

# POLICY Quarterly

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## SPECIAL ISSUE

# Child Poverty

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## Editorial Note

In March 2012 the New Zealand Children's Commissioner, Dr Russell Wills, established an Expert Advisory Group (EAG) on Solutions to Child Poverty, of which I was the co-chair with Dr Tracey McIntosh. The EAG's creation reflected growing disquiet about significant levels of childhood material deprivation in New Zealand and its many damaging consequences. The EAG undertook extensive consultations, prepared numerous working papers and delivered its final report in December 2012. Much of this issue of *Policy Quarterly* is devoted to the nature, measurement and impacts of child poverty and possible solutions.

In the opening article, I pose the question as to why, despite the large increase in rates of child poverty since the 1980s, there have been only modest governmental measures to address it. I also consider, based on comparative data, the effectiveness of various poverty-reduction strategies and highlight the importance of building multi-party support if measures to reduce child poverty are to be durable.

Next, two leading American researchers, Greg Duncan and Katherine Magnuson, focus is on the impact of poverty early in a child's life. Drawing on a range of international evidence, they argue that the timing of poverty is very important because poverty early in childhood can have dramatic effects on brain development, with lasting impacts on adult wellbeing and outcomes. On this basis, the authors suggest that greater policy attention should be directed towards deep and persistent poverty occurring early in childhood.

Bob Stephens, in his contribution, concentrates on the need for a comprehensive, integrated and authoritative approach to measuring poverty, as recommended by the EAG. Stephens argues that no single poverty measure is sufficient and that fixation on any particular poverty threshold must be avoided. As he puts it, the 'afflictions of poverty are not necessarily overcome by jumping over an arbitrary poverty threshold'.

Following this, Kristie Carter, Fiona Imlach Gunasekara and Tony Blakely, examine the complex relationship between trends in income inequality and poverty, with particular reference to New Zealand. The authors highlight that while inequality and poverty are typically assumed to go hand in hand, this is not always the case. A number of scenarios are presented which consider different combinations of increased, decreased or static income inequality and poverty over time.

Moving to the possible policy responses to child poverty, Mark Henaghan outlines the case for a Child Poverty Act. Drawing on recent British experience, he argues that legislation requiring governments to specify poverty-reduction targets (as recommended by the EAG) would help generate stronger incentives for effective policy measures to address child poverty and enhance political accountability for outcomes.

Next, Philippa Howden-Chapman, Michael Baker and Sarah Bierre discuss the impact of poor housing on child development. Importantly, young children spend much time at home and hence the quality of this environment significantly affects children's health and attendance at school. Currently, many New Zealand homes (and especially private rental units) are damp, poorly heated

and badly insulated. Greater investment in better housing is thus imperative.

Ian McChesney's contribution builds on the previous article and explores the concept of 'fuel poverty', defined as the 'inability of a household to afford a sufficient level of energy services in the home'. Energy deprivation can have adverse impacts on physical and mental health, particularly among children. McChesney discusses the emergence and extent of fuel poverty in New Zealand, its characteristics and links to child poverty. He also critiques the policy responses to date and explores several possible solutions.

In the final article on child poverty issues, Susan St John critiques the EAG's recommendations, focusing especially on the crucial issue of income support for families with children. St John assesses the EAG's recommendations against a range of criteria and argues that some of the main recommendations are deficient. She is particularly critical of the proposal for a universal payment for all young children (i.e. irrespective of parental income). Such a policy would, in her view, fail to relieve the poverty currently afflicting many of the children whose parents are dependent on welfare benefits.

The last three articles in this issue of *Policy Quarterly* address issues of a rather different nature, although in two (Chapple and Dwyer) the challenge of child poverty is highly relevant. Simon Chapple's article explores the current government's 'new investment approach' to welfare dependency. This approach marks a significant departure for the management of New Zealand's welfare system and entails assessing the performance of Work and Income on the basis of its capacity to reduce the forward liability of social assistance programmes. Chapple argues that for various reasons, 'forward liability is neither a relevant nor reliable indicator' of performance and that the new regime is unlikely to be effective. Instead, he suggests a different strategy for performance management which, in his view, is more likely to deliver better social outcomes.

Márie Dwyer's article discusses how to improve the quality and coverage of social protection in two small island developing states, namely the Solomon Islands and Vanuatu. Social protection is understood as one of the key pillars of national development strategies aimed at increasing welfare, economic productivity and social cohesion. Dwyer examines the existing social protection programmes, particularly in the areas of income support, education, health and employment. She then discusses how to increase the quality and reach of these services in the face of rapid urbanisation, continuing population growth, sluggish economic growth and limited resources.

In the final article, Janine Hayward considers the possible use of citizens' assemblies in the policy-making process in New Zealand. In light of the recent referendum on the future of proportional representation, she explores the merits and limitations of alternative approaches to constitutional reform. She argues that citizens' assemblies have been useful elsewhere and, given New Zealand's small population and vigorous 'community politics', they could also be effective here for promoting robust and informed debate on constitutional issues.

Jonathan Boston (Co-editor)

Jonathan Boston

# The Challenge of Securing Durable Reductions in Child Poverty in New Zealand

## Introduction

New Zealand has tolerated significant levels of relative child poverty for more than two decades. For a country which once prided itself on being comparatively egalitarian and, more particularly, on being a great place to bring up children, this is surprising. It is also concerning. Child poverty imposes many long-term costs. This is especially the case, according to the available evidence, when poverty occurs during early childhood<sup>1</sup> and when it is severe and/or persistent. These costs afflict not only the children directly exposed to poverty (e.g. in the form of lower educational achievement, reduced lifetime earnings and poorer health outcomes), but also society as a whole. The wider social and economic costs include increased health care costs, lower productivity

growth and higher rates of criminal offending.<sup>2</sup> In short, the empirical evidence suggests that substantial rates of child poverty reduce a nation's prosperity. Hence, on economic grounds alone there is a case for seeking lower child poverty rates. Other considerations, such as the pursuit of fair opportunities for all children, make such a goal even more compelling.

Fortunately, New Zealand's rate of child poverty is by no means the worst within the OECD (see Table 1). Moreover, the situation in 2013 is somewhat less serious than during the 1990s and early 2000s (see Figure 1). Nevertheless, using various approaches to poverty measurement, whether based on relative income thresholds or on rates of material deprivation, child poverty in New Zealand remains a critical social problem. For instance, on one measure of income poverty (i.e. those living in households with equivalised<sup>3</sup> disposable incomes below 60% of the median, after housing costs), the child poverty rate in recent years has been around 25%; this is almost twice the rate experienced during the 1980s, which averaged about 13%. Using a more demanding poverty measure (based on 50% of the median household disposable income, after housing costs), whereas the average child poverty rate during the 1980s was about 8%, in

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Table 1: Child poverty rates at different relative poverty lines (before housing costs)

Country	Poverty line at 50%	Poverty line at 40%	Poverty line at 60%
Iceland	4.7	1.9	10.1
Finland	5.3	1.5	11.9
Cyprus	6.1	1.8	12.1
Netherlands	6.1	2.9	15.4
Norway	6.1	3.1	11.3
Slovenia	6.3	2.9	11.1
Denmark	6.5	3.6	11.4
Sweden	7.3	3.7	12.7
Austria	7.3	3.2	13.6
Czech Republic	7.4	3.8	13.0
Switzerland	8.1	3.2	17.9
Ireland	8.4	3.5	18.9
Germany	8.5	4.6	14.9
France	8.8	3.7	16.8
Malta	8.9	2.9	20.3
Belgium	10.2	4.1	16.6
Hungary	10.3	3.0	20.6
Australia	10.9	4.3	17.6
Slovakia	11.2	6.6	17.0
New Zealand	11.7		19.4
Estonia	11.9	6.1	20.6
United Kingdom	12.1	5.6	20.8
Luxembourg	12.3	4.2	22.4
Canada	13.3	7.3	21.9
Poland	14.5	7.5	22.9
Portugal	14.7	9.6	22.7
Japan	14.9	9.6	20.5
Lithuania	15.4	8.8	24.3
Italy	15.9	9.7	24.2
Greece	16.0	8.1	23.5
Spain	17.1	11.5	23.6
Bulgaria	17.8	12.2	24.4
Latvia	18.8	12.8	25.0
USA	23.1	16.6	31.1
Romania	25.5	17.8	32.3

Source: Innocenti Research Centre (2012, p.12)

Note: The rates cited in this table are generally for 2009, but the New Zealand rates are for 2011.

recent years it has been close to 16%. As highlighted in Table 1, New Zealand's rates of child poverty are somewhat lower if calculated without taking housing costs into account, but even on this basis they are close to double those of the best-performing OECD countries.

Furthermore, the rate of material deprivation<sup>4</sup> among children, based on the official measure used by the European Union, was around 18% in 2008 (just

prior to the global financial crisis). This was significantly higher than the rate in many western European countries and six times the rate of material deprivation among those aged 65 years and older (see Table 2).

International comparisons of this nature, together with the substantial rise in child poverty in New Zealand over the past 25 years, prompt a variety of questions. First, why do rates of child

poverty and material deprivation vary so much across the OECD, and how have some countries managed to achieve relatively low rates for extended periods of time? Second, why did child poverty rates in New Zealand deteriorate so markedly during the late 1980s and early 1990s, and why have such significant rates been tolerated for so long? Third, how might the current rates of child poverty be reduced and, in particular, how might the durability or sustainability of such reductions be enhanced? This article seeks to answer these questions. My reflections draw heavily on the work of the Expert Advisory Group on Solutions to Child Poverty (EAG), of which I was co-chair.

There are, of course, many other issues deserving of attention. Many of these are covered in other contributions to this special issue of *Policy Quarterly*.

#### Child poverty rates – explaining the differences between developed countries

The data presented in Table 1 highlight the large differences in rates of child poverty, based on relative poverty thresholds, across the OECD. Using the 60% poverty line, some countries (like Romania and the US) have rates up to three times those of the best-performing countries; using the 50% poverty line the differences are even more marked. Material deprivation rates among children also vary greatly across the OECD, as indicated in Table 2.

If child poverty rates were broadly similar across developed countries, it might suggest that policy settings make little difference. Decision-makers would then be faced with the stark and discouraging possibility that child poverty is an intractable problem and that the rate of child poverty is largely beyond their capacity to influence. Fortunately, the fact that rates differ so markedly suggests that policies do matter and that child poverty can be reduced. The question then becomes how? More specifically, which policies are the most effective and what conditions are necessary for their implementation? Also, what other factors shape poverty outcomes?

#### Differences in material deprivation rates

Unlike poverty rates based on relative income thresholds, material deprivation

**Table 2: Deprivation rates\* in 13 countries comparing children with older people and the total population in 2007 (Europe) and 2008 (New Zealand)**

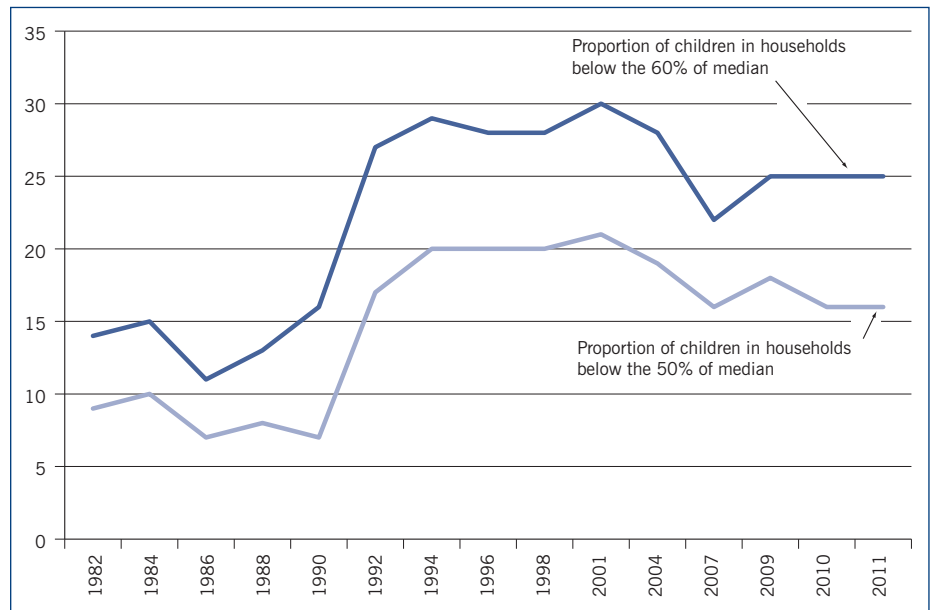
Country	Children 0-17	Aged 65+	Total population
Netherlands	6	3	6
Norway	6	1	5
Sweden	7	3	6
Spain	9	11	11
Germany	13	7	13
Slovenia	13	18	14
Ireland	14	4	11
United Kingdom	15	5	10
New Zealand	18	3	13
Italy	18	14	14
Czech Republic	20	17	20
Hungary	42	35	38
Poland	39	41	44

\* The deprivation rates in this table are based on the proportion of households who lack at least three items from a list of nine because they cannot afford them. All nine items are regarded as essential by the majority of the population.

Source: Perry, 2009, pp30-33

(or hardship) rates reflect actual day-to-day living conditions or standards. Accordingly, one would expect, other things being equal, that rates of childhood deprivation would be higher in countries with lower living standards than in those which are relatively wealthy. Thus, it is no surprise that deprivation rates (across all age groups) are much higher in eastern European countries like Hungary and Poland than in the richer countries of western Europe (see Table 2). But it is also clear that real per capita incomes supply only one of the reasons why deprivation rates differ. For instance, some countries with roughly comparable living standards as measured by GDP per capita (e.g. Germany and Sweden) have different childhood deprivation rates, and some countries with significant childhood deprivation rates (e.g. New Zealand and Britain) have very low rates of deprivation among those aged 65 years or more (e.g. 3–5%). Interestingly, although rates of childhood deprivation (and income poverty) across the OECD are typically higher than those for the elderly (and the population as a whole), there are notable exceptions. Such findings suggest that there are a range of factors, not least policy

**Figure 1: Trends in New Zealand child poverty rates from 1982 to 2011 (based on 50% and 60% of median disposable household income, after housing costs)**



Source: Perry, 2012, 124

settings, which affect rates of income poverty and material deprivation.

#### *Differences in income poverty rates*

As noted earlier, income poverty is measured on the basis of whether equivalised disposable household income is below a specified level of the median income (i.e. the mid-point in the income distribution, not the average). The poverty rate is thus a relative measure and will vary depending on the median income, the income threshold adopted, whether or not housing costs are taken into account (and, if so, how), and the nature of the equivalence scale adopted. The precise methodologies employed to calculate poverty rates are discussed by Bob Stephens elsewhere in this issue, but it is worth noting that disposable income refers to market income that is adjusted for direct taxes, income support (benefits) and tax credits.

Plainly, measures of income poverty reflect the shape of the income distribution within a particular society (especially at the bottom end). While the relationship between income inequality (on various measures) and poverty is complex (see Carter et al. in this issue), broadly speaking, countries with high rates of income inequality (e.g. the US) tend to have relatively high rates of poverty, including child poverty. Conversely, countries with below-average

levels of income inequality, like those in Scandinavia, tend to have lower poverty rates.

The distribution of household disposable income is influenced by many factors, most notably:

- the dispersion of wages and other earnings from employment;
- the dispersion of investment income (e.g. rents, dividends and interest) and private transfers;
- household structure (e.g. the balance of two-parent and sole-parent households, and the extent to which there is 'assortative mating'<sup>5</sup>);
- the degree of polarisation between 'job rich' and 'job poor' households;
- the limited employment opportunities for many unskilled and semi-skilled people; and
- the structure of direct taxes and the level of public cash transfers (e.g. pensions, benefit payments and tax credits).

In brief, the significant variability in income poverty rates (including child poverty rates) across the OECD reflects differences in one or more of these factors, especially the dispersion of wages (and other earnings) and the structure and generosity of tax-welfare systems. Note, too, that poverty rates can be sensitive to relatively small movements (up or down) in levels of social assistance, as such changes can shift large numbers of

households above or below particular poverty thresholds. Specific policy settings, therefore, can have a significant impact on rates of income poverty.

As a general rule, the countries with low rates of relative child poverty (such as Denmark, Finland, Iceland, Norway and Sweden) have rates of market-income inequality below the OECD average, and/or tax-welfare systems that are relatively effective at redistributing income to those in low-income households (Cass and Whiteford, 2009; Whiteford and Adema, 2006). For instance, child poverty rates in the US are high because market-income

inequality is affected by many different variables and few of these are amenable to the direct control of policy makers. Such variables include: the overall structure of the economy and patterns of employment in different sectors; labour market mobility and participation rates; the structure of employment, including working-time arrangements; the nature of labour market institutions, including union density and bargaining coverage; the framework of labour market regulation, including the minimum wage; benefit replacement rates; unemployment rates; and cultural values. Over recent

picture is complicated by the fact that the employment rates (and earnings) of sole parents vary significantly across the OECD and some countries provide relatively generous assistance to sole-parent families. Hence, for instance, although the rate of sole parenthood in Scandinavia is close to or above the OECD average, child poverty rates are nonetheless low. This is because the Nordic countries provide strong incentives for sole parents to find paid employment and supply considerable financial support to enable participation in the labour market (e.g. via heavily subsidised child care and early childhood education). Achieving high parental employment levels is thus a critical mechanism for minimising child poverty. This applies even in a context where the wage dispersion is considerable.

The second broad option for reducing child poverty is to enhance the redistributive effectiveness of the tax-welfare system, particularly in relation to low-income families. Many factors affect the redistributive effectiveness of government policies, including:

- the structure, comprehensiveness and progressivity of the tax system;
- the overall level of taxes;
- the comprehensiveness and generosity of the welfare/social security system, including the design of family assistance programmes and the level of benefit payments/tax credits;
- the eligibility criteria for benefit receipt;
- the balance and structure of in-work and out-of-work benefits; and
- the nature and generosity of social assistance which is tied to the provision of specific goods and services (e.g. cash subsidies for housing and child care).

On the whole, the OECD countries that are most effective in redistributing income combine relatively progressive tax regimes with comprehensive and generous social security/social assistance regimes. With respect to reducing child poverty, key ingredients typically include strong parental employment incentives and related supports, significant family assistance programmes (in the form

## ... countries with comparatively high rates of sole parenthood have greater child poverty than those with low rates of sole parenthood.

disparities are substantial and the tax-welfare system is not very effective in redistributing income between households. By contrast, Canada has a broadly similar level of market-income inequality (i.e. before taxes and transfers) to that of the US, but the tax-welfare system is much more effective in redistributing income to poorer households (OECD, 2011a, p.36). Hence, whereas child poverty rates (using a threshold of 50% of median household disposable incomes before housing costs) in Canada and the US are roughly the same before taxes and transfers are taken into account, after they are factored into the equation, Canada's child poverty rate falls to almost half that of the US (see Table 1).

### *Options for reducing child poverty*

Such an analysis suggests that there are two broad strategies available for reducing the proportion of households with disposable incomes below key poverty thresholds and thereby alleviate child poverty: the first is to focus on reducing market-income inequality, especially on a household basis; the second is to enhance the redistributive effectiveness of the tax-welfare system.

The first option is the more complex and difficult of the two. Market-income

decades there has been a general tendency across the OECD for market-income inequality to increase, but the reasons for this, as well as possible solutions, remain contested (see OECD, 2011a; Stiglitz, 2012). Similarly, there is continuing debate about why the rise in inequality has been so uneven between countries.

Aside from this, social factors that are not necessarily related to the structure of the economy or the labour market also shape the dispersion of household incomes. One of these is the proportion of sole-parent households. On average, sole-parent households have lower disposable incomes than two-parent households. This reflects the fact that: 1) such households have only one working-age adult; 2) both education and employment levels, and thus potential earnings, tend to be lower; and 3) many sole parents are (largely) dependent on cash transfers and other forms of public assistance. Accordingly, child poverty rates among sole-parent households are invariably higher within OECD countries than among two-parent households. Likewise, other things being equal, countries with comparatively high rates of sole parenthood have greater child poverty than those with low rates of sole parenthood. Having said this, the

of tax credits and/or child payments), and benefit systems that are designed to ensure that household disposable incomes are above (or at least not too far below) poverty-related thresholds. Interestingly, the countries with the lowest rates of child poverty generally rely quite heavily on universal (i.e. non-means-tested) forms of social assistance to families.

Additionally, governments across the OECD provide many 'in-kind' services for children (and their families), such as education (at all levels), health care, housing and care services. Although these are not designed primarily as instruments for redistribution, their effect is typically strongly redistributive.<sup>6</sup> Hence, while in-kind services do not directly impact on the inequality of *household disposable incomes* (or income poverty rates), they do affect rates of material deprivation (e.g. the affordability of and access to health care services) and overall levels of societal inequality. The nature, comprehensiveness and generosity of in-kind services must therefore be taken into account in designing strategies to alleviate child poverty and material deprivation.

#### *Achieving low rates of child poverty – political economy considerations*

It is one thing to identify possible strategies, and related policy frameworks, for minimising child poverty; it is quite another to implement them and sustain the required political support over long periods of time. After all, reducing child poverty entails policy interventions that redistribute income in various ways, and redistributive initiatives are inherently controversial. Not only are they subject to (potentially ongoing) ideological opposition and taxpayer resistance, but there is also the perennial challenge of conflicting policy priorities and fiscal constraints. Hence, if effective strategies to alleviate child poverty are to be implemented successfully, and if they are also to endure, the relevant policies require ongoing multi-party endorsement at the parliamentary level and adequate, stable levels of public support. This implies the need for a broad societal commitment to particular values (e.g. a strong emphasis on social justice

and social solidarity, a preference for low levels of poverty, support for childbearing and gender equity, a recognition that the state has a legitimate role in encouraging family well-being and protecting the best interests of children, and so forth). Supportive institutional arrangements are also likely to assist (e.g. an interest group structure that reinforces the predominant societal values and preferences). Achieving the necessary consensus appears to be easier in societies which are relatively homogeneous (especially on the crucial dimensions of ethnicity and religion) and have comparatively high rates of

Thus far, only Scandinavia and a limited number of continental European countries (e.g. Austria and the Netherlands) have been successful in achieving and maintaining low child poverty rates. At the same time, over recent decades various other OECD countries have made concerted efforts for extended periods to reduce child poverty (e.g. Australia, Ireland, Italy and the UK). These anti-poverty strategies have generally been initiated by centre-left governments but have often received a solid level of support from parties across the political spectrum. In policy terms, such strategies have

**...only Scandinavia and a limited number of continental European countries (e.g. Austria and the Netherlands) have been successful in achieving and maintaining low child poverty rates.**

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social mobility. By contrast, societies characterised by deep and entrenched social divisions (such as the US) are less likely to secure or sustain any agreement on anti-poverty strategies.

Adept policy design is also crucial if low child poverty rates are to be achieved and maintained. For instance, the main anti-poverty policies need to be constructed so that they are not undermined by inflation, the inevitable ups and downs of the business cycle or negative external shocks. Maintaining relatively low unemployment levels, as well as high labour force participation rates by those with children, is equally crucial; ultimately this depends on successful macroeconomic management. Additionally, it is helpful, in terms of maintaining cross-party support for low rates of child poverty, to incorporate measures which: a) are politically difficult to change because of the likely electoral costs; and b) ensure support across the ideological spectrum. In this respect, embracing policies with at least some universal coverage appears to be important as this tends to enhance middle-class support for the overall strategy.

usually incorporated a mix of elements, including:

- explicit and generally ambitious medium-to-long-term poverty-reduction targets or high-level political pledges;
- additional cash transfers to families (both working and non-working), typically involving a mix of universal and targeted elements;
- various measures to enhance the employment of sole parents and improve the flexibility of working hours; and
- additional investments in children (e.g. via extra subsidies for child care and early childhood education, longer paid maternity leave, more funding for schools in poorer areas, and improved social support for young mothers) (Cass and Whiteford, 2009; Waldfogel, 2010).

In the case of the UK, a particular focus of the former Labour government's anti-poverty strategy was on assisting families with young children (e.g. 0–5 years) so that the youngest children receive benefits at least equal in value (or higher) than older children. This approach is consistent with

international evidence which highlights the importance of avoiding persistent and/or severe poverty during early childhood.

#### Explaining the rise and acceptance of child poverty in New Zealand

As noted earlier, New Zealand moved from having relatively low rates of child poverty in the early to mid-1980s to much higher rates during the 1990s and into the 2000s. The dramatic rise during the late 1980s and early 1990s was the product of a convergence of factors. Two were especially important: 1) a substantial increase in those receiving social assistance (due to much higher unemployment and an increase in the number of sole parents and those receiving sickness and invalids benefits);

- a reduction in the progressivity of the tax system;
- an increase in relative housing costs (partly due to policy changes); and
- a reduction in the real value of family assistance programmes – partly due to a failure to index fully some forms of assistance (e.g. various tax credit initiatives, primary health care subsidies, etc.).

In response to the dramatic increase in child poverty during the early 1990s, some modest policy changes occurred during the latter part of the National-led government (1990–99), including a small increase in the level of family assistance. No reversal of the 1991 benefits cuts, however, was instituted. Under the

related financial incentives. The IWTC has, however, remained controversial, partly because of certain design features and partly because of the inevitable distinction that is made between families with different levels of engagement with the labour market (see the contribution of St John in this issue of *Policy Quarterly*).

Despite these anti-poverty measures, child poverty rates (on most indicators) have remained significantly above their levels during the 1980s for over two decades. Why have such levels of poverty been tolerated?

Any suggestion that the reason lies in insufficient empirical evidence or inadequate advocacy is difficult to sustain. Although New Zealand does not have official poverty measures, reliable poverty data have been published by the Ministry of Social Development and various academic researchers over many years. Abundant international and local data have also been available on the negative educational, health, social and economic consequences of higher child poverty rates. Thus, policy makers in New Zealand cannot plead ignorance about the nature, extent and likely impacts of child poverty. Likewise, there has been no lack of articulate and well-informed public advocacy. Alleviating child poverty has been vigorously championed for many years by numerous professional bodies (especially in the health care sector), community groups and voluntary organisations (such as the Child Poverty Action Group), as well as several minor parliamentary parties. Of course, this has not prevented much ignorance and denial. Nor has it precluded numerous misunderstandings and myths about child poverty from holding sway (e.g. that there is no ‘real’ hardship in New Zealand; that child poverty is a minor problem and/or does little harm; that there is little that the government can do to improve the situation, etc.). But there has been no shortage of empirical evidence available to counter such myths.

The reasons for New Zealand’s tolerance of significant child poverty for an extended period must therefore lie elsewhere. Three separate but interrelated explanations can be identified: the dominance of market-liberal ideas; the

## Although New Zealand does not have official poverty measures, reliable poverty data have been published by the Ministry of Social Development and various academic researchers over many years.

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and 2) a substantial reduction in the real value of welfare benefits. For instance, between 1987 and 1992 the number of beneficiaries almost doubled while many benefits were cut by 10–30% in real terms. The combined impact of these changes was to reduce the disposable incomes of many families below one or other of the various poverty thresholds.

The increase in child poverty between the mid-1980s and the early 2000s was also exacerbated by other policy changes and wider economic and social trends. These included:

- an increase in the dispersion of wages and other earnings from employment;
- an increase in the dispersion of investment income (e.g. rents, dividends and interest) and private transfers (see OECD, 2011a, overview, p.35);
- changes in household structure, and, in particular, an increase in the proportion of sole-parent households;

subsequent Labour-led government (1999–2008) more significant redistributive policy initiatives were introduced, most notably in the form of extra housing assistance (including income-related rents for state house tenants and changes to the accommodation supplement) and the implementation of Working for Families during 2005–07. The latter involved a revised and expanded package of tax credits for low- to middle-income families. These measures, together with a substantial fall in the level of unemployment and a more modest reduction in those receiving the domestic purposes benefit, brought a significant reduction in child poverty rates between 2004 and 2008 (see Figure 1). Much of this reduction, however, was concentrated in ‘job rich’ households. This is because most job poor households were not eligible for the new in-work tax credit (IWTC), which replaced the former child tax credit in April 2006. The IWTC was designed to enhance labour force participation rates, especially among sole parents, by providing additional work-



related weakening of egalitarian values; and the tendency for the problem of child poverty to be 'framed' in public discourse as a minority ethnic group issue.

Ideologically, a strong market-liberal ethos prevailed within the country's policy community, and especially its most influential policy-making institutions, during the 1980s and 1990s. While this ethos has weakened more recently, the dominant policy concern has remained focused on enhancing economic growth and lifting labour productivity rather than achieving greater equity or reducing poverty. Further, the prevailing orthodoxy has continued to embrace the following assumptions: that boosting economic growth requires a smaller, less active state; that for a small, open economy in the context of economic globalisation and liberalisation, greater income inequality is inevitable (if not desirable); and that benefit rates need to be kept low to maintain adequate work incentives and reduce dependence on the state. From this perspective, higher rates of poverty, including child poverty, are viewed as a largely unavoidable (short-term) by-product of the focus on growth. It is assumed that eventually, however, faster growth will expand employment opportunities and reduce poverty rates, certainly among families with paid employment. Such assumptions and perspectives have been reinforced by a mix of paternalistic attitudes and anti-statist sentiments. Examples include the views that childrearing is solely a parental responsibility, that the state should not interfere in family matters, that child poverty is the result of deficient parenting, that the best solution is for poor people not to have children, and that 'throwing more money at the problem' doesn't work.

Related to this, opinion poll data indicate that there has been a steady decline in support for egalitarian values in New Zealand over the past three decades. As a result, there is now a greater acceptance of income inequality and relative poverty and less support for income redistribution. For instance, whereas in 1992 around 70% of those surveyed endorsed a progressive tax system (with those on high incomes paying a

greater proportion of their income in taxes than low-income earners), by 1999 support had fallen to 60%, and by 2009 to just over 50% (International Social Survey Programme, 2010). Likewise, the proportion of New Zealanders who support government measures to reduce income differences between the rich and poor fell from 50% in 1992 to 40% in 2009, and there was a similar reduction in the proportion of people who thought income disparities were too large. Related to this, less than half the population (43%) agreed in 2009 that the government should provide a decent standard of living for those who are unemployed. In short, increased inequality in New Zealand has gone hand in hand with a shift in values;

and child poverty rates among such groups are at least twice those of the European population on most measures (Perry, 2012). Not surprisingly, therefore, child poverty tends to be associated in the public mind with minority groups, and thus identified as a minority ethnic problem rather than a broader societal issue. Such perceptions, coupled no doubt with elements of racism and negative attitudes to sole parents, may have contributed to an 'us' and 'them' attitude among some European voters and decision-makers. From this perspective, child poverty is viewed as 'their' problem, not 'our' problem; poor children are seen as 'their' children, not 'ours'. Consistent with this, a notable refrain from certain

## **Around 50% of poor children in New Zealand are wholly or partly of Māori or Pasifika ethnicities, and child poverty rates among such groups are at least twice those of the European population ...**

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the once broad and vigorous support for egalitarianism has been significantly eroded. Similarly, increased inequality, coupled with greater socio-economic residential segregation, has no doubt reduced the extent to which wealthy citizens experience and understand the problems which afflict the poor. For instance, children brought up in well-off households in affluent suburbs have virtually no direct experience of material deprivation or hardship. Their living circumstances are far removed from the substantial deprivation experienced by children brought up in households with the lowest 10–20% of living standards (Perry, 2011, p.14).

Finally, there is the issue of policy 'framing'. I am speculating here, but I suspect that ethnic considerations, and related demographic trends, have contributed to the failure of policy makers to take more decisive action to reduce child poverty. Around 50% of poor children in New Zealand are wholly or partly of Māori or Pasifika ethnicities,

members of the public during the consultations undertaken by the Expert Advisory Group on Solutions to Child Poverty in 2012 was the need to 'stop them breeding'.

If the policy problem is framed in such ways, many people might well conclude that child poverty is an issue for the Māori or Pasifika communities to address, not one for society as a whole. Likewise, if child poverty is seen as solely the result of bad choices by certain individuals (e.g. poor parents are having too many children), then the case for action by the state to alleviate the problem may appear less strong.

Parallels can readily be drawn with other countries which have deprived ethnic minorities, like the US (where child poverty is concentrated especially in the black and Latino communities). It is perhaps no accident, therefore, that as demographic changes have altered the ethnic composition of the population and as poverty has become more entrenched within certain ethnic minorities, there

has been a corresponding reduction in public support for policy measures to address child poverty.

#### A way forward: reducing child poverty in New Zealand

To the extent that such an analysis has merit, how might progress be made towards alleviating child poverty in New Zealand, not just temporarily but on a long-term basis? Let me offer several suggestions.

Building robust, durable, public and parliamentary support for the implementation of effective anti-poverty measures will be critical. This is currently lacking. Generating the necessary support will require both

being of all children, regardless of their ethnic background.

More generally, greater public support is needed for effective redistributive policy initiatives and the values which underpin such approaches. In this regard, a focus on *child* poverty, rather than *family* poverty, is likely to be more conducive to capturing the public imagination. Emphasising the expected long-term national *economic* benefits of lower rates of child poverty might also help. After all, reduced poverty is not merely about less hardship and expanded opportunities for deprived children (however critical this might be); it is also about enhancing the nation's prosperity. The message needs to be clear: child poverty benefits no one;

### ... the most controversial of the EAG's recommendations were those proposing a greater reliance on universal forms of social assistance, especially during the early years of a child's life.

astute political leadership and stronger electoral incentives for policy action. The latter, in turn, will require a shift in public attitudes, particularly among better-off New Zealanders. To achieve this, prudent use of all three Aristotelian forms of persuasion might help: *logos* (the use of logic), *ethos* (appeals to authority and ethical considerations) and *pathos* (appeals to the emotions). In practical terms, effective persuasion will entail continuing efforts by researchers and community groups to highlight the empirical evidence regarding the long-term economic and social costs of child poverty; to underscore the harmful impacts of poverty on individual children; to emphasise the shame of tolerating significant childhood deprivation in the midst of plenty; to counter the manifold myths and misunderstandings noted earlier; and to reframe the policy problem so that child poverty is not perceived solely or primarily as a Māori and/or Pasifika concern, but rather as an issue about the rights, opportunities and well-

less poverty means better outcomes and a more secure future for everyone, not just the poor. Equally, the focus should not be on the costs of poverty relief (although these are undeniable), but on the wisdom of investing in our collective future.

In policy terms, a package of initiatives is needed which has the capacity to attract cross-party support. Moreover, such support needs to be durable over multiple elections. As highlighted by the EAG, New Zealand has much to learn from the experience of other countries that have pursued successful strategies to reduce child poverty (see OECD, 2009, 2011b). Such strategies have typically embraced a balanced combination of measures that appeal to a range of political interests. They have also been designed both to relieve poverty and to mitigate its effects. The strategies include (as noted earlier):

- explicit (and ideally credible and achievable) medium- to longer-term poverty-reduction targets to ensure clarity of purpose and accountability for results;

- the specification of clear objectives for the reduction of various negative social outcomes associated with child poverty;<sup>7</sup>
- prudent fiscal and other macro-economic policies to maximise the chances of high employment levels;
- active labour market policies to enable and support high participation rates, and in particular to reduce joblessness among families with children, not least sole parents;
- a mix of cash assistance and in-kind policies;
- a mix of universal and targeted assistance for families with children; and
- levels of income support (via cash benefits and tax credits) that are sufficient to ensure that most low-income families receive disposable incomes above relevant poverty thresholds.

There is, of course, much scope for debate about the precise design of such policy instruments, as well as the inevitably problematic issues of prioritisation, sequencing and affordability. The EAG in its final report made no fewer than 78 specific recommendations. Of these, six were identified as short-term priorities, and a further four as long-term priorities. While some of the priority recommendations have attracted a measure of support from across the political spectrum, others certainly have not. This is hardly surprising, not least because of the substantial fiscal costs of implementing several of the more ambitious longer-term policy measures.

As expected, the most controversial of the EAG's recommendations were those proposing a greater reliance on universal forms of social assistance, especially during the early years of a child's life.<sup>8</sup> This is not the place for a detailed defence of the approach enunciated by the EAG. But various matters deserve stressing. First, the policy debate in New Zealand needs to move beyond a simplistic either/or approach to universality and targeting. The policy terrain is much more complicated than this and many policy options (and sub-options) are available. These include what the 2010 Marmot Review (which focused on how to reduce

health inequalities in England) termed ‘proportionate universalism’ and what Theda Skocpol has referred to a ‘targeting within universalism’ (Mkandawire, 2005, p.17). Second, and related to this, the debate needs to be informed by careful, sober, rigorous analysis and the avoidance of knee-jerk reactions or ideologically-driven rigidity. Third, it is vital to consider the coherence of the overall policy package, not merely the integrity and logic of the individual components. And fourth, while the aggregate fiscal costs of the various options are a critically important consideration, they should not receive absolute or overriding priority. Other criteria also need appropriate weighting, including feasibility, simplicity, compliance costs, political durability, and the effectiveness of the interventions in meeting their multiple objectives.

To sum up, there are compelling ethical, economic and social reasons for reducing child poverty rates in New Zealand. Fortunately, policy makers have the means to do so, at least to some degree. Unfortunately, the political will and incentives appear to be lacking. The challenge, therefore, must be to change the political climate, ideally in a durable manner. This will not be an easy or straightforward task. Nevertheless, for the sake of all those children who deserve a better start in life, it is undoubtedly a task worth pursuing – with intelligence, persuasiveness and vigour.

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- 1 See the contribution by Greg Duncan and Katherine Magnuson in this issue of *Policy Quarterly*.
  - 2 For further details, see the various working papers and reports produced by the Expert Advisory Group on Solutions to Child Poverty: [http://www.occ.org.nz/publications/child\\_poverty](http://www.occ.org.nz/publications/child_poverty).
  - 3 This means that adjustments are made for the size and composition of the households.

- 4 Deprivation rates provide more direct indications of hardship than income-based measures of poverty, and are typically based on the proportion of households which lack a certain number of items (that are deemed by the majority of the population to be essential) because they cannot afford them.
- 5 Assortative mating is a non-random partnering pattern in which individuals with similar backgrounds (including education, socio-economic status and beliefs) mate with one another more frequently than what would be expected under a random mating pattern.
- 6 There are a few exceptions to this generalisation, the most obvious being large universal subsidies for post-compulsory education (which are regressive).
- 7 The EAG recommended that the government develop a comprehensive set of child poverty-related indicators (CPRIs), with explicit targets for at least some of these CPRIs.
- 8 For a critique, see the contribution of Susan St John in this issue of *Policy Quarterly*.

### Acknowledgements

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#### Corrections to note:

Two errors occurred in the article by Geoff Bertram and David Tripe in the November 2012 issue of *Policy Quarterly*. First, the reference to ‘Hosking and Woolford 2011’ ought to have been ‘Hoskin and Woolford 2011’. Second, the attribution of the 2012 Regulatory Impact Statement (RIS) to the Treasury was wrong; in fact the RIS was prepared by the Reserve Bank of New Zealand, although it appeared on the Treasury website. The ‘Reserve Bank of New Zealand’ should therefore have appeared as the author of the ‘Regulatory Impact Statement: covered bonds registration requirements and insolvency protections’.

Greg J. Duncan and Katherine Magnuson

# THE IMPORTANCE OF POVERTY Early in Childhood

## Introduction

Using a poverty line set at 60% of New Zealand's median national income, nearly one in five New Zealand children (19%) was poor in 2011 (Figure 1, based on Perry, 2012). This poverty rate is considerably less than that of the United States and Canada, similar to that of Australia, the United Kingdom, Germany and France, and much greater than in Scandinavian countries. These rates are far from immutable; New Zealand's child poverty rate was much higher in 2004 before social policies were enacted which focused, in part, on the country's child poverty problem.

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Not all social scientists agree that poverty should be defined solely on the basis of income and family size; some instead argue for the utility of indicators based on material hardship. Townsend described poverty as income insufficient to enable individuals to 'play the roles, participate in the relationships, and follow the customary behaviour which is expected of them by virtue of their membership of society' (Townsend, 1992, p.10), and directed his research towards determining income levels that correspond to low scores on a 'deprivation index'. Using a list of 16 deprivation indicators, roughly one in five New Zealand children are deprived on at least six of the indicators (Figure 2, taken from Perry, 2012). This level of deprivation is a third higher than that for adults aged 25 to 64 and three times higher than that for New Zealand's elderly population (Figure 2).

Poor children begin school well behind their more affluent age mates, and, if anything, lose ground during the school years. On average, poor kindergarten children have lower levels of reading and maths skills and are rated by their teachers as less well behaved than their more affluent peers (Duncan and Magnuson, 2011). Children from poor families also go on to complete less schooling, work less and earn less than others.

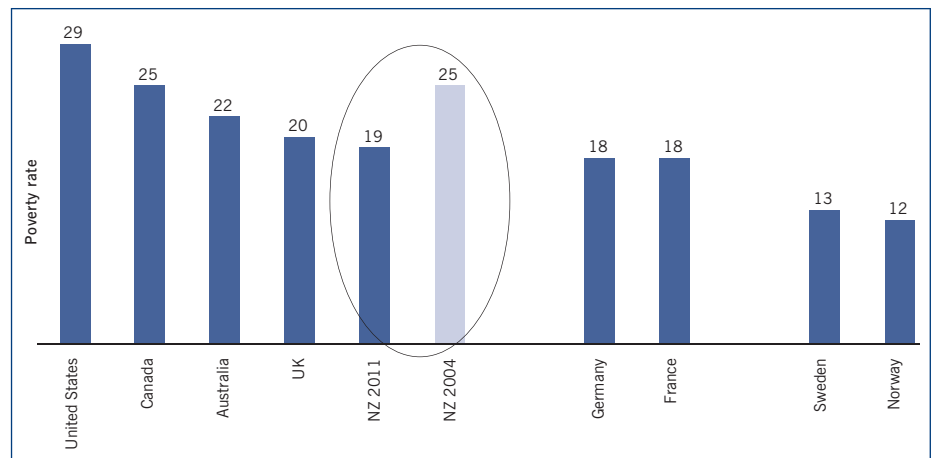
Social scientists have been investigating links between family poverty and subsequent child outcomes for decades. Yet careful thought about the timing of economic hardship across childhood and adolescence is almost universally neglected. Emerging research in neuroscience and developmental psychology suggests that poverty early in a child's life may be particularly harmful because the astonishingly rapid development of young children's brains leaves them sensitive (and vulnerable) to environmental conditions.

After a brief review of possible mechanisms and the highest-quality evidence linking poverty to negative childhood outcomes, we highlight emerging research linking poverty occurring as early as the prenatal year to adult outcomes as far as the fourth decade of life. Based on this evidence, we discuss how policy might better focus on poverty occurring very early in the childhoods of the poor.

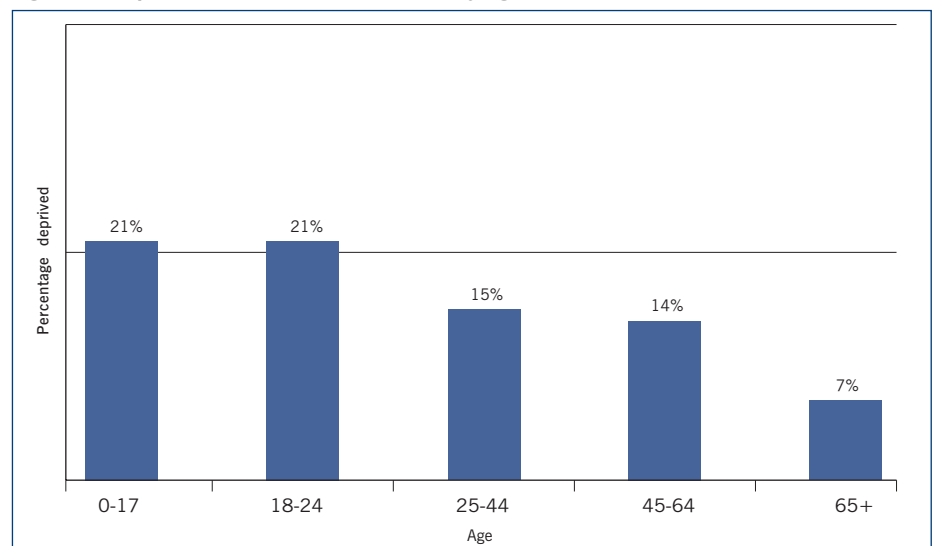
**Poverty and its consequences for children**

What are the consequences of growing up in a poor household? Economists, sociologists, developmental psychologists and neuroscientists emphasise different pathways by which poverty may influence children's development (Figure 3). Economic models of child development focus on what money can buy (Becker, 1981). They view families with greater economic resources as being better able to purchase or produce important 'inputs' into their young children's development (e.g. nutritious meals; enriched home learning environments and childcare settings outside the home; safe and stimulating neighbourhood environments), and higher-quality schools and post-secondary

**Figure 1: Income-based child poverty rates (%), 60% of median, in New Zealand and other countries**

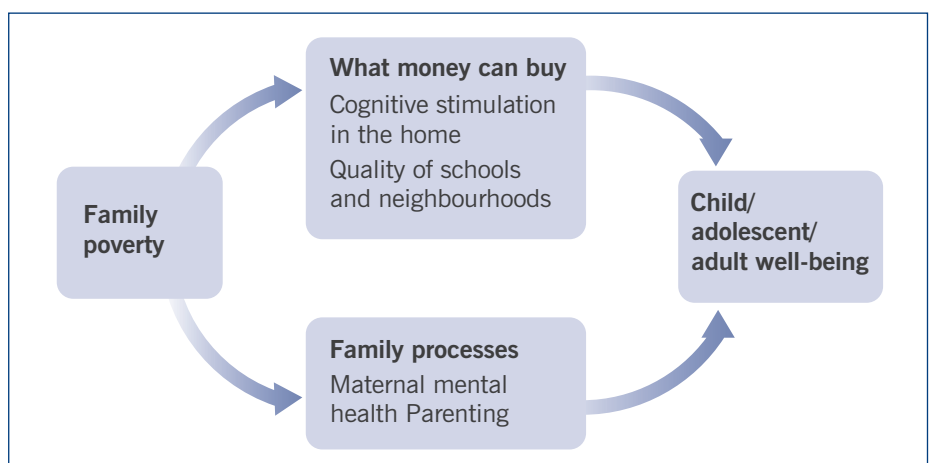


**Figure 2: Deprivation (6+ of 16 indicators) by age in New Zealand**



Source: Perry (2012)

**Figure 3: Why family poverty may hurt children**



education for older children. The cost of the inputs and family income constraints are therefore the key considerations for understanding poverty's effects on children.

Psychologists and sociologists point to the quality of family relationships to explain poverty's detrimental effects on children (Chase-Lansdale and Pittman, 2002). These theoretical models point out that higher incomes may improve

parents' psychological well-being and their ability to engage in positive family processes, in particular high-quality parental interactions with children. A long line of research has found that low-income parents are more likely than others to use an authoritarian and punitive parenting style and less likely to provide their children with stimulating learning experiences in the home. Poverty and economic insecurity take a toll on a parent's mental health, which may be an important cause of low-income parents' non-supportive parenting. Depression and other forms of psychological distress can profoundly affect parents' interactions with their children. But, as we argue below, it is not just the fact that these relationships exist that matters, but when.

### Intensive programmes aimed at providing early care and educational experiences for high-risk infants and toddlers also support the idea that children's early years are a fruitful time for intervention.

#### Why early poverty may matter most

It is not solely poverty that matters for children's outcomes, but also the timing of child poverty. For some outcomes later in life, particularly those related to achievement skills and cognitive development, poverty early in a child's life may be especially harmful. Emerging evidence from human and animal studies highlights the critical importance of early childhood for brain development and for establishing the neural functions and structures that will shape future cognitive, social, emotional and health outcomes (Knudsen et al., 2007; Sapolsky, 2004). Moreover, neuroscience studies show strong correlations between socio-economic status and various aspects of early brain function (e.g. Farah et al., 2006; Kishiyama et al., 2009).

Cunha and Heckman (2007) posit a cumulative model of the production of human capital which allows for the possibility of differing childhood

investment stages as well as roles for the past effects and future development of both cognitive and socio-emotional skills. In this model, children have endowments at birth of cognitive potential and temperament which reflect a combination of genetic and prenatal environmental influences. The Cunha and Heckman model highlights the interactive nature of skill-building and investments from families, preschools and schools, and other agents. It suggests that human capital accumulation results from 'self-productivity' – skills developed in earlier stages bolster the development of skills in later stages – as well as the dynamic complementarity that results when skills acquired prior to a given investment increase the productivity of that investment. These two principles

are combined in the hypothesis that 'skill begets skill'. This model leads to the prediction that economic deprivation in early childhood creates disparities in school readiness and early academic success that widen over the course of childhood.

Intensive programmes aimed at providing early care and educational experiences for high-risk infants and toddlers also support the idea that children's early years are a fruitful time for intervention. The best known of these are the Abecedarian programme, which provided a full-day, centre-based educational programme for children who were at high risk of school failure, starting in early infancy and continuing until school entry (Campbell et al., 2002), and the Perry Preschool programme, which provided one or two years of intensive centre-based education for preschoolers (Heckman et al., 2010). Both of these programmes have been shown to generate

impressive long-term improvements in subsequent education and employment. Perry also produced large reductions in adult crime.

#### A causal story?

Regardless of the timing of low income, isolating its causal impact on children's well-being is difficult. Poverty is associated with other experiences of disadvantage (such as poor schools or being raised by a single parent), making it difficult to know for certain whether it is poverty per se that really matters or other related experiences.

The only large-scale randomised interventions to alter family income directly were the US negative income tax experiments, which were conducted between 1968 and 1982 with the primary goal of identifying the influence of guaranteed income on parents' labour force participation. Maynard and Murnane (1979) found that elementary school children in the Gary, Indiana experimental group (whose families enjoyed a 50% boost in family income from the programme) exhibited higher levels of early academic achievement and school attendance than the control group. No test score differences were found for adolescents, although youth in the experimental group did have higher rates of high school completion and educational attainment. Maynard (1975) analysed data from two rural sites – in North Carolina and Iowa – and found test score gains for second- through eighth-graders in North Carolina but not Iowa.

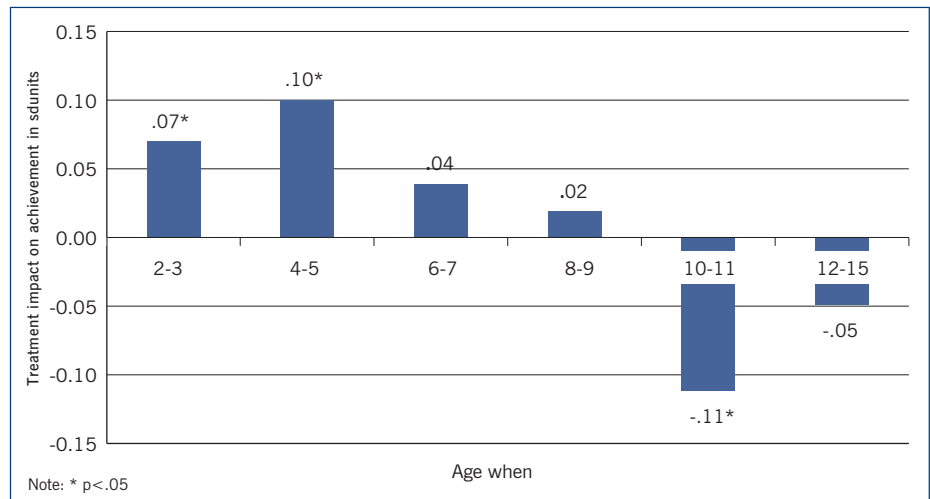
None of the results from the negative income tax experiments bears on the 'early is better' hypothesis, since none tracked the possible achievement impacts on preschool children. Welfare reform programmes undertaken during the 1990s provided income support to some working poor parents through wage supplements, and their experimental evaluations measured the test scores of both school-aged children and children who had not yet entered school when the programmes began (Morris et al., 2005). Data came from seven random-assignment welfare and anti-poverty policies, all of which increased parental

employment, while only some increased family income. All lasted between two and three years. The impacts of these programmes on children's school achievement varied markedly by age (Figure 4). Consistent with the idea that poverty early in childhood may matter the most, treatment-group children between the ages of two and five when the programmes began, most of whom would be making the transition into elementary school during or shortly after the programmes were in operation, scored significantly higher on achievement tests than their control group counterparts. A more sophisticated analysis of the data on younger children suggests that a \$3,000 annual income boost is associated with about one-fifth of a standard deviation gain in achievement test scores (Duncan, Morris and Rodrigues, 2011).

Strong evidence can sometimes be derived from non-experimental studies that take care to ensure they are comparing families who differ in terms of income, but are otherwise similar. Dahl and Lochner (2012) took advantage of the fact that between 1993 and 1997 the maximum US earned income tax credit increased substantially. This enabled the authors to compare the achievement test scores of children before and after the increase in the tax credit. Owing to the nature of their child-based data, the bulk of the children in their analyses were between the ages of 8 and 14 and none was younger than 5. They found improvements in low-income children's achievement in middle childhood that coincided with the policy change.

A second, Canadian-based quasi-experimental study took advantage of variation across Canadian provinces in the generosity of the national child benefit programme to estimate income impacts on child outcomes observed in Canadian achievement data (Milligan and Stabile, 2011). Among children residing in low-income families, policy-induced income increases had a positive and significant association with both maths and vocabulary scores. Both studies estimated similar effect sizes: a \$3,000 increment in annual family income was associated with a one-fifth standard deviation increase in test scores,

**Figure 4: Impacts of earnings supplement programmes on school achievement, by age of child**



Source: Morris et al. (2005)

an amount that was remarkably similar to that estimated in the Duncan, Morris and Rodrigues instrumental variable study. Interestingly, they also found that higher income was associated with a drop in maternal depression, which supports the 'family process' pathway in Figure 3.

**Longer-run consequences?**

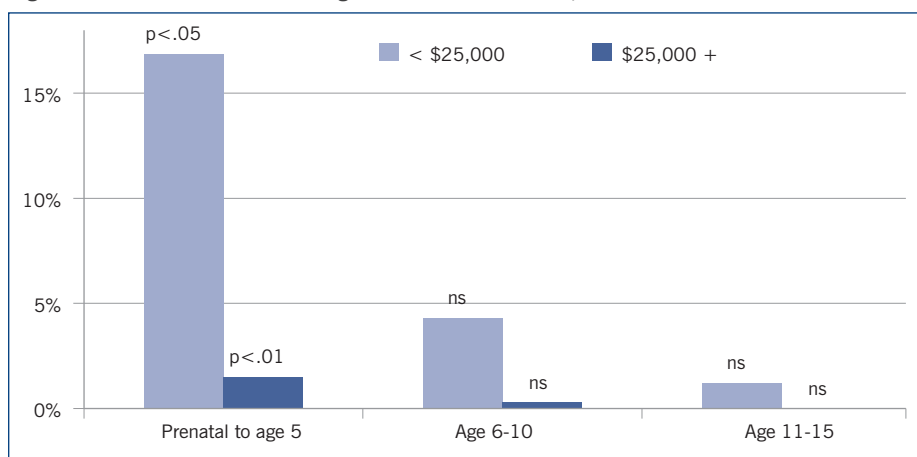
None of this past income literature has been able to examine family income early in a child's life in relation to that child's adult attainments. This limitation comes largely from the lack of data on both early childhood income and later adult outcomes. Only recently has research in both New Zealand and the United States been able to overcome this problem.

Gibb et al. (2012) use data from the Christchurch longitudinal study, which has followed a cohort 1,277 individuals born in Christchurch in 1977. They relate childhood income averaged between ages 1 and 10 to completed schooling and adult income, criminal offending, mental health and teen pregnancy. Low-income children scored worse on all of these measures relative to higher-income children. But when they adjusted for family background factors such as parental education, maternal age, family structure and abusive parenting, as well as childhood IQ and socio-emotional functioning, childhood income had a statistically significant relationship with only two adult outcomes: schooling and labour market success.

Duncan et al. (2010) used recently-released data from the US Panel Study of Income Dynamics, which has followed a nationally representative sample of US families and their children since 1968. The study is based on children born between 1968 and 1975, for whom adult outcomes were collected between the ages of 30 and 37. Measures of income were available in every year of a child's life from the prenatal period through to age 15. This enabled Duncan and his colleagues to measure poverty across several distinct periods of childhood, distinguishing income early in life (prenatal to age five) from income in middle childhood and adolescence. As with Gibb et al. (2012), they found striking simple associations between childhood income (in this case measured early in life) and adult outcomes. Compared with children whose families had incomes of at least twice the poverty-line level during their early childhood, poor children completed two fewer years of schooling, earned less than half as much money, worked 451 fewer hours per year, received \$826 per year more in food stamps, and are nearly three times as likely to report poor overall health. Poor males are more than twice as likely to be arrested. For females, poverty is associated with a more than five-fold increase in the likelihood of bearing a child out of wedlock prior to age 21.

Efforts to adjust for an extensive set of background control variables, all of which

Figure 5: Increase in adult earnings associated with a \$3,000 annual increase in income



Source: Duncan, Ziol-Guest and Kalil, 2010. Shown are estimated associations between adult earnings and \$3,000 increments to income in different childhood stage, with different associations estimated for families with incomes above and below \$25,000. "ns" = not statistically significant.

were measured either before or near the time of birth, showed that childhood income was most powerfully associated with adult earnings and work hours. And attempts to differentiate further by age showed that early childhood income appeared to matter much more than later income. For some measures, such as work hours, there appears even to be a negligible role for income beyond age five. Early income also appears to matter for completed schooling, but in this case adolescent family income seems to matter even more. In contrast, the strong association between overall childhood income and health and non-marital birth seems to be largely attributable to income during adolescence, rather than earlier in childhood.

More detailed analyses show that for families with average early childhood incomes below \$25,000, a \$3,000 annual boost to family income is associated with a 17% increase in adult earnings (Figure 5). Results for work hours are broadly similar to those for earnings. In this case, a \$3,000 annual increase in the prenatal to age-five income of low-income families is associated with 135 additional work hours per year after age 25. In contrast, increments to early-childhood income for higher-income children were not significantly associated with higher adult earnings or work hours. The implication is clear: if we hope that giving parents extra income will bolster their children's chances for success, early childhood is the time to do it.

### Refashioning income supports

Early childhood is a particularly sensitive period in which economic deprivation may compromise children's life achievement and employment opportunities. Research continues to confirm a remarkable sensitivity (and growing number) of developing brain structures and functions that are related to growing up in an impoverished home.

Strong experimental and quasi-experimental evidence links early poverty with child achievement. The effect sizes estimated in these studies are broadly similar. An annual income increase of \$3,000 sustained for several years appears to boost children's achievement by roughly one-fifth of a standard deviation. In the early grades, children's achievement increases by nearly one standard deviation per year, so 20% of a standard deviation amounts to about two months' advantage in school.

Very recent research in both New Zealand and the United States has linked poverty in childhood to adult earnings and work hours. In the case of the US study, which differentiated between income in early and middle childhood, the key finding – that income early in childhood appears to matter much more than income later in childhood for a range of employment outcomes – is quite consistent with the achievement studies.

Taken together, this research suggests that greater policy attention should be given to remediating situations involving deep and persistent poverty occurring early in childhood. In the case of welfare

policies, we should take care to ensure that sanctions and other regulations do not deny benefits to families with very young children. Not only do young children appear to be most vulnerable to the consequences of deep poverty, but mothers with very young children are also least able to support themselves through employment in the labour market.

A more generous, and perhaps smarter, approach would be enacting income transfer policies that provide more income to low-income families with young children. Optimal forms of state intervention will most likely vary between jurisdictions depending on the structure of existing tax, welfare, child support and employment policies, but some basic principles would include the following: in the case of work support programmes, this might mean extending more generous credits to low-income families with young children; in the case of child allowances and child tax credits, this could mean providing larger credits to families with young children.

Interestingly, several European countries gear time-limited benefits to the age of children. In Germany, a modest parental allowance is available to a mother working fewer than 20 hours per week until her child is 18 months old. France guarantees a modest minimum income to most of its citizens, including families with children of all ages. Supplementing this basic support is the Allocation de Parent Isolé (API) programme for single parents with children aged under age three. In effect, the API programme acknowledges a special need for income support during this period, especially if a parent wishes to care for very young children and forgo income from employment. The state-funded childcare system in France that begins at age three alleviates the problems associated with a parent's transition into the labour force.

In emphasising the potential importance of policies to boost income in early childhood, we do not mean to imply that focusing on this area is the only policy path worth pursuing. Obviously, investments later in life, including those that provide direct services to children and families, may also be well-advised. Economic logic requires a comparison



of the costs and benefits of the various programmes that seek to promote the development of disadvantaged children throughout the life course. In this context, expenditures on income-transfer and service-delivery programmes should be placed side by side and judged by

their costs and benefits, and society's willingness to pay for the outcomes they produce.

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Robert Stephens

# DIMENSIONS of Poverty Measurement

## Introduction

In December 2012 the Office of the Children's Commissioner produced a report on *Solutions to Child Poverty in New Zealand: evidence for action* (Expert Advisory Group on Solutions to Child Poverty, 2012a, 2012b). This wide-ranging report provided a detailed analysis of the causes and consequences of child poverty, as well as providing a range of policy solutions to the various dimensions of child poverty. Recommendations were not limited to just increasing the level of disposable income for poor households: the report also made policy recommendations in relation to health care, housing costs and standards, educational attainment,

labour markets and local community support, plus issues of child support, the justice sector and problem debt. All of these recommendations were set in an ethnic context, with specific attention given to the particular issues pertaining to addressing poverty in Māori and Pasifika communities.

The report argued that if solutions to poverty and hardship are to be developed, then it is necessary to know how to define poverty, what are the appropriate ways to measure poverty, which socio-economic groups are more likely to face the risk of being in poverty, and the extent, severity and duration of that poverty.

This article concentrates on the issues involved in measuring poverty. The article recognises that there is no single definition and concept of what constitutes poverty,

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that judgements are required at each stage of the analysis, that the afflictions of poverty are not necessarily overcome by jumping over an arbitrary poverty threshold, and nor will all of those below the specified threshold suffer adverse social outcomes. The article follows the approach taken in the child poverty report, outlining five interrelated ways of measuring poverty, looking at the steps involved in establishing each measure, and providing some New Zealand data on the extent and severity of poverty.

#### The rationale for having a measure of child poverty

The measurement of child poverty is a political exercise, and to be useful for policy purposes requires a social commitment to both mitigating the consequences of child poverty and providing a longer-term solution to address the causes of child poverty. The measurement of poverty enables:

- the determination of which household groupings (number of children in the family, housing tenure, workforce status, ethnicity, tenure status, etc.) are likely to have a greater incidence and severity of poverty, thus permitting better targeting of resources to those in greatest need;
- an analysis of the appropriate mix of cash and in-kind benefits to address the sources of child poverty;
- a tracking of trends and persistence of child poverty through time;
- the monitoring and evaluation of the impact of policy changes on the living standards of the poor;
- the determination of the adequacy of wage rates, basic social security benefit levels and child assistance payments; and
- an assessment approach that enables governments to be held to account for the impacts of their social and economic policies or child poverty.

#### Defining poverty

The child poverty report argued that child poverty should be defined as follows:

Children living in poverty are those who experience deprivation of the material resources and income that

is required for them to develop and thrive, leaving such children unable to enjoy their rights, achieve their full potential and participate as full and equal members of New Zealand society.

The definition indicates that children should be given the opportunity to achieve their full potential, both as children, receiving full educational and

The report also provides data on a before-and-after-housing cost income measure. Housing costs tend to vary independently of income: those with paid-off mortgages tend to have more effective disposable income than those in market rental properties, even if they have the same pre-tax income. However, people can adjust their housing costs by moving to low-cost housing areas, or accepting substandard accommodation.

## The definition [of child poverty] indicates that children should be given the opportunity to achieve their full potential, both as children ... and as adults so that they can achieve their own economic and social well-being.

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social opportunities, and as adults so that they can achieve their own economic and social well-being. The definition also indicates the importance of material and financial resources, and how those resources are distributed between family members. Moreover, the level of financial resources influences child outcomes, and thus the possibility of deprivation in terms of health status, educational attainment and social participation.

#### Measures of child poverty

The child poverty report recommended a suite of child poverty measures, resulting from two frameworks: income and material deprivation.

#### Income

The income measure was divided into two fundamental approaches, one based on maintaining the existing real income level of the poverty line (fixed-line) (Perry, 2012), the other based on maintaining the relative income level of the poor (moving-line). Both approaches set the poverty threshold in relation to the standard of living in New Zealand. Stephens et al. (1995) argued for the moving-line approach, but misleading results occur when average incomes fluctuate.

A large number of issues still have to be resolved:

- 1 What is the poverty threshold? The European Union (EU) used 60% of median household equivalent disposable income, while the OECD uses 50%. Both of these lines are arbitrary. Stephens et al. (1995) provided a rationale for the EU figure, using low-income families to calculate a minimum level of expenditure providing for sufficient food to satisfy nutritional requirements, one heated room, payment for health and dental care, but not having a holiday or meals out. Despite economic and social conditions altering in the intervening 20 years, this 60% estimate is used by the child poverty report.
- 2 What is the measure of income and data source? Income is disposable income, i.e. market income adjusted for the imposition of personal income tax and receipt of social security benefits. The annual Household Economic Survey (HES) is the only data source that adjusts market income for taxes and benefits, using the Treasury TaxWel model which assumes that both taxes and benefits are paid according to the legislation.

The survey has fewer than 3,000 households, giving statistically valid results in total, but it may not for each family composition – single person, couple, sole parent, number of dependent children; by tenure status – owned outright, with mortgage, renting; by ethnicity – European, Māori, Pasifika; by age of head of household, in five-year age groups, including 65+; and by workforce status – one/two earners, benefits plus market income, benefits.

- 3 What adjustments to the poverty threshold should be made to account for differences in family sizes and compositions? Given the same disposable income, a single person has a higher per capita

a 10 percentage point difference from the original poverty line.

#### *Material deprivation*

Material deprivation is an outcome measure, based on the number of consumption items that a family has to go without due to income constraints. Material deprivation looks at the standard of living actually achieved, rather than its potential based on current income. It thus includes the ability to utilise assets (or liabilities), and can include any policy switches, from a tax-mix switch or from cash to in-kind assistance. The measure does not account for misuse of resources, but can account for the need for greater resources to offset costs associated with disability or health care. Again, large

developed, with levels one and two being regarded as having severe or significant hardship.

- 3 What is the data source for the index? A Ministry of Social Development scale, based on survey data, used 40 items, but a restricted set of questions (the Material Well-being Index (MWI)) is now incorporated into the HES data set, allowing income and material deprivation approaches to be combined.
- 4 The MWI needs to be updated on a regular (ten-year) basis to accommodate changing views as to what constitutes a necessity (e.g. home computers are now assumed for school homework).

#### *Severity of poverty*

Those furthest from the poverty threshold are more likely to experience a combination of the various causes of poverty, and thus suffer more severely from the consequences of poverty. The severity of poverty indicates the current level of hardship suffered, as well as the future impact of current poverty on future educational and workforce attainments, health status, and general standards of living throughout the person's lifetime.

The child poverty report suggested that two measures be used: the first based on the poverty gap, or the extent to which those who are poor fall below the moving-line income threshold, and the second based on a combination of those who fall both below the moving-line income threshold and the material deprivation index. Both can be used to show which groups should be targeted if the most severe hardship is to be addressed and how resources can be tailored to address future hardship.

#### *Poverty persistence*

The length of time that one is poor is also related to current and future levels of material deprivation. Those who have been poor for three or four years in a row are more likely to have been unemployed, often a result of low educational attainment, poorer health and substandard housing conditions, all of which tend to reinforce each other. Persistent poverty is also more likely to

## Those furthest from the poverty threshold are more likely to experience a combination of the various causes of poverty, and thus suffer more severely from the consequences of poverty.

income than a couple with three dependent children. Equivalence scales is the technical term used for the means of converting household income to per capita income. There is no correct answer, but all scales recognise that there are economies of scale from living in a family group. The Jensen scales are based on a couple with three dependent children requiring 158% of the income of a couple to achieve the same per person disposable income, and a single person only 65%.

- 4 Should a fixed-line approach ever be adjusted for significant rises in average incomes? In a period of economic growth or significant policy change, the fixed-line approach would mean that the poor would have a continuous fall in their relative standard of living. The child poverty report recognised that, and recommended that the fixed line be adjusted back to the 60% level, either every 10 years or when there is

numbers of judgements have to be made in establishing a material deprivation index.

- 1 What items are to be included in the index? To distinguish the poor from the non-poor, the items have to range from necessities to luxuries. The broad categories cover ownership (phone, computer, insurance); social participation (presents for family, entertainment, holiday); economising (postponed visit to doctor or dentist, buying fewer fruit and vegetables, old clothes); housing problems (dampness, heating); financial problems (not paying bills, unable to borrow); and self-rating (adequacy of income, satisfaction).
- 2 What constitutes poverty or material hardship? The issues here are how to aggregate the enforced lacks into an index, and then what is the proportion of enforced lacks that is required before a family is regarded as being in hardship. Seven categories have been

result in inter-generational hardship.

Measuring persistent poverty requires a longitudinal survey, tracking the same households through time. The measure allows a separation between those who have just one period of poverty (transient), where past asset accumulation permits the household to offset the afflictions of poverty, those moving in and out of poverty, often just moving over the threshold, and those who are chronically poor, being in hardship for many years.

In addition, it is useful to have a measure of the geographical distribution of poverty, showing which areas have a high incidence of unemployment, sole parenting, low household income, etc. Although not all in the area will be poor, the information is useful in determining where to target resources such as additional education and health funding, social service delivery and social housing in order to offset the disadvantages that children growing up in these areas are likely to face.

#### Who are the poor?

Given the large number of dimensions of and ways to measure poverty, it is surprising that there is a high degree of congruence as to which family compositions are likely to be poor. However, at the individual household level the degree of congruence is far lower, with only about half of those who are poor on the income measure also being poor on the material deprivation measure (Perry, 2012). The difference can be explained by the level of asset ownership, the ability to use other resources, and the degree of poverty persistence.

Family groups with a high incidence of poverty tend to be sole parents, those with low or no labour force participation, Māori and Pasifika, families with children, especially larger families, those renting or paying mortgages, and younger households. Many of these groupings are interrelated: for instance, Māori and Pasifika tend to have more children, are on average younger, and have lower employment rates. Those aged 65+ are more likely to own their home outright, whereas younger households are more likely to rent or have large mortgages, giving significant differences in real disposable income after housing costs

**Table 1: Income poverty, 2007**

	Market income incidence %	Disposable income incidence %	Poverty incidence effectiveness %	Structure of poverty %	Poverty gap effectiveness %
All people	23.6	12.4	47.5	100.0	80.5
All children	26.3	16.7	36.5	32.5	72.8
Child, couple	16.8	9.0	46.4	17.4	96.3
Child, sole parent	72.5	56.1	22.6	15.1	53.8
All adults	22.8	11.0	51.7	67.5	84.0
Adults 18–64	15.1	11.2	25.8	58.1	39.5
Adults 65+	65.6	9.9	84.9	9.4	99.0
<b>Workforce</b>					
Benefits	100.0	45.6	54.4	40.8	86.0
Benefits + income	54.3	18.9	65.2	14.3	86.6
1 adult, no benefit	24.2	15.9	34.3	28.4	38.4
2 adults, no benefits	3.7	3.7	–	16.5	16.3

Source: Stephens and Waldegrave (2007)

**Notes:**

- The poverty measure is 60% of median household equivalent disposable income, fixed-line (base 1997) after housing costs.
- The incidence of poverty is measured by the proportion of the total population (or sub-groups) who are below the poverty threshold. Market income covers earnings, dividends, interest, rent, etc. Disposable income is market income adjusted by the payment of personal income tax, and receipt of social security benefits, including child assistance and New Zealand Superannuation.
- Poverty incidence effectiveness is the extent to which direct taxes and benefits reduce the incidence of market income poverty.
- The structure of poverty refers to the percentage of the total poor who fall into each separate household category.
- The poverty gap effectiveness is the extent to which direct taxes and benefits reduce the severity of poverty as measured by the poverty gap.

and thus different levels of material deprivation. Sole parents, especially when their children are young, tend to have lower employment levels. This multi-causality provides policy makers with a range of reinforcing policy instruments. For instance, it may be useful to tailor resources both by ethnicity (Whānau Ora) and by increasing the level of assistance for larger families and providing more assistance for those with younger children.

The way that the results on the incidence and severity of poverty are analysed can also provide further information to policy makers. Using a material deprivation approach may show the extent to which households forgo doctor and dentist visits, or have damp and cold houses, with these constraints indicating that in-kind assistance may be a superior policy option to cash, whereas failure on many dimensions probably indicates a general lack of household income. Equally, just presenting information on the incidence of poverty may provide misleading directions for

policy formulation: Māori and Pasifika may have a far higher incidence of child poverty but, due to their relative small share of the total population, about half of poor children come from a Māori and Pasifika background. Both tailoring resources to Māori and Pasifika and providing universal assistance are required.

Information on the degree to which government policies directly affect the level of poverty is also required. With income poverty, changing income tax rates and benefit levels should influence the incidence and severity of disposable income poverty. Using the material deprivation approach, government policies on home insulation schemes, for example, should reduce the incidence of households suffering from cold or damp houses, with a consequential improvement in the MWI.

#### Income poverty results

The Expert Advisory Group report (2012a) shows poverty incidence rates for 2011, but does not show information

**Table 2: Indicators of material deprivation, by family type (%)**

Economising behaviour	Total	2 parents + children	1 parent + children	65+
Less/cheaper meat	23	28	52	36
Postponed doctor visit	8	9	18	8
Not got prescription	2	3	7	2
Cannot afford glasses	5	6	11	10
<b>Financial problems</b>				
Can't pay utilities	10	12	36	2
Borrowed money	14	13	27	1
<b>Accommodation problems</b>				
Dampness	19	20	19	–
Plumbing	11	11	12	–
Roof needs repair	12	13	9	–

Source: Stephens and Waldegrave (2007)

on the effectiveness of direct government policies. Table 1, based on 2007 data, using a fixed-line, after-housing cost measure, shows that the poverty rate on market income is far higher for sole parents and pensioners, both of whom have relatively low labour force participation. Based on disposable income, over half of sole parents are still poor, whereas New Zealand Superannuation (NZS) has reduced the incidence for those aged 65+ to around 10%: NZS is a very effective poverty reduction policy, especially when the severity of poverty (the poverty gap) is analysed. The low poverty reduction effectiveness for sole parents shows the general inadequacy of the domestic purposes benefit and child assistance. Poverty rates for those in the tax-paying working age group are generally low, as is shown in the bottom part of the table.

#### Material deprivation results

Material deprivation indicates the standards of living actually achieved, rather than what could be achieved from current income: some allowance for the severity and persistence of poverty is covered in material deprivation scores. The results in Table 2 show that on virtually all of the indicators shown, families with dependent children, especially sole parents, have worse outcomes than those of the total population and those aged 65+.

When material deprivation is analysed by family type and income source, those out of the workforce, whether sole- or two-parent families, have the highest degree of material deprivation. Those

family types with market incomes have far higher standards of living, resulting from lower levels of restrictions on the various deprivation indicators due to income constraints. Both Table 1 and the material deprivation data show the importance of market income in reducing poverty, but that market income alone is not always sufficient to alleviate all poverty.

#### Poverty persistence

The level of poverty persistence, or length of time that a family is below the poverty threshold, is partly measured by the degree of income mobility. Imlach Gunasekara and Carter (2012) use the Survey of Family Income and Employment database to show a relatively low degree of income mobility. Over a five-year period, 65% of individuals in the bottom 20% of earners remained in that quintile, and 23% boundary-hopped into the next quintile, while only 5% had moved into the top 40% of the income distribution. At the top end of the income distribution, 71% had stayed in the top 20%, and just 12% had fallen into the bottom three quintiles. The most substantial movements in the income distribution come from people entering work after completing their education and people leaving work following retirement.

As a consequence of the low level of income mobility, there is a significant difference in people's experiences of poverty. Half of the population, and 44% of children, never experienced poverty over a seven-year period, while a further 13% had a one-year transitory experience. However, about 5% of adults and children

were in poverty for the whole seven years, and about the same numbers had four years, five years or six years below the poverty threshold.

#### International comparisons

The child poverty report indicates that the overall degree of material deprivation in New Zealand is higher than in western European countries but lower in than the poorer countries in eastern Europe. However, the incidence of deprivation is unusual, made up of a very high level of deprivation for children and a very low level for adults aged 65+.

In terms of income poverty, using a moving-line 50% median income measure, New Zealand has an above average rate of poverty compared to other OECD countries. The poverty rate for children is much higher than that of northern European countries, well below that of Canada, the United States and Spain, but higher than Ireland and Australia. At the 50% poverty level, the poverty rate for those aged 65+ is very low, but the poverty rate for the whole population is above the OECD average.

#### Conclusions

Poverty can cause serious short- and long-term problems which can range from going hungry, suffering from social stigma, living in substandard housing and being in poor health, to lacking the ability to achieve one's potential. There is a social and economic cost from people living in poverty, and this cost can continue through generations.

If there is a social commitment to addressing the causes and consequences of poverty, then there is a role for government to develop appropriate policy prescriptions. Poverty alleviation also has economic and social benefits, from improvements in productivity to improved education attainments, better health outcomes and social cohesion. The child poverty report put forward a variety of short-and-long-term policies which would go a long way to reducing the causes and offsetting the consequences of childhood poverty. The solutions to poverty should not just come from central government, but require input from local and regional governments, from

community organisations, from family and whānau, and from the individuals themselves.

The provision of appropriate policies requires knowledge of who is poor, and the dimensions of that poverty, including its severity and persistence. Given that there will always be significant financial constraints on policy development, in order to target and tailor policies to the domain of need it is necessary to know which social groupings are more likely to be poor. Measures of poverty thus need to be aligned with causes, consequences and possible policy prescriptions.

The child poverty report recommended a suite of interrelated poverty measures. Several measures are based on disposable income, one on the level of material deprivation occurring within the family, with the others relating to the severity and persistence of that poverty. Using disposable income as the poverty measure tends to focus attention on policy solutions that raise family income, given the existing degree of in-kind benefits, while material deprivation allows policy

makers to tailor in-kind solutions more directly to the source of the deprivation, such as lack of access to health care or to adequate, affordable housing, as well as income. The severity and persistence measures help determine which family types and socio-economic groups should take priority in policy developments.

Measuring poverty is a controversial political activity, and at each stage in the development of a measure judgements have to be made, with the results being both intuitively plausible and politically acceptable. These judgements have to be clearly enunciated and transparent, and informed by evidence and international acceptability. In most cases alternate thresholds should be provided: e.g. 50% and 60% of disposable income; before-and-after housing costs; adjusted by the consumer price index and median earnings; by the types and levels of consumption constraints; and how those items of material deprivation are aggregated into an aggregate order. The alternate thresholds will allow the policy maker the opportunity to enter into a

dialogue about both the measure and the resultant policy prescriptions. Data sources are important, as is the presentation of the results. The results should be presented by a range of household types, ages, number of children, ethnicity, housing tenure, workforce status, and so forth. This will provide a better picture of the causes of poverty: for instance, sole parents have a very high poverty incidence, but the underlying cause may emerge from a consideration of workforce status or number of children.

Without measurement of the incidence, persistence and severity of poverty, policy will be made in a vacuum, and thus may be inefficient or ineffective in targeting and tailoring assistance to those in need. The impact of government policies on poverty rates has to be shown so that the public can give the appropriate brickbats or bouquets to policy initiatives. Thus, as recommended in the child poverty report, the presentation of poverty measurement statistics should be legislated for, allowing regular monitoring and accountability for the results.

## References

- Note: a far more detailed list of references is contained in Expert Advisory Group on Solutions to Child Poverty, 2012a and 2012b.
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# The Relationship Between Trends in Income Inequalities and Poverty in New Zealand

There has been much discussion recently about poverty, particularly child poverty, and the harmful effects of persistent poverty (Perry, 2012; Expert Advisory Group on Solutions to Child Poverty, 2012a, 2012b; Imlach Gunasekara and Carter, 2012). Children who experience many years of poverty are at higher risk of poor child development, worse health outcomes as children and adults, and lower socio-economic status as adults (Duncan, Ziol-Guest and Kalil, 2010; Evans and Kim, 2007; Malat, Hyun and Hamilton, 2005; Najman et al., 2010; Seguin

et al., 2007; Gibb, Fergusson and Horwood 2012; Poulton et al., 2002). This raises special questions around the role of the state in protecting children from harm (and increasing the chances of a healthy and productive future workforce) through child poverty reduction which New Zealand society has not yet resolved. There is also concern about a high level of income inequality (the gap in income between rich and poor) in New Zealand, and reports of executives' high salaries and generous raises frequently trigger debate. Poverty and income inequality are often assumed to go hand in hand, but this is not always the case.

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We aim to investigate the following questions about poverty and income inequality in New Zealand:

- How do trends in child poverty relate to trends in household income inequality?
- Can poverty only be reduced by reducing income inequality (narrowing the spread of income across all individuals)?
- Can income inequality only be reduced by increasing (lower) incomes through redistribution, which makes the rich poorer and the poor richer?

In this article we focus on income poverty, defined as a household income of less than 60% of median household income, where household income is usually after tax and tax credits to reflect the actual disposable income available to households. This is a relative measure of income poverty, a proportion of the population referenced to the current median household income. An alternative measure is to use a median income that is set at one point in time, providing a measure of income poverty that is referenced to a fixed value. Using these definitions, child income poverty in 2011 was around 25% (using the current

median) or 21% (using median fixed at 2007) after housing costs are taken into account, compared to 19% and 15% before housing costs (Perry, 2012). Other ways of estimating poverty include measuring living standards or individual deprivation, which are more direct measures of hardship and consumption and give a picture of the consequences of poverty. However, in this article we focus on income poverty (as a measure of household resources), as it is more commonly collected in household surveys and is widely used in the literature and for international comparisons.

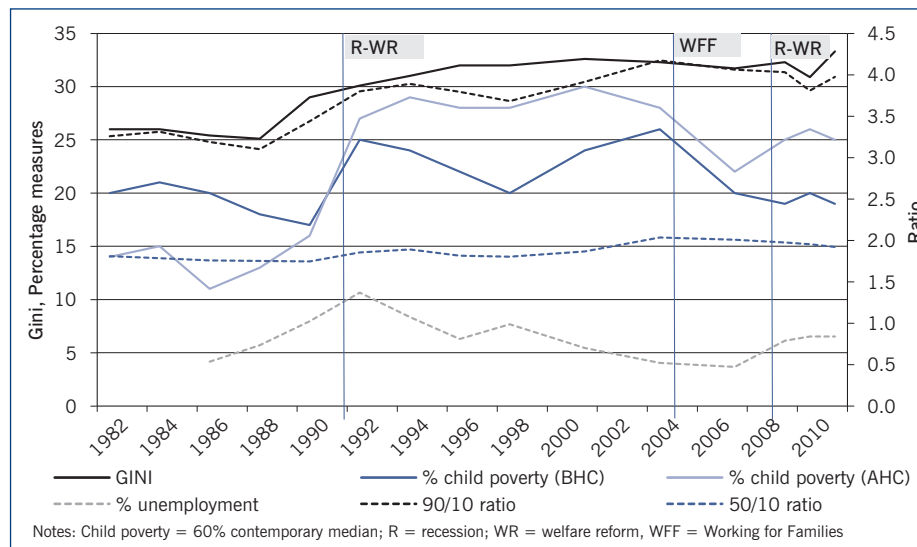
**Table 1: Description of various scenarios of changes in inequalities (using 90:10 and 50:10 ratios) and poverty (less than 60% of median)**

Rank in income distribution	Baseline	Scenario 1	Scenario 2	Scenario 3	Scenario 4
	Baseline	↓inequality** ↓poverty	↓inequality** ↓poverty	<->inequality** ↓poverty	↑inequality** ↓poverty
P90	100,000	105,000	90,000	250,000	500,000
P80	90,000	95,000	80,000	150,000	400,000
P70	80,000	85,000	70,000	100,000	300,000
P60	70,000	75,000	65,000	75,000	200,000
P50 (median)	50,000	50,000	50,000	50,000	50,000
P40	40,000	45,000	45,000	40,000	40,000
P30	30,000*	35,000	35,000	35,000	35,000
P20	20,000*	25,000*	30,000*	30,000*	30,000*
P10	10,000*	15,000*	25,000*	25,000*	25,000*
P90:10	10	7	3.6	10	20
P50:10	5	3.3	2	2	2
	Scenario 5	Scenario 6	Scenario 7	Scenario 8	Scenario 9
	↓inequality** ↑poverty	<->inequality** ↑poverty	↑inequality** ↑poverty	↑inequality** <->poverty	↓inequality** <->poverty
P90	90,000	100,000	500,000	500,000	90,000
P80	80,000	90,000	400,000	400,000	80,000
P70	70,000	80,000	300,000	300,000	70,000
P60	60,000	70,000	200,000	200,000	60,000
P50 (median)	50,000	50,000	50,000	50,000	50,000
P40	30,000*	30,000*	30,000*	40,000	40,000
P30	20,000*	20,000*	20,000*	30,000*	30,000*
P20	15,000*	15,000*	15,000*	20,000*	20,000*
P10	10,000*	10,000*	10,000*	10,000*	10,000*
P90:10	9	10	50	50	9
P50:10	5	5	5	5	5

\* Less than 60% of the median (\$30,000) = in poverty

\*\* Overall inequality (measured by the 90:10 ratio)

Figure 1: Trends in child poverty and income inequalities from 1980 onwards



Source: adapted from Perry (2012), and Ministry of Social Development Household Economic Survey data.  
 Notes: Child poverty = 60% contemporary median; R = recession; WR = welfare reform, WFF = Working for Families

To explore the relationships between income poverty and income inequality, we first present a number of theoretical scenarios which include different combinations of increased, decreased or static income inequality and poverty. We then examine the patterns of income poverty and income inequality (before housing costs) over time, using published data from the cross-sectional Household Economic Survey from 1982 to 2011 (Perry, 2012) and the longitudinal Survey of Family, Income and Employment (SoFIE) from 2002 to 2010 (Imlach Gunasekara and Carter, 2012).

**Theoretical scenarios of changing income inequality and income poverty**

Table 1 describes nine theoretical scenarios where income inequality and poverty change from a baseline state. In this example overall income inequality is the gap between the 90th and 10th percentile income in the sample (the 90:10 ratio). Different measures of inequality (e.g. Gini) can have subtly varying trends given the same income distribution. However, as evident in Figure 1, the 90:10 ratio usually runs in parallel to the Gini (the Gini coefficient is calculated by ranking individual’s incomes from low to high and determining how the share of income is distributed in the population). We also present in Table 1 the level of inequality in the lower half of the income distribution (the 50:10 ratio). In the baseline scenario,

the median or middle value is \$50,000. Anyone with an income of less than 60% of the median (or less than \$30,000 [0.60 x \$50,000]) is classed as being in poverty. The bottom three deciles of households in this baseline sample are classified as being in poverty by this definition (as the 30th percentile income is 60% of the median). Scenarios 1 and 2 give two examples where poverty is reduced by decreasing income inequality through different mechanisms. In scenario 1 all incomes (except the median) increase by \$5,000. This reduces relative inequality (as measured by the 90:10 and 50:10 ratios) and poverty (the proportion of households in income poverty), as a small absolute increase in income has a larger (relative) impact on the income of households at the bottom end of the distribution. Scenario 2 describes a situation where the income of the richer deciles is lowered (e.g. through taxes) and the income of the lower deciles is raised (e.g. through redistributive social policy, such as tax credits), which decreases inequality and poverty. Scenario 3 presents a situation where poverty could be reduced without changing the overall level of relative inequality (90:10 ratio) by raising the level of minimum income as well as some incomes above \$30,000, thus reducing the inequality in the lower half of the income distribution (the 50:10 ratio). This could be achieved (for example) through education and training coupled with improved employment

opportunities, and allowing incomes to increase. In scenario 4 poverty is reduced by raising the incomes in the lower half of the population, but inequalities are increased with much larger increases in income at the higher levels. Scenarios 5 to 9 show different examples of increasing or stable poverty rates, with an increase or decrease in the level of inequality in the population. Mathematical subtleties noted, the key points are that while relative income inequality (e.g. 90:10 ratio) and poverty (e.g. <60% median) usually travel together, they are not completely in step. Manipulations to the shape of the income distribution at ‘sensitive zones’ through levers such as tax can decrease or increase relative poverty without exact mirror changes in relative income inequality across the whole distribution.

**Trends in changing income inequality and income poverty in New Zealand**

*Household Economic Survey (HES)*

Figure 1 tracks the trends in child poverty and measures of income inequality in New Zealand from 1982 to 2011, using data from the annual Ministry of Social Development report examining trends in household income in New Zealand (Perry, 2012). Figure 1 shows that trends in the Gini and 90:10 ratio run in parallel. Through the 1980s into the early 1990s, overall income inequality (as measured by the Gini and 90:10 ratio) and poverty largely moved in tandem, with a decline in both and then an increase. This was primarily due to larger declines in gross household income in the lower compared to upper income groups (Stillman et al., 2012). After the economic recession and welfare reforms in the early 1990s, child poverty declined while income inequality as measured by the Gini continued to increase gradually (although that measured by the 90:10 ratio was essentially stable). Since then, income inequality (by both measures) has remained approximately stable, with a potential increase since 2010 after the global financial crisis and economic recession. It can be seen that child poverty rates have fluctuated more over time, showing the potential impacts of policy and the economic environment on child

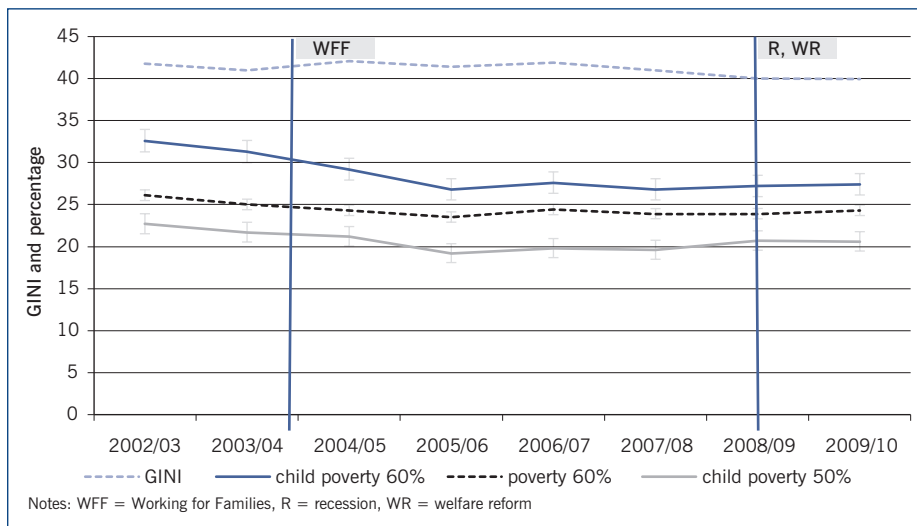
poverty. Figure 1 also suggests that the rise in income inequality (and poverty) in the late 1980s may have been driven by changes in unemployment. However, other major changes occurred within the New Zealand economy and society at the same time, so it is difficult to disentangle these effects.

The period between 1998 and 2004 presents an example of scenario 6 (Table 1), where the rate of poverty is increasing in relation to stable income inequality. The trends after 2004 show a potential effect of the (redistributive) Working for Families package, which included the expansion of family tax credits and the accommodation supplement, and the introduction of the in-work tax credit in 2006. Working for Families was initially targeted at those families on low incomes, and its effect can be seen in the decrease in the 50:10 ratio and the percentage of children in poverty (scenario 3 in Table 1). The trends in the rate of child poverty using the income data after housing costs (AHC) are removed appear to be more sensitive to policy change.

Examining all of this information together, it could be argued that poverty reduction was achieved without narrowing the overall spread of income, because the shifts in income around the poverty line – albeit meaningful and important for families and individuals at this threshold – were not substantial enough to have an impact on the Gini (which measures all points of the income distribution). Similarly, the Working for Families package was more focused on low-income working families, not beneficiary families, meaning that income impacts occurred more above the lowest decile of incomes, resulting in little change in the 90:10 ratio.

As shown in Figure 1, the last decade has been one of significant changes with the potential to affect both income inequality and poverty levels, including the major social policy initiative Working For Families, and the economic downturn, with rising unemployment in the late 2000s. We describe the trends in income inequality and poverty over this time period in more detail, using eight cross-sections of the SoFIE data from 2002 to 2010.

**Figure 2: Trends in poverty, child poverty and income inequalities from 2002 to 2010, using SoFIE data**



**Survey of Family, Income and Employment (SoFIE)**

SoFIE is an eight-year longitudinal household panel survey run by Statistics New Zealand (Carter et al., 2010). Face-to-face interviews were used to collect annual information on income levels, sources and changes (including benefits and family tax credits), as well as employment, education, household and family status, self-rated health and demographic factors. The sample population used for the analyses in this paper was SoFIE participants who were eligible at wave 1 and who responded in all eight waves, giving a sample size of 18,220. The individual was the unit of observation for this analysis, so if there were two or more individuals in a household then their household income was represented two or more times in the analysis population. The sample data were weighted to the longitudinal population in 2002.

Household income was derived by totalling adult annual personal income (before tax) from all sources received within a household for the 12 months prior to the interview date. This was equalised for household economies of scale using the 1988 Revised Jensen Scale (Jensen, 1988). The data presented here is gross household income before tax and housing costs are taken into account, so is likely to overestimate disposable incomes at the lower ends. Note that this is different from the disposable income used in Figure 1 and is likely to show weaker trends over time. The measure

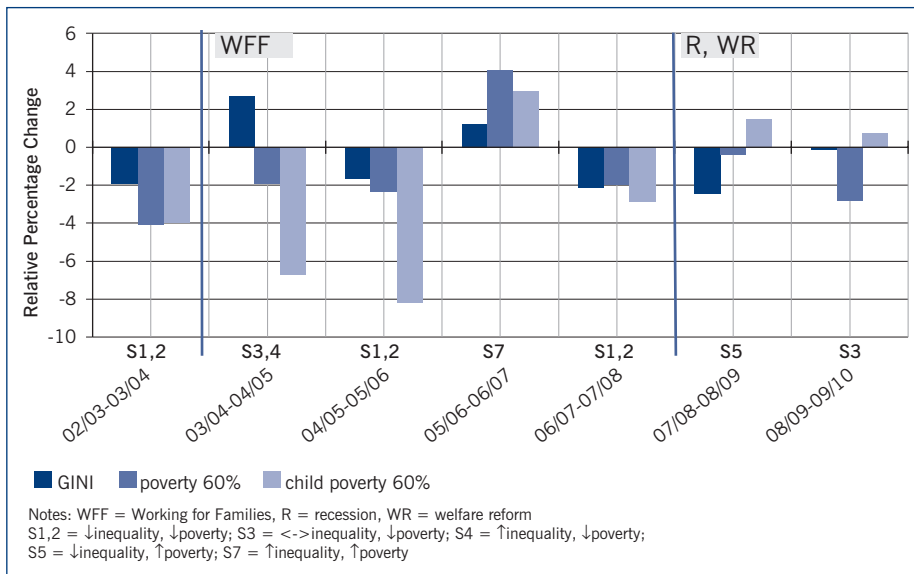
of low income used in this analysis of SoFIE was calculated as less than 60% of the median gross equivalised household income of each wave. Child poverty is the number of children (aged between 0 and 17 in wave 1) living in households below the low-income line in each wave.

Figure 2 presents trends over the eight years of the SoFIE study, and shows that income inequality was relatively stable (as measured by the Gini, using gross household income before housing costs). As shown in Figure 1, the trends in poverty do not exactly mirror the trends in income inequalities over time. Poverty rates declined between 2002 and 2005, then stabilised. The declines in the child poverty rates were steeper than the poverty rate in the overall population, which may be partly explained by the introduction of Working for Families in 2004. Although the rates of inequality and poverty are higher in SoFIE than in the HES data (due to the different income data used), the overall trends are similar over the period from 2002 to 2010. The HES showed a slight increase in Gini from 2010 to 2011.

The overlapping confidence intervals in consecutive years indicate a high degree of internal correlation. However, there are large differences over longer periods of time (with non-overlapping confidence intervals), such as from 2002/03 to 2005/06, for both measures of child poverty (60% and 50% median).

In Figure 3 we present the relative changes between waves of the SoFIE data

Figure 3: Annual changes in percentage in poverty, child poverty and income inequalities from 2002 to 2010, using SoFIE data



in the measures of inequality and poverty and child poverty (calculated by  $[(X_2 - X_1)/X_1] * 100$ ). As indicated in Figure 2, the difference in rates of poverty between consecutive waves is small. However, Figure 3 shows that over the period of eight years different scenarios (from Table 1) of increasing or decreasing inequalities and increasing or decreasing poverty can occur. Although there was a general downward trend in the early 2000s, there was an increase in income inequality, and a substantial decrease in the rates of child poverty can be seen after the introduction of the Working for Families tax credit package in 2004. The changes over time are variable in the late 2000s, particularly after the global financial crisis in 2008–09 when there were decreases in income inequalities and some increases in poverty.

**Discussion**

The relationship between income inequality and poverty is not straightforward. Our data shows that trends in child poverty do not exactly mirror trends in household income inequality. Changes can occur in both inequality and poverty, and vary by what measurement is used.

It can be seen from the data used in Figure 1 (based on the Household Economic Survey) and Figures 2 and 3 (using SoFIE) that the measures of income inequality and poverty are higher in the SoFIE data than those presented using the HES data. The HES data in

the Ministry of Social Development reports uses disposable income (after taxes and tax credits have been taken into account). Therefore, they are more likely to reflect the actual income trends in the population. However, the SoFIE data is useful as it allows us to examine annual changes in inequalities and poverty as they coexist in the data. There were also different survey designs and measurement tools used in the two surveys, which may account for any differences. However, data from both surveys were weighted for the sampling design to represent the New Zealand population at the time of the survey (in the case of SoFIE, the New Zealand population as at October 2002).

It is likely that trends in income inequalities measured using disposable income will correlate with measures of income poverty better than will measures using gross income, as policy changes such as the Working for Families tax credit package aim to increase the income available (disposable) in low- to middle-income households. We compared the trends in the Gini using disposable income with those of gross household income from the HES data (Bryan Perry, personal communication, 17 October 2012) and the overall trends are the same; however, the level of inequality is higher using gross household income (as it doesn't take into account tax credits). It can be seen from Figure 1 that measures of poverty that take into account housing costs are

more sensitive to policy change. Previous New Zealand research has also shown that changes in the rates of poverty and income inequality over time are similar regardless of the method used for calculating poverty or deriving income (equivalisation, gross or disposable) (Stillman et al., 2012).

Some of the misconceptions around the relationship between income poverty and income inequality are simplistic, and do not account for significant influences from both the micro- and macro-economic environment, such as unemployment rates, labour force conditions (such as the minimum wage and temporary/insecure employment levels) and government policy (e.g. benefit to work incentives).

It is important to note that interventions to reduce poverty and to reduce inequality are not synonymous. The recent report released by the Children's Commissioner's Expert Advisory Group on Solutions to Child Poverty recommends that policy attention be focused on poverty rather than income inequality to improve the health (and chances) of New Zealanders as a nation (Expert Advisory Group on Solutions to Child Poverty, 2012a).

**Acknowledgements**

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Statistics New Zealand Security Statement: Access to the data used in this study was provided by Statistics New Zealand in a secure environment designed to give effect to the confidentiality provisions of the Statistics Act 1975. The results in this study and any errors contained therein are those of the authors, not Statistics New Zealand.

# Appendix

## SoFIE information/methods

Household income was derived by totalling adult annual personal income (before tax) from all sources received within a household for the 12 months prior to the interview date, so annual income estimates for wave 1 relate to the 2001–02 financial period (Imlach Gunasekara and Carter, 2012). This was equivalised for household economies of scale using the 1988 Revised Jensen Scale (Jensen, 1988), which is very close to the widely used modified OECD scale. The data presented here is gross household income before tax and housing costs are taken into account, so is likely to overestimate disposable incomes at the lower ends. Disposable (after tax) income was not available from the SoFIE dataset at the time of this analysis.

There are several ways used to summarise the amount of income dispersion or inequality in a single statistic. No one statistic has emerged as the generally accepted way, mainly because each one captures a different aspect of the way the dispersion of incomes changes over time. We use the GINI coefficient as the measure of income inequality. The GINI coefficient is calculated by ranking

individuals' incomes from low to high and determining how the share of income (the proportion of the total sum of incomes from all individuals) is distributed across society, from poor to rich. In a totally equal society, where everyone had the same income, the GINI would equal 0, and in the most unequal society, where one person held all the income, the GINI would equal 1, meaning that a higher GINI indicates a less equal (in terms of income distribution) society.

The measure of low income used in this analysis of SoFIE was calculated as less than 60% of the median gross equivalised household income of each wave. We also investigated a lower cut-off point for low income (<50% median gross equivalised household income), which reduced the magnitude of the proportion of respondents with low income, but is more comparable to rates using disposable income data. Child poverty is the number of children (aged between 0 and 17 in wave 1) living in households below the low-income line in each wave.

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# Why We Need Legislation to Address Child Poverty

Children who live in poverty in New Zealand currently have no legal recognition and no real voice. These children do not choose their circumstances, but are usually born into families experiencing poverty. Children, by their very status as children, have no resources of their own to enable them to improve their own conditions. As a general rule, parents and/or guardians are legally responsible for the emotional and material well-being of the children in their care. But what happens when some parents and/or guardians are unable to provide for the children in their care? Should these children and their families be merely left to their own devices, or should the government as the elected representatives of New Zealand citizens provide assistance? This article considers the growing child poverty problem in New Zealand and the immediate and long-term consequences of poverty, and examines whether legislation addressing child poverty is required.

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### Child poverty in New Zealand: the costs and consequences

Child poverty is notoriously difficult to define. According to the Expert Advisory Group on Solutions to Child Poverty (EAG):

Child poverty involves material deprivation and hardship. It means, for instance, a much higher chance of having insufficient nutritious food, going to school hungry, wearing worn-out shoes or going barefoot, having inadequate clothing, living in a cold, damp house and sleeping in a shared bed. It often means missing out on activities that most New Zealanders take for granted, like playing sport and having a birthday party. It can also mean much narrower horizons – such as rarely travelling far from home ... This is not the kind of country most New Zealanders experience or know much about. But it is the harsh reality for many of our children. (EAG, 2012a, p.1)

New Zealand currently has no definition of child poverty, which makes it difficult for statistics on child poverty to be gathered accurately and consistently across different organisations. The EAG suggests that child poverty 'should be defined in a manner that is consistent with recognised international approaches' (ibid., p.2). The group proposes the following definition:

Children living in poverty are those who experience deprivation of the material resources and income that is required for them to develop and thrive, leaving such children unable to enjoy their rights, achieve their full potential and participate as equal members of New Zealand society. (ibid.)

Regardless of whether the above definition is adopted, New Zealand needs an approved and consistent definition of child poverty before any progress can be made in reducing it.

The current amount of child poverty in New Zealand is difficult to quantify. Using one of the classic measures of child poverty, based on household incomes

after housing costs, as many of 25% of New Zealand children (approximately 270,000) currently live in poverty (EAG, 2012a, p.1). The evidence also suggests that a high proportion of these children are materially deprived, and that such deprivation can have both immediate and long-term consequences for the children affected and New Zealand society as a whole. A recent UNICEF report sums up the significant costs of child poverty thus:

**.... children who are deprived of the basics such as good nutrition and a healthy, warm physical environment are much more likely to develop ongoing physical and emotional health problems ... [they] are unlikely to develop to their full educational, societal and economic potential.**

Failure to provide this protection brings heavy costs. The biggest price is paid by individual children whose susceptible years of mental and physical growth are placed at risk. But societies also pay a heavy price – in lower returns on educational investments, in reduced skills and productivity, in the increased likelihood of unemployment and welfare dependence, in the higher costs of social protection and judicial systems, and in the loss of social cohesion ... the economic argument, in anything but the shortest term, is therefore heavily on the side of preventing children from falling into poverty in the first place. (Innocenti Research Centre, 2012, p.27)

These extremely serious societal and economic costs are experienced not just by the individual children and families, but by society as whole. Consequently, child poverty is a problem that cannot be ignored and left merely to the individuals affected to try and solve. A degree of collective responsibility is required, or

else we abandon children to deprivation. As UNICEF states:

Childhood by its nature, and by its very vulnerability, demands of a civilized society that children should be the first to be protected rather than the last to be considered. This principle of 'first call' for children holds good for governments and nations as well as for the families who bear the primary responsibility for protection. And because children

have only one opportunity to grow and to develop normally, the commitment to protection must be upheld in good times and in bad. It must be absolute, not contingent.

Nor can this principle of first call be side-stepped by the argument that the protection of children is an individual rather than a social responsibility. No one can seriously claim that it is the child's fault if economies turn down or if parents are unemployed or low-paid. (ibid.)

Collective responsibility for child poverty need not be based solely on obvious, altruistic reasons. For New Zealand society as a whole to thrive we need a significant population of healthy, productive adults. However, children who are deprived of the basics such as good nutrition and a healthy, warm physical environment are much more likely to develop ongoing physical and emotional health problems. These children are also unlikely to develop to their full educational, societal and economic potential. As these children become adults

such problems are often amplified, which creates significant ongoing and future costs for all New Zealanders. Therefore, tackling child poverty head on is crucial. As the EAG states:

Currently, the economic costs of child poverty are in the range of \$6-8 billion per year and considerable sums of public money are spent annually on remedial interventions. Failure to alleviate child poverty now will damage the nation's long-term prosperity. It will also undermine the achievement of other important policy priorities, such as reducing child abuse, lifting educational attainment and improving skill levels. (EAG, 2012, p.vi)

### **At the very least we should be able to agree as a society to be accountable for providing the best possible environment for children to thrive, even if we disagree on the means of achieving it.**

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#### **Should New Zealand implement child poverty legislation?**

New Zealand is a signatory to the United Nations Convention on the Rights of the Child. The convention was adopted to ensure (among other things) that children have a universal right to education,<sup>1</sup> 'the enjoyment of the highest attainable standard of health',<sup>2</sup> and 'a standard of living adequate for the child's physical, mental, spiritual, moral and social development'.<sup>3</sup> Child poverty has been found to impact negatively upon affected children's health, education and living standards to a significant degree. Thus, New Zealand as a signatory to the convention needs to take action on child poverty to ensure that all New Zealand children's rights under the convention are upheld.

The biggest challenge lies not in deciding that New Zealand needs to take action against child poverty, but rather determining the best way to do

so. Arguably, the most effective way to take collective action is to pass legislation specifically designed to reduce child poverty. Such legislation would make the government accountable for outcomes and would clearly ensure that reducing child poverty becomes an important priority. However, one piece of legislation alone will not make a difference if other legislation undermines it, and/or if there is insufficient funding to implement it.

The New Zealand government does not have limitless resources and has to make choices about expenditure. Underlying such debates are two differing economic philosophies: the free market model and economic interventionism. Those who subscribe to the free market model believe that the best way to advance the economy is to give maximum

freedom to individuals. They believe that economic growth ensures everyone in the free market will thrive. This model shies away from governmental intervention and regulation and considers that individuals should not usually receive governmental assistance. Those in the economic interventionism camp believe that governmental assistance is necessary for everyone to thrive. Without such intervention, they believe, the 'haves' will continue to prosper and the 'have-nots' will be left behind. Both economic philosophies essentially want the same outcome, a productive and healthy society, but disagree on how to get there. One thing is sure: children cannot compete in any form of market and their well-being is totally dependent on what happens in the adult world. At the very least we should be able to agree as a society to be accountable for providing the best possible environment for children to

thrive, even if we disagree on the means of achieving it.

The United Kingdom recently passed the Child Poverty Act 2010 with the primary purpose of eradicating child poverty. The legislation provides targets relating to the reduction of child poverty and accountability mechanisms. The machinery of the act does not actually correspond to an eradication of all child poverty across the United Kingdom, but rather aims to achieve 'certain baseline levels (which are deemed to be low rates)' (EAG, 2012b, p.10). The act provides four targets, ranging from the 'relative low income target' to the 'persistent poverty target'.<sup>5</sup> It ensures that the government develops child poverty reduction strategies and must report back to Parliament on the progress of these strategies each year.<sup>6</sup> Section 14 of the act requires the secretary of state to 'lay an annual report in Parliament on progress in meeting the statutory targets and in implementing the national child poverty strategy' (EAG, 2012b, p.11). The act also established the Child Poverty Commission to provide advice on the construction of national strategies, and it imposes duties on local authorities and bodies to work with the government to mitigate the effects of child poverty in their local area.<sup>7</sup>

The primary emphasis in the Child Poverty Act is on reducing income poverty. At this stage it is too early to know how successful the act has been. However, as the EAG states:

The most recent set of Households Below Average Income (HBAI) statistics released by the Department for Work and Pensions in June 2012, indicates that over the last year there has been a small drop in the levels of child poverty from 20 percent to 18 percent (approximately 2.3 million children), a reduction of around 300,000. However, this figure rises to 3.6 million, or 27 percent, when housing costs are included in the income measurement. Nevertheless, this figure is still 200,000 less than the after-housing cost measurement for the previous year.

While this downward trend is encouraging, particularly in an era



of 'austerity' politics following the global financial crisis, it is too soon to draw any firm conclusions as to the Act's effectiveness in meeting its targets. Indeed, while there was a small drop in the numbers of children in poverty, the relative poverty target for 2011 was missed by approximately 600,000. Economic conditions, taxation and fiscal policy and the level of government investment in social services will inevitably have a central bearing on outcomes. (EAG, 2012b, p.12)

While this is encouraging, the UK Institute of Fiscal Studies has predicted that child poverty rates in the United Kingdom are likely to rise from 2013, with the relative poverty rates reaching 24% and the absolute poverty rates reaching 23% (ibid., p.12).

The Welsh Assembly also passed legislation in 2010 which specifically tackles child poverty among other issues. The Children and Families (Wales) Measure 2010 (aims to:

[M]ake provision about contributing to the eradication of child poverty; to provide a duty for local authorities to secure sufficient play opportunities for children; to make provision about arrangements for participation of children in local authority decisions that might affect them; to make provision about child minding and day care for children; to make provision establishing integrated family support teams and boards; to make provision about improving standards in social work for children and persons who care for them; to make provision about assessing the needs of children where their parents need community care services or have health conditions that affect the needs of the children; and for connected purposes.<sup>8</sup>

The measure provides a number of 'broad aims,' which include increasing income for households with one or more children; ensuring that, so far as is reasonably practicable, children living in households in the relevant income group are not materially deprived; to reduce

inequalities in educational attainment between children; to ensure that all children grow up in decent housing; to help young persons participate effectively in education and training; and to help young persons participate effectively and responsibly in the life of their communities.<sup>9</sup> The measure places a duty on Welsh ministers and local authorities to prepare and publish child poverty strategies, which must be then enacted into regulations.<sup>10</sup> Local authorities must also provide free childcare services and implement free health and parental support services.<sup>11</sup> The legislation requires Welsh ministers to have due regard to the rights of children and the United Nations Convention on the Rights of the Child.

The legislative models in both England and Wales illustrate legislation

their full potential and participate as full and equal members of New Zealand society. (EAG, 2012b, p.16)

The EAG also suggests that the purpose of the legislation could be to '[a]chieve a sustainable reduction' in both the 'number and proportion' of children in poverty and to '[a]lleviate the socio-economic disadvantage experienced' by those experiencing child poverty in New Zealand (ibid., p.15).

The legislation would also need to set out clear measures for poverty. This is a complex task, which will require significant economic and statistical expertise. Rather than merely focusing on income poverty, measures should also be implemented in other areas, such as housing, education, and health and

## Without the enactment of legislation specifically addressing child poverty, which ensures public visibility and governmental accountability, the sad reality is that child poverty will fall off the political and media agenda.

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which defines child poverty, which sets out targets and strategies for eliminating it, and which places duties on government ministers and local authorities to act in ways designed to reduce child poverty. This ensures that child poverty must be considered when policy decisions are made.

Any New Zealand legislation addressing child poverty would need to provide a definition of exactly what child poverty is. The EAG proposes the following definition of what 'living in poverty' means:

For the purposes of this Act, children living in poverty are defined as all persons aged under 18 years of age who experience deprivation of income and the material resources required for them to develop and thrive, enjoy their rights, achieve


support services. A significant aspect of the legislation would be to place a duty on the minister responsible to gather relevant consistent data each year and to show Parliament where progress has or has not been made. This way, child poverty becomes a matter of public debate and pressure can be brought to bear to ensure that progress is made.

Without the enactment of legislation specifically addressing child poverty, which ensures public visibility and governmental accountability, the sad reality is that child poverty will fall off the political and media agenda. New Zealand can only put the welfare and best interests of children first and deliver the rights for children established by the United Nations Convention on the Rights of the Child if the government steps up and makes child poverty a legislative priority.

- 1 United Nations Convention on the Rights of the Child, 1990, article 28. Further, article 29 declares that education shall be geared towards the 'development of the child's personality, talents and mental and physical abilities to their fullest potential'.
- 2 *Ibid.*, article 24.
- 3 *Ibid.*, article 27. Article 27 further states: 'Parties, in accordance with national conditions and within their means, shall take appropriate measures to assist parents and others responsible for the child to implement this right and shall in case of need provide material assistance and support programmes, particularly with regard to nutrition, clothing and housing.' This article clearly imposes an international obligation on signatories to assist children and their families who are suffering from the effects of poverty. However, the provision is qualified by the proviso 'in accordance with national conditions and within their means'.
- 4 Child Poverty Act 2010 (United Kingdom), introductory text.
- 5 *Ibid.*, ss3–6.
- 6 *Ibid.* ss9–13.
- 7 *Ibid.*, s8; ss19–25.
- 8 Children and Families (Wales) Measure 2010, introductory text.
- 9 *Ibid.*, s1.
- 10 *Ibid.*, ss3–6.
- 11 *Ibid.*, ss7–10.

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**VICTORIA**  
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O TE IPIKORO O TE IKA A MĀUI

**Institute for Governance  
and Policy Studies**  
A research institute of the School of Government

## Post Budget Day Seminar

Friday 17 May 12:30pm-1:30pm  
Lecture Theatre 2,  
Government Building (access via Stout Street)

**Shamubeel Eaquab** *NZIER Principal Economist*  
2013 Budget: The Macro-Economic Outlook

**Derek Gill** *NZIER Principal Economist & IGPS Senior Associate*  
2013 Budget: Macro meso and micro perspectives

**Another Commentator** *(to be confirmed)*  
2013 Budget: a social policy perspective

The IGPS will be hosting a Post Budget day seminar to review the 2013 Budget. The speakers will focus on reviewing the macro- economic prospects, the fiscal policy implications and the social policy developments signalled in the 2013 Budget.

**Shamubeel Eaquab** has worked as a macro economist in the private sector since 2001, both in New Zealand and Australia. His focus and interest is in analytical frameworks to aid economic forecasting, commentary and incisive research into topical areas of economics. He holds a Bachelor of Commerce and Management with Honours in Economics from Lincoln University.

**Derek Gill** has worked on fiscal policy and public sector management for almost his entire working career. His public service career included roles at the Treasury, SSC, the OECD and MSD and in recent years he has extensively researched, taught and published on a range of public policy and management issues, while based at the Institute of Policy Studies at Victoria University. He is a graduate of both Victoria and George Mason Universities.

No RSVP Required

## Education and Poverty: Confronting the Evidence

Friday 31 May 12:30pm-1:30pm  
Railway West Wing, Level 5, Room 501

**Professor Helen Ladd** *Duke University*

Current policy initiatives to improve the U.S. education system, including *No Child Left Behind*, test-based evaluation of teachers, and the promotion of competition are misguided because they either deny or set aside a basic body of evidence documenting that students from disadvantaged households on average perform less well in school than those from more advantaged families. Because these policy initiatives do not directly address the educational challenges experienced by disadvantaged students, they have contributed little—and are not likely to contribute much in the future—to raising overall student achievement or to reducing achievement and educational attainment gaps between advantaged and disadvantaged students. Moreover, such policies have the potential to do serious harm. Addressing the educational challenges faced by children from disadvantaged families will require a broader and bolder approach to education policy than the recent efforts to reform schools.

**Helen F. Ladd** is the Edgar Thompson Professor of Public Policy Studies and Professor of Economics at Duke University's Sanford School of Public Policy. Most of her current research focuses on education policy. She is the author of many books and articles, including a co-authored book on New Zealand educational reforms of the late 1980s and early 1990s, *When Schools Compete: A Cautionary Tale* (Brookings, 2000).

No RSVP Required

**For further information and details of the Seminars  
please visit our website <http://igps.victoria.ac.nz>**

Philippa Howden-Chapman,  
Michael G. Baker and Sarah Bierre

# The Houses Children Live In

## policies to improve housing quality

New Zealand ranks near the bottom of the OECD in its health and safety rating for its children (Public Health Advisory Committee, 2010). One of the key drivers of this is the relatively poor state of our housing. Young children spend virtually all of their time in the home environment, much of which is poor quality rental housing (Baker, Keall et al., 2007). The Children's Commissioner's Expert Advisory Group on Solutions to

Child Poverty (EAG) recently highlighted the broad costs of not maintaining this essential infrastructure for the health of children, their educational opportunities and household income. New Zealand research has clearly demonstrated that improving the quality of housing enhances children's health and attendance at school, while more energy efficient houses reduce our carbon emissions. This article gives an overview of current research and discusses the feasibility of various policies to address this pressing problem.

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**Philippa Howden-Chapman** is a Professor of Public Health at the University of Otago, Wellington, where she teaches public policy. She is director of the He Kainga Oranga Housing and Health Research Programme and the New Zealand Centre for Sustainable Cities. She has conducted a number of randomised community housing trials in partnership with local communities, which have had a major influence on housing, health and energy policy. She has a strong interest in reducing inequalities in the determinants of health and has published widely in this area, receiving a number of awards for her work. She is currently the chair of the WHO Housing and Health Guideline Development Group, and was a member of the Children's Commissioner's Expert Advisory Group on Solutions to Child Poverty.

**Michael G. Baker** is a Professor of Public Health and Co-Director of the He Kainga Oranga Housing and Health Research Programme at the University of Otago. He is also Director of Continuing Professional Development for the New Zealand College of Public Health Medicine, and Co-Director of the Public Health Summer School.

**Sarah Bierre** is a research fellow in the He Kainga Oranga Housing and Health Research Programme at the University of Otago, Wellington. She has researched policies relating to the improvement of the quality of private rental housing and the functioning of the Tenancy Tribunal. She is co-editor of the forthcoming book *How to Build Houses that People can Afford to Live In*.

## Background

Public health professionals, paediatricians, the public and politicians have become increasingly concerned about the appalling rates of infectious diseases in New Zealand, which have increased markedly over the last 20 years (Baker, Telfar Barnard et al., 2012). Three recent surveys of children admitted to hospitals in Auckland and Wellington have starkly highlighted the strong association between poor housing standards and poor child health, a problem which is compounded by overcrowded households.

Trenholme and colleagues obtained information on 508 hospital admissions for lower respiratory tract infection in children under two in Counties Manukau in 2007, a period of relatively low

Canadian national occupancy standard. The quality of the children's housing was also very poor, with 59% of parents reporting that they were usually cold inside their home and 47% living in damp, musty or mouldy conditions. These hospitalised children predominantly live in households without secure tenure, with only 29% living in owner-occupied dwellings. Of the children who live in households that rent, 38% were living in private rentals, 30% were living in Housing New Zealand Corporation (HNZC) houses and 3% were living in 'other' accommodation, including garages, boarding houses, caravans and women's refuges. Overall, these children are more likely to live in more deprived households with 55% of the households, having a community services card and

poverty and poor health in these cross-sectional surveys is backed up by two decades of research on housing and health by researchers at the University of Otago, Wellington. The He Kainga Oranga Housing and Health Research Programme has highlighted that one of the main contributory factors to poor child health in New Zealand is the unsatisfactory physical state of much of our housing stock, in particular our unregulated rental housing stock. Over 70% of all children in poverty live in rental accommodation: 20% in HNZC state housing and 50% in private rental accommodation (Perry, 2012).

He Kainga Oranga has had the quality of several thousand houses assessed by trained building assessors using the Healthy Housing Index and has found a consistent pattern, with private rental housing being on average of poorer quality than state housing, which in turn is on average of poorer quality than houses that are owner occupied. Similar results were found in the BRANZ House Condition Survey (Buckett et al., 2012). The litany of problems is now familiar: poorly insulated, inadequately heated, damp and mouldy housing. Added to this is the stock of 'leaky' homes which have severe weatherproofing issues (Howden-Chapman, Bennett and Siebers, 2010; Howden-Chapman, Ruthe and Crichton, 2011).

New Zealand now has overwhelming research evidence about the advantages of reducing exposure to household crowding (Baker, McNicholas et al., 2000; Grant et al., 2012) and the benefits of home insulation and home heating on health (Howden-Chapman, Matheson et al., 2007; Howden-Chapman, Pierse et al., 2008) and school attendance (Free, Howden-Chapman et al., 2009). Probably the most compelling evidence for the health benefits of housing improvement comes from evaluating the effects of the HNZC Healthy Housing programme. This programme focused on housing improvements (insulation, ventilation, heating), as well as crowding reduction and improved access to primary health care and social services. The largest proportion of households receiving this intervention was in Counties Manukau.

## New Zealand now has overwhelming research evidence about the advantages of reducing exposure to household crowding ... and the benefits of home insulation and home heating on health ... and school attendance ...

New Zealand unemployment (Trenholme et al., 2012). They identified markedly higher hospitalisation rates for Māori and Pasifika children and those living in the most deprived neighbourhoods. Two-thirds of children were potentially exposed to second-hand tobacco smoke, 27% reported no source of heating at home and 33% lived in households where there were four or more children.

More recent results have been even more concerning and suggest that conditions for low-income children are deteriorating. From May to December 2012, the first year of the ongoing US Center for Disease Control and Prevention-funded SHIVERS study,<sup>1</sup> the research team reviewed 2,260 hospital admissions for severe acute respiratory infection at Auckland Hospital; 40% (904 hospitalisations) were for children under 15 years of age. In this population, the effect of the Auckland housing shortage is clear, with 14% living in severely crowded houses and a further 26% living in overcrowded houses, by the

45% being in receipt of a means-tested benefit (unpublished data).

Also in 2012, a study of 106 child admissions to Wellington Hospital in August 2012 identified a similar disturbing pattern of high rates of respiratory admissions in Māori and Pasifika children and a strong association with poor housing conditions (Denning-Kemp et al., 2012). Despite the parents of 40% of these children reporting that their children had a chronic health condition, one third of parents had noticed dampness and mould in their house, 50% stated that their house was colder than they preferred during the past month and 20% lived in uninsulated houses. Twenty per cent of children lived in overcrowded houses, which were disproportionately in highly deprived socio-economic areas.

### The health benefits of improving housing conditions

This dismal association between poor housing, cold indoor temperatures, fuel

Two separate evaluations have shown that this programme was extremely effective at reducing rates of hospitalisation for children living in intervention households (Baker, Zhang et al., 2011; Jackson et al., 2011), which underscores that this is a critical area for further public investment (Howden-Chapman, 2012).

Rising concern about the effects of poor housing standards informed the investigation of policies carried out by the EAG, which was established by the children's commissioner to analyse research and administrative evidence about the extent of child poverty and possible effective solutions (EAG, 2012).

#### **The Children's Commissioner's Expert Advisory Group on Solutions to Child Poverty**

The EAG's main recommendation to the government in relation to housing was that housing should be considered as essential infrastructure and included in the National Infrastructure Plan. Furthermore, current regulatory arrangements were considered inadequate, having not been amended since 1947. The EAG recommended that the government should ensure that all rental housing, both social and private sector, meet minimum health and safety standards, measured by an agreed warrant of fitness (WOF), such as the Healthy Housing Index. The Healthy Housing Index, developed by He Kainga Oranga and BRANZ, includes a health, safety and energy efficiency rating scale – the latter is mandatory in most OECD countries (Keall, Baker et al., 2010). Application of this tool has shown that there is a significant association between the number of respiratory symptoms (wheezing or whistling when breathing, or an asthma attack) of occupants and the number of respiratory hazards in a house (Keall, Crane et al., 2012). A similar association has been found between the number of home injuries (ACC claims) and the number of injury hazards in the house (Keall, Baker et al., 2008; Keall, Baker et al., 2012).

Underpinning the EAG's recommendation was the realisation that policy implementation for a warrant of fitness was crucial: standards should be set carefully, monitored periodically, effectively enforced and increased over

time when justified by available evidence and improvements in technology. Costs associated with the WOF should be borne by landlords, but this could be partially offset through favourable tax treatment of any required improvements. Implementation planning should carefully consider how to reduce the risk of costs associated with improvements required by the WOF being shifted onto tenants. One approach, which is currently being discussed with central and regional government, is to undertake a pilot programme to implement and evaluate the market effects of a WOF for rental housing at both local and regional community levels.

The accommodation supplement is a demand-driven benefit, currently costing

per year until 2020. Social housing refers to housing that is provided based on assessed financial and social need, at subsidised rates, and with active tenancy management (Howden-Chapman, 2004). Social housing can include rental housing or home ownership support to individuals or families. In New Zealand social housing is provided by the government (between 66,000 and 69,000 HNZC properties), local government (around 14,000 units) and community housing providers (around 5,000 units). The EAG considered that social housing can directly mitigate the effects of child poverty and is of critical importance for many low-income families. However, demand for social housing significantly exceeds supply. Hence, increasing the

## **Overall, concerns about housing elicited the highest number of public responses to the EAG. There was almost unanimous support for having a rental housing WOF from the feedback received ...**

\$1.2 billion annually, the second largest benefit after National Superannuation, but the government does not require any minimum rental standards before it is accessed. In the US, the federal housing voucher is paid to landlords, on condition that their accommodation passes the modified English Decent Home standard, similar to the Healthy Housing Index. Although some landlords in New Zealand currently have arrangements with the Ministry of Social Development to be paid directly, there is no requirement that their accommodation meets any standards. Without this quid pro quo, under this current system tenants have little leverage to improve the quality and maintenance of their rental houses or apartments.

Another recommendation from the EAG was that the government address the serious under-supply of affordable housing for families with children living in poverty by taking immediate actions to increase the number of social houses by a minimum of 2,000 units

number of social housing units needs to be a long-term commitment, requiring a considerable capital investment over an extended period of time. Similarly, the EAG wanted consideration of spreading the income-related rent subsidies to community organisations. A related recommendation was that the government should develop a range of measures to increase the ability of low-income households to purchase their own home.

Overall, concerns about housing elicited the highest number of public responses to the EAG. There was almost unanimous support for having a rental housing WOF from the feedback received, including the children's perspectives, community meetings, survey responses and formal submissions. Young people consulted by the EAG highlighted the need to address the quality and cost of housing and overcrowding. Children spoke about the effects of damp, cold houses on their health and described their families struggling or unable to

pay household bills because rents are too high. This often meant no heating, no hot water and the inability to cook. They asked for better insulated homes which are more affordable to heat and told the commission that there is a need for stricter rules for rental properties. The children and young people spoke of a lack of privacy in overcrowded homes, and arguments and tensions which affect family relationships. They also said that overcrowding affects their ability to do homework (EAG, 2012).

#### The case for government action on housing supply and quality

There is abundant evidence that the housing market has failed to deliver both the quantity and quality of housing needed.<sup>2</sup> There are historically low levels of building consents, particularly for affordable housing (New Zealand Productivity Commission, 2012). This situation has caused a growing housing crisis in Auckland, which has the most rapid population growth in the country and has a shortfall of new house construction of at least 4,000 units a year (Johnson, 2012). The situation has been compounded by the Canterbury earthquakes, which have destroyed an estimated 11,000 houses and damaged tens of thousands of others (EAG, 2012).

An inevitable consequence of a shortage of affordable housing is household crowding. A recent report undertaken by the University of Otago and Statistics New Zealand has shown that in the 2006 census, 10% of Māori children under 15 years and 21% of Pasifika children under 15 years were exposed to severe household crowding (i.e. the household in which they were living was short of at least two bedrooms) compared to European children or children of other ethnicities (2%) (Baker, Goodyear et al., 2012). Thousands of children are experiencing severe housing deprivation (Amore, Baker et al., forthcoming), officially defined as lack of access to minimally adequate housing (Statistics New Zealand, 2009). These children are living in situations where they have no security of tenure, little privacy, and in some cases not even basic amenities. These problems

are further compounded by 'functional crowding', where children and other household members all sleep in the same room to keep warm during cold winter months (Denning-Kemp et al., 2012). An important driver for households behaving in this way is fuel poverty (see the separate article on this matter in this issue of *Policy Quarterly*), with an increasing proportion of low-income people who cannot afford to heat their homes (Howden-Chapman, Viggers et al., 2011). Low-income families, some with poor credit ratings, may have little choice but to use prepayment meters, which usually have higher tariffs and often lead to so-called 'self-disconnection' budgeting, which in some cases is for prolonged and disruptive periods (O'Sullivan et al., 2013). Structural and functional crowding also have the obvious potential to greatly increase transmission of infectious disease.

The case for more active government intervention in the housing market therefore appears overwhelming. This need has been recognised already with the current Warm Up New Zealand: Heat Smart programme, which has insulated over 204,000 houses. This programme was supported by several controlled trials (Howden-Chapman, Matheson et al., 2007; Howden-Chapman, Pierse et al., 2008) and economic evaluations (Chapman et al., 2009; Preval et al., 2010; Grimes et al., 2011) showing health benefits and positive benefit-cost ratios of up to five to one. The EAG, among other parties, has recommended that the government extend beyond June 2013 and target the current subsidy programme for insulating homes, with the longer-term aim of ensuring that all remaining uninsulated or poorly insulated homes (estimated at approximately 700,000) are properly insulated and effectively heated. Specific targeting is needed to incentivise landlords to insulate their rental properties, as landlords have been reluctant to take up the two-third subsidies currently available.

A WOF could require basic health and safety features such as insulation and protection from falls. Housing New Zealand should be realistically funded to revitalise its very successful Healthy

Housing programme. This programme could be extended to cover all of its 69,000 properties, which contain many of New Zealand's most vulnerable children (Baker, Zhang and Howden-Chapman, 2012). Better housing conditions would support the government's admirable target of reducing the incidence of rheumatic fever by two-thirds by 2017 (Jaine, Baker and Kamalesh, 2011).

#### Conclusion

Evidence, ethics and economics all point towards the need for greater investment in better housing for children. Housing should be seen as important national infrastructure, with the government using its considerable regulatory powers to improve housing quality in New Zealand. As recommended by the EAG, a good starting point would be a warrant of fitness for rental housing and a reinvigorated HNZC Healthy Housing programme. Establishing a large-scale programme for construction of medium-density social housing in Auckland and Christchurch would also produce many benefits, particularly if it involved the community housing sector. Not only would such housing reduce crowding and improve child health, it would also provide a valuable economic stimulus and help retain skilled labour in New Zealand.

- 1 The Southern Hemisphere Influenza and Vaccine Effectiveness Research and Surveillance (SHIVERS) project was established in October 2011. It is a multi-centre and multidisciplinary collaboration between the Institute of Environmental Science and Research, Auckland District Health Board, Counties Manukau District Health Board, University of Otago, University of Auckland, WHO Collaborating Centre at St Jude Children's Hospital and the US Centers for Disease Control and Prevention. The SARI surveillance is funded by the US Department of Health and Human Services, Centers for Disease Control and Prevention (1U01IP000480-01). It is a key component of the SHIVERS project. The SARI surveillance protocol development and platform establishment are carried out by Sue Huang, Sally Roberts, Colin McArthur, Michael Baker, Cameron Grant, Deborah Williamson, Adrian Trenholme, Conroy Wong, Susan Taylor, Graham Mackereth, Don Bandaranayake, Nikki Turner, Nevil Pierse, Richard Webby, Diane Gross, Jazmin Duque, and Marc-Alain Widdowson on behalf of the SHIVERS investigation team.
- 2 This issue is explored in a forthcoming book, *How To Build Houses That People Can Afford to Live In*, edited by Sarah Bierre, Philippa Howden-Chapman and Lisa Early and published by Steele Roberts.

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# Child Poverty the ‘fuel poverty’ dimension

Children ... spoke about damp and cold houses affecting their health, and wanted rental properties to be safer and healthier. They noted that more insulation of homes would make heating homes more affordable, as they reported that families are struggling to pay household bills, which leads to no heating, no water, and the inability to cook.  
(Expert Advisory Group on Solutions to Child Poverty, 2012)

Fuel poverty can be broadly described as the inability of a household to afford a sufficient level of energy services in the home. Energy services are the things people need and desire from their use of energy, such as warm and comfortable rooms, hot water, lighting, and cooked food. Having a sufficiency of energy services is widely accepted as indispensable to modern

living and peoples’ quality of life, while a state of energy deprivation can have an adverse impact on physical and mental health, well-being and social functioning (Boardman, 1991; Pantazis, Gordon and Townsend, 2006). As the Expert Advisory Group on Solutions to Child Poverty noted, fuel poverty is a contributing factor in the breadth and depth of child poverty in New Zealand.

This article will background the emergence of fuel poverty and outline its main characteristics in New Zealand with particular reference to child poverty.<sup>1</sup> I will examine and critique the policy response to date and explore several policy options. The perspective I bring is through having ‘a foot in each camp’ – by

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having a background in policy work for local and central government agencies, and involvement with front-line service delivery in a fuel poverty-focused charitable trust. Housing policies, including specific proposals such as a house 'warrant of fitness', will not be explored here, since Philippa Howden-Chapman is covering this ground elsewhere in this issue of *Policy Quarterly*.

### The emergence of fuel poverty

The term 'fuel poverty' was first coined in the United Kingdom in the 1970s to describe the adverse social impacts of cold homes and energy deprivation resulting from the large energy price increases occurring at that time, economic recession, and fuel supplier disconnection policies (Boardman, 1991). It took over two decades for the term to become officially recognised, but in 2001 the UK government adopted a formal definition of fuel poverty as part of a policy initiative that elevated the reduction and elimination of fuel poverty to one of its main energy goals. A household was considered to be in fuel poverty when it 'needs to spend more than 10% of its income on all fuel use and to heat its home to an adequate standard of warmth' (UK Government, 2001). The definition contains a very useful concept – what a household needs to spend to achieve a sufficiency of energy services – but the specific formulation of the expenditure to income ratio and the 10% threshold has proven problematic. The current UK government has proposed that fuel poverty should in future be defined as households having the twin attributes of low income and high relative energy costs (Department of Energy and Climate Change, 2012).

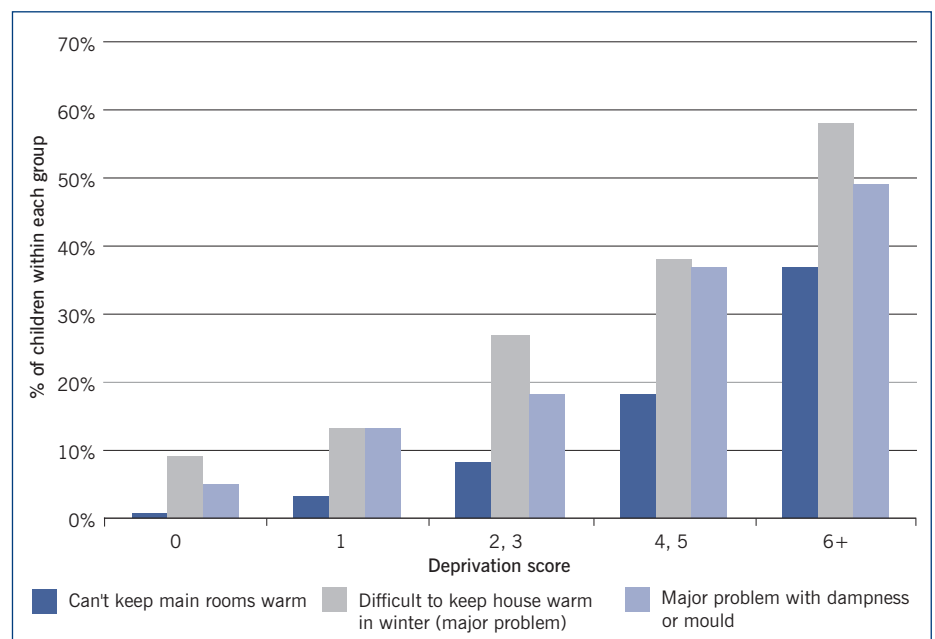
The 10% expenditure threshold has been used in various analyses of fuel poverty in New Zealand, but application of this formulation heavily weights the presumption of fuel poverty to low-income, single-person and elderly households. There is undoubtedly energy deprivation among the elderly, but studies of deprivation and poverty more generally clearly show that, in terms of both numbers and depth, households with children comprise the majority of the socially deprived (Perry, 2012).

The largest number of at-risk households are those with children, with one-parent families displaying the highest rate of deprivation. Indicators of fuel poverty align closely with indicators of social deprivation more generally (McChesney, 2012).

Children typically experience two types of negative consequences from their family being in fuel poverty. The first is the high likelihood of living in cold and damp houses that are under-heated, or not heated at all during the winter. The 2008

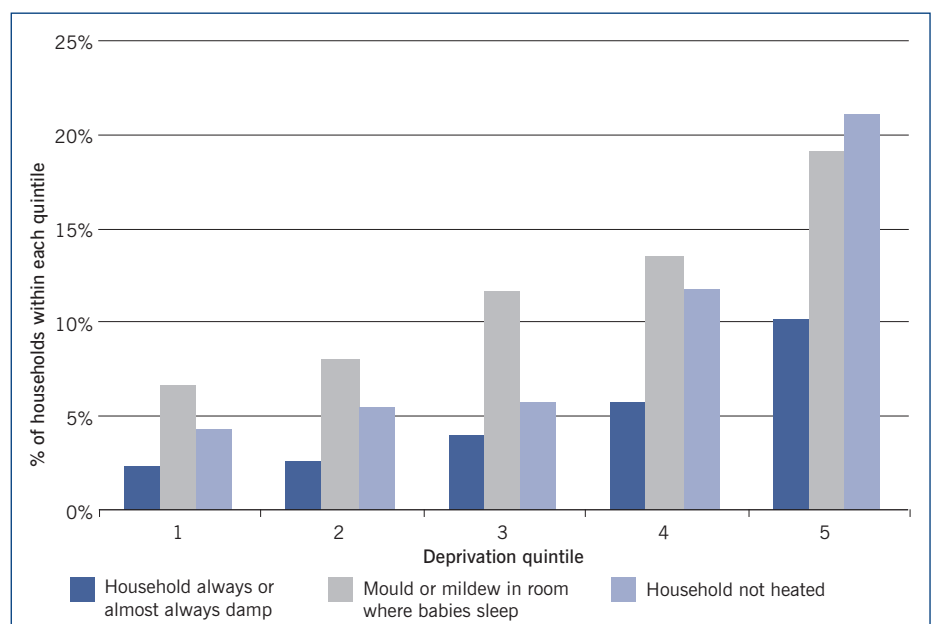
New Zealand Living Standards Survey found 9% of children living in homes where main rooms cannot be kept warm, 17% where there is a major problem with dampness and mould, and 22% where there is a major problem with keeping the house warm in winter (Perry, 2009). The incidence of these indicators displayed a strong deprivation gradient (see Figure 1). The *Growing Up in New Zealand* study, reporting on babies at 9 months of age (data was collected during the 12 months to January 2011), found 18.4%

Figure 1: Rate of fuel poverty indicators for children by deprivation group



Source: Perry, 2009

Figure 2: Incidence of fuel poverty-related indicators, Growing Up in New Zealand households 2010-11



Source: Morton et al., 2012

of households 'putting up with feeling cold to save on heating costs' (Morton et al., 2012). Progressively higher levels of mould, condensation and dampness, and houses lacking heating were found in more deprived areas (see Figure 2).

A second consequence of fuel poverty is that children may experience periods when their household suffers electricity disconnection. Disconnection may occur through a formal process initiated by the electricity supplier for late or non-payment of electricity bills, or as a result

#### Causes and responses

Fuel poverty has emerged and risen in New Zealand in parallel with poverty and child poverty more generally, and shares some of the same drivers (e.g. low household income relative to outgoings, social dislocation). Other drivers are unique to this issue, in particular the costs faced by families in providing an adequate level of energy service provision. These energy costs are determined by a mix of market conditions (e.g. prevailing energy tariffs), house characteristics (e.g. loca-

### **... improved energy service affordability gained through insulation and efficiency programmes have, for most low-income households, been swamped by relentless increases in electricity costs experienced since the early 1990s.**

of families with prepayment meters enduring periods without power because they cannot afford to top up their meter. Difficulty with paying bills on time and disconnection are also strongly associated with higher levels of deprivation more generally (Perry, 2009).

Disconnection greatly disrupts the structure of family life, especially if it is recurring. Household stresses are increased and families are forced into a range of short-term coping behaviours, some of which are unsafe and risky for children (e.g. using candles for lighting, and various unflued portable gas appliances). Disconnection compromises a range of social necessities, including food storage and cooking (and the ability to feed children well), and washing, as well as exacerbating cold homes issues (O'Sullivan et al., 2011). It is estimated that in 2011 about 50,000 households were disconnected for some period due to inability to pay. This represented a significant increase from three years earlier, when guidelines were developed by the then Electricity Commission and the industry in efforts to minimise disconnection (Electricity Authority, 2010).

tion, orientation to the sun, insulation, heating system) and behavioural drivers (e.g. choices, knowledge and skill in managing costs effectively).

Government energy policy decisions have been an underlying driver of fuel poverty trends, producing both positive and negative outcomes. The most profound have been policies relating to electricity prices. Up to the late 1980s electricity pricing incorporated a social element by providing lower electricity prices for residential consumers through a cross-subsidy from commercial and industrial users. The electricity reforms initiated in the late 1980s set out to establish a competitive, commercial model for electricity (i.e. as a commodity traded within a market rather than being priced by government with mixed objectives, including social, in mind). Responding to concerns that the electricity reforms (and income and benefit reforms occurring at the same time) would leave many households vulnerable, the government's 1992 Energy Policy Framework specified one of the desired outcomes as 'basic energy services remain accessible to all members of New Zealand society' (New Zealand Government, 1992). Improving

the efficiency of energy use in households was seen as an effective way of addressing energy affordability and cold homes concerns, while also being positive for the environment, and hence became the main response focus. The government's current Warm Up New Zealand: Heat Smart insulation retrofitting programme is the most recent evolution of household energy efficiency initiatives that began in 1995.

Two decades on from the 'basic energy services ... for all' sentiment, how well has this outcome been achieved? By 2012 an estimated 175,000 houses, occupied by those on low incomes, had been insulated in ceilings and/or under floors via government programmes (including Housing New Zealand Corporation rental houses). Over half of the installations have occurred since 2009 when the Warm Up New Zealand: Heat Smart programme began. In addition, partial funding for heating appliances for a much smaller number of houses was made available from 2009 to 2012.

But improved energy service affordability gained through insulation and efficiency programmes have, for most low-income households, been swamped by relentless increases in electricity costs experienced since the early 1990s. Average tariffs have increased by 70% in real terms, and in the last decade the gap between average residential tariffs and those paid by commerce and industry has widened considerably (Figure 3). Bertram (2012) identifies the reason for the increase in the last decade as the practice of electricity generator-retailers carrying out 'fair value' asset revaluations within an essentially unregulated environment. Households appear to have borne the brunt of these price increases. Given that the sector has been responsible for only a little over 35% of electricity consumption growth since 2000, why households alone should have received such high price increases is unclear, except perhaps that they have been largely captive to Ramsey pricing practices (where producers concentrate price increases on the most inelastic sector of the market). The overall results have been strongly regressive: energy costs in relation to income for households in the lowest income quintile

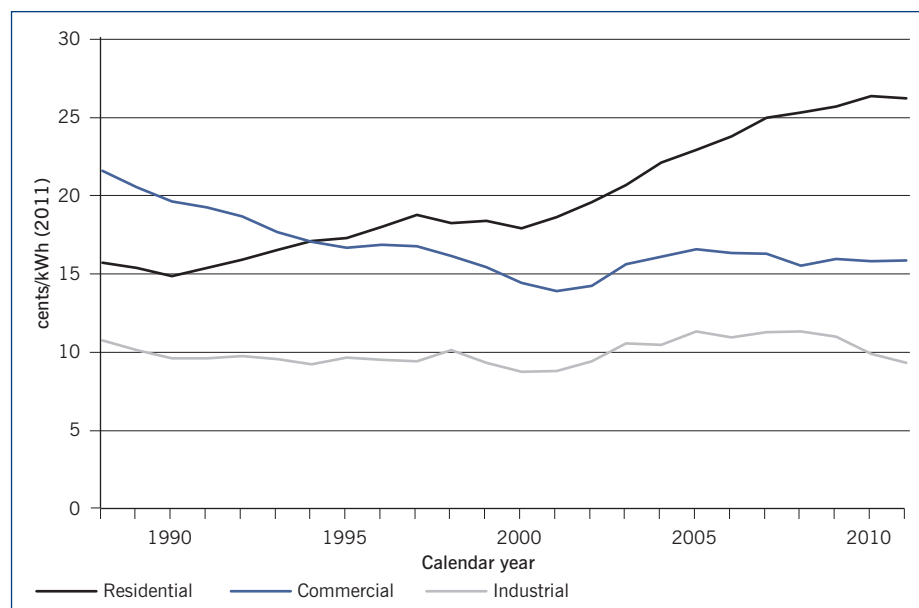
have almost doubled from less than 5% in the late 1980s to over 9% in 2010 (McChesney, 2012).<sup>2</sup>

Meanwhile, the desired outcome of universal access to basic energy services was quietly retired from energy policy, beginning in 2007 when the scope of energy services was reduced, with all reference to energy services universality finally dropped from the New Zealand Energy Strategy in 2011. This change appears to have been made as a matter of government priority to focus on the short-term actions of Warm Up New Zealand: Heat Smart and electricity supplier switching, since public submissions apparently did not suggest that the universality provision be dropped and neither did officials recommend it (Ministry of Economic Development, 2011). The path taken here is consistent with Bromell's (2012) depiction of recent governments' exasperation with 'utopian' outcome statements and strategies, turning the focus instead to specific actions via a 'command and comply' approach. To the current government's credit, the rate of insulation achievement in low-income homes in just three years of the Warm Up New Zealand programme exceeded the total for the prior 15 years. The danger, however, is that energy policy becomes defined and preoccupied by the delivery of short-term outputs, and that the wider purpose becomes lost.

#### Evaluation, interpretation and political drivers

An evaluation of health, energy and employment impacts of Warm Up New Zealand: Heat Smart was carried out in 2010–11 (Grimes et al., 2012; Telfar Barnard et al., 2011). The central estimate indicated a net benefit of about \$1.05 billion<sup>3</sup> at a 5:1 benefit-cost ratio for insulation. The Energy Efficiency and Conservation Authority (2012) saw this as affirmation of the insulation focus of the programme. But the evaluation showed quite clearly that the benefits are strongly asymmetric: 99% of the benefits are health-related, with 74% deriving from reduced mortality among elderly persons who had previously been hospitalised (representing just 0.1% of the households reached by the programme). The other

Figure 3: Real average electricity prices to end user groupings



Source: Ministry of Economic Development, 2012

health benefits, which include reduced hospitalisation and pharmaceutical costs, and imputed benefits from previous studies (e.g. less time off work), are also largely derived from households where a member had a pre-existing health condition. The health benefits were concentrated in the houses of those on low incomes: benefits per household were 2.5 times higher for households where a member had a Community Services Card than for general income households. Thus, it seems reasonable to deduce that the vast majority of the (quantified) benefits of Warm Up New Zealand derive from a minority of households, and that a significant number of houses currently being insulated under the scheme are not achieving an overall net benefit. Grimes et al. (2012) concluded as much by suggesting a targeting strategy to 'low and middle income earners and other at-risk groups in terms of illness' (p.28).

However, under the pressure of achieving the high-level target for the scheme (which is expressed in aggregate houses insulated) and restricted budgets, Warm Up New Zealand appears to be moving in the opposite direction. In 2011–12, only 39% of houses insulated under the scheme were occupied by Community Service Card holders and 61% were general income houses; by comparison, in the first year of the scheme the ratio was almost reversed, at 64:36 (Energy

Efficiency and Conservation Authority, 2010, 2012).

The Warm Up New Zealand: Heat Smart evaluation also covered heating appliances, of which a limited number had begun to be partly funded in 2009. Fuel poverty groups had long advocated for heating appliance grants because giving at-risk households access to efficient heaters with low running costs (i.e. log burners and heat pumps) is fundamental in providing affordable heat. Low-income households typically use heaters with high running costs because they are cheap to purchase (e.g. plug-in heaters and unflued LPG heaters), but running costs at typically 25–40 cents per kilowatt hour are three to six times higher than the low-running cost options. However, the evaluation found negative overall benefits for heating, a finding that led to most heating subsidies being discontinued in 2012.<sup>4</sup>

For those working with families in fuel poverty the decision to discontinue funding for heating appliances has been a step backward, especially as the decision appears to be grounded in a questionable evaluative methodology, and with little attempt to question whether the Warm Up New Zealand sample truly represented those most in need of heating. For example, the evaluation did not include or value the additional warmth gained as a private benefit by household occupants,

arguably the largest form of benefit from efficient heating.<sup>5</sup> Moreover, the circumstance of many of those securing heaters under Warm Up New Zealand is highly self-selecting because there are still significant cost barriers for the most needy. Neither, seemingly, has the very high desirability of replacing unflued LPG heaters with safe and cheap-to-run alternatives been factored in. Discontinuing a heating grant also effectively discriminates against those whose houses do not allow for insulation (e.g. they are constructed with skillion roofs or concrete floors, or lack access to the underfloor space).

I have previously commented on the divergence between government programmes which were increasingly

and facilitating electricity supplier switching.

- Projects targeted to specific household types – for example, CEA has run a Warm Babies project since 2001 in partnership with other agencies and referral networks in order to provide a warm and safe environment for new babies. Ironically, much of the focus of the programme has been to provide efficient heating appliances, a task made much easier with Warm Up New Zealand: Heat Smart, and which now will need to be revisited.
- Heating appliances – prior to Warm Up New Zealand: Heat Smart funding, CEA was installing efficient heating systems into as many needy

similarly built up local knowledge and expertise, and have developed their own set of responses to local circumstances and needs.

In my experience, officials place little value on this experiential information – it 'lacks rigour', or can be discounted because it comes from an advocatory stance. But, as argued above, 'official' evaluations and interpretations are not free from their own limitations and biases. In my view, much could be gained from bringing together and refining these different forms of information and insight – similar to Bromell's (2012) argument for creating better 'public value' around policy advice and interventions.

#### The way forward

The reality of fuel poverty, and its contribution to child poverty, requires a rethink of priorities and procedures around the energy interventions that the government is currently supporting.

At the heart of the issue is clarity about the problem to be addressed. 'Fuel poverty' has not been formally recognised as the policy problem. Official aversion to the term 'fuel poverty' has not helped, and neither has lack of agreement around a definition (there has rightfully been disquiet about adopting the UK 10% threshold definition). The policy agenda has been driven by related issues (e.g. 'cold homes', uninsulated homes, health costs, poor energy efficiency), and 'solutions' have been dominated by an insulation mindset. Lack of clarity around the policy problem produces negative flow-on effects (e.g. information that could better inform the issue is not seen as relevant and hence is not identified or collected).

This issue needs policy recognition. A good start would be to revisit the 1992 Energy Policy Framework and elevate the desired policy outcome that all households should be able to access a basic level of energy services into the current New Zealand Energy Strategy. In itself this would be relatively meaningless unless it genuinely informs the policy process, and policy actions and agency alignments flow from such a commitment. For example, it should trigger more focused, and disaggregated, monitoring. There

## ... by recognising that individual circumstances of fuel poverty can vary enormously, and designing responses appropriately to reflect this diversity, well-designed and tailored energy interventions can make a big difference.

focusing on a few standardised activities, and the way the fuel poverty-focused NGO I am associated with, the Community Energy Action Charitable Trust (CEA) approached its task (McChesney, 2008). I outlined a 'gap analysis' – the gap between the outputs provided by central government programmes, and the additional actions pursued by CEA in order to meet the needs of households as perceived and presented to it. An updated list includes:

- Curtains – supplied through donated and recycled curtains, using both paid staff and volunteers, and partnering with other community agencies (currently over 60) to identify households in need.<sup>6</sup>
- Energy advice – CEA now employs three specialist home energy advisers funded through a mix of locally-derived funding and user charges. The services offered include telephone advice, home energy checks and reports, problem solving,

houses as funding would allow.

The reason is simple: insulation on its own does not transform a cold, hard-to-heat home into a warm, affordably heated one. With Warm Up New Zealand funding the ratio of heating to insulation installations in 2011 was about 0.4:1.0 (Community Energy Action Charitable Trust, 2012), still perhaps lower than ideal but reasonable within funding limitations.

- Discretionary funding/flexible customer payment arrangements – CEA has operated a discretionary funding pool to enable households that would otherwise be unable to meet their financial contribution to Warm Up New Zealand: Heat Smart projects to proceed.

These are some of CEA's experiences, having built up a considerable pool of knowledge through operating in Christchurch for almost 20 years. Other organisations in other areas have

is a need to move beyond monitoring household 'averages', or Warm Up New Zealand aggregated totals, to capture relevant information on those most at risk. Are those households most at risk accessing the assistance available to them, for example?

A redefined problem identification should logically lead to an examination of policy effectiveness, funding priorities, and the scope for more effective targeting of the assistance monies available. This task would be ably assisted by making use of front-line networks, with their ability to identify those households most at risk and facilitate appropriate interventions.

Finally, there needs to be an examination of institutional responsibilities. At present no single government agency has an 'umbrella' policy overview of fuel poverty. Given that this is essentially an issue of social policy, logically the Ministry of Social Development should be taking on this role. In terms of programme delivery, the current model demands review because it is essentially based on a competitive funder-provider model for delivering large numbers of insulation retrofits. Fuel poverty demands an emphasis on localised approaches

– tapping into existing social provider networks and working collaboratively, matching solutions to needs (i.e. looking at the 'quality' of response, not just quantity), harnessing local voluntary networks and self-help approaches, and so on. In particular, an alternative model, based on greater local autonomy for programme design and funding decisions, and built around a 'quality partnership' approach, needs serious consideration.

### Conclusions

Addressing fuel poverty is a very important dimension of the child poverty challenge. Children have strongly articulated the negative consequences of living with energy deprivation – the cold homes, health impacts, and social dislocation caused by electricity disconnection – and the Expert Advisory Group on Solutions to Child Poverty (2012) has reflected this in a number of its recommendations.

Because of the diverse drivers of fuel poverty, there are limits to which energy interventions alone can, and should, be expected to resolve this issue. But, by recognising that individual circumstances of fuel poverty can vary enormously, and

designing responses appropriately to reflect this diversity, well-designed and tailored energy interventions can make a big difference. After almost two decades of experience with various forms of energy intervention, we have a fairly good idea of what works and how we can do better.

In the current 'authorising environment' of available funding, I believe we can be much more focused and effective in addressing fuel poverty. The challenge, perhaps, will be to the authorising environment of institutional arrangements: to recast the policy problem around 'fuel poverty', and to reframe programme delivery around a greater level of local autonomy and leadership.

- 1 The analysis undertaken in New Zealand on fuel poverty to date typically does not allow the separate identification of child 'fuel poverty' from fuel poverty in general.
- 2 This ratio is an imperfect measure of affordability but does serve to highlight the change in relative costs.
- 3 This is based on 2009–2013 programme commitments using a 'central scenario' with 4% discount rate.
- 4 Some funding is still available for clean heating appliances associated with localised polluted airsheds, but wider availability as an intervention to help address fuel poverty has been discontinued.
- 5 The evaluation of insulation also did not include this benefit, although it is likely to be of lesser importance to the overall benefits than would be the case for heating.
- 6 There are now six curtain banks operating in communities throughout New Zealand, several being sponsored by Genesis Energy.

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Susan St John

# Preventing, Mitigating or Solving Child Income Poverty? The Expert Advisory Group 2012 report

In March 2012 the Expert Advisory Group on Solutions to Child Poverty (EAG) was established by the Children's Commissioner to make recommendations that, if not fully 'solving' child poverty, would realistically reduce and mitigate its effects. The advice was to inform the Ministerial Committee on Poverty, whose focus was specifically on tangible gains 'getting value for money in a tight economic climate' (Commissioner for Children, 2012).

As the final report outlines, approximately 270,000 New Zealand children live in poverty, some for long periods of time and often in considerable deprivation (EAG, 2012a). The consequences of this

for the well-being of families, for society, and the young children themselves are beginning to be appreciated by the wider New Zealand community. This newfound understanding is one clear achievement of

the work of the EAG, and the many other organisations which have laid out the causes and consequences of child poverty before the public over many years.

The EAG describes child poverty as multidimensional, requiring a holistic approach. Many of the 78 recommendations reflect this concern. Nevertheless, as Working Paper 3 argues from the literature, sufficient money income, regardless of the source of that income, is the important and key element of family and child well-being (EAG, 2012b). While many other aspects of policy, such as health and housing, are critical, and are well addressed by the report, the EAG agreed that as an essential part of the package the incomes of families must be improved significantly. In terms of measurable outcomes, it is only if incomes increase that numbers below income-determined poverty lines will reduce.

This article focuses on only the income policy recommendations in the final report. The main ones, found in the section titled 'Tax credits, benefits and income support' (pp.38-43), are summarised in Box 1. Working Paper

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**Box 1: The Expert Advisory Group solutions for family income assistance**

- 1 In the short term, the maximum family tax credit for all children to rise to the first child over-16 rate of \$102 per week. This requires an increase of \$9.25 per week for a first child aged 0–15 years; \$37.54 per week for additional children aged 0–12; and \$28.48 per week if aged 13–15.
- 2 The rate for children aged 0–5 to subsequently rise further.
- 3 In the longer term, to amalgamate the parental tax credit, the minimum family tax credit and childcare subsidies to give a universal payment which reduces as the child ages and is targeted from 6 years on.
- 4 Child support pass-on of \$10 per week where applicable

Source: Expert Advisory Group, 2012a and 2012 c

**Box 2: Policy development framework**

- 1 Clarify the problem.
- 2 Set clear objectives (aims) for policy.
- 3 Make aims measurable or quantifiable.
- 4 Select policy criteria and economic thinking.
- 5 Assess a full range of policies that might achieve the objectives.
- 6 Select and design the best policy; project expected costs and outcomes.
- 7 Implement policy.
- 8 Measure outcomes against clearly-stated, measurable objectives.
- 9 Review unintended consequences.
- 10 Evaluate policy against criteria; confirm that the problems and the underlying economic model have been properly conceived; and suggest improvements.

Source: adapted from St John and Dale (2012)

10 (EAG, 2012c) also informs this critique, although many policy changes recommended in that paper were quite extreme and were not picked up in the final report. The conclusion assesses the EAG report’s recommendations and analysis against the criteria of cost-effectiveness, the requirement to have an evidential basis, and the account taken of the economic and fiscal context.

**Following a framework for policy development**

Here a simple framework, set out in Box 2, is first used to clarify the steps in the EAG’s development of policy recommendations. Given that policy recommendations have not yet been implemented, steps 7–10 are best thought about in principle, although they should be part of any policy process which seeks to understand why existing policy has not worked to meet the poverty reduction objectives.

*Clarifying the problem*

As set out in the foreword to the final report, the EAG intended its work to result in ‘better outcomes for the most needy and deprived children.’ The executive summary says that it is not true that New Zealand is a great place for the 270,000 children living in poverty. The ‘problem’ of child poverty was described as costly for these children themselves, with statements such as: ‘childhood poverty can leave life-time scars’ (EAG, 2012a, p.vi).

In defining the problem of child poverty there was an emphasis on a ‘rights’ approach: the rights of every child to an adequate standard of living and to achieve their full potential. The EAG implied that it is a moral issue that these rights are denied by poverty: ‘No child should experience severe and persistent poverty, least of all in a land of abundance.’ (EAG, 2012a, p.i). Moreover, Working Paper 10 outlines the key obligations under

articles 26 and 3.1 in the United Nations Convention on the Rights of the Child (UNCROC) as priority considerations in designing policies to address child poverty:

Article 26 of the UNCROC, recognising the right of children to social security and the corresponding obligation of the government to implement measures necessary to achieve full realisation of that right. Article 3.1 of the UNCROC, recognising the best interests of the child to be given primary consideration. (EAG, 2012c, p.5)

As well as the ‘rights of the child’ approach to justifying eliminating child poverty, child poverty was described in the final report as having very high costs to society in terms of forgone output and productivity. The costs for society were quoted as \$6–8 billion per annum (EAG, 2012a, p.vi). Child poverty was seen as making it difficult to achieve desirable social goals, such as lower rates of child abuse and better educational attainment, which in turn affect economic performance. The problem was conceived as most damaging when very young children were in poverty as ‘many significant aspects of child development occur in the earliest years’ (EAG, 2012a, p.vi).

So, at a high level, the problem was understood comprehensively, in part requiring normative or moral judgements of what is right, and in part relying on positive arguments about the impact on and costs to the economy. Some of the working papers had described the children who are most likely to experience poverty, such as Māori and Pasifika children, but a clear picture of where these children are found was missing in the final report (see pages 51-53 below). Also missing was a clear description of current policies for family incomes and analysis of why existing policy had not worked, despite the intent to take an evidential approach and the numerous references made to past limitations, such as:

A major reason for these problems is that the current policy instruments are not well-designed, do not



function well together as a system, and may even in some cases work against each other. (EAG, 2012c, p.3)

#### *Set clear objectives (aims) for policy*

The EAG was adamant that 'the best interests of the child must be at the heart of any new policy package' (p.39). By implication this meant that real relief of the poverty of children would be paramount. By examining the goals and objectives outlined it is clear that the EAG saw the need to address, immediately, severe deprivation and its persistence. However, it discussed reducing poverty in the long term as an additional and separable goal:

The recommendations we are proposing will have a mix of goals, including alleviating the worst material hardship now as well as reducing the extent of poverty over the longer term. (EAG, 2012a, p.39)

#### *Select measures*

Using a common measure of a poverty line based on 60% of the median disposable household income after housing costs, the EAG noted that of the 270,000 children in poverty, 170,000 fell below the 50% line and thus were in the deepest poverty (EAG, 2012a, p.4). The intent of the EAG was clearly to address the worst poverty: 'we have focused on solutions that reduce severe and persistent child poverty' (EAG, 2012a, p.vi). It could be expected, therefore, that the EAG would aim to reduce the child poverty rate significantly on the 50% measure.

Another core priority was to take an investment approach in the first years of a child's life, as that was seen to have the biggest marginal returns. To achieve this, the EAG drew on the capabilities approach of Amartya Sen as suggesting that 'adequate financial resources enhance the capability of children and families to function well and have lives that they have reason to value' (EAG, 2012a, p.29). Therefore, one measurable outcome for the EAG might have been that incomes of families with infants would specifically and significantly increase.

In the final EAG report a key recommendation was the setting up

of a statutory-based poverty reduction strategy. The government was exhorted to legislate a Child Poverty Act, monitor five official measures of poverty and 'set targets to reduce child poverty' (EAG, 2012a, pp.37-8). Child poverty-related indicators were also to be monitored in education, health, social inclusion, disability and quality of life.

The report said that a 30-40% reduction in child poverty was needed 'with even more ambitious targets for reducing severe and persistent child poverty'. Moreover, such targets should incorporate 'an accelerated rate of poverty reduction' for Māori and Pasifika so that they 'achieve parity ... with other children' (EAG, 2012a, p.38).

**Reflecting the background paper's belief in the value of paid work, there is little acknowledgement of the unpaid work of child-rearing and nurturing, and the opportunity costs of such care which often are only visible when someone else has to be paid to do it.**

Thus, it can be inferred for the purposes here that child poverty was to be reduced by the EAG's recommendations as measured on both the 50% and the 60% lines, and on other measures of deprivation, with particular and short-term urgency in addressing the severe and persistent child poverty that disproportionately affects Māori and Pasifika children.

#### *Select policy criteria and economic thinking*

Typically, criteria of cost-effectiveness, economic efficiency, equity and administrative simplicity are used in policy analysis. These have a normative content: the size of the trade-offs are not usually known with precision and normative positions tend to be adopted as to the importance of the trade-off costs.

Cost-effectiveness is the extent to which the policy objectives are met at least cost. A highly-targeted payment that lifts the poor families significantly

is cost-effective but some may argue that there are significant trade-offs, such as efficiency and administrative simplicity costs. In general, efficiency costs are perceived as lowered incentives to work, thus affecting economic growth.

The EAG acknowledged that fiscal constraints required cost-effectiveness, and that policy should have a good evidential base. It did not go to great lengths to examine the evidential base, namely how economic efficiency, requiring the minimisation of disincentives to work, was actually affected by various policy options.

The criterion of equity may be less important when the goal of policy is inherently to improve equity, but is worth having in its own right, encompassing as

it does notions of horizontal as well as vertical fairness. In terms of this exercise, vertical equity is fundamentally about improving child poverty. If one group is to get more, another group must get less in a purely distributional exercise; how much more and what groups should get less is a normative judgement. Horizontal equity, commonly taken as self-evident, requires that children in the same horizontal position be treated the same. If some poor children are treated less generously than others, a greater poverty of the former group can be inferred. The EAG did not discuss this aspect of equity or whether current policy was falling short in ensuring that obligations under UN Convention on the Rights of the Child were being met.

As is often the case in policy reforms, administrative simplicity is an underrated criterion and gets only a cursory mention in the background documents and in the final report.

Behind the development of any policy will be an implicit view of how the world works. Glimpses of theories or models that informed the EAG policy development can be found in the final report. These glimpses were informed by background paper 10, which takes a strong stance reflecting a profound belief that for almost all parents, including sole caregivers of very young children, paid work is the way out of poverty, that financial incentives matter, and that incentives are effective.

Raising benefit rates can be an effective strategy in reducing child poverty, but it can be costly and may reduce incentives for paid employment. (EAG, 2012a, p.31)

Reflecting the background paper's belief in the value of paid work, there

In spite of an acknowledgement that 'the In Work Tax Credit (IWTC) is one of the means government uses to reduce child poverty' (EAG, 2012a, p.26), there is an implicit belief that work incentives are effective, and that the reason the IWTC is denied to the poorest families has a rational basis:

IWTC-type arrangements are widespread across the OECD. Their attractiveness is that they encourage more parents into paid employment, and enhance equity by: raising incomes of children in low income working poor families, and addressing transport and childcare costs that non-working parents and nonparents do not face. (EAG, 2012c, p.26)

While acknowledging that 'Some see this reward only to children whose

of inequality in the pre-tax, pre-benefit distribution. For those countries, such as New Zealand, with more market income inequality, the tax and benefit system has to work harder to achieve distributional goals. Second, countries have widely different systems of in-kind provision, such as subsidised child care, health care and education. New Zealand has a high degree of user pays charges in these social services. For example, it is not uncommon for parents to pay over \$200 a week for day care for 3–4 year olds, even with the 20 hours' free subsidy. Third, countries differ in the way the tax system itself affects low-income people. So, in Australia, for example, the first \$18,000 of income is tax free and GST is only 10%, with exemptions to help the poor. This contrasts with the flattish tax structure and 15% GST with no exemptions in New Zealand.

Nevertheless, it would have been useful to ask how children are supported in Australia, for two reasons. First, we have a somewhat similar colonial heritage, and proximity. To be too far out of line with Australia on family policy would have to be based on sound reasons, especially in light of the current imbalance in the flow of young New Zealand families to Australia. Second, Australian child poverty problems are less severe and their child tax credits are given to all low-income children on the same basis, so there may be lessons to learn from policy design.

What is more surprising in the EAG report is the lack of analysis of existing New Zealand policies that aim to reduce child poverty. The complex mix of tax credits that make up Working for Families was announced in 2004 by the minister of social development, Steve Maharey, who claimed that they would deliver a child poverty outcome comparable to that of Scandinavian countries. On the 50% measure, he expected the rate of child poverty would fall from 14.7% to 4.3% by 2007 (Collins, 2005). So why not examine why, in spite of this programme, there was no such fall for these, the poorest children? In fact, Perry (2012) shows that the proportion under the 50% line remained at roughly 16% for the four years 2007–2011, after a slight fall from the early 2000s. Even using a stringent definition, the material deprivation of children actually

## The complex mix of tax credits that make up Working for Families was announced in 2004 by the minister of social development, Steve Maharey, who claimed that they would deliver a child poverty outlook comparable to that of Scandinavian countries.

is little acknowledgement of the unpaid work of child-rearing and nurturing, and the opportunity costs of such care which often are only visible when someone else has to be paid to do it.

Research indicates that a parent obtaining full-time paid employment with sufficient earnings is the most important event to lift children out of poverty. An adequate safety net is also required for those who are unable to work and to acknowledge the impact of economic conditions where jobs are scarce. (EAG, 2012a, p.38)

It is unlikely that the majority of the Expert Advisory Group members actually thought exhorting parents to full-time work was relevant to meeting the immediate needs of the 170,000 children in severe poverty.

parents are in employment and poor as discriminatory and hence undesirable' (EAG, 2012a, p.26), the counterargument is made that there are other highly discriminatory policies, such as paid parental leave and the policy to give child support pass-on to children supported by a sole parent on a benefit. But the fact that other policies also discriminate does not justify the exclusion of around 234,000 children from the IWTC, the aim of which includes child poverty reduction.

### *Assess a full range of policies that might achieve the objectives*

While the EAG had discussions with many overseas experts, it did not report on any detailed analysis of what works well in other countries. In general that was a wise decision, as international comparisons are fraught with danger, for three reasons. First, countries start with different degrees

increased, from 15% in 2007 to 21% in 2011 (Perry, 2012, pp.124, 166).

Specifically, by 2007 the Working for Families aim to reduce child poverty by 30% on the 60% measure and 70% on the 50% measure had clearly been ineffective for the very poorest. Bryan Perry, the Ministry of Social Development's leading poverty analyst, wrote: 'WFF had little impact on the poverty rates for children in workless households' (Perry, 2012, p.131). Why was this result not analysed, and is this the elephant in the room?

In light of the actual recommendations from the EAG, it would have been expected that the debate over universal versus targeted provisions, and especially why universal approaches work best for children, might have been a key discussion. The EAG relied heavily on the OECD's generalisation that countries with universal child support programmes achieved lower poverty rates. But this is not true of the United Kingdom, for example, and it would be simplistic to attribute New Zealand's lower poverty rates in the 1980s to the universal family benefit of the time. Universal payments that meet poverty objectives are expensive and require progressive taxation for fiscal sustainability. In a world of accelerating inequality and low tax, the arguments for a universal payment become harder to make. The section which discusses this issue reflects ambivalence in the report: 'Our recommendations include a mix of universal and targeted forms of assistance, depending on the policy context' (EAG, 2012a, p.32).

#### *Select and design the best policy; project expected costs and outcomes*

In selecting the policy recommendations the EAG was not given access to Treasury modelling capability, and there are few indications of serious costing and distributional analysis. The lack of costing is disturbing, given the intent to consider the fiscal constraints. Instead, there is a rough ballpark figure of \$1.5–2 billion for the policies set out in Box 1, suggesting that a dramatic fall in child poverty should have been the outcome. The EAG was a diverse group and did not reach a consensus agreement on several key aspects of what were the best policy choices.

#### *Evaluation*

The steps above suggest that after implementation, outcomes should be measured against the quantifiable objectives. Other steps that should be taken are to ask if there are unintended consequences; to evaluate policy against criteria; to confirm that the problems and the underlying economic model have been properly conceived; and to suggest improvements. By using this frame, there might have been some examination of current policies and their outcomes and unintended consequences, and a revisiting of the rationale of the underlying thinking.

In particular, a thorough examination of each part of the existing set of tax credits was required, including the family tax credit (FTC), the minimum family tax credit (MFTC), the IWTC and the

circumstances (ill health, or high housing or transport costs) that reduce their living standards (Perry, 2012, p.4). Conversely, there are some families below the income poverty line who may not be in hardship because of access to whānau support and other resources. It may also be that when families first come onto the benefit they have income from work as part of their annual income. As discussed in Perry (2012), children in families below the 50% poverty line are largely found in benefit-dependent families. The government had been told on many occasions of the degree of deprivation in this group. For example, a report for Ministry of Social Development in 2007 entitled Pockets of Significant Hardship raised alarm bells about some families who were falling below even the 40% line (Centre for Social

**... while Working for Families was of most benefit to 'working' families, two out of every five poor children are still found in such families. This suggests that Working for Families was necessary but not sufficient for all working poor families.**

parental tax credit (PTC) that make up the Working for Families package. What is the evidence that the work incentive aspects of the complex mix have achieved their objectives? Is each tax credit well designed? Are there problems not foreseen, such as the way the system fails to protect low-income children in a recession or natural disaster? What is the cost of each part of the package? What are the efficiency costs of, for example, the MFTC with 100% effective marginal tax rates? How many children and families get each part of the package? How are Māori and Pasifika children affected? Who misses out and why?

#### *Who are the poor children who need a solution?*

As Perry notes, there is not a perfect fit between the families in hardship and those below the conventional poverty lines: thus, some families with income above the poverty line may have special

Research and Evaluation, 2007).

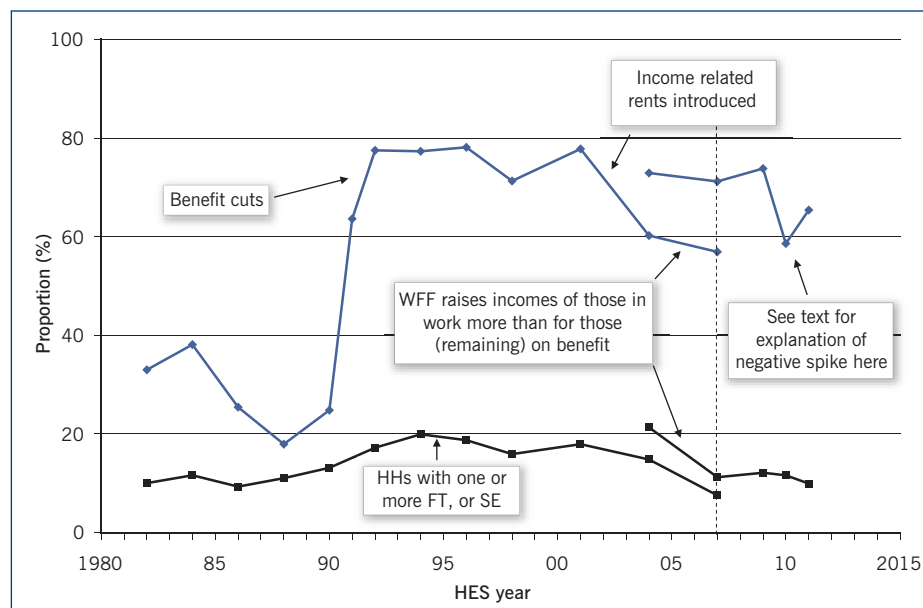
For the non-working poor, after the introduction of Working for Families child poverty rates became very much worse than for working families:

[C]hild poverty rates in workless households are consistently several times higher than those for children in working households (three to four times higher in 1992 to 2004, six to seven times higher from 2007 to 2011 after WFF). (Perry, 2012, p.131)

But while Working for Families was of most benefit to 'working' families, two out of every five poor children are still found in such families. This suggests that Working for Families was necessary but not sufficient for all working poor families:

the WFF impact was significant for this group, with the rate in 2007 (11%) half what it was in 2004 (22%); nevertheless, on average from 2007 to

**Figure 1: Poverty rates for children in 'workless' and 'working' households (after housing costs 60%, fixed line)**



Source: Perry, 2012, p.131

2011, around two in five (40%) poor children still came from working families – down from just over one in two (52%) in 2004 before WFF. (Perry, 2012, p.131)

We also know that the incidence of child poverty is much higher in larger families:

Children in households with three or more children generally have poverty rates considerably higher than those with only one or two children (e.g. 28% and 18% in 2011, and similar in 2007, 2009 and 2011). In 2011, children in these larger households made up just under half of all poor children (48%). (Perry, 2012, p.126)

However, this means that just over half of children in poverty are in one- or two-child families. Many of these families will have just one child under 5. We also know, and the EAG acknowledges, that young children are more likely to be in poverty (27% aged 0–11) than older children (22% aged 12–17) (p.5). But this is a slender difference and one that does not support the conclusion reached in Working Paper 10 that the assistance for older children should fall. This idea, based on the belief that all parents of older children are more able to work, was not explicit in the final report. Instead, the EAG says that the new child payment

should have the highest value during the first five years of a child's life, reduce as the child ages and be targeted based on family income from age 6 onwards (EAG, 2012a, p.41).

In December 2011, parents depending on a main benefit, including around 100,000 sole parents on the domestic purposes benefit (DPB), were caring for 234,600 children aged 0–18 years (Ministry of Social Development, 2012b, p.34). Of these children, 180,845 were cared for by DPB recipients (Children's Social Health Monitor, 2012, p.4). But we must not lose sight of the other 54,000 children supported on other benefits. The couple rates of unemployment, sickness and invalid's benefits are very low and do not make any allowance for children. This, combined with the harsh clawback rates on these benefits, suggests that these 54,000 children are likely to be at serious risk.

When full-time work is impossible, part-time work has the potential to improve a family's living standards. Some sole parents on the DPB have additional weekly income and it is fair to surmise that those families are probably better off as a result. But the number on the DPB declaring extra income is small, about 20,000 (Ministry of Social Development, 2012a) and the proportions have fallen, reflecting the harshness of the clawback provisions. Additional income

for beneficiaries is penalised on the presumption that full-time work is the only kind desirable, and part-time work should be discouraged. It is a weakness or omission that the EAG report did not consider such nuances around the levels, adequacy and clawback features of social welfare benefits.

To understand why child poverty is such a big problem it is important to study and reflect on the history of child poverty. While some data were given, this dimension is missing from the EAG report. Contemporary elements of this history are set out in Figure 1.

As Perry explains, child poverty rates in workless families were very high from 1992 to 2001 (after the benefit cuts) and were typically just under 80% using the after housing costs 60% fixed line measure (CV-98). The introduction of income-related rents was effective in reducing the child poverty rate from 2001 (78%) to 2004 (60%) for children in workless households. In the significant fall in the rate of child poverty in working families after Working for Families in 2005, the IWTC played a key role:

The fall in child poverty rates from 2004 to 2007 for children in one-F[ull]-T[ime]-one-workless 2P[arent] households was very large (28% to 9%), reflecting the WFF impact, especially through the In-work Tax Credit. (Perry, 2012, p.126)

In contrast, Perry notes, Working for Families 'had little impact on the poverty rates for children in workless households' (ibid., p.131). And we can take no comfort from the dip in the figure post-2008:

The significant drop in poverty rate for children in workless households from the 2009 to the 2010 HES is likely to reflect the fact that many of the 'new' beneficiaries came from employment, and although identified as 'workless' at the time of interview still had sufficient income in the 12 months prior to interview to keep the household above the poverty line. (ibid.)

To summarise: the 170,000 children below the 50% poverty line are in the worst poverty. At least one third of these

are in one-child families and half of all children in poverty are in one- or two-child families. In addition, it is clear that while working families were helped by Working for Families, about 100,000 of the 270,000 poor children are in 'working' families, i.e. families not on benefits. This suggests that even the full Working for Families package is not sufficient for their needs, and suggests caution in cutbacks, such as those set in train in the 2011 budget (discussed below). The EAG is silent on such current policy issues.

Much of the problem for working families is driven by high housing costs, suggesting that an important focus of the EAG should have been on housing costs. While quality of housing was considered in the report, there is little discussion of the costs of housing. The role of the accommodation supplement is lightly touched on with vague recommendations (little more is said in the relevant section in Working Paper 18).

#### **The EAG's recommendations: do they achieve the objectives?**

The major recommendation of the EAG final report was to align the maximum rates of the family tax credit for all children, as set out in Box 1. The EAG suggested that that would give on average another \$17 per week per child. The one-child families who currently get an FTC of \$92.70 would gain only another \$9.25 a week. Given that 50% of approximately 100,000 sole parents on the DPB have only one child (Ministry of Social Development, 2012a), at least 50,000 of the poorest children would get minimal immediate help. While some focused help from the EAG might be at hand from the \$10 per child pass-on of child support, this recommendation does not provide extra for all children and, besides, the recent amendment of the Child Support Act has ruled out any pass-on.

Because the FTC rate increases would be paid to families on higher incomes it is also an expensive policy. For example, a five-child family with children under 13 on around \$121,000 of household income is currently entitled to no FTC (but is still getting \$90 from the IWTC per week). The FTC for this family would increase to around \$160 a week. This is

probably desirable, as New Zealand is well behind Australia in helping higher-income families with young children, but this expenditure on higher-income families would not have an impact on child poverty.

The paying of more to families well up the income scale also flies in the face of political reality. As mentioned, budget changes in 2011 have already set in train a series of automatic changes out to 2016 which reduce the generosity of Working for Families for all families above \$35,000 of total income.

The elephant in the room is the IWTC. What is the function of this payment? At the high cost of \$592 million per annum (about 21% of total Working for Families tax credits), is it fulfilling its objectives of incentivising work which necessitate

would be 'achieved by pooling the current family-focused benefits and tax credits' (EAG, 2012a, p.41). Background paper 10 reveals that the IWTC was omitted in this amalgamation, however, and would presumably remain. The new child payment would have the highest value during the first year of a child's life and reduce as the child ages and be targeted on family income from age 6 onward.

The EAG say that a universal payment would 'give proportionally more to children in poorer families, while recognising that all parents with young children face significant costs', and 'be simple and transparent, with relatively low transaction and compliance costs and have virtually 100 percent take-up from birth' (p.41). These justifications for such a universal approach for all children

**Ominously, the EAG suggest that the child payment could replace a number of existing child and family supports ... [and if] the IWTC is included, many of the poorest will get little if any more than they currently get, but with the possibility of getting less in childcare subsidy as well.**

it being paid so far up the income scale while its child poverty-reducing benefits are denied to the poorest children?

The EAG's second main proposal was to 'subsequently and incrementally' raise the rates further for children aged 0–5 years inclusive (EAG, 2012a, p.39). At the very least this proposal requires a detailed analysis of how current policies are inadequate. Currently, neither paid parental leave nor the parental tax credit work well for the poorest children, or for many other newborns for that matter (St John and Familton, 2011). Here, as in other parts of the system, New Zealand is well behind the inclusive approach taken in Australia, where all newborns are assisted either by a much more inclusive and generous parental leave payment or by a baby bonus of \$5000.

In the longer term, the EAG suggested a fully universal child payment for children aged 0–5 years inclusive. This

under 6 are weak if the objective of child poverty is kept in mind. Logically, if these children aged under six are to be helped only by a universal payment, unless the payment is set higher than current levels there will be no impact on child poverty. But a third of all children are under the age of 6, so to pay each of them even only what is currently provided in the full Working for Families package would very expensive. To give each of them an average of \$7,000 a year would cost \$2.4 billion, nearly the whole of the current cost of Working for Families.

Ominously, the EAG suggest that the child payment could replace a number of existing child and family supports, including the FTC, the MFTC, the PTC and the childcare subsidy. If the IWTC is included, many of the poorest will get little if any more than they currently get, but with the possibility of getting less in childcare subsidy as well. On the other

hand, if the IWTC is not included in the wrap-up (and it appears not to be), higher-income working families would be over-compensated. A much stronger, more realistic case could have been made for a universal payment for just the first year of a child's life, where all child subsidies, including childcare, the PTC, FTC, IWTC and tax-funded paid parental leave, are amalgamated to give a payment of a significant amount.

The EAG recognised the problems with the IWTC – ‘We recommend that the government reform the In-Work Tax Credit (IWTC) to better assist families in poverty’ (p.41) – and lists some possible options:

- 1 amalgamating the IWTC with other in-work credits and redistributing the available funding to low-income families with children;

## ... the declaration that ‘Every child in New Zealand has the right and should have the opportunity to grow up without experiencing severe or persistent material deprivation’ (p.8), the EAG’s specific recommendations on income support fall far short.

- 2 making the payment larger, but abating the assistance more quickly to ensure those with the lowest in-work family incomes benefit most;
- 3 altering the work-hours test and thresholds; making the value of assistance more closely related to the number of children;
- 4 having a time-limited IWTC to assist the initial transition to work (e.g. for six to 12 months).

Unfortunately, there is no guidance or distributional analysis or costing of any of these options. Some of them would transform the very nature of this very significant poverty alleviation measure. First, the amalgamation of the IWTC with other ‘in-work credits’ is hard to fathom. There is no discussion of these other in-work tax credits. Those with a work focus are the very minor PTC and MFTC, neither of which is explained in the report. Missing here is the important

possible amalgamation of the IWTC with the FTC which would be highly redistributive and have an immediate impact on the worst child poverty. Perhaps this is not an option because, as the EAG believed:

While such a change would increase the incomes of many families in greatest need, it would no longer provide an incentive and support for families moving from welfare benefits to low-paid work to help ‘make work pay’. (EAG, 2012a, p.41)

Second, making the IWTC larger without analysis of who gets it obscures the result that it would simply go far further up the income scale. Already it is questionable that high-income families, for whom the IWTC is abated last, actually need a work incentive. Third, altering the

work-hours test and thresholds displays a misunderstanding of the IWTC: the tax credit does not have a separate family income test, as background paper 10 (p.16) suggested; rather, there is a test that a family has to be off-benefit. Making the IWTC more closely relate to the number of children is a concession that, rather than being a work incentive, this is a payment for children. Fourth, a time-limited IWTC to ease the transition to work would cost a tiny fraction of the existing cost of the IWTC, and, while a completely different approach, may be a much more sensible one to providing a work incentive.

### Discussion

The EAG placed a good deal of emphasis on public consultation, and highlights this comment in the discussion of taxes and benefits: ‘Surely it’s not too hard to see that an overhaul of our taxation/wage system is long overdue’ (EAG, 2012a, p.39).

Exhortations to overhaul the taxation/wage system, to have an independent review of all tax credits for children, and to put children at the centre of social security legislation ring hollow in the absence of explaining to government exactly how its tax credits and income policy currently fail to put the best interests of children first. For example, Working for Families puts paid work at the centre and excludes from a large part the very target group the EAG is concerned about. Also, current policies for the income support of newborns are woefully exclusive and work very badly for many of the poorest families.

The EAG was very concerned about take-up rates of all benefits, including the in-work payments, noting the difficulty many families had in negotiating the complex maze. Was the complexity of the system necessary to deliver the objectives of Working for Families? If not, the current situation is very serious indeed.

[R]espondents emphasised that, because accessing information about benefits and income support is not straightforward and, once accessed, difficult to interpret, many families need assistance to determine what their child and family may be entitled to receive. (EAG, 2012a, p.40)

There is no analysis of current policy on indexation provisions: for example, a group of poor working families on around the minimum wage get less over time as the threshold of abatement is reduced to \$35,000 by 2016 from \$36,875 in 2011, and the rate of abatement increased from 20% to 25%. Also, Working for Families is indexed only to prices and only when cumulative inflation exceeds 5%. Making no mention of current policy makes it difficult for anyone to understand what new changes the EAG is proposing:

We recommend that the government index all child-related income support, benefits and tax credits to ensure support keeps pace with productivity growth in the broader economy. (EAG, 2012a, p.40)

Finally, covering itself for not having completed the job it was challenged to do, it says:

We recommend that the government commission an independent and comprehensive review of all child-related benefit rates and relativities, with a primary goal to reduce child poverty (EAG, 2012a, p40).

Looking at the adequacy of benefits is clearly important, given that 60% of children in poverty are in families on benefits, many below the 50% line. Unfortunately, for the EAG, like the Tax Working Group and the Welfare Working Group before them, it fell into the too-hard basket. Exhorting government to do this job, the EAG itself gave no direction. Neither could it resist making sure that the work solution to child poverty was a substantial qualifier to any review:

There has been no assessment of the value of welfare benefits in real terms for several decades, nor of their relationship to tax credits such as in-work payments. These ought to be reviewed both from an income support perspective, and in terms of encouraging gainful parental employment that is effective in reducing child poverty and meeting children's developmental needs. (EAG, 2012a, p.41)

## Conclusion

Against the criteria of cost-effectiveness, requirement to have an evidential basis, and account taken of the economic and fiscal context, and the declaration that 'Every child in New Zealand has the

right and should have the opportunity to grow up without experiencing severe or persistent material deprivation' (p.8), the EAG's specific recommendations on income support fall far short.

The proposals fail to give many poor children the significant income boost that is needed. The poverty relief achieved is expected to be seen largely in big, younger families, but the mechanism chosen is not cost-effective in terms of the policy objectives and the need to remember the fiscal constraints. The outcomes for Māori and Pasifika are not assessed. Getting value for money in a tight economic climate means taking a look at the evidential base of what is done currently, careful analysis of what is and what is not working, including all tax credits and paid parental leave, and making suggestions that will actually lift the 170,000 poorest children significantly above the 50% poverty line. Previous independent and detailed analysis, such as St John (2011), St John and Dale (2012) and St John and Craig (2004), were ignored.

The EAG cited material from Perry (2012) which suggested that a couple with two children on 50% of median household income would need an extra \$100 per week to be lifted to the 60% line. This gives some indication of the scale of redistribution needed. The EAG estimated that the implementation of their recommendations would cost around \$1.5–2 billion (EAG, 2012a, p.33), so a demonstrable significant alleviation of the hardship of our most vulnerable children

should at the very least have been the outcome. Instead, the recommendations of the EAG further entrench the relative poverty of the 170,000 poorest children, as did Working for Families, by not offering them a politically realistic and cost-effective solution, and by not addressing the human rights implications of continuing to deny them a significant child poverty alleviation measure, the IWTC.

The setting up of an independent panel of experts, at arm's length from the government, through the Office of the Children's Commissioner had the potential to make some real progress towards fixing the problem of child poverty. The EAG achieved a significant body of work and made a range of thoughtful recommendations in many areas. There are numerous political and other aspects that have not been explored here, such as who was chosen to be on the group and why, what contribution was made by each member to the whole, and how has the final report and its recommendations been received and what is the likelihood of them being enacted. Any exercise like this is enormously costly in time and energy for those involved, and this article salutes all the individuals who contributed so much. Virtually all members were unpaid, and the EAG budget was inadequate for the seriousness of the issues they were expected to address. It is also acknowledged that even perfect recommendations require the fertile ground of political receptivity for there to be real progress.

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Simon Chapple

# Forward Liability and Welfare Reform in New Zealand

In November 2012, Gabriel Makhlof, the secretary to the Treasury, gave a wide-ranging speech to the Trans-Tasman Business Circle which discussed, among other things, recent reforms in the welfare system. He described the new ‘investment approach’ as a significant change to the New Zealand welfare system, which he suggested would effectively get people back into work, reduce poverty and increase living standards. The overarching welfare reforms announced and being implemented by the current government are in large part constructed around this investment approach, which provides a central policy narrative to the reforms. The centrality of the investment approach is expressed via the operational use of a measure of what is variously termed

‘forward liability’, ‘future liability’ or ‘long-term liability’ of the welfare system as the key performance management tool for Work and Income. Forward liability (the term exclusively used here) is basically the total current and future fiscal costs of welfare, appropriately discounted.

Makhlof is correct in his assessment that the investment approach marks a significant departure in terms of performance management for the New Zealand welfare system. The purpose of this article is to critically examine the new model and its likely effectiveness, with a view to better understanding its strengths and its weaknesses. The perspective taken is one of mainstream public economics and labour economics.

## **The origins of the investment approach**

The investment approach has a long genesis. One source is a paper written by Rob Brown and Helene Quilter of the then Department of Social Welfare for the 1997 Beyond Dependency conference (Brown and Quilter, 1997). This paper contains both the strengths and weaknesses of the investment approach as it has more recently emerged. Having identified

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the policy problem as the growth in welfare benefit dependency, Brown and Quilter argued for a forward-looking and intertemporal vision of the welfare system as the basis for finding effective policy solutions. This vision was described as the 'new approach', and was outlined fairly briefly. The approach involved acknowledging the 'fiscal, economic and social costs of long term dependency' and hence concluding that '[policy] initiatives must be seen as investments against the future costs'. Welfare dependency needed to be conceptualised as a future contingent liability on the government: 'We need new models and disciplines', Brown and Quilter write, 'that borrow concepts from finance and accounting, something akin to a balance sheet, to recognise that long-term dependency is a cost which will fall to future tax-payers' (Brown and Quilter, 1997, p.46). Critical to understanding the investment approach is this lineage in accounting rather than economic concepts of costs.

In 2010 the National-led coalition established a Welfare Working Group to undertake a fundamental review of New Zealand's welfare system. The main explicit task of the group was to identify how to reduce long-term welfare dependency, a very similar problem to that addressed by the Beyond Dependency conference. One of the terms of reference of the review was a consideration of 'How welfare should be funded, and whether there are things that can be learned from the insurance industry and ACC in terms of managing Government's forward liability' (Welfare Working Group, 2011, p.36). There is a clear echo here of Brown and Quilter, but also the suggestion that the corporatised ACC forward liability funding model, developed in part to set ACC premiums, had been successful, and had similar applicability to welfare.

The final Welfare Working Group report made a number of recommendations regarding the desirability of an investment-based approach. The report defines forward liability as 'The expected costs associated with an individual being in the welfare system over their working life', and proceeds to argue that 'The welfare system needs to recognise the value of investing early to

reduce the long-term social, economic and fiscal costs of welfare dependency. Adopting an actuarial approach to measuring the forward liability will therefore be an important feature of any reform' (Welfare Working Group, 2011, pp.vii, 2). The report proposed that the welfare agency would 'be held accountable for improving work outcomes for people of working age at risk of long-term welfare dependency and reducing the long-term costs of welfare dependency (as measured by the forward liability)'.

Thus, forward liability would become a key plank in the performance management system:

The use of forward liability and the independence of the delivery agency are the key mitigation strategies. These ensure the delivery agency is incentivised to focus on investing to reduce long-term cost and has the operational independence to implement the new welfare system. (ibid., pp.17-18)

The Welfare Working Group took the view that there was a one-to-one relationship between enhancing employment and reductions in forward liability, recommending that:

employment support and programmes be rigorously selected on the basis of improving employment outcomes and therefore reducing long-term cost (the forward liability), and expenditure be continually re-directed to programmes that are most effective in meeting this objective. (ibid., p.25)

Of the twin strategic planks of forward liability performance management and independence of operation of the welfare agency along ACC lines, only the former reform was in the end adopted by government.

Following the recommendations of the Welfare Working Group, Taylor Fry, an Australian actuarial firm, was asked by the Ministry of Social Development (MSD) and the Treasury to assess the feasibility of adopting this long-term investment approach to achieving better employment, social and financial outcomes and to set out how aggregate future liability would be calculated. Rather than considering employment and social gains from moving a person off benefit, Taylor Fry's response to the brief

## In economic terms, the fiscal costs of welfare benefits are simply distributional transfers from taxpayers to benefit receivers.

was to focus on developing a model measuring only future fiscal liability of people being on a benefit (Taylor Fry, 2011). Their discussion proceeds as if reducing the forward fiscal liability and maximising employment and social outcomes were synonymous activities (Taylor Fry, 2011, e.g. pp.3, 8, 13). No discussion is entered into of issues underlying this very strong and indeed critical presumption. The best way of maximising employment and social outcomes is simply taken to be minimisation of the forward liability.

### What does forward liability measure?

At the cost of some generalisation, the forward liability defined by Taylor Fry is primarily the discounted expected future value of government benefit payments. But these fiscal accounting costs are not the economic costs of raising money to fund welfare. It is the deadweight costs of taxation, typically in New Zealand taken to be 20 cents in the dollar, that are the true economic costs, a point well made elsewhere by the Treasury (New Zealand Treasury, 2005).

In economic terms, the fiscal costs of welfare benefits are simply distributional transfers from taxpayers to benefit receivers. This redistribution, which may be considered desirable or undesirable partly depending on one's distributional

value judgements, is not an economic cost as conventionally considered.

Thus, the fiscal focus of the forward liability approach amounts to a performance model focused on achieving a particular target for the intertemporal redistribution of income by the benefit system between beneficiaries on one hand, and other taxpayers on the other. Achieving the forward liability target may have positive or negative consequences on other outcomes, such as employment, poverty or living standards, but these outcomes are merely derivative, since the welfare agency is not tasked to improve these outcomes, let alone optimise them.

### **... many of the recent problems bedevilling the ACC system have involved reductions in long-term liability – the performance target – achieved by the agent running down the unobserved long-term asset of ACC income-related payments.**

#### **Forward liability and consideration of the other balance sheet components**

In the standard private sector accounting model, the balance sheet approach equates assets to liabilities plus equity. The aim of a profit-maximising enterprise is generally taken to be managing the enterprise's assets and liabilities so as to maximise equity – the difference between the two. Applying this to the welfare system suggests that the reform has not explicitly addressed measuring the corresponding intertemporal asset in the welfare system. Indeed, what would be the point of New Zealand as a society holding a forward liability in the welfare system if there was not a corresponding asset associated with it?

It is a useful exercise to ask what the components of the asset corresponding to the forward liability might be. Current and future benefit payments are part of that forward asset, since they comprise the income protection which the system is intended to deliver. The question then is how to value these intertemporal benefits. It is generally accepted that on average a dollar paid to a beneficiary will generate

higher marginal utility of income than a dollar to the average taxpayer, since the average beneficiary is poorer than the average taxpayer (Fujiwara, 2010). This declining marginal utility of income would make the forward asset larger than the forward liability. In addition, another part of the intertemporal asset is the psychological gains to those not in the system of knowing that there is a welfare benefit to fall back on should they not find work, fall sick, or separate with responsibility for a child. Finally, there may be utility generally gained from citizens living in a society which they perceive as more socially just. The net

difference between the forward assets and the forward liability might reasonably be described as the forward equity of the welfare system. Given the considerations outlined above, net social equity would likely be positive.

If neither the forward equity nor the assets of the welfare system are measured by a performance management system, any agent (welfare agency) which is set a forward liability target by the principal (government) will be indifferent as to whether this performance goal is achieved via reduction of the forward asset, arguably the undesirable outcome, or an increase in the forward equity, arguably the desirable outcome. For example, policies which reduce the take-up of welfare benefits by those who remain eligible for a payment are likely to reduce the forward asset more than the forward liability. Yet in a system where only forward liability is used for performance management, achievements by the agent in dissuading legitimate benefit claimants by various administrative or other means will be seen as successful business behaviour.

Arguably, many of the recent problems bedevilling the ACC system have involved reductions in long-term liability – the performance target – achieved by the agent running down the unobserved long-term asset of ACC income-related payments. The political and media voice exercised by aggrieved former ACC clients who have suffered from the removal of this asset has ultimately reflected asset erosion information back to the centre, creating a significant political scandal. It is worth noting that these feedback loops regarding asset erosion resulting from simply managing forward liability are likely to be weaker for the welfare system than in ACC, since an informed middle-class voice is likely to be stronger for ACC payments than for welfare beneficiaries.

#### **Forward liability and measurement error**

There are further problems with forward liability as a performance management tool. These problems revolve around the noise-to-signal ratio in the forward liability measure. Changes in forward liability are measured with significant uncertainty and error. They are primarily affected, but to an uncertain extent, by social and economic factors outside the control of the welfare agency, and are dependent on a wide variety of debatable accounting assumptions. These inherent uncertainties around the measure of forward liability create a signal extraction problem for the principal (in this case the newly-created Welfare Board supervising Work and Income). To what extent is any given change in forward liability a consequence of the actions of the welfare agency, of measurement error, or of the broader social and economic context which drives the bulk of observed changes in forward liability? There is no experimental counterfactual available regarding the forward liability effects of an alternative pattern of actions by the welfare agency.

As an additional consequence of this fundamental uncertainty, there are strong incentives on the part of the agent – in this case Work and Income – to devote considerable resources to litigating changes in forward liability, claiming credit for the gains and distributing blame for the increases outside the system.

The principal will then need to devote significant resources to this litigation process. These problems seriously weaken the utility of the forward liability measure as a central tool for performance management, even on its own terms.

#### **Forward liability and employment**

If welfare reform is intended to generate additional transitions from benefits into employment, the question needs to be addressed of whether reductions in forward liability will lead to not simply enhanced but optimal employment outcomes, as Taylor Fry's report believes. Is a reduction in forward liability a good proxy for a positive employment outcome? The answer is no.

Movement by people off a welfare benefit may occur for non-employment reasons, including to re-partner, emigrate, move into further education, go to prison, or move into the black or grey economy (employment transitions into the grey or black economy are considered here, realistically, to be undesirable outcomes). Equally, people may not enter the benefit system, despite becoming eligible through a lack of employment, because of stigmatisation, lack of information regarding entitlement, dissuasion by high transactions costs and system complexity, or through mental health difficulties or cognitive problems.

Finally, even if gaining employment and moving off benefit could be mapped onto each other in a one-on-one fashion, the proposed forward liability model values all employment gains as equal to the dollar reduction in benefit payments arising from benefit exit. That is to say, the forward liability model values the additional earnings that people make, and any other positive (or negative) consequences of these earnings and work, including for their families and children, at zero. If positive employment outcomes are valued at zero, then the agent has a strong incentive to rationally under-invest in positive outcomes, compared to all the other reasons for a reduction in the number of people on a benefit.

International experience of policy changes which have been evaluated as raising the exit rate from unemployment benefits, hence involving reduction in

forward liability, in the New Zealand context, have been shown to not generate a positive employment outcome. For example, in the United Kingdom, both Manning (2009) and Petronglo (2009) show that the introduction of the 1996 job seeker allowance reform involved higher unemployment benefit exit, but at the same time failed to move those people into employment.

#### **Long-term benefit dependency and forward liability**

The stated policy problem addressed by the 2010 Welfare Working Group was long-term benefit dependency; their report was actually entitled Reducing Long-Term Benefit Dependency. There is consequently a huge puzzle at the heart of

intertemporal net fiscal savings is to place more resources into choking off benefit inflows, thus leading to a rise in both relative and absolute long-term benefit dependency.

So why spend a lot of money and time developing a forward liability performance measure which bears an uncertain and sometimes perverse relationship to the asserted, readily- and cheaply-observed ultimate target of long-term beneficiaries? The first best option, surely, is to manage performance via a long-term benefit dependency reduction target.

There are two plausible explanations for the failure to develop a performance management system around the share of long-term beneficiaries: a lack of

## **Long-term benefit dependency can be directly measured from current welfare records in almost real time, with great accuracy and at minimal additional cost.**

the group's performance management and welfare reform recommendations. Long-term benefit dependency can be directly measured from current welfare records in almost real time, with great accuracy and at minimal additional cost. Forward liability, on the other hand, requires considerable expensive actuarial resources to produce millions of dollars, cannot be measured in anything like real time (the proposal is to produce it annually) and contains a high and uncertain amount of noise in relation to the ultimate measure, long-term benefit dependency.

Additionally, achieving a forward liability target may or may not involve reducing long-term benefit dependence. The low-hanging fruit for achieving a forward liability reduction are those which offer the biggest net fiscal saving. Long-term beneficiaries offer a gross fiscal saving. While benefit savings from moving them off benefit are considerable, the fiscal cost is also very high. It is quite conceivable that the optimal strategy for reducing forward liability and generating

analytical rigour on the part of the working group, or pursuit of an agenda which actually has little to do with aiding long-term beneficiaries.

#### **Cost-benefit analysis: the alternative investment model**

If an intertemporal approach to effective resource allocation in the welfare system is taken to be relevant, the most obvious investment model is not the accountants' or actuaries' forward liability model. Rather, it is the very standard economists' cost-benefit approach. Such an approach is laid out in the Treasury's cost-benefit primer (New Zealand Treasury, 2005) and in terms of social cost-benefit analysis of employment programmes by Fujiwara (2010). A similar approach is deployed empirically in the context of optimal investment in active labour market programmes in Denmark by Jespersen, Munch and Skipper (2004). Such an approach allows a coherent, rational consideration of economic and social gains from placing people off-benefit and into work.

If such a cost-benefit analysis approach is taken, then the discounted stream of forward employment benefits, incorporating all benefits (and costs) to the person and to society from getting someone working, from each available labour market programme should be compared with a specified cost, again appropriately discounted if it has an intertemporal dimension. Each person on a benefit will have the active employment programme allocated to them which leads to the highest discounted stream of net benefits.<sup>1</sup> Each person on welfare would then be ranked from those generating the highest to those generating the lowest net

enables examination of post-programme monthly PAYE earnings over time, with information currently available on a lag of about one year (this lag may feasibly be shortened to about three months). In addition, the IDI provides information on programmes and a means of assessing whether benefit payments decline as a consequence of such programmes. Treasury work on the efficiency costs of taxation allows an estimation of the efficiency gains from reductions in benefit payments. Future developments in the IDI will allow integration of justice and health data, so these outcomes can be factored into the cost-benefit calculation.

is on the programme (\$15,000), being \$35,000 in total. Since liability is \$5,000 higher if the programme is undertaken, no investment will take place.

Now consider the same decision under a cost-benefit analysis. The cost of the programme is the cost of the training programme plus the deadweight tax costs of funding it. Thus total costs are \$24,000. The benefits from the programme are the \$30,000 gross earnings in year two plus the reduction in taxation deadweight from not having to pay welfare in year two (20% of \$15,000). Total benefits are \$33,000. Consequently, net benefits from the programme are \$9,000, meaning, contrary to the forward liability model, investing in the training is efficient.

The forward liability model values a reduction in welfare benefits of one dollar at a dollar, while the cost-benefit analysis values it at 20 cents. The cost-benefit model values one dollar of earnings at a dollar, while the forward liability model values earnings at zero. Consequently, the forward liability model means a greater investment in reducing benefit payments and less investment in obtaining positive employment outcomes. It is scarcely necessary to point out this oddity in a model which is supposed to have an employment focus. Of course, there will be cases where both models draw the same conclusion about investment, but, generally, an optimal investment decision will differ considerably due to valuation differences.

## The forward liability model values a reduction in welfare benefits of one dollar at a dollar, while the cost-benefit analysis values it at 20 cents.

benefits from the particular programme which is most beneficial to them. Total funding available for active employment programmes would then be allocated according to this ranking, starting by funding investment in the person with the highest net benefit. Funding would be allocated until the prior allocated fund runs out, or all programmes giving positive benefits are funded, whichever is the first. If the allocated fund still leaves a margin of people on welfare for whom net benefits are positive, then funding can be increased in the following budget round. Equity weights can readily be included.

The information requirements for doing cost-benefit analysis perfectly are in excess of what is currently feasible. However, it is useful to set out this ideal, in order to examine the extent to which the forward liability actuarial approach is a step in the right direction towards such a model, and how that model might be amended or supplemented to push it further in the right direction.

Can a cost-benefit approach be employed in practice which approaches more closely over time the ideal outlined above? The answer is yes. Statistics New Zealand's integrated data initiative (IDI)

A cost-benefit analysis is the economists' preferred investment model. As is well known, economic costs and benefits are not equal to an accountant's costs and benefits, which underpin the forward liability model. But does the difference actually matter in practice for decision making?

Consider a simple example where there is a successful training intervention which takes one year to complete and costs \$20,000. People then go off benefit for annual earnings of \$30,000. Assume, for illustrative ease, that there are only two years to be considered and there is no discount rate. The annual welfare benefit is \$15,000. The deadweight cost of taxation is 20%.

In this simple example, an agent making an investment allocation under a forward liability performance measure would not invest in the training programme. On the other hand, a rational resource allocation made using a cost-benefit analysis would lead one to invest in the programme. The forward liability without the programme spending is the sum of benefits paid in the two years, or \$30,000. If the programme goes ahead, the new liability is the cost of the programme (\$20,000) plus the benefit paid in year one when the beneficiary

### Arguments defending the forward liability approach

One argument which has been offered in support of the liability model is that while acknowledging that the model is imperfect, as indeed all approaches to performance management are, the performance of Work and Income has been so poor for long-term beneficiaries that the new model will bring huge improvements. A variation on this thesis is that MSD has overly focused on easier-to-place unemployment beneficiaries, ignoring other beneficiaries because they need higher investment to shift them off benefit. It is worth noting, however, that the recent State Services Commission performance improvement framework

(PIF) assessment is glowing in its praise for the performance of the ministry, and does not criticise it on these dimensions.

The responses to those arguments are fairly straightforward. First, there is no need for an actuarial model of liability to shift the focus onto long-term or non-unemployment beneficiaries. As already pointed out, these groups are easily observed in the existing data. Second, the actuarial model will in any case produce the wrong set of interventions and for the wrong people since it fails to value employment and social outcomes of interventions in a rational fashion. Third, there is a current, well-developed mechanism for ministers to set priorities for MSD in the standard statement of intent system. There is no suggestion anywhere in the State Services Commission's PIF assessment of any fundamental problems here as regards MSD. On the face of it, the liability solution is being offered up to address a non-existent problem.

#### **An alternative performance management framework**

It is worth sketching out an alternative performance management framework to forward liability, one which could readily be incorporated into the existing MSD statement of intent. The starting point for consideration of the welfare system must be that it has multiple strategic performance objectives, and that it seeks both equity and efficiency goals. Consequently, it is not a system which can be readily managed by an overriding, unitary performance framework like forward liability.

The two main strategic objectives of welfare are paying adequate benefits to those eligible for them and supporting transitions off benefit into sustainable employment. Assignment theory suggests that two performance goals means that at least two broad performance measures should be imposed on the agent by the principal. In terms of paying benefits to those eligible, there is a need for performance measures based on non-take-up of benefits. In this regard, it is noteworthy that the Department of Work and Pensions in the United Kingdom has published take-up by person and

by expenditure amounts by benefit type since 1997. Overseas evidence suggests that non-take-up is a major issue for welfare systems (Hernanz et al., 2004). It is unfortunate that no regular non-take-up tax-benefit information is produced in New Zealand.

There is also a need to judge systemic performance by measures of over- and underpayments, as well as compliance with benefit conditions such as job search requirements and not living with a partner if on a sole-parent benefit. New Zealand evidence shows that overpayments and underpayments to those on benefit and non-compliance with benefit eligibility

people who welfare records showed were receiving a domestic purposes benefit self-reported that they were partnered or living as married (Chapple and Crichton, 2012). Again, these numbers are suggestive of considerable systemic underperformance.

Thus, the key performance measurement areas should be underpayments, overpayments and benefit take-up, with the performance aim being to minimise the first two and maximise the last.

The performance of the employment service in generating work can follow the approach outlined in Nunn, Bickerstaffe and Mitchell (2009) and use long-term

## **In the long term, policy makers need to set their sights higher than simply incentivising employment programme performance in terms of earnings outcomes.**

conditions may be significant systemic issues. In path-breaking work based on representative surveys of beneficiaries, Meimand (1997) reported that 13% of beneficiaries were overpaid and 3% were underpaid during the 1996-1997 year. The annual net overpayment was \$195-219 million. Updating this figure for consumer price inflation and the 2012 number of beneficiaries gives a rough current annual figure for benefit overpayment of between \$275 and \$300 million. Extraordinarily, this pioneering study was never updated to regularly assess changes in welfare system performance. Work undertaken by the Department of Labour and based on matching Household Labour Force Survey and administrative welfare records showed that in 2011: 1) about 10% of people who welfare records showed receiving an unemployment benefit reported to the Household Labour Force Survey that they were actually in full-time employment (30 plus hours per week), and hence were ineligible for the benefit; 2) more than a third of people on an unemployment benefit self-reported that they were not actively seeking work, and one in five expressed no intention to seek work in the coming year; 3) about 10% of

measures of monthly PAYE earnings as a measure of welfare attributable to employment services, increasingly augmenting this with a consideration of impacts on broader social outcomes, within a cost-benefit framework.

#### **The policy process behind the liability model**

That major welfare reforms have been undertaken which include basic flaws in problem identification, design of performance management indicators, and in understanding of core economic concepts is concerning. One would have expected these issues to have been picked up by senior Treasury and State Services Commission officials as part of a robust internal policy advice process. Equally, the Taylor Fry actuarial report does not seem to have been sent out by the Treasury to external peer reviewers, including people with a public economics and labour market economics background, which seems a significant oversight. It is difficult to see how someone with an understanding of Treasury's cost-benefit primer or the mainstream public economics which underpins that document would have arrived at the forward liability performance model.

Equally, the interdepartmental policy process must also bear some of the responsibility. Despite the (then) Department of Labour being the government's primary adviser on employment policy, and the fact that welfare reform was generally and explicitly understood to be about getting beneficiaries into work, the political arm of government decided that the Department of Labour had no central role to play in the policy development and advice process on welfare reform. Despite this exclusion, the Department of Labour had an independent opportunity to offer free and frank advice and point out known weaknesses in the forward liability model in their 2011 briefing to the incoming minister. They did not take the opportunity to offer their advice on this issue at that point.

Finally, significant questions must be asked of the problem identification through the PIF process managed through the State Services Commission, the Treasury and the Department of the Prime Minister and Cabinet. When that process fails to identify any significant performance management issues with MSD at the same time as the same arms of government implement radical changes to MSD's performance management system,

this further suggests some substantial within-agency issues.

#### Conclusion

There are many problematic aspects of the forward liability investment model which is being applied in the welfare system. The problem definition surrounding welfare reform and the performance management approach of MSD has been poor, the forward liability solution has not been carefully unpicked, and reasonable alternatives to this model have not been acknowledged, let alone examined in detail.

Arguably, the welfare system does need much better, independent and regularly-collected indicators of performance in terms of benefit take-up, underpayments and overpayments, and compliance with benefit conditions, as well as cost-benefit indicators of the effectiveness of programmes in generating better employment and earnings outcomes. But forward liability – fundamentally a measure of intertemporal income redistribution – is neither a relevant nor reliable indicator in that context. At best, it is no more than an expensive and partial cul-de-sac.

In the long term, policy makers need to set their sights higher than simply

incentivising employment programme performance in terms of earnings outcomes. They need to value, measure and reward operational solutions which directly involve better social outcomes for getting people off benefits and into work – better outcomes not simply for parents, but for their children also, as well as wider society. Again, only if these broader outcomes are explicitly measured and valued will an intertemporal investment approach have any chance to deliver these better outcomes. Only then will Makhlouf's claims that an investment approach will reduce poverty and improve living standards have operational, as opposed to rhetorical, content.

<sup>1</sup> See Behncke, Frölich and Lechner (2009), Mitnik (2007) and Frölich (2008) for models of allocation of programmes to those with socio-demographic characteristics predicting programme effectiveness. Such allocation models have been used in practice in the employment programme area.

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Máire Dwyer

# Social protection in Vanuatu and the Solomon Islands

A decade ago the idea that governments and international agencies would support development policies that provided regular and reliable transfers to those in poverty would have been seen as most improbable ... With minimal fanfare social protection has moved onto national and international policy agendas. (Barrientos and Hume, 2008)

Social protection programmes – that is, those which address access to health, education and other basic services, and protect or replace income – are expanding in developing countries. For many, social protection policies have been important in the acceleration of progress towards achieving the millennium development goals (MDGs). Barrientos and Hulme (2008) argue that, along with economic growth and human capital development, social protection is now a third pillar in national development strategies which aim

to increase national levels of welfare, raise economic productivity and strengthen social cohesion.

Social protection programmes offer more than improved living standards for the poor. Well-designed social protection programmes can enhance the productivity of the labour force, the resilience of society and the stability of the political process. In middle-income countries, social protection programmes such as Bolsa Familia in Brazil and Oportunidades in Mexico have reduced

income inequality and enhanced the lives of the poor, and contributed towards broader development goals such as economic growth.

The importance of formal systems of social protection in even the poorest countries is now being recognised. The International Labour Organization (ILO) report on ‘decent work’ in the United Nations-designated group of 48 least-developed countries noted:

those countries that have already graduated from Least Developed Country (LDC) status, namely Botswana (1994), Cape Verde (2007) and the Maldives (2011), have followed strategies of gradual extension of social security coverage and have invested strongly in social protection. (ILO, 2011a, p.78)

This article discusses social protection prospects in two Pacific countries that are both members of the LDC group, the Solomon Islands and Vanuatu. It draws on studies of social protection

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**Table 1: Population and economic profile of the Solomon Islands and Vanuatu**

	Solomon Islands	Vanuatu
Population estimate (mid-2011)	539,900	251,800
Population growth rate	2.3%	2.6%
Urban population as % of total population	20.5%	24.4%
Population aged 0–14 years (estimate)	39.5%	37.9%
Human Development Index (HDI) (incl. life expectancy, education, health status, living standards) rank out of 187 countries.	142	125
Gross national income (GNI) per capita	\$US1110	\$US2870
Debt as % of GNI	61.7%	41.6%
Tax revenue as % of GDP	36.3%	16.1%
Government expenditure as % of GDP	40.5%	23.4%

Source: Asian Development Bank (2012)

undertaken for the ILO in 2011–12 (Dwyer and Bangalini, forthcoming; Dwyer and Hebala, forthcoming) which built on earlier ILO studies (ILO, 2006a; ILO, 2006b). It describes the economic and social context of the Solomon Islands and Vanuatu, including existing social protection programmes and their coverage. It then discusses the areas where programmes could be developed and the potential for stepping up social protection in both countries.

#### Social and economic context

The Solomon Islands' and Vanuatu's LDC status reflects their vulnerability (including vulnerability to hazards, such as tropical cyclones, earthquakes, volcanic eruptions, tsunami and climatic events), as well as the challenges of small, widely-dispersed populations, human resource weaknesses, high levels of basic needs poverty, and, in the Solomon Islands, recent ethnic tensions and political unrest.

The populations of both countries are geographically scattered, and culturally and linguistically diverse. Both countries gained independence, and democratic government, relatively recently (Solomon Islands in 1978 and Vanuatu in 1980). Most people in the Solomon Islands and Vanuatu depend on subsistence activities (especially agriculture and fishing) for at least part of their livelihood, and urban populations are small and rapidly growing. Along with Papua New Guinea, they have low levels of out-migration compared to other Pacific Island countries and therefore little in the way of funds remitted from families abroad (Gibson and Nero, 2008).

International aid provides an estimated 18% of gross national income (GNI) in Vanuatu (AusAid, 2012c). In the Solomon Islands the Regional Assistance Mission doubles this figure to around 40% of GNI (Solomon Islands Government and UNDP, 2010). GNI per capita (see Table 1) is relatively low, especially in the Solomon Islands, compared to other Pacific Island countries (Gibson and Nero, 2008). Compared with other LDCs, however, both the Solomon Islands and Vanuatu are high-income, low-growth economies (ILO, 2011a, Figure 1.4, p.12).

#### Existing social protection arrangements

Social protection regimes in Vanuatu and the Solomon Islands do not fit easily into the welfare typologies of developed countries. Both have features that align with Esping-Andersen's conservative model (Esping-Andersen, 1990), which emphasises the role of family and self-provision, with a minimal role of the state in redistribution. There is a strong emphasis on the *kastom* or traditional forms of collectivity that provide social protection, within families and by *wantok* (clan members). These traditions involve obligations and are linked to communal land tenure. Beyond health and education, the state has not played a strong role in social protection.

#### Social protection programmes

Vanuatu and the Solomon Islands have similar government-provided or -legislated programmes. Education and health services are largely government-provided (alongside church-based and

NGO services) via current revenues (including donor support). For those in the formal workforce there are compulsory retirement savings regimes via national provident funds (NPFs) and employers cover the costs of other work-based provisions.

The formal workforces, however, are small. In Vanuatu, of the 99,000 labour force members (2009 census), over 16,000 were employers or self-employed, over 52,000 engaged in subsistence or unpaid work and 25,000 were employees. However, in 2009 there were only 16,642 active members (60% of them male) in the Vanuatu NPF retirement savings scheme (Vanuatu Government, 2011a). This suggests that the NPF, and possibly most other employment-based social protection laws, reach fewer than 20% of the labour force. Similarly, in the Solomon Islands there were 41,096 active members of the Solomon Islands NPF in 2010 (around 60% male), which is just under 20% of the 2009 labour force of 214,716 (Solomon Islands National Statistics Office, 2012).

#### Education

Primary education has become 'fee free' in recent years, in large part through donor support related to the MDG-focus on primary education. Secondary and tertiary education incurs fees. At primary schools, fee-free policies are considered an important element in the increase in enrolments and achievement of gender parity in both countries, as well as in increased literacy rates (Pacific Islands Forum Secretariat, 2012). Secondary school completion is low in both countries, and particularly so for girls in the Solomon Islands. Supply constraints (teachers, equipment and facilities, including girls' boarding facilities) affect the quality and availability of secondary education in both countries.

#### Health

Basic health services (primary and secondary) are provided free or, in the case of Vanuatu, with low charges for some hospital services. Both countries are seeking to improve the quality and breadth of the services available and face some challenges in terms of achieving



improvements across key health goals (as measured by the MDGs) (Pacific Islands Forum Secretariat, 2012).

More finance is needed to improve and expand the health systems in both countries. Investigations by the World Bank (2010) into the implications of different funding options in the Solomon Islands concluded that a contributory social health insurance was not viable due to the administrative costs of collecting from the high proportion of people outside the formal labour force, as well as the lack of appropriate administrative and technical capacity to collect and manage such a programme. User fees were also not considered viable, as revenue raised was likely to be outweighed by the costs of administering those fees, and the poor would also be less likely to use services. Overall, it assessed the current publicly-provided and free public health service as being efficient and pro-poor.

#### *Social protection associated with employment*

Employment law in both countries includes minimum wage provisions and obligations on employers to provide pay for sick leave and maternity leave, severance pay (in the case of Vanuatu) and contributions towards an annual paid passage home (100% of costs for all employees in the case of the Solomon Islands, and to cover 75% of travel costs for civil servants in Vanuatu). Legislation also provides for lump-sum worker compensation in the case of injury or death at work.

These provisions are dependent on employers being both willing and able to meet their obligations, as there are few resources for enforcement and many anecdotal cases of employers not meeting their obligations. 'Under the table' agreements are common. Apart from the case of worker compensation, where employers are obligated to take out private insurance (not all do so, and private insurers manage risk via exclusions), there is no risk-sharing around the costs of social protection. Individual employers, no matter how small, are liable to provide paid maternity leave from their own resources. This is likely to contribute to the low levels of formal female employment in both countries. Where employers go out of business, there is

no fund to pick up their responsibilities for redundancy. Payments, for example in the case of serious injury, tend to be lump sums rather than periodic.

The NPFs' compulsory savings schemes are funded by employee and employer contributions. Lump sums are paid on death, disablement or retirement. While some retired people set up businesses with their lump sums, and thereby generate their own income stream, it is thought that most lump sums are depleted soon after retirement. There are no products to convert savings into annuities.

There are no statutory social protection programmes to cover long-term illness, disability, old age or unemployment (apart from severance pay in Vanuatu), and none provide for the income protection needs of the 80% of the labour force who are self-employed or in the subsistence

- labour exchange or cooperative labour groups for tasks such as clearing land or house-building;
- gift-giving both in relation to special feast days and to mark lifecycle events such as births, weddings and deaths;
- inbuilt norms of social obligation that should make it almost impossible for an individual or family literally to starve;
- an understanding that gifts typically will be repaid, or reciprocal assistance will be forthcoming in the future from those who draw down on it today.

Thus, traditional support is provided within arrangements which reinforce cultural mores and obligations in relation to land and other resources (including money). Obligations are limited by the resources available as well as the strength

**“the recent focus on millennium development goals particularly MDG 1 to eradicate extreme poverty and hunger ..(has) shown the extent to which traditional supports fall short in preventing poverty and vulnerability”**

economy. In both countries there are small-scale credit unions and union-based funds which provide savings and credit arrangements and, in some cases, benefits (for example, to cover the costs of travel for medical purposes). Schemes that provide benefits through pooled contributions operate on a pay-as-you-go basis and typically manage overruns by suspending or cutting entitlements.

Parliamentarians also have funds to provide support for their constituents; these are discretionary and are reported to reinforce clan-based patronage and obligations.

#### *Traditional forms of social protection*

Ratuva (2005) identified key features of traditional social protection common to all Pacific Island countries as:

- access to land for all who require it;

of ties.

In Vanuatu, the Ifira community (of about 2000 people) has developed categorical grants using revenue received from annual leases on Iririki island, properties in the capital, Port Vila, and a stevedoring arrangement with government until 2050. It provides pensions for those over 50 (8,000 vatu (\$NZ100) per month), scholarships for secondary students and Christmas and New Year payments, and has developed rules in relation to entitlements for those marrying outside the community.

Apart from studies of migrant remittances, there is limited information about the reach and impact of traditional support in the Pacific. It is household surveys, and the recent focus on the millennium development goals, particularly MDG 1, to eradicate

extreme poverty and hunger, that have shown the extent to which traditional supports fall short of preventing poverty and vulnerability. The 2005/06 household survey in the Solomon Islands found that 23% of population (32% in the capital, Honiara, and 19% in rural areas) faced difficulty meeting food and essential non-food items (basic needs poverty). In Vanuatu, the 2006 household survey found basic needs poverty affected 16% of the population, but 33% in the capital, Port Vila, and 11% in rural areas.

Kidd et al. (2010) identified weak economies as contributing to stresses on traditional support. They also identified particular pressures from urbanisation, including pressure on

development (Barrientos and Hulme, 2008).

For many in Vanuatu and the Solomon Islands, 'social protection' is strongly linked to addressing the needs of the most vulnerable only, including protection from violence. For others it relates to contributory social insurance programmes for the formally employed. Some development partners and NGOs are also very attached to the idea of providing services, rather than transfers where people then choose how to spend their money. There is also some caution about government expanding into areas of welfare which have been the domain of traditional support.

On the other hand, the MDG focus over recent years means that both

to 'employment rich' development. Two relatively new approaches that are strengthening social protection in relation to employment are:

- programmes which enhance security within the informal sector through business training covering accounts and added value, micro-finance, and improving health and safety for some key areas of informal activity (e.g. the UN women marketplace project: <http://www.unwomen.org/2012/08/safer-spaces-and-better-markets-in-the-pacific-islands/>).
- the distribution of 'work' via minimum wage work programmes. 'Cash for work' is now a common approach taken in disaster relief. On a much larger scale is the World Bank-led Rapid Employment Project (REP) in Honiara, which aims to increase the income of the urban poor by providing short-term employment to its target groups of low-skilled women and youth. By March 2012, less than two years into its five-year programme (which is now being extended), REP had provided work for over 10,000 people who were employed for an average of 15 days each. Projects include building walkways and cleaning streets and waterways. While this programme is short-term, there is potential to build towards an 'employment guarantee' public works programme, such as those in India which offer a guarantee of a minimum number of days paid work per year to target groups and therefore constitute a guaranteed supplement to subsistence activities. In both countries there is likely to be potential to develop employment programmes within climate change adaptation work.

Initiatives around jobs and tackling unemployment are largely funded by donors, and donor funding is likely to be needed to continue any substantial employment initiatives. In both countries many employment programmes are both small scale and short-term. There is scope to rationalise programmes and develop more comprehensive and longer-term approaches.

## Initiatives around jobs and tackling unemployment are largely funded by donors, and donor funding is likely to be needed to continue any substantial employment initiatives.

urban and peri-urban populations to share land and income, the difficulties in providing housing and services to squatter settlements on land belonging to traditional owners, the poor quality of employment and earning opportunities available to new urban populations, and the loosening of traditional ties.

### Strengthening social protection

Within both the Solomon Islands and Vanuatu, improving and expanding education and health services is a top priority in the social protection area, and there is still a way to go to lift the quality and reach of these services. Other basic services (water and sanitation) also fall short. Beyond this, social protection is a relatively new concept for both governments and many of the development partners they work with. Moreover, social protection lacks an agreed definition, and the focus varies from addressing social risk that constrains development to ensuring basic needs are met, to a rights-based approach to human

countries now have more evidence about poverty and hardship, and the groups most affected by poverty. Grappling with how to achieve the MDGs has led to a deeper understanding of the linkages between social and economic well-being, including the importance of non-formal economic activity. Three areas where social protection programmes could be strengthened are discussed below. These are: tackling jobs and unemployment; improved social protection for the formally employed, and cash transfers.

### Tackling jobs and unemployment

As elsewhere in the Pacific, neither Vanuatu nor the Solomon Islands are generating enough new jobs for labour force entrants. The lack of paid work for youth has been identified as a priority challenge in both countries and, particularly in the Solomon Islands, is seen as a risk for future stability. Female paid employment is also low.

Within their development strategies, both countries pay considerable attention

### *Improved social protection for the formal sector workforce*

While the formal employment sector is very small (less than 20% of the labour force in both countries), the current arrangements for sick pay, injury compensation and maternity pay are not enforced and do not cover risks effectively. The ILO's labour law reform programme, under way in both Vanuatu and the Solomons via partnership with governments, employers and unions, is working towards improvements in social protection laws covering employees, such as maternity pay within a social insurance arrangement.

Currently the social protection available to employees in the formal sector is funded directly by employers in real time (in effect, work-based benefits that are part of total remuneration), apart from savings for retirement where balances are available to employees at retirement or if disabled or to families in the case of death. Therefore, even though improvements in this area are not the highest priority from a needs perspective, they would not require government funding. Improvements here have the potential to smooth costs and reduce risks (as in the case of maternity pay) for individual employers and are likely to make it more attractive to employ women and to create new jobs. Periodic rather than lump sum payments to employees who are disabled at work and retired would help them maintain their welfare over time.

However, the skills required to determine levies, forecast costs and manage risk are not present in either country: no government or quasi-government bodies have a social security function, and private insurance is small scale and largely overseas-owned and managed. The NPFs gather contributions, maintain individual accounts, make investments, pay dividends and pay out lump sums. Even within this narrow range of activity, both have had past financial problems. In the face of massive opposition, the Fiji NPF recently reduced the level of pensions due to an actuarial crisis contributed to by increases in longevity. The NPFs in the Solomons and Vanuatu are reluctant to expand their operations into the more risky world of periodic payments

for retired members. Moreover, sharing risks across a population (as opposed to within a family or broader kin or tribal network) is an alien concept to many. These barriers are major, and any moves towards social insurance, whether run by NPFs or directly by government (funded by tagged contributions), will require considerable stakeholder engagement and human resource development.

### *Cash payments*

Internationally, there has been considerable growth in low-level transfers to older people, and, in the case of children, particularly cash transfers that are conditional (for example, on attendance at school or health checks). In Vanuatu and the Solomon Islands, household surveys have shown

contributory pensions on a universal basis. However, there has been no analysis of the impact of these old age pensions on poverty in Pacific countries.

Finally, technological advances make it possible to administer payments simply, even in the most remote areas. Around the world, pensions are now delivered to cell phones, to debit cards, and in cash via mobile banks and biometric smart cards. The rapid spread of mobile phones and internet in both countries indicates readiness to use this technology.

If a cash payment programme is going to endure, it needs to be prioritised within government budgets. Preliminary costings of low-level universal payments to older people and for children suggest costs in the range of 0.4%–0.8% of GDP

## **Expansion of social protection programmes to incorporate regular cash transfers and employment guarantees requires funding, and fiscal space is easier to find when the economy is growing.**

that, on average, older people (particularly widows) and children are more likely to be in poor households. Children in female-headed households are more likely than other children to be in poverty.

AusAID's review of research on informal social protection concluded that poverty-targeted cash transfers may not be appropriate for traditional societies in the Pacific because they would be seen as divisive by selecting some families, or even different ethnic groups, for special support not offered to other citizens. They might also accelerate migration from rural to urban areas (AusAID, 2012d). Administrative costs associated with targeting in a society dominated by subsistence and informal activity are likely to be very high.

Moreover, universal pensions are an established idea in the Pacific. The Ifira people in Vanuatu make universal payments to older people, and Samoa, the Cook Islands, Kiribati, Nauru, Niue and Tuvalu pay older people small non-

for both countries, depending on the assumed level of payment (UNESCAP, 2010; AusAID, 2012b). People with disabilities are another group suggested for universal transfers (AusAID, 2012d).

The Solomon Islands is arguably more ready to consider cash payments than is Vanuatu. The country's National Development Strategy 2011–2020 has signalled an intention to develop a policy on social security to support the vulnerable in the Solomon Islands (Solomon Islands Government, 2011). It has a wider revenue base than Vanuatu, with around 18% of government revenue coming from income tax and a growing proportion of revenue from taxes on mining. There is, however, some caution about the future sustainability of an old age pension as longevity increases.

The Vanuatu government's Priorities and Action Agenda 2006–2015 focuses on primary sector development and getting the conditions right for private sector-led economic growth and development,

as well as better provision of education and health. The more recent National Population Policy 2011–2020 provides a framework for many social protection policies, albeit with somewhat of a safety net focus. In particular, it has a goal to reduce hardship and poverty among the elderly, widowers, people with disability and other vulnerable people. There is no discussion about cash payments as a means to achieve this goal. In Vanuatu, taxation is largely from sales tax and import duties. Sales tax is regressive in impact and increasing taxes of this nature to fund universal cash transfer programmes is likely to shift hardship to other parts of the population.

### Conclusions

Political will and fiscal space, as well as institutional capacity, are needed to successfully expand social protection. Within Vanuatu and the Solomon Islands, there is increased understanding of the limits of traditional supports in the face of urbanisation, rapid change and slow growth.

An important area of focus is how to provide greater protection for people working outside the formal workforce. Attention to employment opportunities and, if possible, guarantees is likely to benefit some of the most vulnerable

workers, including women in rural areas. In the light of mixed millennium development goal progress, governments are recognising that policies need to support people to achieve a decent standard of living from a mix of informal work, subsistence activities and some formal employment (including short-term migration for agricultural work in countries like New Zealand), because it is not realistic to expect the formal sector to provide jobs for everyone in the near future.

In Vanuatu there is interest in supporting cooperatives to replicate and scale up activities that encourage the growth of self-reliance and social protection at the community level. A major plank of the Solomon Islands National Development Strategy is to improve livelihoods for those with subsistence lifestyles. These are important issues, but not ones that wear the ‘social protection’ label. The ‘pump priming’ impacts of transfers would support employment and rural development (the Namibia old age pension illustrates this).<sup>1</sup>

Expansion of social protection programmes to incorporate regular cash transfers and employment guarantees requires funding, and fiscal space is easier to find when the economy is growing. It is no accident that social protection

expansion over the last decade has largely occurred in rapidly-growing developing and middle-income countries. Income transfers are a new concept to most, although a major element of the social security provided by the Ifira community in Vanuatu. Universal categorical payments are likely to be both feasible administratively and acceptable. The key issue for both countries will be finding fiscal space in government budgets.

Even though governments do not need to find new funding to develop better work-related protections for employees and annuities from retirement savings, the insurance elements involved are likely to be more challenging for Vanuatu and the Solomon Islands due to the lack of capacity around actuarial work and managing risk. However, pooling risk more effectively across employers – particularly for maternity pay and worker compensation – is likely to better enable employers to create jobs.

<sup>1</sup> See <http://www.youtube.com/watch?v=RGStuWQxAo>.

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# Local Government Strategic Planning in Theory and Practice

*By the Local Futures Research Project*

*Local Government Strategic Planning in Theory and Practice* is the second and final monograph of the Local Futures Research Project, a study of strategic policy and planning in local government, funded by the Foundation for Research, Science and Technology and based at the School of Government, Victoria University of Wellington. The book describes and analyses the experiences of a sample of local and regional councils as they worked with their communities to prepare Long-Term Council Community Plans under the Local Government Act 2002.

The authors critique the design and implementation of community strategic planning under the Act with a focus on the relationship between theory and practice. They also consider the implications of recent amendments to local

government legislation, including the creation of the Auckland Council and modifications to strategic planning and management requirements.

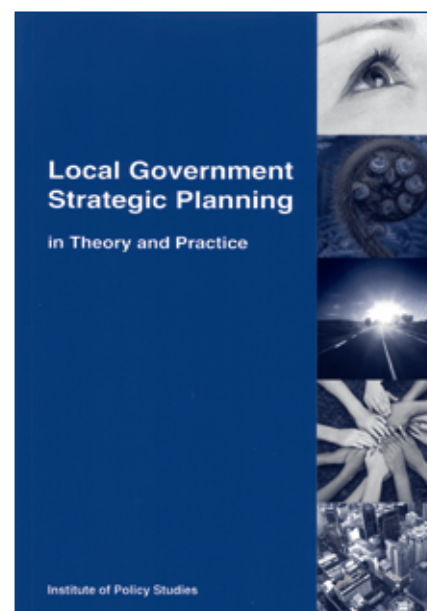
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Janine Hayward

# Citizens' Assemblies and Policy Reform in New Zealand

In 2011 New Zealand held a referendum on the future of its voting system for general elections. Following the referendum, the current voting system was retained, and the Electoral Commission reviewed the system and made recommendations for change in late 2012. In early 2013 the government's response to those recommendations is still awaited. Recognising the importance of this process, this article considers an alternative approach to electoral reform, drawing on the experiences of Canada's and Holland's use of citizens' assemblies in the electoral policy-making process. The article considers the merits and limitations of citizens' assemblies for electoral reform, particularly in the New Zealand context. It proposes the form and function of a

citizens' assembly on electoral reform in New Zealand to complement the reform process. Overseas experience demonstrates that, with some caveats, a citizens' assembly remains a possibility for electoral reform and other constitutional policy change in New Zealand in the future.

## **New Zealand's electoral referendum and MMP review**

At the 2011 general election a referendum asked New Zealand voters two questions: first, 'should New Zealand keep the Mixed Member Proportional (MMP) system?'; and second, 'if New Zealand were to change to another voting system, which voting system would you choose?' Voters

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were offered the following options: first past the post (FPP), preferential voting (PV), single transferable vote (STV) and supplementary member (SM). In the lead-up to the referendum, the New Zealand Electoral Commission was tasked with the role of educating the public on the referendum, on MMP and on the alternative voting systems offered.

The voters' responses to the first question triggered one of two subsequent steps. If more than half of voters taking part had preferred not to keep MMP, a second, binding referendum would have been held at the general election in 2014 to decide between MMP and the most popular alternative system, FPP. In fact, 56% of all participating voters wished to keep MMP. Under the Electoral Referendum Act 2010, this result triggered an independent review of MMP by the Electoral Commission, beginning in 2012. The commission was required to consider the following aspects of MMP: the two thresholds for the allocation of list seats; the effects of the ratio of electorate seats to list seats on proportionality in certain circumstances; the rules allowing candidates to contest an electorate and be on a party list, and list members to contest by-elections; and the rules for ordering candidates on party lists. Māori representation and the number of members of Parliament were excluded from the review. The review provided multiple opportunities for the public to express views, including two chances to make written and oral submissions, as well as opportunities to attend public hearings and to participate in hearings by video/telephone for those remote from major urban centres. In November 2012 the commission made its final recommendations to government (Electoral Commission, 2012); government has yet to respond to these recommendations.

Under New Zealand's unwritten and non-entrenched constitution, Parliament enjoys supreme sovereignty; the triennial election of representatives to the House is arguably the most powerful constitutional check on the executive. It is prudent, therefore, to reflect on the strengths and limitations of the electoral reform process. How can we ensure, most

importantly, that the choice voters made on this important issue was an informed one? New Zealand's use of referenda for electoral reform is innovative (Lundberg and Miller, 2012). But can ordinary people make enlightened political decisions through referenda? We know that most citizens today are not sophisticated political creatures; in fact, they are poorly informed and barely interested in politics (Fournier et al., 2011).

A desire to engage citizens meaningfully in policy-making and reform led to innovative experiments in Canada and the Netherlands with collective, deliberative citizen decision-making for electoral reform. These

citizens; and *epistemic democracy*, the idea that, taken collectively, ordinary citizens can make reasonable choices. All three cases required a group of citizens to learn about electoral systems in order to recommend a preferred system. In Canada the assemblies' recommendations were put to binding public referenda; in the Dutch case a recommendation was delivered to government. Each assembly preferred a different electoral system. The Dutch assembly had 143 members, and operated from March to November 2006. Early in the process the assembly opted to retain the existing proportional representation system and identify modifications to it. The assembly

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experiences provide evidence that, under the right circumstances, citizens can be trusted to learn, deliberate and make reasoned decisions about their own government. Acknowledging the possible benefits of citizens' assemblies, this article will consider whether a citizens' assembly might have been used in New Zealand's recent reforms, and, consequently, whether such an assembly might be worth considering for similar constitutional reform in New Zealand in the future.

### Citizens' assemblies for electoral reform

Between 2004 and 2007 in British Columbia and Ontario (Canada) and in the Netherlands, governments established citizens' assemblies on electoral reform to design the best electoral system for their respective communities. In the broadest sense these three citizens' assemblies tested important democratic ideals: *participatory government*, the active involvement of ordinary citizens; *deliberative democracy*, education and debate among ordinary

submitted these recommendations to a newly-elected government. In April 2008 that government announced that it would not implement the assembly's proposals. The Ontario assembly, which operated from 2006 to 2007, was the smallest of the three, with 103 members. Ontario, like British Columbia, was using the FPP electoral system; the assembly recommended a change to a form of MMP. This was put to a binding referendum in October 2007 (in conjunction with a general election). The proposed change failed to meet the necessary threshold of voter support (Fournier et al., 2011).

The criteria used to judge the 'success' of these assemblies are, obviously, varied and contested. All three processes delivered on schedule and within budget. But if success means implementing change, clearly these processes are found wanting. As discussed below, however, the assemblies themselves, as a process of citizen engagement and learning, have much to recommend them as policy-making tools.

The British Columbia citizens' assembly has been particularly well documented and is thus a useful case to examine in more detail to consider its usefulness in policy making. The assembly grew from British Columbian premier Gordon Campbell's commitment to tackle public apathy in electoral politics (Carty, 2004). In 2004, 160 citizens in British Columbia were 'near-randomly' selected to spend 11 months assessing the province's electoral system. The government asked these citizens, known as the British Columbia Citizens' Assembly on Electoral Reform,

The 11-month assembly process was in three phases. Throughout the year participants devoted an estimated 30 hours per month to their assembly work, for which they were paid an honorarium and expenses. For the first few months of the year they learned about electoral processes over six weekends. Experts in electoral systems spoke to the assembly, and the citizens read widely on the topic and engaged in group discussions within the assembly. A second, consultative phase included 50 public hearings and meetings across the province, attended by assembly

passed in 77 out of 79 districts, meeting the second threshold. But it gained 57.7% of the province-wide vote and therefore fell just short of the 60% overall support required. With such a close result, the provincial government agreed to hold a second referendum on the same proposal in May 2009, to coincide with the provincial election. This time STV failed decisively, receiving 39% support across the province, and a majority in no more than 9% of the districts (Fournier et al., 2011, p.8).

#### Lessons from citizens' assemblies

The British Columbia citizens' assembly, along with the cases in Ontario and the Netherlands, being well documented' reveal the benefits and limitations of a citizens' assembly as a policy-making tool. Broad principles of design can be drawn from these three cases. Assemblies must be randomly selected, and seen to represent (in terms of composition) the community from which they are drawn. Assemblies must have sufficient time to learn, to consult with the public and to deliberate. This requires extensive infrastructure, adequate resourcing, and time (Fournier et al., 2011, p.151). The assembly's mandate must be very clearly specified, and it must focus on an appropriate question. The assembly must establish principles by which to judge the options available.

Overall, in the literature there is enthusiasm that 'democratic agents of democratic renewal can be designed' (Warren and Pearce, 2008, p.6). An assembly is considered a model of how to 'engage and empower citizens to deliberate and decide on selected public policy questions' (Institute on Governance, 2007, p.2). Despite the assembly engaging only a tiny proportion of voters, there is also optimism that, with appropriate time and resources, citizens can be motivated to learn about and make reasoned decisions on complex matters. Analysts found an 'elevated degree of involvement among participants' in all three assemblies, with extremely high levels of engagement, participation and attendance throughout the process (Fournier et al., 2011, p.149). In Ontario, the average absence over the 12 weekends was just two members (in a group of 103), which 'speaks strongly to

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to consider whether the existing first-past-the-post system could be improved upon, and, if so, to recommend a new electoral system. This recommendation would be put to all British Columbian voters in a referendum, and the results legislated by government if the public voted for change. Described as an 'innovative gamble' (Warren and Pearce, 2008, p.xi) and a 'bold public policy initiative of historic proportions' (Elton, 2003, p.234), this citizens' assembly was the first of its kind in Canada.

Citizens for the assembly were selected through random ballot using information available on the electoral role, but the process ensured gender equity and regional distribution: one man and one woman were selected from each of the 79 ridings (electorates) in British Columbia. The selection process was 'skewed' to ensure the assembly reflected the spread of age in the British Columbian population. Two self-identifying aboriginal citizens were added through a subsequent random selection process when it was clear that none had emerged through the first process.

members. A website received written submissions and proposals. Members then came together for a weekend to share and digest what they had learned, before moving into the final, deliberative phase of the process. Over six weekends the members identified core values, and key features of an electoral system, in order to identify appropriately the option best suited to the needs of British Columbia. A 'significant movement of opinion' occurred during the deliberation phase, when preferences shifted from the mixed member proportional voting system to the single transferable vote. This has been described as a 'preference reversal that was rooted in the understandable reconsiderations fostered by the deliberative process itself' (Fournier et al., 2011, p.78).

In December 2004 the assembly issued a report recommending that the province adopt STV. In May 2005 this recommendation was put to a referendum: STV would be adopted if 60% of the province-wide vote, and a majority in 60% of the electoral districts, voted for STV. In the event the proposal



members' commitment to the project' (Rose, 2007, p.15). Ordinary citizens acquired an extensive knowledge and understanding of electoral systems throughout the process, achieving decision-making that appeared to be of a remarkably high quality. These findings have led assembly architects to conclude that 'citizens have the capacity to shed their apathy, overcome their ignorance, and reason conscientiously about an unfamiliar and complex political issue' (Fournier et al., 2011, pp.149-51).

Finally, it is important to note that a deliberative assembly offers a *collective agreement* (after the three phases of learning, consultation and deliberation) rather than individual preferences expressed through a referendum. As Cutler et al. (2008, p.166) argue, a referendum alone offers voters little 'opportunity or incentive to pause from ordinary pursuits to consider the question closely by themselves, much less in the company of others'. The collective preferences of assembly members showed stability, or changed in ways that could be explained. Moreover, the three assemblies chose different electoral systems as a consequence of the different features of their respective communities. Each assembly's decisions were not considered to be driven by a small number of vocal or influential members, and neither did the staff or academic experts participating in the process appear to influence the outcomes (Fournier et al., 2011, p.150).<sup>2</sup>

But how much trust did the wider public have in the decision-making of these assemblies? In other words, 'do voters trust the judgment of citizen representatives, even if ... [the voters'] understanding of the proposal is not informed by a similar process of education and deliberation?' (Warren and Pearse, 2008, p.17). In the case of the British Columbia assembly, it was found that the citizens' assembly drew its legitimacy – in its own eyes and in the eyes of the wider public – from the near-random selection process and from the belief that they were a representative sample of the general public (Fournier et al., 2011, p.148). In British Columbia in particular, the fact that the assembly was considered to resemble the province

demographically seems to have led the 'populist voters' to trust the assembly and to support its recommendation.<sup>3</sup>

The Canadian and Dutch experiences also reveal the limitations of assemblies as policy-making tools. The effect of assemblies on participants beyond their specific mandate, for example, should not be overstated. 'Participation in these assemblies did not have a major impact on individuals' general outlooks towards political actors, fellow citizens and themselves. It may have created more interested and involved individuals,

as sound ones by stakeholders, politicians and the public. (Rose, 2008)

#### **A citizens' assembly for New Zealand?**

In 2007, when the Electoral Finance Bill was proposed, the Green Party noted that it was not appropriate for self-interested members of Parliament to consider this matter, and suggested an amendment to create a citizens' assembly (New Zealand Parliament, 2007). The proposal was rejected by the House after a brief and dismissive debate. National MP Wayne

## **The experiences of citizens' assemblies in Canada and the Netherlands demonstrate that ... MPs may have been too quick to dismiss the capacity of ordinary citizens to learn about and make informed decisions concerning complex policy issues ...**

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but it did not produce "better" citizens' (Fournier et al., 2011, p.125).

Furthermore, an assembly 'ought to be used sparingly under exceptional circumstances' (ibid., 2011, p.155). This discussion has focused on assemblies for electoral reform, but, more broadly, any electoral or constitutional question is a possible case for an assembly, particularly questions that should not be left to self-interested elected officials (Ferejohn, 2008, p.213). 'It makes no sense for government ... to decide the rules of the game [of government]' (Vander Ploeg, 2003, p.221). As Jonathan Rose, chair of the Ontario assembly, explains:

Assemblies are ideal when politicians have a conflict of interest, when there is no obviously right answer or when it is important to hold a public conversation on an issue. Because they are independent of government and have a transparent process, they are imbued with authority and legitimacy – the hallmarks of their process. Since they have no agenda, their recommendations are viewed

Mapp questioned the value of a citizens' assembly, saying: '[e]veryone in this Chamber is a citizen. Every person here has been elected. It is an assembly. This is the place where we debate the legislation.' Green MP Metiria Turei spoke in defence of the idea and objected to Mapp's dismissive attitude, saying: 'I take note of Mr Mapp's very poor analysis of the importance of having the public engaged in such a process.' She also criticised the government's quick rejection of a process to engage the public in campaign finance reform. National MP Tim Groser questioned the capacity of an assembly to grapple with the complex issues surrounding campaign finance. He said:

This is a bill of such complexity that the Minister herself has admitted she does not understand it. It is a bill of such complexity that Helena Catt, the chief executive of the Electoral Commission, says she does not understand it. But at least these two persons drawn from each of the electorate lists – at random, ... – will be able to clarify it. ... This

amendment would be an absolute disaster, and we implore ... the Labour Party not to go there.

The experiences of citizens' assemblies in Canada and the Netherlands demonstrate that, at the very least, these MPs may have been too quick to dismiss the capacity of ordinary citizens to learn about and make informed decisions concerning complex policy issues such as voting systems and, presumably, electoral finance law. Imagine for a moment that New Zealand MPs had greater confidence

MMP review. The process would follow the established three phases of learning, public consultation and deliberation. The assembly could be asked to decide, first, whether New Zealand ought to keep MMP. If it decided that it should, as the referendum did, the assembly could subsequently review specific features of MMP (as the Electoral Commission has done), and make recommendations to Parliament. If the assembly decided, however, to propose a change to another system, it could review the alternatives and recommend the best alternative

as in the Dutch case, is for an assembly to make its recommendations directly to Parliament. This ushers in a second problem the assembly sought to avoid, of self-interested politicians making the final decision and ignoring an assembly's recommendations (as was the Dutch experience).

### Conclusion

Citizens' assemblies have proven to be useful policy tools overseas in electoral reform. They show that citizens have the capacity to overcome political apathy, and learn and make reasoned choices about complex policy issues. It is worth reflecting on the benefits to New Zealand of using a citizens' assembly for important constitutional policy reform, such as the recent electoral reform process, or other constitutional issues arising in the future. Assemblies have their limitations, and challenges remain in integrating assembly recommendations in a decision-making process. But New Zealand's small population base and geographical space, combined with 'heightened levels of intimacy, community, access and accountability' in politics (Lundberg and Miller, 2012, p.4), make it ideally suited for citizens' assemblies to promote, at the heart of the policy process, an informed, robustly-debated policy choice by New Zealand citizens.

## Citizens' assemblies ... show that citizens have the capacity to overcome political apathy, and learn and make reasoned choices about complex policy issues.

in New Zealand voters, and had agreed to legislate to create a citizens' assembly for New Zealand's recent electoral reform process. How might this assembly be constituted, and what might its mandate and terms of reference be?

As in British Columbia, New Zealand's electoral roll could be used to randomly select and invite voters to participate in the assembly process. Those who indicated a willingness to be involved would proceed to a selection process which could ensure, through near-random selection, participants from each electorate who represent the New Zealand population in relation to age, gender, and ethnicity in relation to Māori voters. If two citizens from each electorate (including the seven Māori electorates) were selected, this would produce a 140-person assembly. Presumably most meetings would be in Auckland, due to the population spread. But the population size and geography of New Zealand makes the logistics of an assembly practical and possible.

The assembly itself could be given a very tightly focused objective and terms of reference such as those identified by the recent referendum and the subsequent

voting system. This decision might then be put to a referendum for all voters.

The limitations of citizens' assemblies ought not to be forgotten, however, and two questions arise from this theoretical assembly for New Zealand. The first is the problem of integrating a citizens' assembly with a public referendum. This was done with both Canadian assemblies, and in both cases the assemblies' preferences (for change) were defeated at the referendum. As one commentator notes, 'how can it make sense to ... place the ... wisdom [resulting from an assembly] at the disposition of a feckless and ignorant majority' (French, 2012, p.67) via referendum? Put another way, why place so much emphasis on the learning and education of citizens and the value of their reasoned opinion and then place the final decision with a process which clearly does not meet those principles? Given New Zealand's history of referenda in electoral reform, it is almost impossible to imagine the New Zealand public accepting a decision made without a public referendum, regardless of how legitimate they consider the findings of an assembly. The other possibility,

1 Richard French expresses reservations that the analysis thus far has come from those involved in the assembly process. He notes the 'celebratory, at times euphoric, tone to the Warren and Pearce collection' and the 'more balanced view' of the subsequent edited collection by Fournier which reviews all three cases. See French (2012), pp.65 and 73.

2 Lang (2008, p.86), however, questions this.

3 The composition of the assembly has been the subject of some criticism and questions about who ought to be included for deliberative assemblies to be truly 'representative' of their communities. See in particular James (2008), pp.107-8.

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