Is it worth working now?
Financial incentives for working mothers under Australia’s new tax system

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It must be emphasised that NATSEM does not have views on policy. All opinions are the authors’ own and are not necessarily shared by NATSEM.

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Abstract

The introduction of A New Tax System in July 2000 included substantial changes to social security payments, including family assistance and child care subsidies. Most of these payments are income tested, so that as a family’s income increases the amount of government assistance they receive is reduced.

This paper analyses the impact of increasing income and child care costs on the financial incentives for women with children to increase their participation in paid work. It examines the work incentives using the Effective Tax Rates model in STINMOD, NATSEM’s static microsimulation model of the tax and transfer system.

Author note

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Acknowledgments

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General caveat

NATSEM research findings are generally based on estimated characteristics of the population. Such estimates are usually derived from the application of microsimulation modelling techniques to microdata based on sample surveys.

These estimates may be different from the actual characteristics of the population because of sampling and nonsampling errors in the microdata and because of the assumptions underlying the modelling techniques.

The microdata do not contain any information that enables identification of the individuals or families to which they refer.
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1 Introduction

Australia has a tightly targeted system of social security and family assistance payments, which aims to provide assistance to those in need whilst keeping the costs of the system under control. One result of this balancing act is that most major government cash payments are income tested, with most also being subject to an assets test. This system can create high effective tax rates for people receiving government cash payments, which may reduce their work incentives. These concerns are not new (Beer 1998a, 1998b, 2002; Harding and Polette 1995; Ingles 1997, 2000; Polette 1995; Whitlock 1994).

One of the aims of A New Tax System (ANTS) was to reduce effective tax rates and boost work incentives. In the white paper on ANTS, the Treasurer said: ‘The new system will also give much greater recognition to the costs of raising a family. … Work incentives for low and middle income families will be greatly improved’ (Treasurer 1998, p. 15). The measures to improve work incentives included reducing the taper rate on family assistance from 50 per cent to 30 per cent and reducing the overlap between income tests on family payments (Treasurer 1998, p. 52), as well as reducing the taper rate on pensions (including for lone parents) from 50 per cent to 40 per cent (p. 20).

Despite the major changes associated with ANTS, the issue of high effective tax rates and their impact on work incentives remains a concern for policy makers (Abbott 2002; Reference Group on Welfare Reform 2000; Vanstone and Abbott 2002). A recent study on the distribution of effective marginal tax rates (EMTRs) by Beer (2002) found that families with dependent children were the most likely to face high EMTRs. (An EMTR is the proportion of a one dollar increase in private income which is lost to income tax and income tests on social security and family assistance payments. Put another way, it is the proportion of an extra dollar of private income that the family doesn’t get to keep.)

Distributional studies such as Beer (2002) tell us who and how many in the population experience high EMTRs at a given point in time. However, they do not tell us how an individual family’s effective tax rates change for income changes of more than a dollar or how the interaction of the tax and social security systems can limit the financial incentives to increase work hours. Hypothetical studies such as Beer (1998b) and Ingles (2000) provide an indication of the work incentives for particular types of families and highlight potential problem areas. Following the methodology in Beer (1998b), this study uses effective average tax rates (EATRs) to analyse the impact of increasing income and child care costs on the financial incentives for women with children to increase their paid work. EATRs are derived from EMTRs – they are
essentially the weighted sum of EMTRs over a range of private income (rather than a single dollar).

It must be emphasised that this study only measures the immediate financial incentives to work. A mother may choose to work – including when the financial incentives to do so are low or even negative – for a number of reasons, such as career progression, the need to keep skills current, the psychological benefits of working (interaction with other adults – and time away from her children!) and to provide a higher standard of living in retirement through greater accumulation of superannuation.

This paper focuses on couple families with children where one of those children is under school age and attends long day care. Some cases of lone mothers are also examined to see how the financial incentives for lone mothers differ from those for partnered mothers. Section 2 describes the methodology and gives details of the hypothetical families modelled. The results for each hypothetical family are presented in Section 3 and Section 4 draws some conclusions.
2 Methodology

2.1 The STINMOD model

The results in this paper are generated from STINMOD, NATSEM’s general purpose static microsimulation model. STINMOD contains two models: a distributional model and a hypothetical effective tax rates (ETR) model. For this paper, the hypothetical ETR model from STINMOD/02B has been used.

Most analyses of effective tax rates look at EMTRs. EMTRs are defined as the proportion of a one dollar increase in private income which is lost to income tax and income tests on government cash payments. EMTRs are useful when examining the minute detail of how the tax and social security systems interact to create financial disincentives to work. For example, extremely high EMTRs often occur over very small ranges of private income and would be easily missed if the increase in private income was larger than one dollar. However, EMTRs are not so practical for examining the decision to engage in paid work or to increase the amount of paid work, since very few people increase their private income by a dollar at a time. A more realistic unit of analysis is the hourly wage, since an hour of work and the resulting wage is the smallest unit over which a person could reasonably expect to have some influence. Using a change in private income of more than one dollar means that the analysis is conducted in terms of effective average tax rates (EATRs), which are mathematically the same as the weighted average of the EMTRs over the range of private income (Ingles 1997). Being a weighted average, EATRs tend to exhibit less volatility than EMTRs.

For an individual, disposable income is their private income less any income tax they have to pay (including Medicare levy and surcharge and net of any tax offset for which they are eligible) plus any government cash benefits they receive. This paper adopts the same definition of family disposable income as Beer (1998b, p. 96): ‘the sum of the individual’s disposable incomes less the family’s net child care costs’.

The tax rates and thresholds used in this paper are those for the 2002/03 financial year. Rates for social security and family assistance payments are those applying in the period 1 January to 19 March 2003.

Some factors that may influence EATRs have been excluded from this paper. STINMOD assumes that where a payment is assets tested, the assets of the family are lower than the asset limit so that their payment is unaffected. All families are assumed to have no rent costs, so they are not eligible for Rent Assistance or state public housing subsidies. We have also assumed that none of the people in the

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hypothetical families has a Higher Education Contribution Scheme (HECS) debt. The exclusion of these factors will tend to understate the EATRs in this paper.

The only cost of working modelled in this paper is the cost of formal child care, specifically, long day care. Other costs associated with working, such as travel, are not included in the modelling.

All families in this study are assumed not to have private hospital cover, thus becoming liable for the Medicare levy surcharge when their income reaches the threshold.

### 2.2 Families modelled

The hypothetical families modelled in this paper include those modelled in Beer (1998b) as well as some lone parent families. Where the family includes a father, he is assumed to be working full-time. Table 1 shows the characteristics of each family modelled.

<table>
<thead>
<tr>
<th>Description</th>
<th>Father’s income</th>
<th>Mother’s hourly wage</th>
<th>Number of children</th>
<th>Cost of child care</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low income couples with one child in care</td>
<td>515</td>
<td>11.70</td>
<td>1,2,3</td>
<td>4.30</td>
</tr>
<tr>
<td>Lower middle income couples with one child in care (lower middle income mother)</td>
<td>759</td>
<td>16.00</td>
<td>1,2,3</td>
<td>4.30</td>
</tr>
<tr>
<td>Lower middle income couples with one child in care (low income mother)</td>
<td>759</td>
<td>11.70</td>
<td>1,2,3</td>
<td>4.30</td>
</tr>
<tr>
<td>Upper middle income couples with one child in care</td>
<td>1005</td>
<td>20.00</td>
<td>1,2,3</td>
<td>4.30</td>
</tr>
<tr>
<td>High income couples with one child in care</td>
<td>1708</td>
<td>32.90</td>
<td>1,2,3</td>
<td>4.30</td>
</tr>
<tr>
<td>Low income couples with one child in cheaper care</td>
<td>515</td>
<td>11.70</td>
<td>1,2,3</td>
<td>3.50</td>
</tr>
<tr>
<td>Low income lone mother with one child in care</td>
<td>-</td>
<td>11.70</td>
<td>1</td>
<td>4.30</td>
</tr>
</tbody>
</table>

*Source: Beer (1998b) and NATSEM calculations*

Given the large number of factors that influence a family’s disposable income, there are obviously many hypothetical family types that could be modelled in this paper. As discussed in Beer (1998b, pp. 98–99), the factors that influence the family’s disposable income include:
Is it worth working now?

- the father’s weekly income;
- the mother’s hourly wage;
- the number of children in the family;
- the number of children attending formal child care; and
- the amount the family pays for child care.

**Income**

The choice of income for the hypothetical families makes a significant difference to the outcomes. There are several ways that you could choose incomes so that they were at least partly related to the incomes prevailing in the Australian labour force. One option is to choose incomes related to the centralised wage fixing system, for example, the federal minimum wage and the C10 tradesperson’s rate in the *Metal Industries Award* (both used as benchmarks in the Safety Net Review case before the Australian Industrial Relations Commission – see AIRC 2003). Another option, and the one adopted in this paper, is to follow the methodology of Beer (1998b) and use the ABS Survey of Income and Housing Costs (SIHC). In this case, the 1997/98 SIHC was used. All married men with wage and salary income working full-time were sorted in order of income and divided into four groups of equal size (quartiles). The group with the lowest wage and salary income are in Quartile 1; those with the highest incomes are in Quartile 4. For each quartile, the average weekly wage and salary income was computed and uprated to 2002/03 values using changes in male full-time adult total earnings over that period (ABS 2002). The results are shown in Table 2.

**Table 2** *Estimated average weekly income from wages and salaries for married men working full-time, 2002/03*

<table>
<thead>
<tr>
<th>Quartile</th>
<th>Average income from wages and salaries $ pw</th>
</tr>
</thead>
<tbody>
<tr>
<td>One</td>
<td>515</td>
</tr>
<tr>
<td>Two</td>
<td>759</td>
</tr>
<tr>
<td>Three</td>
<td>1005</td>
</tr>
<tr>
<td>Four</td>
<td>1708</td>
</tr>
</tbody>
</table>

*Source: Australian Bureau of Statistics 2000 and 2002*

A similar process was used to derive the hourly wage rates for married women. An hourly wage rate was calculated for all married women with wage and salary income in the SIHC, then split into quartiles, with Quartile 1 containing the women with the lowest hourly wage rates. The average hourly wage rate for each quartile

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was then calculated and uprated to 2002/03 using changes in female full-time adult total earnings\(^1\). The hourly wage rates for married women are shown in Table 3.

**Table 3**  
*Estimated average hourly income from wages and salaries for married women, 2002/03*

<table>
<thead>
<tr>
<th>Quartile</th>
<th>Average income from wages and salaries $ pw</th>
</tr>
</thead>
<tbody>
<tr>
<td>One</td>
<td>11.70</td>
</tr>
<tr>
<td>Two</td>
<td>16.00</td>
</tr>
<tr>
<td>Three</td>
<td>20.00</td>
</tr>
<tr>
<td>Four</td>
<td>32.90</td>
</tr>
</tbody>
</table>

*Source: Australian Bureau of Statistics 2000 and 2002*

Unlike the earlier study by Beer, this paper also includes lone mothers. The wage rates for lone mothers were derived from the SIHC, using the same method as for married women. These are shown in Table 4.

**Table 4**  
*Estimated average hourly income from wages and salaries for lone mothers, 2002/03*

<table>
<thead>
<tr>
<th>Quartile</th>
<th>Average income from wages and salaries $ pw</th>
</tr>
</thead>
<tbody>
<tr>
<td>One</td>
<td>11.70</td>
</tr>
<tr>
<td>Two</td>
<td>14.80</td>
</tr>
<tr>
<td>Three</td>
<td>19.30</td>
</tr>
<tr>
<td>Four</td>
<td>28.50</td>
</tr>
</tbody>
</table>

*Note: For lone mothers in Quartile 1, the wage rate derived from the SIHC and uprated was $9.60, which is significantly lower than the federal minimum wage for adults ($11.80). Although it is conceivable that a young lone mother could be employed at this wage rate if she was subject to junior rates, inspection of the SIHC data suggested that the low wage rate arises from problems with the data rather than a concentration of lone mothers attracting junior rates in Quartile 1. To overcome this problem, we used the wage rate for Quartile 1 of married women ($11.70) instead, though we acknowledge that this is not an ideal solution.*

*Source: Australian Bureau of Statistics 2000 and 2002*

Applying the theory of assortative mating (Becker 1973), the married women are assumed to be married to a man from the same income quartile, so that an upper income woman earning $32.90 per hour (quartile 4) is married to an upper income man who earns $1708 per week (quartile 4). Similarly, a lower middle income woman earning $16.00 per hour (quartile 2) is married to a lower middle income

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\(^1\) Other uprating factors were considered for the female hourly wage rate (such as female total earnings) but rejected in favour of using a consistently defined uprating factor for both men and women.
man earning $759 per week (quartile 2) and so on. For comparison, we have also included a couple where a lower middle income man earning $759 per week is matched with a low income woman earning $11.70 per week.

**Child Care Costs and Usage**

In this paper, we assume that each family has only one child aged under 5 requiring long day care. Older children are aged between 6 and 12.

The hourly rate paid for child care can have a dramatic effect on the disposable income of families using paid child care, because Child Care Benefit generally covers only part of the cost of care. Data on hourly rates of child care are scarce. For example, the ABS Child Care Survey conducted in 2002 only asked about the amount paid for care after Child Care Benefit (ABS 2003). Imputing the cost of care before Child Care Benefit would be difficult and not very accurate. Instead, we obtained fee information by ringing a small number of long day care centres in each state and territory and arrived at an average hourly rate of $4.30. The cheaper child care centres charged a rate closer to $3.50 per hour.

Assuming that the mother is the primary provider of care, an increase in the number of hours she works will increase the number of hours of paid child care she uses. There are many ways that the mother could spread her hours of work, and how she does this will affect the number of hours of paid child care her children need (see the discussion in Beer 1998b, pp. 110–111). For convenience, we follow the same pattern of child care usage as Beer 1998b (described in Beer 1997 and reprinted in Appendix A of this paper). Briefly, the pattern of child care usage assumes that the mother works for up to 7 hours a day, and always works a full day before she starts working on another day. The mother needs to allow one hour each day for travel time and, if she works more than four hours on a given day, an hour for a lunch break, so that when she works a 7 hour day, she needs 9 hours of child care.
3 Results

3.1 EATRs for partnered mothers

For each of the families described in Table 4, the results below show how the family’s disposable income and EATRs change according to the number of hours the mother works.

*Low income couples with one child in care*

Figure 1 shows the disposable income for a family where the mother earns an hourly wage of $11.70 and the father is earning $515 per week. The family is assumed to pay $4.30 per hour for one child in child care. The figure shows that when the mother works a small number of hours each week – between 1 and 9 hours – the family’s disposable income increases gradually. Once the mother reaches around 10 hours of work, however, the family’s disposable income increases very slowly – and at some points it actually falls. Between 10 and 19 hours of work per week, the mother’s extra private income causes almost no increase in the family’s disposable income. Once the mother goes from working 19 hours to 20 hours or more the family’s disposable income starts to increase at a much faster rate.

![Figure 1](image)

Data source: NATSEM calculations

NATSEM paper
Where the couple have three children, they are financially worse off when the mother works 12, 13, 15, 26 or 29 hours per week than if she had worked one hour less. If she increases her work from 10 to 20 hours per week, the family’s disposable income increases by less than $2.50. That would hardly buy you a sandwich, let alone a milkshake to go with it!

You can also see in Figure 1 that the family with one child experiences a greater increase in disposable income (in both percentage and dollar terms) than the other families. This is due mainly to the fact that families with more children receive more Family Tax Benefit Part A (FTB-A). As a result, the range of private income over which maximum rate FTB-A is withdrawn is larger for families with more children. Because the income testing away of maximum rate FTB-A generally results in higher EATRs, larger families have slower increases in disposable income. So, while the family with one child starts receiving base rate FTB-A when the mother works 19 hours a week, the family with three children is still receiving more than the base rate of FTB-A even when the mother works 35 hours a week. The family with one child gains an extra $136 per week when the mother goes from not working to working 35 hours per week, while the family with three children only gains an extra $80 per week.

Figure 2 shows that the families with one, two and three children all experience a broadly similar pattern of EATRs. Initially, their EATRs are quite low as the mother’s extra earnings do not affect the family’s social security or family assistance entitlements and she does not pay income tax. The family’s net child care costs are the only factor in their EATR. But very quickly, the mother’s extra income starts to

**Figure 2**  EATRs for a family with the father earning $515 per week and the mother earning $11.70 per hour with one, two or three children – one child in child care at $4.30 per hour

*Data source: NATSEM calculations*
affect the family’s government payments. When she works 4 hours a week, she begins to lose the small amount of Parenting Payment Partnered to which she is entitled. Combined with the 30 per cent taper on Family Tax Benefit Part B (FTB-B), the Medicare Levy at the shade-in rate of 20 per cent and the additional costs of child care, this causes the family’s EATR to jump up to 83.4 per cent (in the case of the couple with one child).

Once the mother is working 8 hours a week, the family’s EATRs generally remain above 60 per cent. The main factors contributing to the EATR are the 30 per cent taper on FTB-B and maximum rate FTB-A, income tax, the Medicare Levy and the increasing net costs of child care. The highest EATR of 119.1 per cent occurs when the mother in the family with three children goes from 11 to 12 hours of work per week.

Note that the family with one dependent child experiences considerably lower EATRs once the mother is working 20 hours per week. At this point, the family only receives the base rate of FTB-A, which reduces their EATR by 30 percentage points. As Figure 2 shows, the families with more children experience high EATRs over a larger range of private income, thanks to their higher thresholds and initial entitlements to FTB-A. The family with three children receives more than the base rate of FTB-A even when the mother works 35 hours a week, whereas with two children is eligible only for the base rate of FTB-A when the mother works 32 hours a week or more.

**Lower middle income couples with one child in care**

Families where the mother and father earn slightly more experience larger increases in their disposable income as the mother’s hours of work increase. This is due, in part, to the higher hourly wage of the mother – $16.00 per hour rather than $11.70 per hour. The higher income of the father also means the family spends less time in the range of private income where social security and family assistance payments are being withdrawn. The main influences on their EATRs are income tax, Medicare Levy and net child care costs. When the mother in the family with one child goes from not working to working 15 hours per week, her family’s disposable income increases by $122 per week, while increasing work from 15 to 35 hours a week sees disposable income rise by a further $138 per week. For the family with three children, weekly disposable income increases by only $50 when the mother goes from not working to working 15 hours a week, and rises by a further $130 per week when her hours of work jump from 15 to 35.

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Families with slightly higher incomes do not experience EATRs quite as high as low income families – the highest EATR for the lower middle income families is 107.1 per cent (when the mother in the family with three children goes from 11 to 12 hours of work per week). The lower EATRs are most notable for the family with one child.
child, because this family only receives base rate FTB-A even before the mother starts working and her higher wage rate means that her FTB-B entitlement reduces faster than for a low income mother. The spike in EATR at 26, 29 and 33 hours results from having to pay for two extra hours of child care for one extra hour of work at these points. At 35 hours of work per week by the mother, the family’s EATR is 59.6 per cent. The only factors affecting the EATR at this point are income tax, Medicare levy and net child care costs.

If instead of earning $16.00 per hour the mother’s wage rate was $11.70 per hour, the family’s increase in disposable income would be much smaller. Working 35 hours per week at $11.70 per hour the mother (with one child) would add $172 to the family’s disposable income compared with not working; at $16.00 per hour, her 35 hours of work would add $259 to the family’s disposable income. This smaller, slower increase in disposable income can be seen in Figure 5. The EATRs for the family are higher when the mother’s hourly wage is lower, mainly because the net cost of each hour of child care constitutes a larger proportion of her hourly wage. Her lower wage rate also means that FTB-B takes longer to be income tested away – the family’s FTB-B entitlement reaches zero when the mother works 14 hours at $16 per hour compared with 19 hours at $11.70 per hour (see Figure 6).

Figure 5  Family disposable income for a family with the father earning $759 per week and the mother earning $11.70 per hour with one, two or three children – one child in child care at $4.30 per hour

Data source: NATSEM calculations
Is it worth working now?

**Figure 6** EATRs for a family with the father earning $759 per week and the mother earning $11.70 per hour with one, two or three children – one child in child care at $4.30 per hour

<table>
<thead>
<tr>
<th>Hours worked by mother per week</th>
<th>EATR (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>5</td>
<td></td>
</tr>
<tr>
<td>10</td>
<td></td>
</tr>
<tr>
<td>15</td>
<td></td>
</tr>
<tr>
<td>20</td>
<td></td>
</tr>
<tr>
<td>25</td>
<td></td>
</tr>
<tr>
<td>30</td>
<td></td>
</tr>
<tr>
<td>35</td>
<td></td>
</tr>
</tbody>
</table>

**Data source:** NATSEM calculations

**Upper middle income couples with one child in care**

At even higher levels of income, with the father earning $1005 per week and the mother’s wage rate at $20.00 per hour, the family receives larger gains from the mother’s work than lower income families, as Figure 7 shows. Going from not working to working 20 hours per week leads to an increase in family disposable income of almost $210 per week (around 25 per cent) and increasing from 20 to 35 hours increases disposable income by between $78 and $96 per week, depending on the number of children. The slight falls in disposable income when the mother goes from working 28 to 29 hours per week for families with one child or 32 to 33 hours per week for families with two children result from the addition of the 30 per cent taper on base rate FTB-A to their tax, Medicare levy and net child care costs.

Figure 8 shows that even at quite high levels of income the family can face EATRs that would make them seriously consider whether the extra hours of work were worthwhile. For example, if the mother works an extra hour and goes from working 7 to 8 hours per week, the family faces an EATR of 75.3 per cent, due to a combination of income tax, withdrawal of FTB-B and net child care costs. Similarly, when the mother goes from working 28 to 29 hours per week, the family’s EATR is 80.1 per cent (or 110.1 per cent in the case of the family with one child). This EATR is the result of income tax, Medicare levy and net child care costs (plus the 30 per cent taper on base rate FTB-A for the family with one child). The most significant contributor to the EATR at this point is the net cost of child care, which adds 48.6 percentage points to the family’s EATR.

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Is it worth working now?

**Figure 7** Family disposable income for a family with the father earning $1005 per week and the mother earning $20.00 per hour with one, two or three children – one child in child care at $4.30 per hour

![Graph](image)

Data source: NATSEM calculations

**Figure 8** EATRs for a family with the father earning $1005 per week and the mother earning $20.00 per hour with one, two or three children – one child in child care at $4.30 per hour

![Graph](image)

Data source: NATSEM calculations

**High income couples with one child in care**

Mothers in high income families experience faster increases in disposable income than lower earning mothers, as you can see by comparing the scale in Figure 9 with the scale in earlier figures. A mother earning $32.90 per hour in a family where the
father earns $1708 per week increases the family’s weekly disposable income by between $298 and $343 per week (depending on the number of children) when she goes from not working to working 20 hours per week. Increasing her work from 20 to 35 hours adds a further $236 to the family’s weekly disposable income. The total increase of $579 (with one child) is more than four times the $136 that a mother in a low income family adds to her family’s disposable income when she goes from not working to working 35 hours per week. Put another way, a high income family gets to keep just over half of the mother’s full-time earnings, while the low income family keeps less than a third.

Figure 9  Family disposable income for a family with the father earning $1708 per week and the mother earning $32.90 per hour with one, two or three children – one child in child care at $4.30 per hour

Data source: NATSEM calculations

Mothers in high income families face lower financial disincentives to increased workforce participation than other mothers. Nevertheless, they still experience high EATRs some of the time, though these tend to occur when the mother is working only a few hours per week. The most notable feature of Figure 10 is the large spike in the EATR at 7, 8 and 9 hours for the families with one, two and three children respectively. This spike is caused when the family’s taxable income crosses the Medicare levy surcharge threshold. At this point the family pays an extra one per cent of their taxable income, increasing the father’s Medicare levy from $25.60 to $42.70 per week. This adds an extra 52 percentage points to the family’s EATR, which demonstrates the potential for extremely high EMTRs that sudden-death income tests create. Of course, if the family has private hospital cover, they are not subject to the Medicare levy surcharge and such high EATRs at these points would not exist.

NATSEM paper
Figure 10 **EATRs for a family with the father earning $1708 per week and the mother earning $32.90 per hour with one, two or three children – one child in child care at $4.30 per hour**

Data source: NATSEM calculations

**Low income couples with one child in cheaper child care**

What would be the effect of cheaper child care on disposable incomes? If a low income couple could access child care at $3.50 per hour, rather than $4.30, their disposable income would be higher. As you can see in Figure 11, the disposable incomes of the families with cheaper child care rise faster than for families paying $4.30 per hour for child care. This gap widens over time, as child care usage is related to the number of hours worked by the mother. When the mother works 35 hours per week, her family’s disposable income is $36 per week higher if she can access cheaper child care. The general pattern of income increases is still quite similar for these families, irrespective of whether they pay $3.50 or $4.30 per hour for child care.
3.2 EATRs for lone mothers

To enable comparisons over time, this paper has closely followed the methodology used by Beer (1998b). In that paper Beer looked at the financial incentives to work for partnered mothers only. How do the work incentives for lone parents compare with those for partnered mothers? This paper gives preliminary results for lone mothers, with one lone mother family modelled – a low income lone mother with one child in child care. Figure 12 compares the disposable incomes for two mothers earning $11.70 per hour with one child – one mother has a partner and the other does not. Interestingly, the difference in disposable income between the two families is almost the same when the mothers do not work or work 35 hours per week – around $220 per week. The disposable income of the partnered mother’s family does not increase as quickly as the lone parent’s when the mothers increase their hours worked from 4 to 19 per week. This causes the difference in disposable income to drop to $158 per week. When they increase their working hours up to 35 hours per week, the partnered mother enjoys more rapid increases in disposable income, so the income differential widens again.
Is it worth working now?

Figure 12 Family disposable income for a family with a lone mother earning $11.70 per hour or a father earning $515 per week and a mother earning $11.70 per hour with one child – one child in child care at $4.30 per hour

Data source: NATSEM calculations

As Figure 13 shows, both mothers experience high EATRs at some stage as they increase their working hours, with the partnered mother facing her highest EATRs between 8 and 19 hours per week. The lone mother’s highest EATRs occur when she increases her work from 20 to 35 hours per week. The partnered mother’s EATRs are

Figure 13 EATRs for a family with a lone mother earning $11.70 per hour or a father earning $515 per week and a mother earning $11.70 per hour with one child – one child in child care at $4.30 per hour

Data source: NATSEM calculations

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high when she works just a few hours a week because the combination of her income and her partner’s income of $515 per week means she loses the small amount of Parenting Payment Partnered to which she was entitled, as well as reductions in FTB-B and maximum rate FTB-A. In contrast, the lone mother’s first few hours of work keep her below the income test threshold for Parenting Payment Single (PPS). It is only when she goes from working 6 hours to 7 or more that she starts to lose some of her PPS. Preliminary work suggests that the situation for other lone mother families is similar.


4 Conclusion

This paper examines the financial incentives for mothers to increase their workforce participation. It follows the methodology in Beer (1998b) and looks at the EATRs for families with different income levels and numbers of children.

Low income couples with children often gain very little disposable income when the mother increases her hours of work. Indeed, for some increases in hours the family can actually be financially worse off. Families with more children tend to gain less disposable income because they receive more FTB-A, which is then withdrawn over a wider range of private income. This also contributes to the generally higher EATRs for families with more children – for every hour that a low income mother with three children works above 8 hours per week, she loses at least 60 per cent of her hourly wage to tax, income tests on government cash payments and net child care costs.

For lower middle income couples with children the picture is a little brighter. The higher initial income and the mother’s higher hourly wage allow them to “escape” from the extremely high EATRs that the low income families experience. For most increases in hours worked the mother faces an EATR of at least 40 per cent – and often above 60 per cent. Families with one child experience lower EATRs because they are only entitled to the base rate of FTB-A, which reduces their EATR by 30 percentage points for the first 16 hours the mother works, compared with a family with three children.

Upper middle income couples with one child face higher EATRs than couples with more children when the mother’s hours increase from 25 to 35 per week. Over part of this range, the family’s base rate FTB-A is withdrawn. The couple with three children are protected from this by the higher threshold applying to them.

Even high income couples with children can face high EATRs, if they do not have private hospital insurance. For high income families, the additional costs of child care make up a smaller proportion of the mothers hourly wage rate than for lower income families so their disposable incomes increase faster.

A lone mother with one child keeps the same in dollar terms as a partnered mother with one child when they go from not working to working 35 hours per week. Though both mothers face high EATRs for some hours worked, they do so at different times – the partnered mother’s highest EATRs occur in her first 20 hours of work, while the lone mother encounters her highest EATRs when she increase her work from 20 to 35 hours per week.

The results of this paper suggest that some mothers face a difficult decision to return to work or increase their hours of work. The interaction of the tax and social security

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systems and the additional burden of increasing child care costs mean that for some types of families, particularly those on low incomes, the financial incentives to work can be quite small. While high income couples get to keep half of the mother’s earnings when she goes from not working to working 35 hours per week, low income couples get to keep less than a third.

If you subscribe to the stepping stone argument – that a low paid casual or part-time job now may lead on to a higher paid job with more hours in the future – then this result should be worrying. The very people who stand to benefit from greater participation in the workforce are the ones who face the highest financial disincentives to do so. Furthermore, while in the long run it may be worth working even when the family is financially worse off now, those on low incomes are the least likely to have the financial capacity to do this.
### Assumed hours of child care usage per week per child aged under 5 years

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*Source: Beer (1997)*
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