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Taxation Income Sharing Tax Credit Bill

Submission to Select Committee

1. Summary

- Father & Child Trust is a social and community service agency working with fathers and families.
- Income Splitting neutralises any taxation effect of parental choices as to their role division (caregiver/provider). At present equal earnings of the two parents are encouraged by taxation.
- Income Splitting recognises the family as an economic unit.
- Recognition of the family as an economic unit has positive psychological benefits which may increase stability of relationships between young parents.
- Income Splitting is likely to reduce benefit fraud.
- Income Splitting will make Working for Families more effective as less of it flows back to Inland Revenue as taxes.
- Income Splitting should be administered through the PAYE system, not through Working for Families or any other income subsidy system.

2. Father & Child Trust

Father & Child Trust is a registered non-profit with branches in Auckland and Christchurch, providing social and community services since 1997. Our mission statement is:

To provide fathers and their families with help, information and support, and to improve fathers' access to family services.

Our objectives are:

To work with families by helping individual fathers work towards the best relationship they can have with their children under the given circumstances, supporting and actively helping them to remove the barriers impeding this goal, and making information available that helps their parenting.

To work with organisations by working towards equal parenting opportunities for mothers and fathers, where family support services are accepting of the choices parents make in dividing the caring of their children between them and encourage a joint primary responsibility for their children. Father & Child has an educational mission towards organisations delivering these services, working with them to achieve inclusive delivery.

“New Zealand communities where fathers and mothers are supported equally and have access to the resources and help they need to work together for the welfare of their children.”

To work with communities by networking and encouraging fathers to share any parenting related issues with each other, to actively engage with their children, be part of their local parenting communities and achieve confidence in parenting. Father & Child provides places where this can happen, and disseminates typical fathers' stories through magazine publications, internet and other media.

3. 'Income Splitting'

Father & Child Trust is non-political, and only very rarely do we make a submission about a bill under consideration before parliament. The families we work with need to be comfortable to approach an organisation for help, and this can be difficult if an organisation has a political profile that is at odds with the political views of the person requiring help. We are very conscious about avoiding to create such a barrier to our services.

We have always supported the tax scheme known as 'income splitting', however, because it aligns with our core value of a joint responsibility of both parents to raise their children. Where parents live together this creates an economic unit through which resources flow towards the children. Under the present tax system this economic unit is not recognised as such in terms of income tax, but it *is* recognised in terms of Working for Families or the Unemployment Benefit. This means that at present Inland Revenue works on the basis of a framework which is inconsistent when it comes to families.

Father & Child is especially concerned that present tax law penalises certain choices that parents make, notably the choice of having one primary income earner and one primary caregiver. We are not aware of any research that this role division creates negative outcomes for children, and neither does there appear to be any political argument why this role division should be financially discouraged. **Father & Child believes that parents need to be empowered to make their own choices about role divisions when it comes to parenting, and any tax incentive for any particular choice should be removed. The bill under consideration does this.**

Much has been made of the fact that the main beneficiaries of 'income splitting' are higher income earners. This argument is beside the point. Higher taxes for higher income earners are a matter for a progressive tax system, and are therefore a political decision to make. Higher taxes should not be the result of an entirely random factor such as how earnings are distributed between parents. A couple with children earning a certain amount of income should be taxed the same as another couple with children earning the same amount of income, regardless of how the income is distributed between the parents.

4. Parents with a new baby

'Income Splitting' will most likely benefit the bulk of parents with a new baby. A large majority of parents with a new baby decide that one of them will care for the baby full time for those early months, even years. The benefits of this are implicitly recognised in Parental Leave legislation. This means that during those early months only one of the parents has an income, and is taxed on it as an individual.

Choosing to work equally and generate an equal income almost from the day a baby is born is neither practical nor desirable, yet this is the option creating the lowest tax rate for the parents. Most mothers (and some fathers) spend at least some time caring for their baby fulltime and in order to do so either take extended parental leave or quit their job altogether. The stay-home parent is not able to claim a benefit, as the parents are recognised *as an economic unit* and the earning parent's income is taken into account. It is bizarre that, on the other hand, this economic unit is then not recognised for the purpose of taxation and the family is financially penalised as a result. **The bill under consideration removes this penalty.**

5. Social Issues

It has been argued that the bill would provide a financial incentive for parents to 'stay together' and that this would therefore favour one family type over another.

Father & Child provides services for families in any situation they may find themselves in, regardless of whether the parents live together or not, and we do not promote any particular family model. This is the parents' choice.

Again, this argument is beside the point. The present tax situation also favours one family type over another: the type where both parents earn a roughly equal amount of income (or are able to claim so through setting up a company or partnership if self-employed) over those who earn different incomes.

It is doubtful whether taxation would play any role at all for parents when deciding whether they should split up. Financially this is an expensive choice regardless of taxation issues: a second household needs to be set up, for example, and other resources that were shared before may now have to be bought again. If incomes are vastly different, the lower income earner will overall be cut off from the earnings of the higher income earner and this will result in a drop in living standard. Some of this may be offset by Child Support payments, but the amount of this depends on the care arrangements for the children. For the higher income earner the loss of Income Splitting will create a financial disincentive, but this is more than offset by the fact that the higher income earner can now keep most of their earnings for themselves.

It is argued that Income Splitting will make little difference for people on low incomes. 'Little' is a relative term: For a person earning \$80,000 or so a year, the amount of \$10 extra per week is inconsequential. For a couple on a combined income of \$30,000 or so, it represents a significant amount in the budget that is being felt. Father & Child Christchurch provides a budgeting service for low income earners, and even such small amounts are not taken for granted by people whose outgoings consist almost entirely of primary living costs such as rent, food or power.

We are confident that Income Splitting can make a big difference especially for young people on low incomes. A common type of benefit fraud for young people is claiming the DPB for one parent even though the other parent is effectively living at the same place. That other parent is sometimes also on a benefit, but more often they are on a low wage. The Working for Families scheme has gone some way in 'legalising' some of those families. Income Splitting would provide a further financial incentive, and in many cases would eliminate any financial incentive of claiming the benefit.

For young parents in their early twenties or younger, Income Splitting and the implied concept of parents as an economic unit, is psychologically important and fosters economic independence (from the government). A relationship that feels it has to hide its existence from the government because of financial disadvantage is more vulnerable to breaking up, because it cannot develop a sense of 'doing it together'. Income Splitting strengthens the value of financial income provision within the relationship, but it also strengthens the claim of the lower income earner to the 'family' share of this income. We find that such concepts of economic unity, or 'family' overall, are very strong psychological incentives for young males especially. **The bill under consideration provides this psychological incentive and is, in our opinion, likely to reduce benefit fraud and improve stability of low-income relationships.**

6. Administrative Issues

The bill under consideration proposes to have Income Splitting administered together with the Working for Families scheme. While we acknowledge the reasoning behind it (using an existing system; consideration for compliance costs for employers etc) we believe it is unfortunate.

Working for Families is a subsidy paid to low-to-moderate income parents out of the general tax take. Income Splitting is an adjustment to tax parents equally to other parents earning the same amount. In the public mind it should not be confused with another taxpayer subsidy to families. Administering Income Splitting together with Working for Families would, however, create that impression. **Income Splitting should, ideally, be made available through the PAYE system.**

There is a link, however, between Income Splitting and Working for Families: since Working for Families entitlement is calculated on the basis of *before-tax* combined income, most of this entitlement currently flows back to Inland Revenue as taxes for those couples with only one (larger) income compared to those with two (smaller) ones. It is another anomaly of the present system that Working for Families does not take the higher

taxation of single-income families compared to dual-income families into account. The bill under consideration removes this anomaly.

Signed on behalf of Father & Child Trust:

Harald Breiding-Buss

General Manager