

Does the Living Wage Ensure an Adequate Standard of Living for Families?

Introduction

New Zealand was once held up as a model of egalitarianism to other countries. Today New Zealand is far from being that leader, with high income and wealth inequality and an unacceptable level of family poverty and homelessness. Children are particularly affected, suffering the highest levels of material deprivation in New Zealand (Perry, 2016).

Living Wage Movement Aotearoa New Zealand (LWMA) has argued that raising wages is the best way to address this problem. They believe the minimum hourly wage rate is too low and that employers ought to pay a higher 'living wage rate' (LWR). Currently (in 2017) the margin between the minimum wage rate of \$15.75 and the LWR of \$20.20 is \$4.45.¹

Since 2013 when the LWR was first introduced, more employers have signed up to be living wage employers. Recently,

the Wellington City Council implemented policies to pay a living wage rate, not just to its employees, but to all staff of council-controlled organisations (Devlin, 2016). The new mayor of Auckland, Phil Goff, has also committed to paying the LWR, first for those directly employed, and then for contracted workers (Furley, 2016). In 2017, 64 firms or organisations are identified as 'accredited living wage employers.'

This article argues, however, that while better wages are essential, on their own

they are an insufficient response, especially to the inadequacy of family incomes.² Higher basic wages must be accompanied by strengthening the generosity and effectiveness of tax-welfare policies (Boston, 2013). To this end, changes to the way the living wage rate is calculated are suggested.

The living wage in New Zealand

Over the last decade the living wage movement has gained prominence in countries such as the United States and the United Kingdom. The living wage campaign first emerged in New Zealand in 2012 as a response to the increasing disparity between high- and low-income groups. The key drivers of the movement in New Zealand have been dissatisfaction with stagnant wages, and the belief that 'wages should be based on need and not left to the market' (LWMA, 2016a). One of the key aspirations is 'to reduce poverty'. In particular, Living Wage Movement Aotearoa New Zealand places a strong emphasis on child poverty. Its website refers to there being 'up to 285,000 children ... living in poverty and of those children 40% come from families where at least one adult is in full time work or self-employed' (LWMA, 2016b).

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Defining the living wage

The report of an investigation into defining a living wage for New Zealand describes the living wage rate as 'the hourly wage a worker needs to pay for the necessities of life and participate as an active citizen in the community' (King and Waldegrave, 2012, p.3). Unfortunately, the terms 'living wage' and 'living wage rate' are often used interchangeably. Importantly, having sufficient money to live on is a function both of the living wage rate *and* the number of hours worked.

The living wage reflects the basic expenses of workers and their families for commodities such as food, transportation, housing, childcare, health, education and

to maintain adequate living standards for a household of two adults and two children. Participants are asked to find commonly used budget items and give an estimate of the total cost. An overall expenditure level is also calculated using secondary data sources, such as the Statistics New Zealand Household Economic Survey (HES), cost estimates provided by the University of Otago food costs survey, and the Ministry of Business, Innovation and Employment's tenancy bond database.

In the initial exercise to set the LWR, the focus group results were judged to give an income that was 'much higher than researchers expected'. The average of HES

supplement is estimated.³ King and Waldegrave produced a range of final 'disposable household income levels' for different gross income values. The desired disposable income was then selected and the relevant gross hourly wage rate determined as the LWR (King and Waldegrave, 2012, pp.44-5).

Updating the living wage rate

The LWR has been updated on a regular basis by the Family Centre Social Policy Research Unit (King and Waldegrave, 2012, 2014). The method is to link the LWR to growth in 'average ordinary time hourly earnings'. Changes in this variable are published every quarter by Statistics New Zealand (Statistics New Zealand, 2014, 2016a, 2016b).

In 2014 King and Waldegrave also reviewed and updated values for rents, food costs and other living costs. While the cost inflation-based estimates and the expenditure estimate gave a higher increase for the LWR than the movement in the average ordinary time hourly rate (2.1%), it was decided to use the wage adjustment.

The living wage rate of \$20.20 an hour delivers the required standard of living only if the couple actually works 60 hours a week, 52 weeks of the year.

recreation. The actual standard of living achieved by families who are paid the LWR hinges critically on the subtle interplay of five main factors:

- the gross hourly rate;
- the number of hours worked;
- the taxes payable, including effects of GST;
- the value of tax credits for children;
- the social wage of tax-funded health, education and housing assistance.

Calculating the living wage

Commissioned by the living wage movement, King and Waldegrave (2012, 2014) constructed a model to find the living wage rate that enables an 'income necessary to provide workers and their families with the basic necessities of life. A living wage will enable workers to live with dignity and to participate as active citizens in society.' The methodology proceeds in two steps: first, the determination of what total disposable income is necessary for a given standard of living; and second, the gross wage rate required to achieve this.

First, focus groups are used to identify an average level of expenditure required

values for various categories such as 'food', 'housing', 'clothing and footwear' and 'childcare' spent by the lower-income groups (deciles 1-5) was taken to be a more realistic measure (King and Waldegrave, 2012, p.8). The annual expenditure calculated on this basis became the 'disposable household income' needed to ensure the required standard of living.

The next step finds the gross income level (before income tax, and other deductions such as KiwiSaver, are taken into account and tax credits are applied) for a family of a given structure that achieves the necessary level of effective disposable income (after these adjustments). The LWR estimates are based on a family that has two children under 13, and one and a half income earners who between them work 60 hours per week for 52 weeks per year.

Entitlement to Working for Families tax credits (the in-work tax credit and family tax credit) is determined by the initial gross income for households with two dependent children. Then, depending on the initial gross income of the family and actual rent paid, an accommodation

The rate of \$18.80 is chosen as the 2014 recalculated living wage, because the living wage is a wage in the market, and it was decided the updates should relate primarily to movements in wages rather than the CPI or the higher household costs as measured by HES. (King and Waldegrave, 2014, p.3)

It is intended that the LWR be recalculated and the methodology reviewed after five years, implying that there will be a review in 2017. In the meantime, the wage link was used to update the LWR in 2017.

King acknowledges that the use of the wage adjustment for determining the LWR each year is dependent on policy on transfers remaining unchanged:

Because such policy changes tend to be infrequent, it is possible to maintain the currency of the living wage rate over the medium term by linking it to annual wage movements,

as happens with the New Zealand living wage. (King, 2016, p.21)

For 2017 the LWR of \$20.20 corresponds to a gross (before-tax) income of \$63,024 for the standard family. The final disposable income of \$59,887 deemed to produce the desired living standards for this family is made up of Working for Families tax credits of \$5,932 and after-tax income of \$53,955. While in 2017 some families on this gross living wage amount may be entitled to a small accommodation supplement, especially if in high rent areas, this policy is ignored in the analysis below.

Critiques of the living wage

Undoubtedly, workers who would otherwise have been paid the minimum wage benefit significantly when paid the higher LWR. Nevertheless, there are some concerns that go to the heart of how the LWR is constructed.

The Treasury (2013) outlined some of the limitations found in the methodology adopted by Family Centre Social Policy Research Unit. In particular, their report criticises basing the living wage on a household of two adults and two children, when the group on low incomes is actually very diverse. Families comprised of two parents and two children are only 6% of the group earning below the LWR, and hence scarcely representative. Treasury also noted that the LWR will be too high in low-housing-cost regions and insufficient for those living in high-cost regions.

Statistics show that 47% of poor children in New Zealand come from sole-parent households, while 64% of all the sole-parent households are identified as being poor, in contrast to 15% of two-parent households (Perry, 2016, p.151). Poverty rates for children in full-time working families are much lower than for those in beneficiary families, and about three out of five of poor children come from families not supported by a full-time worker (ibid., p.137)(Perry, 2016). Paying the LWR is clearly not sufficient to address, let alone eradicate, child poverty in New Zealand (Scott, 2014; Treasury, 2013).

The Treasury report also suggests that at the living wage rate, adults who are single would be relatively overpaid

compared to adults with dependent children. In response to this particular criticism, the Family Centre Social Policy Research Unit says:

even though a single young person generally has lower costs than a family of four, a living wage enables young people to save, pay for further education or eventually place a deposit on a house. (King and Waldegrave, 2014, p.7)

Undoubtedly, an increase in the wage level would have a significant and welcome

In theory, in a targeted system of income support, payment of the LWR will increase income over the threshold and reduce the amount of state-funded Working for Families credits received. But it also runs the risk of facilitating more deliberate reductions in the value of these tax credits over time.

In the case of the UK, Mabbett notes that a packaging of the living wage with reduced tax credits has given rise to a 'looking glass world', where policies are sold as a package but actually work in opposite directions:

In theory, in a targeted system of income support, payment of the [living wage rate] will increase income over the threshold and reduce the amount of state-funded Working for Families credits received.

impact in easing the financial burden of the young with student loan debts and allow them to enhance their savings. Other groups, however, such as sole parents, large families, or two-parent families with only one working, may continue to find it difficult to save, repay student loans or buy a house, even at the current LWR.

Deborah Mabbett from the UK raises concerns about the practical implications of the living wage concept, arguing that a living wage cannot act as a substitute for social security. She warns that the framework of the living wage campaign implicitly endorses an ideological norm of a certain family structure and behaviour. The concern is that those who do not live in families of the preferred type and/or work enough hours for whatever reason do not achieve the living wage outcome. It must be acknowledged that even the standard family may struggle to achieve 60 hours a week for 52 weeks of the year. The danger is that their plight may be dismissed as evidence that they just need to increase their work effort.

The Prime Minister's current favourite profile: a family with two children where both adults work full-time on the minimum wage. They will, he claims, be better off by 2020 under the government's new policy combo of reduced tax credits and a higher living wage. A quick check of HMRC statistics shows that there are just 135,000 households receiving tax credits (out of 3.3 million working households) comprising a couple with children where both adults work full-time. (Mabbett, 2015, p.465)

Thus, as in the UK, a cost-cutting government may encourage the living wage movement so that it can push more of the costs of children onto employers by eroding children's payments over time. Thus, the deliberate attrition of Working for Families in New Zealand (see below) may be less resisted if more families earn a living wage rather than a minimum wage.

Table 1: Working for Families Tax Credits, children under 16, 1 April 2017

	Maximum 2017 values (weekly)
Family Tax Credit (FTC), first child	\$92.73
- additional child under 13	\$64.44
- each additional child 13-15	\$73
In Work Tax Credit (IWTC), one to three children	\$72.50
- each additional child	\$15
Threshold, joint income (annual) abatement rate 22.5%	\$36,350

Were there alternatives? In the UK case Mabbett argues:

A more robust approach to the living wage would have been to take a stand on the appropriate role for in-work benefits. For example, the living wage could have been set to ensure that a single person in full-time work could make a living without needing benefit top-ups, and estimates of the additional costs faced by those with children could then have been used to make the case for adequate child benefits and childcare provision. The available data suggest that the living wage estimated this way would be above the new minimum ... On this basis, it would be crystal clear that low-income families with children need support from the state even when a living wage is paid, and that increases in minimum wages do not substantially alter this fact. (ibid., p.467)

This approach is also taken by Australian Council of Social Service, described as a 'peak body of the community services and welfare sector and a national voice for the needs of people affected by poverty and inequality':

Our starting point is that the Federal Minimum Wage (FMW) should be designed to at least provide a decent living standard, well above poverty levels, for a single adult and that the tax-transfer system should meet the basic costs of raising children in a low income family. The FMW should not be directly designed to cover the costs of children because that role is best performed by the social security system. However the FMW together with family payments should be sufficient to prevent a family from falling into poverty. The minimum wage itself should be set well above

poverty levels, in keeping with Australian public policy tradition, and the need to maintain a gap between maximum social security payments and minimum wages to preserve work incentives. (Australian Council of Social Service, 2016)

Interestingly, the New Zealand Council of Trade Unions has advocated for a substantially higher minimum wage set at two thirds of the average wage. In 2016 this rate was \$19.88, almost exactly the level of the 2016 LWR.

The minimum wage needs to be two-thirds of the average wage, this would make it much fairer (two-thirds of the average wage would be \$19.88 per hour). Working people have been advocating for this change as a way to make real and measurable progress in improving the lives of some of our poorest families. (New Zealand Council of Trade Unions, 2017)

In spite of questions about the basis of the living wage calculations, the living wage campaign has succeeded in securing higher wages for an increasing number of low-waged workers in a climate hostile to such improvements. This has helped stem the drift to an ever-widening of the income distribution, and growth in profits at the expense of wage income. However, there has been little attention paid to the critical issues of cutbacks to family assistance or a questioning of the fundamental basis of the living wage calculation itself.

How Working for Families works

Given the critical importance of tax credits in the achievement of the desired standard of living from the LWR, this section briefly explains how Working for

Families works.

Child tax credits, family benefits, basic income, family rebates and tax relief are possible ways for society to help families with the costs of raising children and to prevent poverty. Child-related payments in New Zealand now come under the umbrella of Working for Families, a system of weekly, child-related tax credits paid to the caregiver targeted on total family income. The main family-related tax credits, the family tax credit and in-work tax credit, replaced the existing tax credit system and were fully phased in by 2007, making a significant difference for those families who gained access to the maximum entitlement. All low-income children qualify for the family tax credit, while the in-work tax credit is available only to families with parents who work the required hours each week (30 hours each week as a couple and 20 hours per week as a single parent).

Indexation of tax credits is a vitally important issue. Unlike New Zealand Superannuation, which is updated annually to the consumer price index (CPI) but also linked to the net average wage, family-related tax credits are adjusted only when cumulative inflation reaches 5% (see St John and Dale, 2010). The last adjustment under this rule was on 1 April 2012, when all but the rate for those aged over 16 were increased. Table 1 summarises the maximum weekly payments to households for children under 16 in 2017 (Inland Revenue, 2017).

The inflation rate is measured to the year ended September to give Inland Revenue enough time to implement the adjustment in the following April. As cumulative inflation since September 2011 had not exceeded 5% by September 2016, no inflation adjustment to any part of Working for Families was made in 2017. By 2018, cumulative inflation is likely to be approximately 7%, and after six years an adjustment would have been expected. However, increases to family tax credit rates announced in the 2017 Budget for 1 April 2018⁴ appear to be instead of the legislated adjustment. Hence, unless there is a change of government later in 2017, and a subsequent change of policy on family income assistance, the new family tax credit rates appear likely to remain unindexed for several years.

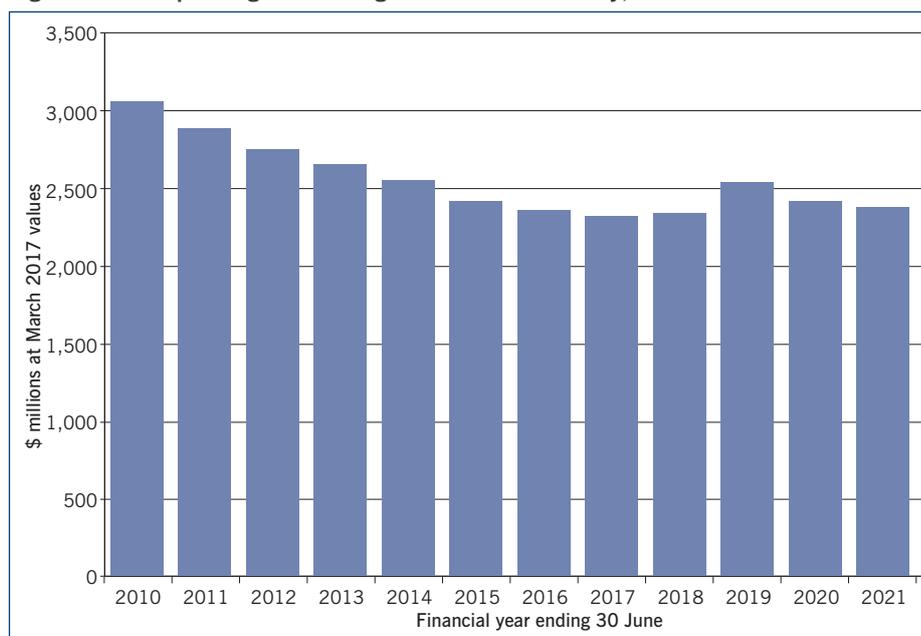
If the living standards of low-income families are to be protected, all parts of family assistance must be, at the very least, adjusted automatically for inflation every year. Arguably, they should be linked to average wages, the same as for New Zealand Superannuation and the LWR itself. This is very important in times of low measured CPI inflation but high housing and increased living costs for most families (Statistics New Zealand, 2016a).

Far from automatic indexation, the 2010 Budget froze the threshold for abatement at \$36,827. The 2011 Budget introduced further cost saving by, over time, increasing the rate of abatement from 20% to 25% and further reducing the abatement threshold to \$35,000 (Inland Revenue, 2017). For every dollar earned above the threshold, the abatement rate is first applied to the family tax credit, which is eventually reduced to zero, then to the in-work tax credit. From April 2016 the rate of abatement was increased from 21.25% to 22.5% and the maximum in-work tax credit entitlement had a belated, one-off inflation adjustment from \$60 to \$72.50.

Overall, the loss of indexation to all parts of the Working for Families package is illustrated in Figure 1, which shows the decline in real expenditure on Working for Families. By 2017 another \$700m was needed to restore spending to 2010 levels (keep the bars the same height). The cumulative loss to families from 2010 to 2017 was around \$2 billion. The projected expenditure for 2018/19 shown in Figure 1 is higher because of the changes to Working for Families outlined in the 2017 Budget (Treasury, 2017), but real spending then continues to fall away again.

Table 2 clearly demonstrates the slow erosion of Working for Families. For working families the biggest impact is from the failure to update the income threshold at which abatement becomes effective. If the threshold, currently \$36,350, had been price-adjusted (to the CPI) from 2005 when it was \$35,000 to the first quarter of 2017, it would be \$45,000, or \$50,916 if adjusted by wages. To illustrate: if a family on \$35,000 in 2005 entitled to the full Working for Families experienced the average growth in wages, its income would be \$50,916 in the first quarter of 2017, but its entitlement

Figure 1: Real spending on Working for Families (Treasury, 2017)



Source: Treasury, 2017

Table 2: Weekly Working for Families (children aged under 13) adjusted to CPI and growth in average wages

	Nominal values WFF 2005-7	Adjusted for CPI to Q1 2017	Adjusted for changes in average wage to Q1 2017	Actual 2017-2018	New 2018-2019
FTC	\$82	\$105	\$117	\$92.73	\$101.98
-each additional child	\$57	\$73	\$81	\$64.44	\$91.25
IWTC					
one to three children	\$60	\$75	\$83	\$72.50	\$72.50
Plus \$15 for each additional child	\$15	\$19	\$21	\$15.00	\$15.00
Threshold, joint income (annual)	\$35,000	\$45,000	\$50,916	\$36,350	\$35,000

to Working for Families would have been reduced by \$3,277 per annum using the actual 2017 threshold.

Critiques of Working for Families

A major problem was that when Working for Families was introduced, the poorest families gained some extra from the family tax credit but they were excluded from the in-work tax credit and there were offsets to core benefits, which meant that 'the WFF package had little impact on the poverty rates for children in workless households' (Perry, 2016, p.142).

Being paid the LWR is no guarantee of enough hours of work or immunity from recessions, sickness or redundancy. The in-work tax credit has been criticised on many grounds, including that it

discriminates against the poorest children and is in breach of the fundamental human rights legislation. In casualised labour markets, families can lose entitlement to the in-work tax credit, worth a maximum of \$72.50 per week, or more for larger families, simply by losing hours of work. The rise in informal work without guaranteed adequate hours or other protections increases the vulnerability of these families and their risk of debt.

A second problem is that policies set in place from 2010, as described above, have steadily undermined Working for Families for low-income working people. There is no secure legislated basis to protect Working for Families and, despite some one-off increases, the direction signalled

Table 3: Parameters of Working for Families faced by the standard living wage family (two children under the age of 13)

	Actual Values Q1 2017	Fully adjusted for changes in the average wage 2005-07 to Q1 2017
FTC two children, \$per week	\$157.17	\$198
IWTC two children, \$per week	\$72.50	\$83
Total Max WFF	\$229.67	\$281
Annual max entitlements	\$11,943	\$14,611
Threshold, joint income (annual)	\$36,350	\$50,916

for 2018 indicates ever-tighter targeting will continue. These changes affect the ability of the living wage to achieve the required outcome, even for families who are working full time at the LWR.

The interdependence of the living wage rate and Working for Families

As explained above, estimation of the LWR incorporates adjustments for Working for Families. This section asks two hypothetical questions: for the standard family on which the LWR is based, what would the gross rate have to be if there were no Working for Families?; and what would the LWR be if Working for Families had been properly adjusted since its inception?

Setting family tax credits to zero, the corresponding hourly LWR as calculated for 2012 would be \$21.16. Updating this for wage growth using the same method used by King and Waldegrave to update the LWR suggests that the LWR for July 2017 would be approximately \$23.23, or around \$3 an hour more than the current 2017 LWR of \$20.20. Of course, the higher LWR would apply to all workers and be too much for a worker without children, but not enough for families with more than two children or on fewer hours than the standard family.

The second question asks: what would the LWR be if Working for Families had been properly adjusted since its inception? If the Working for Families threshold and the entitlement amounts had been adjusted in accordance with the rise in the average wage rate, the LWR could be correspondingly lower. Again, determining this is a hypothetical exercise, as Working for Families has never been adjusted for average wages. Table 3 that shows the wage-adjusted Working for Families maximum for the standard two-

adult, two-child family is \$14,611. The wage-adjusted abatement threshold is \$50,916. Had this family earned \$53,101 gross, its after-tax income would be \$45,768. Adding the wage-adjusted abated Working for Families of \$14,119 would achieve the 2017 living wage disposable income target of \$59,887. This means the gross LWR for 2017 could be \$17 per hour.

Both of these calculations are illustrative only, but show the importance of these tax credits and how they are indexed in determining the adequacy of the LWR.

Discussion

The living wage is based on a model family profile that is unrepresentative of actual households. The living wage rate of \$20.20 an hour delivers the required standard of living only if the couple actually works 60 hours a week, 52 weeks of the year. For example, if one of the parents (usually the mother, working part time) cannot work due to care-giving responsibilities (for young children, a disabled child, or a sick parent) or events such as an earthquake or recession, the family would lose her gross income but gain an additional Working for Families tax entitlement of \$4,727. While this extra Working for Families entitlement has a vital role in cushioning the loss of the partner's income, it does not allow the family to have a living wage standard of living.

While the living wage movement has done well in getting more employers to sign up to the LWR, as higher wages are desperately needed, the LWR and Working for Families must operate as complementary mechanisms to achieve the shared goal of improving family income adequacy and preventing poverty.

Wages are too low, not because Working for Families subsidises greedy employers, but due to a range of factors,

including loss of union power. Mabbett's comments for the UK are relevant here:

Wages do indeed seem to be in something of a low-level trap, but not because tax credits are keeping them there. Most people in low-paid work do not receive tax credits, because they are too young (under 25) or do not have children. The main reasons why wages have stayed so low lie elsewhere: the erosion of unemployment benefits, the lack of financial support for students, the elastic supply of labour from elsewhere in the EU, the government's own pay policy for public sector workers and, of course, the decline of collective bargaining. (Mabbett, 2015, p.466)

All families, not just those on the LWR at 60 hours a week but the bulk of other families with fewer hours of work or supporting more children, need a robust system of income support. Instead, the Working for Families programme has been dangerously undermined and is in urgent need of restoration and improvement. As the Council of Trade Unions notes:

While Working for Families softens the effects of low wages for those households who qualify, some minimum wage workers do not qualify and its benefits are weakening as a result of thresholds not being adjusted for inflation. The government forecasts it will spend \$2.392 billion on it in the year to June 2016 and \$2.352 billion in the year to June 2017 compared to \$2.796 billion in the year to June 2010 – worth \$3.066 billion in June 2016 dollars. There has therefore been a sharp fall in Working for Families support (22 percent between 2010 and 2016) in real terms. (New Zealand Council of Trade Unions, 2016)

While the 2017 Budget signalled an increase in real spending on the family tax credit for 2018, as shown in Figure 1, the price has been a lower abatement threshold of \$35,000 and a higher abatement rate of 25%. This particularly

affects the living wage standard family working 60 hours at the LWR.

The accommodation supplement, for those families who qualify, recognises the impact of higher housing costs and is tailored to different regions and for different family configurations. As noted, this payment has been of minor significance for the standard family at the living wage income level and has been ignored in this article. This issue should be revisited, however, in the promised 2017 review of the living wage calculations in light of the rapid increase in housing costs in some areas, and the increases to the accommodation supplement from 2018 announced in the 2017 Budget.

More importantly, there must be greater awareness of the inverse relationship between the LWR and Working for Families and an active support of the enhancement of Working for Families as an intrinsic part of achieving adequate living standards for all family types.

Perhaps the review might also consider a different starting point. If the LWR is set to ensure that an adult without children working 40 hours has a living wage, it should be clearer how important it is to strengthen and solidify into legislation a reform of Working for Families. All working families of different configura-

tions on the LWR should have a living wage standard of living.

- 1 Other groups have promoted pay equity and equal pay with some success. A recent settlement sees a significant rise in the hourly rate for careers in the long-term care industry (Kirk and Williams, 2017). At the heart of all these campaigns is the belief that the minimum wage is too low.
- 2 This article updates our earlier paper published by the Child Poverty Action Group: *Children and the Living Wage* (St John and So, 2017).
- 3 The accommodation supplement is not applicable at 60 hours at the living wage and is ignored here.
- 4 The families income package (Treasury, 2017) increases the rates of the family tax credit so that there will be two weekly rates from 1 April 2018, \$102 for the first child and \$91 for subsequent children, offset by a reduction of the threshold to \$35,000 and an increase in the rate of abatement to 25%.

Acknowledgment

The authors are grateful to Jonathan Boston for his comments on an earlier version of this article

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