

## **Breaking the Cycle of Family Joblessness**

Jessica Brown

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## Executive Summary

Despite Australia coming off the back of a remarkable economic boom and enjoying historically low unemployment rates, in late 2008 almost one in eight Australian children lived in a family where no parent worked. Unbelievably, this figure is actually a marked improvement: family joblessness reached its peak in the mid-1990s when more than one in six children lived in jobless households.

While there has been some improvement, the statistics on family joblessness still paint a depressing picture. Despite experiencing a lower unemployment rate than most developed countries, Australia has the second highest proportion of jobless families in the OECD. While this represents a considerable social and economic cost to Australia, the biggest cost is borne by the children of jobless parents, who are significantly disadvantaged compared to their peers.

Family joblessness not only leads to welfare dependency and child poverty but also inferior health, social and developmental outcomes for children. Consequently, there is a broad consensus that the high level of family joblessness in Australia is unacceptable.

While the drop in family joblessness over the past decade can be partly explained by strong economic conditions, policy changes undoubtedly also played a role. This provides a clear map for policy makers who wish to avoid the recent gains being reversed. Parents are jobless for various reasons, and a multi-pronged policy approach is required:

- Reductions in the tax burden faced by workers will provide an incentive for jobless parents to move from welfare into work, as they will get to keep more of their new income. Despite budget pressures, the Rudd government must not abandon its commitment to tax cuts;
- A robust 'welfare to work' regime sends the message that everyone who can work should do so, providing assistance for jobless parents to find work and penalising those who don't. Tougher welfare rules implemented over the past decade have certainly contributed to the drop in family joblessness. The Rudd government should resist winding back mutual obligation requirements, which will inevitably cause the number of jobless families to rise;
- Any attempt to tackle family joblessness must include the continued reform of the labour market. Wage setting and industrial relations policies must be governed by a 'jobs first' policy, with a key objective being the continued creation of low-skilled jobs. During a downturn, it is preferable for people to have the option of lower-paid jobs, rather than simply being forced onto the unemployment queue.

Thanks to policy reforms and good economic conditions, the number of jobless families has been dropping but as the country slides into recession, there is a danger that that these gains will be reversed. If tax, welfare, and labour market reforms are wound back, this danger will become a certainty. While the recession seems inevitable, good public policy means that a jump in the number of jobless families needn't be.

## **Abbreviations**

|               |  |
|---------------|--|
| <b>ABS</b>    | Australian Bureau of Statistics                        |
| <b>EITC</b>   | Earned Income Tax Credit                               |
| <b>EMTR</b>   | Effective Marginal Tax Rate                            |
| <b>FTB</b>    | Family Tax Benefit                                     |
| <b>LITO</b>   | Low Income Tax Offset                                  |
| <b>LSAC</b>   | Longitudinal Study of Australian Children              |
| <b>NATSEM</b> | National Centre for Social and Economic Modelling      |
| <b>OECD</b>   | Organisation for Economic Co-operation and Development |
| <b>PPP</b>    | Parenting Payment (Partnered)                          |
| <b>PPS</b>    | Parenting Payment (Single)                             |

# Breaking the Cycle of Family Joblessness

## Introduction

Despite Australia coming off the back of a remarkable economic boom and enjoying historically low unemployment rates, in late 2008 almost one in eight Australian children lived in a family where no parent worked. Unbelievably, this figure is actually a marked improvement: family joblessness reached its peak in the mid-1990s when more than one in six children lived in jobless households. While there has been some improvement, the statistics on family joblessness still paint a depressing picture. Despite experiencing a lower unemployment rate than most developed countries, Australia has the second highest proportion of jobless families in the OECD.<sup>1</sup> This represents a considerable social and economic cost to Australia, but the biggest cost is borne by the children of jobless parents, who are significantly disadvantaged compared to their peers.

Family joblessness leads to welfare dependency and child poverty, and inferior health, social and developmental outcomes for children. Consequently, there is a broad consensus among governments, welfare groups, academics, and the public that the high level of family joblessness in Australia is unacceptable. A chief objective of the Howard government's mutual obligation agenda was to reduce the number of jobless families,<sup>2</sup> and the Rudd government has signalled this as a key plank of its social inclusion strategy.<sup>3</sup>

The aim of this paper is to examine family joblessness and its causes by focusing specifically on families (couples and sole parents) with dependent children, and explore policy solutions. The first section will build a picture of family joblessness in Australia, including trends and characteristics of jobless families. The second section will argue that the lessons of the past decade have demonstrated that a broad policy mix of welfare reform, tax reform, and industrial relations reform is required to effectively tackle family joblessness. If the drop in family joblessness is to be maintained, these policy reforms should be built on rather than abandoned.

A multi-faceted policy response is required because there is no single problem of family joblessness. Parents may be jobless for several reasons. They may be unemployed but looking for work and claiming unemployment benefits. They may be sole parents caring for young children and eligible for welfare support. They may have a disability or be caring for a child or family member with a disability. They may be a jobless couple disengaged from the workforce and reliant on welfare. Finally, they may be jobless but have another source of private income, which means they do not rely on government payments.

Broad-based tax reform that enables low-paid workers to keep more of their earnings is vital to make work an attractive proposition, and to make work seem worthwhile compared to claiming welfare payments. Welfare reform that reinforces the message that everyone who can work should do so, assists jobless parents in finding a job and provides the necessary 'help and hassle' to move them back into work. Welfare eligibility rules can be tightened further to require more claimants to seek work. Finally, policies that create an environment conducive to the creation of low-skilled jobs will ensure the availability of work for jobless parents. Industrial relations reform should focus on fostering a flexible labour market; policies that reduce the cost of low-skilled labour will result in greater job creation.

**Work, not welfare,  
is the best weapon  
to fight child poverty.**

## The impact of joblessness

Family joblessness accounts for much of the child poverty in Australia. We score consistently below the 'best performing' countries on child poverty—not because our welfare system isn't generous enough but because there are so many families where no one works.<sup>4</sup> Tackling family joblessness would go a long way towards overcoming child poverty, and the OECD concludes that work, not welfare, is the best weapon to fight child poverty.<sup>5</sup>

Though a disproportionate number of jobless families are poor, poverty is not the only problem. A large body of research has established the damaging effects on children of growing up in a jobless family.

Children in jobless families are *more* disadvantaged than children in low-income working families, and there is some evidence that parents can inadvertently ‘transmit’ unemployment and welfare dependency to their children, either because their children share the same characteristics that make them more likely to be dependent or because they have ‘learnt’ a culture of welfare from their parents.<sup>6</sup>

Children need an enriching environment for their development. Poor, jobless households are not only less able to provide such an environment but they are also less able to provide schooling and extra-curricular activities.<sup>7</sup>

Parents with very low incomes tend to be more stressed, which affects their parenting behaviour and, consequently, their children’s emotional adjustment.<sup>8</sup> Children whose parents don’t work have more health problems than those with working parents,<sup>9</sup> and they are at increased risk of social and emotional problems.<sup>10</sup> Parental unemployment has been found to be associated with depression in adolescents.<sup>11</sup> Jobless families may become socially isolated because of the stigma of unemployment.<sup>12</sup>

There is some evidence that ‘providing children with a positive role model of a working parent affects their own attitudes to work.’<sup>13</sup> Children in jobless families can form a pessimistic view of the labour market after observing their parents’ experiences, which, in turn, lowers their motivation to succeed at school or at their own jobs.<sup>14</sup> Young people are more likely to be dependent on welfare if their parents are also on welfare.<sup>15</sup> According to the Australian Institute of Health and Welfare:

Jobless households are disproportionately likely to be reliant on welfare, have low incomes and experience financial stress, and members of these households report worse physical and mental health and lower life satisfaction than members of households where someone is employed.<sup>16</sup>

## Part I: A picture of jobless families in Australia

### *The rise and fall of family joblessness*

The 1980s and 1990s saw an alarming rise in the level of family joblessness in Australia.<sup>17</sup> Paul Miller found that in 1979, about one in every 600 couples was jobless—by 1994, this had increased to about one in every 96 couples. This increase was not caused by a lack of jobs: employment had grown overall. However, many of the new jobs were taken by women whose

**In 1979, about one in every 600 couples was jobless—by 1994, this had increased to about one in every 96 couples.**

partners were already working. New job creation led to an increase in two-earner households rather than a decrease in jobless households.<sup>18</sup>

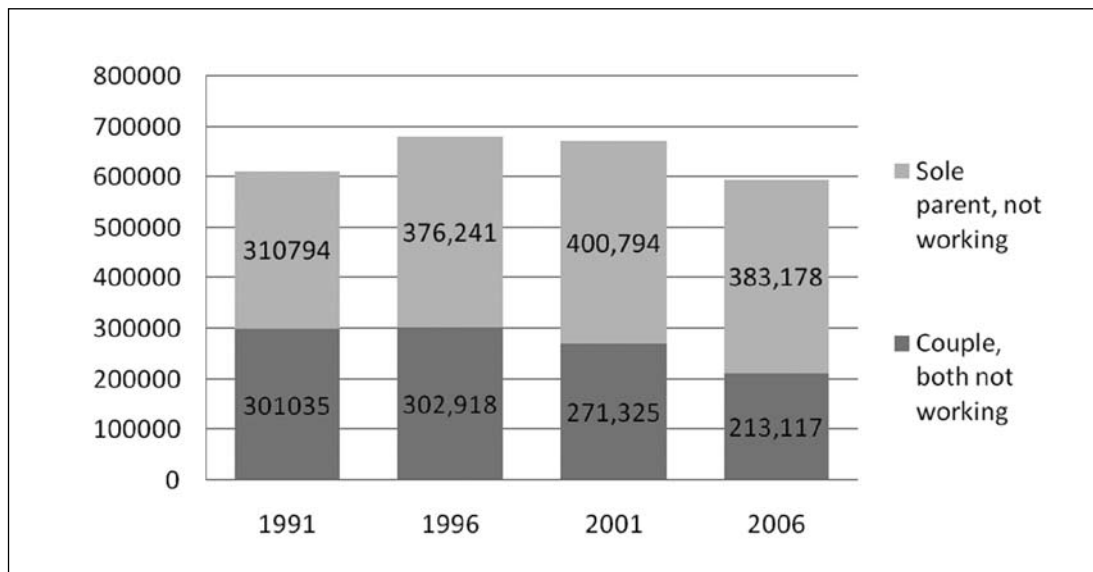
Robert Gregory pointed to the growing divide between ‘work rich’ and ‘work poor’ families, finding that while in 1979, 11% of children lived in jobless families, by 1998 this figure had increased to 18%. The duration of families’ unemployment also grew, with the proportion of unemployed people who were out of work for over one year more than doubling. This meant that more families stopped working and stayed unemployed for longer.<sup>19</sup>

The high watermark of the family joblessness epidemic was the mid- to late 1990s. Dawkins, Gregg and Scutella<sup>20</sup> found that in 1999, more than 17% of children lived in jobless families. They described a major demographic shift away from traditional sole-breadwinner families towards two-earner families, jobless couples, and sole parents—painting a picture of ‘rising individual employment and rising family joblessness.’ Employment growth in the mid- to late 1990s largely benefited couple families; and from this time onwards, sole parents made up a steadily increasing proportion of jobless families.<sup>21</sup>

Throughout this period, the growth in jobless families rose and fell with changes in the broader economy. However, while family joblessness increased after both the 1980s and 1990s recessions, each time it failed to recover to its pre-recession level.<sup>22</sup> Though many jobless families remained in the labour force and found work during the period of economic growth after the 1990s recession, many more withdrew altogether (people who are unemployed but seeking work are considered to be still in the labour force: they will take a job when it becomes available). By 1998, nearly three-quarters of jobless families were not in the labour force at all.

After two decades of rising family joblessness, studies in the early 2000s began to detect a drop. Scutella and Wooden found that by 2001, the proportion of children living in jobless households had dropped to just under 15%.<sup>23</sup> Similarly, the National Centre for Social and Economic Modelling (NATSEM) found that the total number of children living in jobless households dropped from about 16% in 1995–96 to about 14% in 2005–06.<sup>24</sup> The Longitudinal Study of Australian Children (LSAC) and the Melbourne Institute of Applied Economic and Social Research arrived at similar findings,<sup>25</sup> confirmed by Census data (see figure 1).<sup>26</sup> The ABS Labour Force Survey indicates that the proportion of children who live in jobless families has continued to gradually drop, with 12.6% of children 14 and under living in jobless households in November 2008.<sup>27</sup>

**Figure 1:** Jobless families 1991–2006



**Source:** Australian Bureau of Statistics<sup>28</sup>

One potential problem with these figures is that they show only how many children are living in a jobless family at a particular ‘point in time’ and not over a longer period of time. They may overstate the problem of family joblessness because long-term jobless families are grouped together with families who may be out of work for short periods of time. While they are useful in demonstrating overall trends, they give little insight into the number of families experience long-term or chronic joblessness.

Longitudinal data from the Household, Income and Labour Dynamics in Australia (HILDA) Survey provide a better picture of how many families remain jobless for long periods of time. Between 2001 and 2005, 26.5% of all children experienced family joblessness at some point. However, only 5.5% of children were in families who were jobless for all five years, while another 15% of children experienced family joblessness for between two and four years. While nearly 70% of children in single mother households experienced family joblessness at some point during 2001 and 2005, almost 30% of these were in jobless families for all five years. Another 31% were in jobless families for between two and four years.<sup>29</sup>

**While nearly 70% of children in single mother households experienced family joblessness at some point during 2001 and 2005, almost 30% of these were in jobless families for all five years.**

### *Characteristics of jobless families*

Besides providing insights into the level of family joblessness in Australia, the studies discussed above also present a clear picture of the ‘risk factors’ for family joblessness, and provide some clues for policy makers about where to focus their efforts. Children who live in couple households, who have older parents, and whose parents have a tertiary education have the lowest risk of living in a jobless household.<sup>30</sup> On the other hand, families are more likely to be jobless if the parents:

- are very young (15–20 years old) or much older (60–64 years old)
- have young children
- have four or more children
- are single, rather than married or cohabitating
- have lower levels of educational attainment
- are born in a non-English speaking country
- are Aborigines or Torres Strait Islanders
- live in a rural area
- have long-term health problems or a disability.<sup>31</sup>

Some other interesting trends have also emerged. The improvements in family joblessness between the mid-1990s and the mid-2000s were not uniform—while some areas improved remarkably, others went backwards.<sup>32</sup> Whole neighbourhoods have become increasingly work-rich or work-poor,<sup>33</sup> meaning that family joblessness is overwhelmingly concentrated within some communities and practically nonexistent in others.

People also tend to partner with other people who have similar characteristics as themselves, amplifying the risk of family joblessness. Partners of an unemployed person are more likely to be themselves unemployed compared with partners of an employed person.<sup>34</sup> When one person in a household is not working, there is an above average chance that other family members will also not work.<sup>35</sup> A ‘welfare culture’ can develop within a family (or a whole community), which leaves children of jobless parents with a propensity to be jobless and welfare dependent themselves as adults.<sup>36</sup>

#### *Sole parent families*

Jobless families are increasingly likely to be headed by a sole parent. NATSEM found that in 1995–96, about 50% of all jobless families were sole parent families. By 2005–06, this had increased to 65%.<sup>37</sup> However, while the *number* of jobless sole parent families continues to increase inexorably, the *risk* of sole parent families being jobless is dropping. Census data show that the proportion of sole parent families who were jobless dropped from about 56% in 1996 to about 47% in 2006.<sup>38</sup> Despite this improvement, the probability of being jobless is still significantly greater for sole parent families than for couple families. Children in sole parent families are about 10 times more likely to live in a jobless household than children in couple families.<sup>39</sup> Sole parent households are also more likely to remain jobless for longer than couple families.<sup>40</sup>

**Out of the half a million or so jobless families with children aged 14 and under, only about 52,000 are actually looking for work.**

#### *Labour force status*

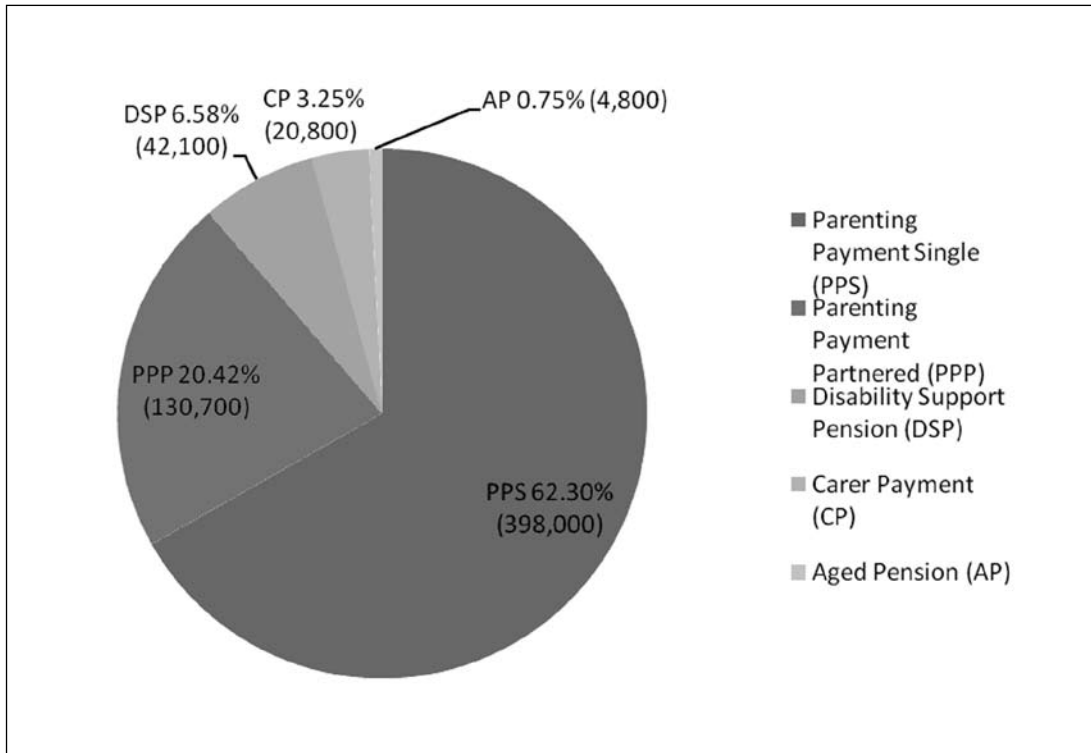
Less than 10% of jobless families are actually *unemployed*, meaning that more than 90% do not participate in the labour force at all. Out of the half a million or so jobless families with children aged 14 and under, only about 52,000 are actually looking for work. There are about 358,000 sole parents, and about 144,000 couple parent families who are not working and not looking for work.<sup>41</sup> A 2001 survey found that of the families who were not looking for work, about 29% said they were undertaking home duties, while 15% said they had a disability or caring responsibilities.<sup>42</sup>

Most families receive government payments of some kind, and data about which payments they receive provide some clues as to why they might be jobless. Family Tax Benefit (FTB) A is a means-tested payment given to all low- and middle-income families regardless of their work status. Parents can continue to receive FTB A until their income reaches between \$100,000 and \$160,000 depending on the number of children and their age, so it is safe to assume that most

jobless families (excluding those who receive large amounts of child support or another source of income) would receive it.

In 2006–07 about 640,000, or 35%, of FTB A recipients were also on some form of income support. Some payments allow recipients to work part-time or are designed to supplement the income of a low-earning partner, so they are not necessarily an indication that a family is jobless. Nevertheless, these figures indicate the proportion of families who rely on government benefits for all or part of their income. Figure 2 shows the number of families who received income support payments in 2006–07.

**Figure 2:** Family Tax Benefit A recipients who also received income support payments (2006–07)



**Source:** Department of Families, Housing, Community Services and Indigenous Affairs<sup>43</sup>  
 Figures do not add up to 100% because of rounding.

The largest group of income support recipients on FTB A were those receiving Parenting Payment Single (PPS), the payment for sole parents. However, more than 35% of PPS recipients were also working full- or part-time, so we cannot assume that all income support recipients were jobless.<sup>44</sup> Despite this, it is clear that a significant proportion of jobless families rely on government payments as their primary source of income.

*Income and poverty*

Jobless families are overwhelmingly likely to have low incomes. The measurement of poverty is controversial because it is difficult to define and is subject to many interpretations. The ‘poverty line’ is usually drawn as a percentage of the median income, typically 50% and is, therefore, a measure of living standards compared to the rest of a country’s population. While people at the bottom of the income distribution are the most likely to be deprived, a widening or narrowing of the income distribution may mask or artificially enlarge the poverty rate.<sup>45</sup>

**A significant proportion of jobless families rely on government payments as their primary source of income.**

Nevertheless, relative measures of poverty are commonly used in social science literature, and poverty rates do give us some valuable information about the lowest income earners in a society.

Dawkins, Gregg and Scutella found that in 1997, just over half of all sole parent households lived in poverty. However, nearly 80% of *jobless* sole parent households lived in poverty.

Similarly, 22% of all couples with children were in poverty, compared with 67% of jobless couples with children. Differences of this magnitude were recorded for every year in their study, indicating that family joblessness is a clear risk factor for a family living in poverty.<sup>46</sup>

More than 60% of Australia's impoverished families are jobless, and about 35% of Australian children living in poverty do so because they live in a jobless sole parent household—compared to an OECD average of 15%. A reduction in parental joblessness would have a marked effect on child poverty in Australia: if sole parents began working full-time at the minimum wage, they would immediately cross the poverty line.<sup>47</sup>

Income is a rather crude way of measuring a family's standard of living as it doesn't take into account factors such as the number of family members, home ownership, or the indirect costs of working such as child care. Nevertheless, it gives a broad picture of the economic position of working families compared to jobless families. Census data show that a parent's work status has a significant impact on a family's weekly income.

In 2006, nearly half of all couple families with both partners working full-time had a high income (in excess of \$2,000 per week), with a further 36% earning a moderate income (\$1,000–\$2,000 per week). Couples with one full-time and one part-time worker, and couples with one full-time worker, are also likely to have a moderate income. However, the picture is quite different for couple families with no workers. About one-third of jobless couple families have low incomes (\$500–\$1,000 per week), and another 20% have very low incomes (less than \$500 per week).

A similar story emerges when the weekly incomes of sole parents are examined. Just over 40% of full-time sole parent families have moderate incomes, with another 10% earning high incomes. In contrast, about 36% of sole parents who are not in the labour force earn low incomes, and another 36% earn very low incomes. About 50% of all unemployed sole parent families earn very low incomes, with another 34% earning low incomes. It is clear that joblessness has a major impact on a family's income and, consequently, their standard of living.

## Part II: Why do families remain jobless

Part I of this paper examined family joblessness in Australia, outlined trends over time, and explained the characteristics of jobless families. It found that the 1980s and 1990s saw an inexorable rise in the number of jobless families; however, this trend seems to have peaked in the mid to late 1990s. Family joblessness has been steadily dropping since then and, today, about one in eight children lives in a jobless household.

Part II of this paper will argue that a multifaceted policy response is required to tackle family joblessness because the reasons for parents being jobless are varied. Jobless parents may decide that it is not worth their while to move from welfare to work for little extra income: this reluctance could

be overcome by reforming taxes to make work more attractive. Some parents may not want to work, or may lack the skills and confidence to do so: a tough welfare-to-work policy requiring welfare claimants to seek work as well as providing them with assistance to do so is required. Finally, policies that contribute to a flexible labour market and lower the cost of hiring low-skilled workers will result in greater job creation, ensuring work is available for jobless parents.

**A multifaceted policy response is required to tackle family joblessness.**

The number of jobless families cannot ever be zero. Some parents have a legitimate reason for not working, such as disability or caring responsibilities.<sup>48</sup> The goal, therefore, is not to eliminate family joblessness altogether, or to push all jobless parents into work irrespective of their circumstances. The goal is to recognise that the welfare of children (and parents) is usually best served by having at least one parent working, and that family joblessness imposes social and economic costs on the rest of society. Public policy should, therefore, aim to minimise the number of children who live in families where no parent works.

### *Tax reform: Making work worthwhile*

The tax and welfare systems provide varying incentives and disincentives, which people respond to when deciding whether and how much to work. By removing disincentives and increasing

incentives, policy makers may be able to convince more jobless parents to work. Most people will rationally decide that working is worth their while when they are able to earn sufficiently more money from working than they would by remaining on welfare. There are two ways to achieve this: increase the income available from work, or decrease the income available from welfare.

Australia's welfare system is relatively unique. All income support payments, such as Newstart Allowance and Parenting Payment, as well as family payments such as Family Tax Benefit, are funded out of general taxation. Strict income and assets tests ensure that payments are targeted only at low-income earners. In contrast, many other countries have contributory social insurance schemes. Eligibility is determined by work history, meaning that payments may be relatively more generous for higher income earners.

There are positives and negatives to both systems. Australia's means-tested system is as good at reducing poverty and redistributing income to the poorest people as many social insurance systems, but it manages to do so at a greatly reduced cost because benefits are targeted at those who need them most.<sup>49</sup> However, the downside is the inherent disincentive for people to increase their income through work.<sup>50</sup> As a person's income increases, their benefit is gradually withdrawn and their tax bill increases. The result is high effective marginal tax rates (EMTRs): People can lose much of their new income in tax and lost welfare payments when they move into a job, meaning the difference between work income and welfare income is effectively reduced.

For example, a sole parent or a couple with two children under five faces an average effective tax rate of between 60% and 70% when moving from welfare into a minimum wage job. This means they effectively earn between \$4.50 and \$5.20 per hour, not including expenses such as travel to work.<sup>51</sup> Some jobless parents might rationally decide that moving from welfare to a low-paid job is just not worth their while. Could reform of the means-tested welfare and family payments systems overcome this, effectively increasing the 'in-work' income of these families and providing a greater incentive to work?

**Some jobless parents might rationally decide that moving from welfare to a low-paid job is just not worth their while.**

A family can move from joblessness to having one full-time worker at the minimum wage without losing any of its family benefits. Replacing these means-tested payments with a universal 'flat-rate,' or reducing the rate at which they are withdrawn, would reduce EMTRs faced by middle-income earners but would have no effect on EMTRs faced by jobless families moving into low-paid work.<sup>52</sup> To reduce EMTRs faced by jobless families, income support payments—such as Parenting Payment and Newstart Allowance—would need to be reformed.

Jobless parents can earn a small amount of private income before their income support payments are reduced, but after this their welfare income reduces dramatically. Depending on the payment received and the amount earned, parents lose between 40 and 60 cents for every extra dollar earned. The result of this is dramatic. Sole parents moving from welfare to a minimum wage job lose about two-thirds of their Parenting Payment income, lowering the difference between in-work and welfare income and, therefore, diminishing the incentive to work. Reform of these income support payments could, therefore, have a dramatic effect on the number of jobless families. A reduction in the PPS taper rate in 2000 resulted in almost 9,000 extra families in work.<sup>53</sup>

There are, however, significant problems with this approach. Many commentators argue that all families face the same costs in raising children and should be compensated by the taxpayer to the same degree,<sup>54</sup> so arguments that family payments should be made universal or extended up the income scale are based on principle as well as practicality. However, the same argument cannot be made for income support payments. While some groups have called for the introduction of a universal 'basic income,'<sup>55</sup> this does not have mainstream political support, and most agree that income support payments should be targeted at the lowest income people. Reducing the taper rates would mean more people qualify for income support—increasing the cost to the taxpayer and pushing the problem of high EMTRs (and welfare dependency) further up the income scale. Tight means-testing of income support payments, despite its disincentive effects, is a necessary evil.

Another way to alter the incentive effect is to change the conditions on which payments are made available. Peter Whiteford argues that family payments should be redesigned so that eligibility is conditioned on workforce participation by introducing benefits such as paid parental leave and increased childcare subsidies.<sup>56</sup> This would effectively alter the difference between in-work income and welfare income because payments would not be available unless both parents were working.

In response to this dilemma, the United States moved from a focus on poverty relief for jobless parents to a system of in-work benefits for low-income families.<sup>57</sup> The Earned Income Tax Credit (EITC) subsidises the wages of low-income working families, making work relatively more attractive than welfare. The EITC's value increases as very low-income families earn more money through work, and this has had a positive effect on parents' workforce participation. One study found that the EITC was responsible for 60% of the increase in single mothers' workforce participation between 1984 and 1996.<sup>58</sup> A similar 'working tax credit' in the United Kingdom has been effective in increasing parents' workforce participation.<sup>59</sup>

In Australia, the key policy instrument for increasing the incentive to work has been the Low Income Tax Offset (LITO), which effectively increases the tax-free threshold for low-income earners to \$14,000. Further increases to the LITO are scheduled in the coming financial years.<sup>60</sup> There are some limitations to this policy, though. Because the LITO is gradually withdrawn as income increases, it simply pushes the disincentive effect up the income scale.<sup>61</sup> Unlike an EITC, the LITO provides a tax break to all low-income earners even if their income is solely derived through welfare, meaning the policy targets poor people but doesn't necessarily encourage them to work.

In 1998, the 'Five Economists' argued for an earnings credit similar to an EITC. In exchange for the credit, the value of award wages would effectively decrease over time to stimulate more employment at the unskilled and low-skilled end of the market. The proposal aimed to create both the 'supply' of jobs as well as the 'demand' for jobs.<sup>62</sup> The proposal received a lot of publicity, but there doesn't appear to be any sign that it will be taken up by government. This could be because of the many potential drawbacks. Like the LITO, an earnings credit could just push the disincentives up the income scale.<sup>63</sup> While it may increase the number of people in work, it would do little to reduce welfare dependency overall, as more families would become reliant on the taxpayer for part of their income. It could provide a disincentive for low-income workers to increase their hours or move into better paid jobs for fear of losing their earnings credit,<sup>64</sup> and could shift the tax burden inequitably towards secondary earners. The effect of this has been seen in the United States where the workforce participation rate of married mothers fell after the introduction of the EITC.<sup>65</sup> Perhaps for these reasons, an EITC or earnings credit does not appear to be on the political agenda in Australia.

A simple alternative for increasing work incentives and avoiding these problems is broad-based tax reform that includes an increase in the tax-free threshold or a decrease in the lowest marginal tax rate.<sup>66</sup> This would increase incentives for jobless parents to work as they would keep more of their new income. It would also lower the tax paid by individual workers regardless of their income, and would therefore contribute to overall tax relief. However, because it would not be targeted as an EITC or earnings credit (and, therefore, not as effective in reducing family joblessness), it would 'cost' the government significantly more in lost tax revenue.

Buddelmeyer, Freebairn and Kalb studied the effects of these policy changes on increasing work incentives in Australia; investigating the efficacy of reducing the taper rate on income support payments; lowering the bottom tax rate; increasing the tax-free threshold; increasing the LITO; and introducing an EITC. They found that reducing the taper rate would be the least effective policy option. While the number of jobless households would fall, overall workforce participation would also decrease. This would also lead to a cost blow-out. The other four proposals all had positives and negatives. While a reduction in the bottom marginal tax rate or an increase in the tax-free threshold would have the largest *overall* effect on labour supply, the EITC would have the biggest impact on reducing the number of jobless families because it is tightly targeted at low-income earners.<sup>67</sup>

All the options for increasing work incentives have drawbacks. While a specific reform to lure jobless families into work—such as an EITC or earnings credit—would have the greatest effect, it would inevitably involve other compromises. In light of this, it seems that the best policy direction is one of broad-based tax relief to increase incentives to work across the board.

The drop in family joblessness over the past decade coincided with a series of income tax cuts and the introduction of the LITO. These measures, combined with increasing wages, ensured that jobless families could earn sufficiently more income through work than by remaining on welfare. The Rudd government plans to continue with tax cuts and to gradually increase the value of LITO. This reform is vital if the rate of family joblessness is to continue dropping.

### *Welfare reform*

Financial incentives may successfully lure some jobless parents into the workforce, while others may need extra assistance or compulsion. Australia's welfare system has been substantially reformed over the past few decades. Instead of an unconditional right to welfare, jobless people are now expected to take reasonable steps towards finding employment. Australia's welfare-to-work agenda was part of a worldwide trend<sup>68</sup> that saw the unemployed penalised for failing to comply with job search requirements, along with governments taking a more active role in helping the jobless find work.

In Australia, the Keating government's 'Working Nation' package included job search assistance for welfare claimants for the first time, as well as penalties for those who did not meet job search requirements. This policy was expanded under the Howard government, and became known as 'mutual obligation.' Jobseekers would be offered help to find work, but would also be required to search for jobs. Those who did not comply were penalised. Furthermore, the long-term unemployed would have to undertake mutual obligation activities such as training, volunteer work, or 'work for the dole.' In response to ballooning numbers of Parenting Payment and Disability Support Pension claimants, the Howard government also introduced some limited part-time work requirements for these groups.<sup>69</sup> Up until 2006, sole parents could claim PPS, and a couple parent whose partner was not working could claim PPP until their youngest child turned 16. They were under no obligation to find work.<sup>70</sup> Since 2006, Parenting Payment recipients have been required to seek part-time work when their youngest child turns seven.<sup>71</sup>

**The best policy direction is one of broad-based tax relief to increase incentives to work across the board.**

These reforms were not without controversy. Welfare groups, as well as some academics and commentators, claimed the rules were unnecessarily punitive. Groups such as the Australian Council of Social Services, the St Vincent de Paul Society, and the Brotherhood of St Lawrence argued against welfare-to-work on the basis that the penalties imposed on jobseekers who fail to meet requirements caused unnecessary hardship,<sup>72</sup> and others such as Cox and Priest argued that the reforms unfairly targeted sole parents.<sup>73</sup>

Despite these criticisms, welfare-to-work reforms were followed by a significant drop in the unemployment rate as well as a steady drop in the number of jobless families. It is difficult to know how much of this is due to the reforms and how much is due to broader economic conditions. While the efficacy of programs such as Work for the Dole can be measured by looking at the number of participants who find work afterwards, it is much more difficult to measure the net effect: How many people would have got a job anyway?<sup>74</sup> Peter Saunders of the Social Policy Research Centre argues that both 'push and pull' factors contributed to falling joblessness in the late 1990s and 2000s. Economic conditions improved and more jobs became available, while welfare-to-work made working relatively more attractive than joblessness.<sup>75</sup>

Ann and John Nevile have undertaken two comprehensive studies of the Work for the Dole program, a key component of the welfare-to-work agenda, which gives some clues as to the success of welfare-to-work. They find that Work for the Dole 'is a valuable labour market program helping participants find work.'<sup>76</sup> The federal government's own impact study found that people who undertook Work for the Dole programs were significantly more likely to leave welfare.<sup>77</sup> The Melbourne Institute of Applied Economic and Social Research has found that people

who leave unemployment for low-paid jobs or part-time jobs have a better chance of moving to better jobs,<sup>78</sup> demonstrating that a 'jobs first' policy is effective in helping families escape poverty.

Therefore, it seems clear that the design of the welfare system affects the level of family joblessness.<sup>79</sup> Despite this, welfare groups are pressuring the Rudd government to dilute welfare-to-work legislation.<sup>80</sup> A senate committee has recommended changes seeking to have penalties for welfare claimants who do not meet job search requirements reduced,<sup>81</sup> so it is possible (and even likely) that the government will implement changes that undo some of the welfare-to-work reforms. A weakening of mutual obligation requirements could lead to an increase in the number of jobless families.

Welfare-to-work reforms must not be abandoned or weakened if family joblessness is to be effectively tackled. Some consideration could even be given to further reforms. For example, the federal government has committed to providing 15 hours of free preschool to all four-year-olds,<sup>82</sup> and this might provide an opportunity to require Parenting Payment recipients to look for low hours part-time work after their youngest child turns four. If parents are unable to find jobs, they could volunteer at their children's school or pre-school (along with some job search) as a useful way to gain some experience to re-enter the workforce. Alternatively, this time could be used to learn new skills, which will help parents re-enter the workforce when their children reach school age, such as English language classes, literacy and numeracy classes, or computer classes.<sup>83</sup>

**Welfare-to-work reforms must not be abandoned or weakened if family joblessness is to be effectively tackled.**

While the philosophy of welfare-to-work should not be diluted, some ongoing refinement of the system may be justified. For example, NATSEM points out that under new rules introduced in 2006, some Parenting Payment recipients will be moved to Newstart allowance when their children reach school age. This will result in these parents facing higher EMTRs and, thus, greater disincentives to join the workforce.<sup>84</sup> Changes to welfare-to-work rules to correct issues such as this may be warranted. Nevertheless, Peter Saunders, who is a Distinguished Fellow of the CIS, argues

that it is reasonable to expect people to move from welfare to jobs when they become available regardless of the EMTR they face.<sup>85</sup> While it is preferable to correct anomalies such as this, care must be taken to ensure the 'work first' message is not lost as a result of any changes. It is clear the welfare-to-work principle can push parents who don't want to work into the workforce, while also helping those who lack the confidence or skills to find jobs.

Tougher welfare rules implemented over the past decade have undoubtedly contributed to the drop in family joblessness. There is a real danger that if mutual obligation requirements are wound back, the number of jobless families will again rise. The lessons from these reforms suggest that further tightening welfare eligibility requirements, such as requiring parents to work when their children reach pre-school age, will have a significant effect on the level of family joblessness. The link between welfare rules and family joblessness is clear.

*Jobs, Jobs, Jobs*

While some jobless parents will respond to greater incentives and penalties, for others the problem is simply a lack of available jobs. Until recently, unemployment was at record lows, and the most pervasive problem with the labour market was a skills shortage: The idea that someone could not find work was almost unbelievable. However, economist Bob Gregory argues that low official unemployment rates during the boom masked 'hidden' unemployment—people such as sole parents and older men on Disability Support Pension, who had been out of the workforce for a long time or who didn't have the skills required for the available jobs. While demand for skilled labour was high and growing, demand for unskilled labour had almost evaporated.<sup>86</sup>

With unemployment rising, this trend will undoubtedly intensify. Beyond creating incentives for jobless parents to work, and penalties for those who don't, policy makers must also create an environment that is conducive to the creation of low-skilled jobs, where most jobless families and welfare recipients are clustered.<sup>87</sup>

There is a general acknowledgement that the level of the minimum wage has some effect on low-skilled job creation. Ian Harper, chairman of the Australian Fair Pay Commission, the body that sets the minimum wage, has confirmed his belief in the relationship between wages and unemployment rates.<sup>88</sup> In its submission to the 2009 minimum wage review, the federal government argued that its principal objective is ‘supporting Australian jobs and employment opportunities,’ while employer groups argued that raising the minimum wage could dampen job growth.<sup>89</sup> Peter Saunders notes that Australia’s minimum wage is among the highest in the OECD, and argues that lowering it could encourage the growth of low-skilled employment.<sup>90</sup>

Simply lowering the minimum wage, however, is problematic. Besides being politically unpalatable, any narrowing in the gap between welfare income and work income would reduce the incentive to work. While more jobs might be created, the lowest paid jobs might provide an unacceptably small income. For Saunders, ‘the real challenge is not to maintain minimum wage levels, but to reduce direct wage costs incurred by employers of low-skilled labour without unduly harming the living standards of low-income households.’<sup>91</sup> This could be achieved either by providing an ‘in-work’ welfare payment or by reducing the tax burden faced by low-income workers to offset low wages.

**While some jobless parents will respond to greater incentives and penalties, for others the problem is simply a lack of available jobs.**

The ‘Five Economists’ argued that the growth of award wages could be arrested as a trade-off for government subsidies to low-income workers. This would stimulate more employment at the unskilled and low-skilled end of the market, creating a greater ‘supply’ of jobs.<sup>92</sup> The Australian Industry Group has argued that the Rudd government should bring forward tax breaks for low-income earners to decrease the likelihood of a minimum wage increase.<sup>93</sup>

The government’s industrial relations policy, the legislative framework which regulates employers’ relationships with their employees, also has an effect on job creation. The Howard government’s ‘Work Choices’ legislation was criticised for being too harsh on employees, and Howard’s 2007 election loss was widely attributed to voter backlash over the policy. The Rudd government’s new ‘Fair Work’ legislation is viewed by some as a necessary correction, but other commentators have warned that the changes will result in job losses.<sup>94</sup> It remains to be seen how the legislation will affect job creation and retention in practice. While a detailed exploration of industrial relations is beyond the scope of this paper, the experience of the past clearly demonstrates the effect that it can have on unemployment and family joblessness. Winding back industrial relations reforms could lead to a jump in the number of jobless parents.

Tax and welfare policies that provide incentives for jobless parents to join the workforce, or compel them to do so, are useless if there are no jobs available. Any attempt to tackle family joblessness must necessarily include the continued reform of the labour market. Wage setting and industrial relations policies must be governed by the ‘jobs first’ policy, with a key objective being the continued creation of low-skilled jobs.

### *Conclusion and recommendations*

A multi-pronged approach to tackling family joblessness is needed because jobless families are so heterogeneous. Some are out of work because they genuinely can’t find a job. For these families, policies that make hiring staff more attractive to businesses might have the biggest impact. Others—for example, sole parents—might weigh up the small amount of extra income they gain from working with the extra time away from their children and decide it’s just not worth it. For these families, tax relief to make work more attractive could alter their calculations. Some jobless parents are ‘dutiful but defeated’<sup>95</sup>—they say they want to work but have lost the confidence and skills to do so—and others simply do not want to work. For these parents, tough rules around welfare eligibility provide an extra ‘push’ into the workforce.

After rising continually throughout the 1980s and 1990s, the rate of family joblessness has been slowly but steadily dropping for the past decade. Undoubtedly, this is partly due to good economic conditions, but as the economy deteriorates the level of family joblessness may again rise. Nevertheless, it is certain that changes to public policy during this time have also influenced

the level of family joblessness. Tax relief, tougher welfare rules and a more flexible labour market all contributed to a decline in the number of jobless families. This experience provides a valuable guide for policy makers who want to ensure the level of family joblessness continues to drop:

- Governments should ensure that working is more financially attractive than receiving welfare by reducing the tax burden faced by workers. This can be achieved by targeting low-income workers through an EICT; however, this can result in other disincentives to work further up the income scale. Broad-based tax reform is more ‘expensive’ but avoids this problem. As tax cuts and higher wages have made working more attractive over the past decade, the number of jobless families has fallen.
- Policy-makers should not abandon or dilute the welfare-to-work message: everyone who can work should do so. The tightening of welfare rules has contributed to a decline in the level of family joblessness, and winding these back could result in rising family joblessness. Work requirements for jobless parents could even be expanded further by requiring parents of pre-school children to work.
- Tax and welfare reforms make no difference if there is no work available. Policies that create an environment conducive to the creation of low-skilled jobs will ensure that there is work available for jobless parents. Industrial relations reform should focus on fostering a flexible labour market, and policies that reduce the cost of low-skilled labour will result in greater job creation.

The small but steady reduction in family joblessness over the past decade is a good news story: the challenge now is to ensure that the trend continues. Reducing family joblessness is vital because of the devastating impact it has on children. Children of jobless parents have worse health, educational, developmental, and behavioural outcomes than children of working parents. Children often live in poverty because their parents are not working, and may even ‘inherit’ the propensity for joblessness from their parents, meaning that disadvantage and dependency is passed down through the generations.

**The current economic downturn is a dangerous time to unwind tough welfare rules and labour market flexibility, which could intensify rising unemployment.**

During both the recessions of the 1980s and 1990s, the number of jobless families understandably grew, but most worrying was the fact that many families did not return to work when the unemployment rate later dropped. This experience should guide future policy making. The current economic downturn is a dangerous time to unwind tough welfare rules and labour market flexibility, which could intensify rising unemployment. During a downturn, it is preferable for people to have the option of lower-paid jobs, rather than simply being forced onto the unemployment queue.

Solving the problem of high family joblessness will require reform of the welfare, tax, and industrial relations systems. The enormity of the challenge perhaps lends a clue as to why the problem still exists. Nevertheless, the evidence is clear: children who grow up in a jobless family are significantly disadvantaged compared to those who don’t. All sides of the political spectrum recognise this is a pressing issue that must be solved, and the low rates of family joblessness in other countries indicate that it is this is an achievable goal. The experience of the past decade provides a clear road-map for policy makers who want to continue to reduce family joblessness. With unemployment set to rise, it seems likely that the level of family joblessness will increase too. Tax, welfare, and labour market reform can limit the fall-out.

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