Treasury.

Figure 4.6. Assistance to couples with two children¹
Per cent of APW, 2003



1. Assistance is calculated as the difference between net income after taxes and transfers for a family with and without children with the same gross earnings, expressed as a percentage of the Average Protection Worker (APW) wage.
2. The principal earner is assumed to earn 75%, 100% or 125% of APW and the secondary earner earns 67% of APW wage.

Source: OECD tax-benefit models.

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- ¹. The balance of evidence also suggests that as long as high quality childcare is provided, maternal employment can be beneficial to children not only through the quality of the care itself, but also because of the extra household income generated (Ministry of Women’s Affairs, 2004).
- ². In the Competent Children project, when the children were aged 10 years, 32% of their mothers were in full-time jobs, 46% were in part-time work and 22% were not in paid employment. Just over half of the mothers who were not in paid employment would like paid work, and cited as barriers the availability of work with flexible hours and decent pay rates, availability and affordability of childcare or after school care and the need to care for younger children (Wylie *et al.*, 2001).
- ³. The average age of children in these households were five years for couples with one child, seven for couples with two children and eight for couples with three or more dependent children. It would be reasonable to assume that households with younger children, incomes would be lower and childcare costs higher than these averages.
- ⁴. The gains to society of increasing maternal employment need to be carefully assessed, as they do not flow directly from increasing paid hours worked. Shifting someone from unpaid work across the boundary and into paid work boosts GDP, but does not, in itself, raise living standards. Instead gains to living standards are obtained in two ways; *First*, if women who would choose to work if they had more affordable childcare

have higher productivity in the workplace than in the home then the more efficient allocation of available economic resources would raise economy-wide productivity. *Second*, reducing periods of absence from the workforce avoids the associated deterioration in the individual's human capital, which otherwise puts a brake on productivity growth through human capital. The overall effects also depend on the general equilibrium outcomes, *i.e.* once all the impacts have worked through the economy, including those that would result from the cost of raising tax revenue to pay for the additional subsidies.

5. There were twice as many women as men reporting under-employment in the Household Labour Force Survey of December 2004. The under-employed currently work part-time but say they would prefer to work longer hours.
6. A shift towards targeting alternative characteristics instead would also conceivably be easier to administer and less stigmatising than focussing on household income.
7. In 1997, a requirement on the lone parent to be available for part-time work when the youngest child was aged 14 or older was introduced and the threshold was lowered to age six, as from 1999. These requirements were changed in 2003, where work requirements were replaced by an obligation for benefit recipients to participate in an annual personal development and employment planning process, where each year the beneficiary must establish some objectives for him/herself with a case manager.