Eradicating Child Poverty in Britain: Welfare Reform and Children since 1997

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Abstract
In 1997 the new Labour government in the UK inherited a situation where nearly one in 5 children lived in a household where no adult worked and around one in 3 lived in relative poverty. Children had replaced pensioners as the poorest group in society. The incoming government set about an ambitious set of reforms deigned to reduce poverty and worklessness amongst families with children. This policy reform agenda contained some features akin to the welfare reform process being undertaken in the US since 1996. But with one fundamental difference, that welfare payments to jobless families rose rapidly and there is no time restriction in access to these payments. This paper describes the key features of the welfare reform process and documents the reforms to welfare payments and in particular contrasts them with the US system. The results show that the reformed UK welfare support system, taxes and benefits, for children is more generous to low-income families with children but less for better off families. So the UK system is more progressive among families with children. The paper goes on to look at the emerging evidence of the impact of the UK policy reform process on poverty and welfare dependence.

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Introduction

''Our historic aim will be for ours to be the first generation to end child poverty.''

(Tony Blair, Beveridge Lecture, 1999)

Perhaps the most ambitious commitment made by the current Labour Government in the UK is its stated intention to eliminate child poverty within a generation—defined as 20 years. In this chapter we discuss the Government's motivation for this initiative, what the Government means when it talks about child poverty, and the welfare reform strategy developed to achieve it. We then discuss what the reform package has accomplished so far. We follow this with a look at future developments the Government has announced or proposed but not yet implemented. We conclude with a short discussion of what we see as the strengths and weaknesses of the Labour program.

Motivation

We do not address here the factors leading up to and influencing Labour's child poverty initiative. Rather we concentrate on the economic and social evidence on which the Government bases its commitment. This evidence falls into three parts: how the changing British economy has affected the ability of working-age adults to secure incomes above poverty levels, the particularly stark deterioration in the circumstances of Britain's children relative to other groups, and the mounting evidence that deprivation in childhood adversely affects a person's long-term outlook. The importance attached to this evidence is apparent in a number of Treasury publications, in particular analyses of developments in the labour market (HM Treasury, 1997), the problems of inactive workers (HM Treasury, 2001), and poverty dynamics and life-chances (HM Treasury, 1999a).

The Changing Economy

Of the many changes in the British social economy over the past two decades that have affected the ability of working-age adults to secure incomes above poverty levels, four are particularly important: (1) growth in workless households, (2) increased earnings inequality, (3) reduced earnings mobility, and (4) an increased wage loss from spells of unemployment.

(1) Britain has one of the highest employment rates among developed nations, with 75 percent of working age adults in work (a fraction below that in the US). Although this aggregate employment rate has been pretty stable, the share of households with at least one working age adult but no one employed has grown sharply, from 8 percent in 1979 to 17 percent in 2000 (Gregg and

Wadsworth, 1996 and 2002a). The latter compares with around 10 percent in the US (Gregg, Scutella and Wadsworth, 2002). Over the same period, the number of UK households where all adults are in work has increased. About a quarter of this rising gap is due to a relative increase in single adult households, with the rest due to a polarization of work that produces both more workless and more fully employed households (Gregg and Wadsworth, 2002a).

(2) Among developed nations over the period 1979 to 1995, the UK was second only to the US in its absolute increase in the ratio of the 90^{th} earning percentile to the 10^{th} (OECD, 1996). Male wage inequality continued to grow in the UK between 1990 and 1996, but at a slower rate than in the 1980s. Since 1996 wage inequality has changed little (Tables A28 - A33, Office of National Statistics, 2000; for more detail and interpretation, see Machin, 1999; or Gosling, Machin and Meghir, 2000).

(3) The extent of mobility up and down the UK earnings distribution has fallen sharply since the late 1970. For example, 29 percent of men in the second lowest earnings decile in 1979 were still there a year later. By 1988, this measure of earnings persistence had risen to 37 percent (Dickens, 1999, p 218), and it has been broadly stable since.

(4) On average, men who lose jobs and take up unemployment-related benefits return to work on, and remain at, lower wages than in their previous jobs. The past two decades in the UK have seen this wage loss grow (Nickell et al, 1999; Gregg and Wadsworth, 2000a). What is more, job loss is not evenly distributed across the labour force. For example, the lowest paid tenth of men are twice as likely not to be earning a year after a job loss as are those in the middle of the earnings distribution (Dickens, 1999).

Taken together, these four trends suggest that lifetime earnings inequality may have risen even faster than the inequality evident in conventional cross-sectional measures. In addition, reductions in income tax rates and a failure to increase welfare benefits in line with average real incomes have further increased after-tax income inequality (Johnson and Webb, 1993; Clark and Leicester, forthcoming). These developments have contributed to a general increase in poverty in the UK, with growth in poverty among children especially marked.

Income Poverty and Worklessness in Households with Children

Over the last twenty years, children have replaced pensioners as the poorest group in UK society. While average incomes among elderly households, even among the poorest fifth, have risen in real terms, the poorest fifth of children in 1996/7 were in households with real incomes no higher than those of the corresponding group in 1979 (Gregg, Harkness and Machin, 1999). Poverty during childhood—defined, following traditional UK practice, as household income less than 50 percent of the national mean—is now almost evenly split between in-work poverty (an earner in the household) and workless poverty (no working adult present). [1] In 1996/7, nearly 20 percent of UK children lived in households where no adult worked, up from 7 percent in 1979 and 4 percent in 1968. Ninety percent of these children were in poor households, creating a large spike in the income distribution substantially below the poverty line.

The UK, at 20 percent, has a substantially higher share of children living in workless households compared with other developed nations. The country with the next worst record in 1996 was Ireland, at 15 percent. In all other European countries the share of children in workless households in 1996 was 11 percent or less (OECD, 1998, p 12). Even before the current emphasis on getting people off welfare, only 10 percent of US children lived in a household where no adult worked (OECD, 1998; Dickens and Ellwood, 2001).

The increase in the proportion of UK children in workless households is driven by more lone parents being workless (due partly to a small decline in lone parents' employment rates, but also to an increasing propensity for lone parents not to live with other relatives), a rise in the number of lone parent households, and an increase in the proportion of workless couples.

The increase in child poverty over past decades, on the other hand, is due to an increase in the incidence of poverty for all family types combined with an increased proportion of children in lone parent families, who have much higher poverty rates than do couples with children. For example, one-quarter of all children living with two parents were in poverty in 1996/7, up from one-tenth in 1979 (Gregg, Harkness and Machin, 1999). Over the same period, poverty rates among children of lone parents rose from one in two to two in three, whilst the proportion of all children living with a lone parent rose from around one in ten to a little more than one in five.

[1] Income is adjusted for household composition using the McClements scale: this uses a couple with no children as a reference household, and adjusts incomes of households with different compositions. There is no agreement on what the right equivalence scale should be, but the UK Government and academics have used this one for over 20 years. As is the case for the US poverty line, the main advantage of the McClements scale is consistency (these issues are explored further in Banks and Johnson, 1993). Income is also calculated after subtracting housing costs; this helps regional comparisons and problems comparing expenses for homeowners and renters. The definition used by the current UK Government is discussed later in this chapter.

Comparative studies suggest that the US has higher child poverty levels on a within-country relative income measure, but lower levels on an absolute measure—such as the US official poverty line—because US living standards are higher across the distribution. For example, on the same relative poverty definition (50 percent of mean income before taxes and housing costs, adjusted for family size) the US whole-population poverty rate rose from 25 percent in 1979 to 32 percent in 1999 (Dickens and Ellwood, 2001), while in the UK it rose from 11 percent to 26. But 29 percent of UK children were living on incomes below the US poverty line in 1995 (Bradbury and Jantti, 1999) compared with 21 percent of US children (Dalaker, 2001).

The Impact of Deprivation on Life Chances

Growing acceptance among UK policy makers that childhood deprivation has longer-term consequences was probably the most crucial factor in the assembling the political will to address childhood poverty. That children growing up in deprived households and communities do less well in terms of life chances has long been documented in cross-sectional correlations, but these cannot establish causal links. More recently, a literature has emerged that suggests that financial deprivation has an identifiable impact on educational attainment, wages, employment rates and other social outcomes in adulthood—even after controlling for child ability and family background (Blanden et al, 2002; Gregg and Machin, 2000a and 2000b).

The UK literature relies mainly on the birth cohorts of the National Child Development Survey of 1958 and the British Cohort Study of 1970. These surveys follow children from birth through to adulthood, giving a wider range of individual child and family characteristics than is common in other available evidence. These data reveal (1) an increased intergenerational income correlation as income inequality rises and (2) evidence that children growing up in financially deprived households underachieved in terms of education, were more likely to contact with the police and probation services, and experienced higher unemployment and lower wages in adulthood. Since these studies can control for a wealth of aspects of child and family background but not for residual unobserved family or child differences, they may somewhat overestimate the impact of financial deprivation. A more important limitation is that they cannot say conclusively, since some of the studies relate to childhoods in the 1960s, whether the effects identified are associated with relative or absolute deprivation. These limitations are not true of the US evidence that child-based interventions can make a difference to child outcomes for a range of deprived children, which was perhaps equally influential in the debate. In particular, evidence that the Head Start program (Currie and Thomas, 1995) or the Abercedarian Project (Ramey and Ramey, 1998) made substantive differences to child development for children from low income families suggests that, whatever the causal origin, educational disadvantage among deprived children is malleable by policy intervention.

Measuring and Defining Child Poverty

The Prime Minister's pledge to end child poverty is a dramatic one, and appears to be deeply felt. The Government has been slow to translate this formally into a specific and measurable target, however, for both institutional and intellectual reasons. First, the UK has never had an official poverty definition: welfare programmes do not have an income cut-off such as (say) 150 percent of the poverty line, as is common in the US.

The closest equivalent—which is often used by academics, commentators, and, indeed, the Labour Government on occasion—is a relative definition of poverty, counting a household as poor when its income is below some point in the income distribution. The most common definition used since 1999 has been 60 percent of median household income (adjusted for household size, and after subtracting housing costs). This is similar to the European Union's preferred indicator of poverty, which also uses 60 percent of the median before housing costs but different adjustment scales for household composition.[2] Measuring incomes after housing costs results in 4.4 million UK children (34 percent) living in relative poverty in 1996/7 (the year before Labour came to power), compared with 1.7 million (14 percent) when Labour last held office in 1979. This is the single statistic most commonly used by the Government to describe its "inheritance". The 1996/7 relative poverty line corresponds (in 1996/7 prices) to annual disposable incomes after deducting housing costs of £8,013 and £9,458 for a couple with (respectively) one and two children; before deducting housing costs, the numbers are £9,225 and £10,889. In 1996, the official US poverty standards for the equivalent families were £8,344 ($12,516) and £10,691 ($16,036) (see Bureau of Census, 2000).

Using this definition, the Government set itself a short-term target to reduce child poverty by a quarter of its 1998 level by 2003 (DWP, 2001). But use of a poverty measure based on relative income has disadvantages that are well recognized by the Government. One is that rising living standards and rising poverty rates can occur simultaneously, as indeed was the case in Ireland in the latter half of the 1990s. Although these two events are mathematically completely consistent, they may well not accord with the politicians' or the populace's view of what poverty is, which may undermine the credibility of an anti-poverty campaign. Another significant problem, which is true of both relative and absolute measures defined in terms of income, is that an income-based poverty line will show the effects of income transfer programmes almost immediately, whilst programmes to reduce long-term disadvantage or the damaging effects of living in a low-income household will barely register. This is particularly important, given that UK policy-makers tend to think about child poverty not simply in terms of relative (or absolute) low incomes, but also in terms of childhoods that can be damaging due to a sustained lack of financial resources in a household. This anti-poverty agenda is, thus, part of a wider "opportunity agenda" (HM Treasury, 1999a), which aims to reduce the incidence and severity of circumstances that have long-term adverse repercussions for individuals.

Partly to address these issues, the Government has produced a range of "poverty" indicators since 1999 that cover relative incomes and absolute incomes—as well as education, health, crime, and labour market outcome incidences. Thirteen of these are directly related to children (Department for Work and Pensions, 2002). But a multitude of indicators gives no clear standard by which to judge when child poverty has been "abolished". The Government, therefore, is currently debating openly how to "[measure] poverty in a way that helps to target effective policies and enables the Government to be held to account for progress" (DWP, 2002b). The debate is looking at four options: (1) maintaining the multi-dimensional indicators, (2) aggregating some subset of these into a single index, (3) focusing only on income-based measures, and (4) measuring relative low incomes and material deprivation simultaneously—as does the official poverty measure now adopted by the Irish government (Nolan and Whelan, 1996; for the theory; Callan et al, 1999; for the practice).

The material deprivation measure is increasingly common in the European literature on poverty. It counts people as poor if they lack socially perceived necessities, which might include adequate food consumption, clothing, and other basic commodities. There have been a number of such studies in the UK, none of which, unfortunately, are directly comparable. The most recent is the Poverty and Social Exclusion Survey (Gordon et al, 2000).

The Strategy

The policy response to child poverty and its consequences has three main components: (1) raising direct financial support to families with children; (2) reducing worklessness in households with children; and (3) ameliorating the long-term consequences of child poverty.

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[2]The main difference is that younger children are given a higher weight than in the UK McClements scales. This places the child poverty rate for the UK on the EU basis half way between the before housing cost measure and the after housing cost measure, at about 28 percent in 1998.

1. Raise direct financial support for families with children, targeted on—but not exclusive to—low-income families

The most immediate and obvious response to observed low incomes in many families with children is to increase the net transfers available through the tax and benefit system. Between 1997/8 and 2002/3, spending on the four main programmes that provide financial support for families with children is predicted to increase by 58 percent (or £7.8 billion a year, around £1,100 for each family with children in the UK [3]). Around a third of this increased expenditure for children has the sole goal of reducing the relatively low incomes experienced by the poorest children. This child-specific support has been buttressed by increased general support for low earners. A National Minimum Wage (NMW)—the first in the UK—was established in 1999. Reforms to the National Insurance scheme (roughly equivalent to the Old Age, Survivors, and Disability Insurance programs in the US) lowered costs for low-age workers and their employers. The starting rate of income tax was lowered from 20 to 10 percent to further increase take-home earnings in low-skilled entry-level jobs.

The new child-specific resources have been delivered through both expanded tax credits and cash transfers. The tax credits include the Working Families' Tax Credit (WFTC), the associated Childcare Tax Credit, and the Children's Tax Credit. Increased cash payments have come in Income Support benefit rates for children (mainly paid to workless families) and in the universal Child Benefit. Although the WFTC has received more press and analytical attention than any of the other reforms aimed at increasing the generosity of support for families with children, this emphasis is misleading. The changes since 1997 should be considered together, because they combine to form a systematic overhaul of the structure of financial transfers to the 7 million families and the 13 million children in the UK. Their inter-relationship is made clear in the Government's announced plan (discussed below under Future Directions) to merge all the major parts of financial support for children into a new child tax credit in 2003 (Inland Revenue, 2001; HM Treasury, 2002).

Here is how the child-specific reform package differs from the programs that went before. Before the 1998 budget, support for children came from four sources: a universal per child transfer (Child Benefit) normally paid to mothers; extra payments in means-tested benefits for those not working (Income Support or Jobseekers' Allowance) normally paid to the family head; a refundable tax credit for working families (Family Credit) paid to the mother; and one of two related non-refundable tax credits available to

[3] This estimate, in 2002 prices, is from a micro-simulation model, and includes only the cost of the changes to child benefit, family credit/WFTC, income support for families with children, and the children's tax credit compared with a world where child support was unchanged in real terms between 1997 and 2002. It does not count the saving from abolishing the married couples' and related allowances. Families with children will also have been affected by budgetary reforms affecting all families: These overall impacts are summarized in Figure 4.1 in Brewer, Clark and Goodman, 2002.

one taxpaying earner per family (normally the father). Starting with the March 1998 budget, the Government has increased the generosity of all four of these, and all but the Child Benefit have undergone structural change.[4]

Increased generosity of Child Benefit. The 1998 and 1999 Budgets together raised the real level of Child Benefit by 27 percent for the eldest child, with inflation-only increases for younger siblings.[5] The increases in support for children in means-tested benefits have been focused on younger children: between April 1997 and 2002, in real terms weekly payments for children aged 0-4 rose by £15 a week—an 82 percent real increase—and those for children aged 11-15 rose by £6.50. The result is that financial support for children up to age 15 has been equalized—older children had previously received more generous support. This reform partly reflects recognition by the Government that poverty rates were higher among families with younger children and partly facilitates the proposed move to a child tax credit, with its emphasis on simplicity and transparency.

As in the US, Britain increasingly uses the tax administration service to target transfers to families with children. The UK has an individual system of income tax with an exact with-holding system. Credits and allowances appear in a person's tax schedule, which employers then use to assess and deduct income tax directly from wage or salary payments. Allowances are typically less generous than in the US, so people start paying income tax at lower annual incomes (Gale, 1997; Brewer, 2001; for more comparisons of the US and UK tax systems).

Children's Tax Credit. This credit (which will only exist between April 2001 and April 2003, when it will be merged into the proposed new Child Tax Credit) is a non-refundable tax credit that replaces two mutually exclusive and equal-valued tax credits: the Married Couple's Allowance (MCA) and the Additional Person's Allowance (APA). The overall impact is that, since 1999, married couples without children have lost a tax break, and families with children, regardless of their marital status, have seen a tax break more than double in value. The MCA and APA were available to all taxpayers, but the Children's Tax Credit is withdrawn at 6.7 percent from people paying higher rates of income tax (over £34,515 from April 2002), similar to the Child Tax Credit in the US. It is doubled in value for families who have a child under 1 year old.

[4] There was one cut: lone parent benefit, a small addition to child benefit for lone parents, was abolished for new claimants in 1998. The cost estimates presented here do not account for the consequential saving, but the Figures later on do.

[5] Rates correct as of April 2002. Real-terms comparisons for Child Benefit use the RPI index, other benefits use the ROSSI index (which is the RPI index less housing costs)

Working Families' Tax Credit. The WFTC is an evolutionary reform to the existing in-work benefit, Family Credit. Announced in the Labour Government's first full budget in spring 1998 and available to claimants from October 1999, it is available to families with children where any adult member is working 16 hours a week or more. It consists of a per-family element—the same for couples and lone parents—and per-child elements. There is a very short flat zone where the maximum award is paid, and the credit is phased out beyond earnings of £94.50 a week at a rate of 55 percent of after-tax income. For a person on the basic rate of income tax and paying National Insurance contributions (like payroll tax), this adds up to a total effective marginal tax rate of 69 percent, a rapid rate of withdrawal compared with the combined phase-out faced by Earned Income Tax Credit (EITC) claimants in the US.[6]

The WFTC is more generous than its predecessor, as both the family and the child elements have been increased. For a family with one child, the WFTC is worth a maximum of £86.45 a week—or around $6,700 a year, substantially more than the EITC in the US. Each additional child raises the maximum credit by £26.45 a week. But most of this increased generosity in the maximum value of the WFTC has been matched in the level of out-of-work support, and so has by itself made little difference in the financial gain from moving from welfare to work. In addition, families can earn more before support is withdrawn, and the withdrawal rate has been lowered. These changes have increased support for those in full-time or better-paid part-time work (i.e. earning more than £94.50 a week in 2002 prices) and extended eligibility for in-work support to a large number of families.

Childcare Tax Credit. This new refundable credit pays parents up to 70 percent of formal, registered childcare costs up to a (generous) maximum of £135 a week for 1 child (£200 for more than 1 child). The Childcare Tax Credit entitlement is a supplement added to the credits in WFTC and is treated in the same way as WFTC in all respects. It is, however, restricted to households where all parents are in paid work, although lone parents have been the prime beneficiaries to date. This represents a substantial increase in generosity of support for childcare costs over the regime under Family Credit, which only offered a childcare cost disregard rather than a direct cash payment.

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[6] In other words, for most WFTC claimants, the WFTC withdrawal adds 38 percentage points to the effective marginal tax rate. This rate measures what proportion of an extra pound of income is lost to income tax and national insurance payments, as well as withdrawn welfare benefits and tax credits. The higher the effective marginal tax rate, the lower the incentive to work for any additional earnings.

2. Reduce the number of children living in workless households

The second part of the strategy is to reduce the numbers of workless families with children. This part of the strategy contains elements designed to improve the financial returns to employment, a reform of welfare administration to develop work-oriented case management of the welfare dependent population, and improvements in childcare opportunities.

Reform of tax and benefits structure. This reform, described above as increasing the direct financial support to families, is not neutral in its impact on the financial attractiveness of employment. The package was deliberately slanted toward increasing the net gains from employment, or, in the jargon, to "making work pay". The specific work incentive features are two. First, the maximum weekly earnings level at which withdrawal started under the old Family Credit system was £77.15. This has increased by £13.70 in real terms. Thus, earners can keep 100 percent of what they earn up to a higher earning level than before. Second, the withdrawal rate was lowered from 70 percent to 55 percent of net-of-tax income, implying that less is taken out of each additional pound earned above the level at which withdrawal starts.

These reforms generally increased support for full-time or better-paid part-time work. For lower-paid, part-time lone parents, the improved incentives come mainly through the increased support for childcare costs in the Childcare Tax Credit.

Case management. The New Deal employment strategy also involves development of a case management approach to promoting work by welfare recipients. This was already partially developed for those claiming unemployment-related benefits in the UK, but has been extended substantially under the New Deal framework. Nearly all welfare participants are now contacted by a Personal Adviser to establish if they want to work or participate in a program to improve job-readiness. The New Deal for Lone Parents and the New Deal for Partners are particularly relevant for families with children—groups that had previously been ignored in strategies to encourage employment.

National childcare strategy. This strategy aims to create childcare opportunities for all those wishing to use them. Out-of-work parents, and especially out-of-work lone parents, identify the absence of available and affordable childcare as a major barrier to increasing employment (Finlayson and Marsh, 1998; Shaw et al, 1996). The essential problem appears to be that, given wages available to mothers, the supply price of formal childcare is too high to create demand in low- and even middle-income areas. The Government strategy here is to both reduce the effective cost to parents and to stimulate supply. The Childcare Tax Credit described above affects the demand side by directly helping parents afford paid childcare places. The supply side of the strategy consists of a guaranteed half-day place in a pre-school for 4 year olds (run by state schools that provide full-time schooling for 5 to 7 year olds, and soon to be extended to 3 year olds), Early Excellence Centres, and Neighbourhood Childcare Centres, which provide subsidized childcare in some of the poorest communities and encouragement for schools or Local Authorities to run After School Clubs and holiday play schemes.

3. Reduce incidence and severity of scarring factors from childhood and early adulthood

The third major arm of the strategy is to try to reduce the impact of deprivation on educational attainment, and to limit the carry-over of social problems to adulthood. There is a diverse range of initiatives targeted at key life-stages or events, generally originating from the Social Exclusion Unit attached to the Prime Minister's Cabinet Office (Social Exclusion Unit, 1998). These cover teen pregnancy, children leaving social care, and homelessness among the young. In addition, a failure to connect to stable employment during the teenage years has been identified as causally linked to higher unemployment and lower wages in adulthood (Gregg, 2001; Arulampalam, 2000). The New Deal for Young People aims to eliminate long-term youth unemployment, and to improve matching with sustained employment among youth. Chapter 6 provides details on this aspect of reducing long-term disadvantage. Here we focus on those parts of the strategy directed at low educational attainment.

On international assessments of comparable reading and math abilities among adults, the UK—along with the US—has a high variation in standards and a large number of adults with low levels of literacy and numeracy (Layard, McIntosh and Vignoles, 2000). Schools with high levels of child poverty among their pupils underachieve on school-leaving exams and generally have fewer pupils staying in education after the minimum leaving age of 16. To what extent this underachievement is due to teaching quality or the attendant problems the children bring with them remains controversial. Since income itself can only be partially responsible for this low achievement, it makes sense not only to improve incomes but also to address the education deficit directly. Sure Start, school attainment in poor areas, and Educational Maintenance Allowances (EMAs) tackle this deficit from birth through to the end of the teenage years.

Sure Start. Sure Start is perhaps the most important of these initiatives so far. Its design was loosely motivated by the US Head Start program (Currie and Thomas, 1995), but there are large differences in the details. Sure Start is targeted on children aged 0 to 4 living in the most disadvantaged communities in the country. It aims to promote physical, social, and emotional development of children, and hence to make them more ready to learn by the time they enter into school. So far Sure Start programs operate in some 200 poor communities, but there are well-developed plans for expansion. These do not always overlap with the childcare centres mentioned above, but overlap and co-ordination is increasing as both expand.

Raising educational qualifications on leaving school. Successive governments have developed an extensive series of tests to assess child development through the education system. These are undertaken at ages 7, 11, and 14. Final examinations on leaving secondary school (always referred to as GCSEs, which stands for General Certificates of Secondary Education) are undertaken at 16. These tests are increasingly used to assess the value-added made by a school, and to highlight under-performance. Schools have regular inspections by Government-appointed inspection teams, and failing schools may be closed or have their senior teaching staff replaced. Local Authorities are also assessed for the support structures they supply. Again, failing areas may lose local control and be replaced by private-sector management consortia. One of the key aims of this near-continuous assessment regime is to raise standards of achievement amongst poorly performing pupils and schools. This is being supported by extra financial resources directed at children with greater learning needs, rather than explicitly focused on poverty. There has been no attempt, however, to break with nationwide pay scales for teachers (which allow only for a small "London bonus") to make teaching in schools serving more deprived areas more attractive to high-quality teachers.

Educational Maintenance Allowance. Compulsory full-time education ends at age 16, and the one third of young adults who cease full-time education at this point are those, unsurprisingly, with fewer qualifications and from less well-off families. Educational Maintenance Allowances (EMAs)—means-tested cash payments to young adults who continue in post-compulsory full-time education—are being piloted in a number of disadvantaged areas, and will be available nationally from 2004. They are designed to raise educational participation, retention, and achievement after age 16. Four variants are being piloted, with the maximum weekly payment ranging from £30 to £40 per week subject to full school attendance, plus retention bonuses each semester, and a final achievement bonus. As well as the financial amounts, the variants are also testing whether it matters to whom in the household the payments are made.

The evaluation strategy is to compare outcomes of young adults in areas where the EMA is available with outcomes of young adults in similar areas where the EMA is not available. A matching approach based on propensity scores is used to control for differences in young people's characteristics that might influence their educational outcomes. So far, the evaluation has focused on whether EMAs have affected participation. Results indicate that they increased it. Amongst young people eligible for the full allowance—approximately one third of young people in the pilot areas, with gross family incomes under £13,000—participation increased by around 7 percentage points. Since the increase in participation was lower for those eligible for less than the full amount of EMA, the average effect over all young people eligible for some payment was an increase of around 5 percentage points (Ashcroft et al, 2001). As data emerges, the evaluation will go on to assess impacts on attendance and course completion.

What the Reform Package Has Accomplished So Far

The reform package aims to reduce child poverty—not only through increases in child-specific financial support, but also through reductions in the numbers of children in workless households, particularly lone parent households. The latter goal is to be achieved through reductions in marginal deduction rates and increases in the overall returns to work. This section looks, in turn, at what the reform package has done to (1) numbers of children in poverty, (2) overall financial support for families with children, (3) marginal deduction rates and overall returns to work, and whether the incentives embodied in the reforms are, in fact, changing behavior —i.e., increasing employment among lone parents.

1. Numbers of children below the poverty line

As of April 2002, there are two ways to analyse the impact of the reforms on incomes, and on child poverty. Micro-simulation models can predict the first-round changes in incomes that should arise through the reforms, compared with a base system of no real changes to taxes and transfers. The use of relatively high phase-out rates for in-work and means-tested benefits means that the beneficiaries from the extra money directed towards families with children since 1997 are heavily concentrated in the poorest households (Figure 1). Households with children in the second and third income deciles see disposable incomes rise by over 6 percent, whereas families in the top three deciles gain by less than 1 percent. Of course, the general focus on children in successive budgets means that all these households are gaining relative to households without children.[7]

Figure 1: **Estimated income gains for families with children from increases to child support, 1997-2002**

Micro-simulations can also estimate the impact these reforms would have on child poverty. A number of different studies of the impact of the reforms between April 1997 and April 2001 (a slightly different period from that used in the rest of this chapter, but one that corresponds to the Labour government's first term in office) all suggest around 1.2 million children would be lifted out of

[7]These calculations do not analyse changes in the personal taxes and benefits that affect all families: This is shown in Brewer, Clark and Goodman (2002). The effect of Labour's first-term in office on family incomes overall is analysed in Clark, Myck and Smith (2001). None of these simulations allows for behavioural changes from the reforms.

relative poverty, assuming nothing changed between April 1997 and April 2002 except taxes and benefits (Piachaud and Sutherland, 2001; HM Treasury, 2001; Brewer, Clark and Goodman, 2002). This assumption is, of course, unrealistic. It is also potentially misleading, given that the UK Government has explicitly accepted that its notion of child poverty is a relative one and real incomes are generally rising. A better way, then, to assess the impact of the reforms on child poverty is to use actual data on the changing distribution of incomes. The latest official data cover the 2000/1 financial year, and show that the number of children poverty had fallen by 0.5 million since 1996/7.[8] Between 1996/7 and 2000/1, the poverty line grew by some 10 percent in real terms: if we disregard this, and merely count the number of children in 2000/1 in households below the 1996/7 poverty line (fixed in real terms like the US Census Bureau's poverty thresholds are), then child poverty would have fallen by 1.3 million, or 30 percent, in just 4 years.

The changing shape of the income distribution for children is shown in Figure 2. As can be seen, the increased generosity of the package is helping to raise incomes of the poorest families with children in real terms. It is also moving the large spike in the income distribution of children closer toward the relative poverty line, although it has so far has pushed only a small minority of children across this line. This shows how hard large reductions in relative poverty are to achieve. On a more encouraging note, real incomes of the poorest fifth of children are rising rapidly for the first time in twenty years. If the spike continues to move to the right faster than the poverty line, the impact on relative poverty will be greater.

Figure 2: The changing real income distribution for children in low-income households

2. Increased financial support to low-income families with children

As noted above, the reform package includes four major programs designed to increase the disposable incomes of families with children: the Children's Tax Credit; the WFTC; a higher level of Income Support; and a more generous Child Benefit. The effect of these changes is compared with the situation before reform in Figure 3. Panel A of the figure shows the total cash support available for a live-alone parent with two children under 11 under the pre-reform (1997) support package. Panel B shows the total support available to the same stylised family post-reform (as of April 2002). (A figure for couples with children would be identical except for the income support payments, which would be higher in both cases). The figures do not show the impact of the generous Childcare Tax Credit, because it is difficult to choose a single value of childcare costs that is plausible throughout the

[8] Analysis of data covering the last 6 months of 2000/1 – which fully captures the large increase in children's allowances in means-tested benefits in October 2000 – shows a fall of 650,000 children since 1996/7: see Brewer, Clark and Goodman

indicated income range: This omission makes the reformed system appear less generous than it is to those working but on a low income and with some formal childcare costs.

Figure 3: Total financial support by gross income, before and after reform

The real world impact is always more complicated than these sorts of charts imply. In particular, the Figure does not capture all the potential interactions between welfare programmes and tax credits. The two programmes of concern are Housing Benefit, which supports low-income households with rental costs (owner-occupiers normally get no housing support), and rebates against local taxes, known as Council Tax Benefit. Both of these benefits are withdrawn as income rises, but crucially—unlike the EITC in the US—WFTC awards count as income when calculating awards of these benefits. There are two implications for families with children with relatively high rents or local taxes. First, the extra generosity of WFTC awards over Family Credit may be largely offset in smaller HB and CTB awards. Second, such families will also be on multiple benefit withdrawals with effective marginal tax rates of over 70 percent. In fact, the introduction of the WFTC has substantially reduced the number of households who are in work but facing effective marginal tax rates over 70 percent (as shown in Table 1 in the next subsection). The large number of families with children where no adult works are much more likely to be claiming Housing Benefit than those currently in work, and hence the impact of the WFTC on the incentive to work 16 or more hours remains muted by its interaction with Housing Benefit.

How does this situation compare with its US counterpart, the EITC? This question is particularly appropriate given Chancellor Gordon Brown's assertion, when the UK Government first announced that it was interested in reforming in-work support, that it would examine "the advantages of introducing a new in-work tax credit for low-paid workers… [and] would draw upon the successful experience of the American earned income tax credit, which helps reduce in-work poverty" (Hansard, 2 July 1997). Even now, there is a strong political resonance between the WFTC and the EITC: In the words of the respective political leaders in the late 1990s, both support "hard-working families" and "reduce child poverty".

A direct financial comparison between the WFTC and the EITC (Brewer, 2001) suggests that the UK system is substantially more generous. But this comparison can be misleading, because the WFTC reduces entitlements to other benefits whereas the EITC represents truly additional income. What is less often realized is that the structure and administrative details of the WFTC

(2002); the official source is DWP, (2002e). There were some relatively small increases in child support in financial 2001, that are not captured by this data.

(following its predecessor, Family Credit) are also quite different from the EITC. Although the tax authority in the UK (the Inland Revenue) administers the system, the WFTC has little direct connection to the rest of the tax system, unlike the EITC, and does not operate as an annual tax rebate. Instead, it is paid either directly through the wage packet, or fortnightly, if it is paid to a non-working individual whose partner satisfies the work condition. For new jobs, the size of the award is assessed on expected weekly earnings. For claimants with stable jobs, it is calculated by looking at the past four pay cheques (seven if paid weekly) and then paid at the same rate for six months, regardless of changes in income.

This desire to get money to claimants quickly—rather than waiting for the end of the tax year—is primarily motivated by two concerns. First, most taxpayers in the UK have their income tax correctly withheld by employers, and only the rich, the self-employed, and those with complex tax affairs file a tax return. Second, people entering work on low wages would be worse off in work without the WFTC, because of the relatively high level of out-of-work benefits compared to the US. This means that the "real-time" work incentives of the WFTC are stronger than those provided by the EITC (Walker and Wiseman, 1997).

Of course, the WFTC and the EITC are not the only ways that the UK and US governments support families with children. In both countries, children are recognized in the benefit system by in-work refundable credits and by non-refundable tax credits or extra tax deductions or allowances. However, the vagaries of perception and political economy mean that these support systems are often presented from very different perspectives, making them difficult to compare.

In Figure 4 we summarize the two systems by comparing the full annual budget constraint—the relationship between gross income and income of taxes and benefits and welfare payments—for a live-alone lone parent with children in the UK in 1997 and 2002 with that in the US in 2001. The UK's system of financial support for children was broadly in line with that in US at lower incomes prior to the current reforms, but the reforms have made it substantially more generous. It is also more redistributive among families with children, with higher net tax rates at higher incomes than the US. The US system has been necessarily simplified: These figures do not include state taxes, state EITCs or Medicaid; we include Food Stamps; and we have assumed the TANF system operating in Florida, a relatively low-benefit state (Committee on Ways and Means, 2000, p 384). Housing support and help with childcare costs are ignored in both countries.

Figure 4: Disposable income after welfare and tax payments, by gross income, UK before and after reform, and US in 2001

Figure 4 gives a representation of the total budget. Figure 5 shows the supports specifically dependent on children, by calculating the cash difference in the budget constraints of a single person and a live-alone lone parent with 2 children.[9] In the UK (Panel B), financial support for children falls in cash terms as income rises, apart from the short phasing in of the non-refundable children's tax credit. This is not true in the US. First, the phase-in of the EITC gives a range where support increases with income at the lowest incomes. Second, after the EITC has been phased out, the value of the child exemptions and the head of household filing status increase with income. A striking feature of the US system is the trough after the EITC has been withdrawn and before the tax allowances and deductions increase in value (from around $50,000), discussed more in Ellwood and Liebman (2000).

Figure 5: **Financial support for children, by gross income, UK and US**

3. Marginal deduction rates and overall incentives to work

Marginal deduction rates for working families have changed as a result of the WFTC reform. The reduction in the headline phase-out rate from 70 percent to 55 percent and the fall in the number of families entitled to rent support have reduced the number of families on very high marginal deduction rates. But the increased generosity of WFTC has increased the number of families on some form of benefit phase-out. Before the WFTC was introduced, around 750,000 households had marginal deduction rates of over 70 percent, and 130,000 had rates over 90 percent (Table 1 shows these as 8.4 percent and 3.7 percent, respectively of all employees with children). The WFTC reduced these numbers to 250,000 (4.3 percent) and 30,000 (1.4 percent), respectively, but the numbers on marginal deduction rates of 60 percent or more rose by nearly 200,000, to just under a million. This may be an acceptable trade-off. However, if the WFTC continues to expand further up the income distribution, the terms of the tradeoff will rapidly deteriorate.[10]

Table 1: Distribution of marginal deduction rates faced by employees with children before and after reforms

The rates in Table 1 are above those typically found in the US because of the higher phase-out rates used in the UK. But work incentives are not universally worse in the UK, because a large discontinuity in the budget constraint in the UK makes families

[9] So, for example, it does not show the full award of food stamps for a 3-person household, but the difference between a 1 person and 3-person household. The same applies for the UK. This is the approach used by Ellwood and Liebman (2000), who look at the tax treatment of US families with children, and in Battle and Mendelson (2001), who compare systems of support in the UK, US, Australia and Canada.

become eligible for WFTC at 16 hours work a week. In fact, both countries seem to have good financial incentives for lone parents to do some work—assuming full take-up of all entitled benefits—but poorer incentives for lone parents to increase earnings beyond part-time or minimum-wage jobs (Brewer, 2001).

With respect to improving incentives to work more generally, the WFTC (including the Childcare Tax Credit) and the Children's Tax Credit combine to increase the financial returns to working rather than being on welfare. The intention is to induce entry into work, and so further reduce child poverty. This is because a reduction in the number of children wholly or nearly-wholly supported by the state is probably vital if the numbers in child poverty—given the use of a relative definition—are to be reduced. We look first at the gain to taking a job and then the effect of increasing earnings once in work.

Table 2 shows how the reforms have altered the financial gain to work—the difference in zero-income position on benefits and in-work income after taxes and benefits—for some benchmark families. (These calculations ignore in-work costs, but our focus on *change* in the gain to work minimises the impact of this omission.) The reforms have slightly improved the financial gain to work at 16 hours a week, but have had more of an impact on the incentive to do full-time work, particularly for lone parents (first row). For the first earner in a couple, the full-time minimum wage work (second row). The values for a single person (3rd row) show that the reform package has had very little impact on those without children.

Table 2: The effect of the reforms on the financial gain to work for parents with children

The other rows show variations on this theme. Because it is withdrawn as income rises, housing benefit typically dulls the financial incentive to work, and it also reduces the increase in the cash gain to work brought about by the WFTC (compare rows 4 with 1, 5 with 2 and 6 with 3). Working in the other direction, though, the Childcare Tax Credit produces a large improvement in the (net of childcare costs) gain from moving to work for a lone parent paying £50 a week for childcare (7th row of table; £50 a week childcare costs is slightly higher than the average of those currently claiming the Childcare Tax Credit). The negative aspect of the reforms is that entry into work by a second adult in a family where the primary worker earns £300 a week (the last row in the table) has seen a sharp drop in the financial incentive. Such a person had the highest return to full or part-time employment in

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[10] Table 1 assumes full participation in all income-related transfer programmes. This is a fair assumption for income support, where participation rates amongst eligibles is over 95 percent, but for family credit and WFTC, where participation rates are lower (72 percent and 62 percent, respectively, measured, respectively, in summer 1999 and summer 2000). Sources: WFTC take-up rates from McKay (2002), FC take-up rates from Marsh et al (2001). Take-up rates of other means-tested benefits from Department of Work and Pensions (2001b).

1997, but in the 2001 scenario has some of the lowest financial gains to employment (the first wage in this stylized two-earner family is sufficient to get the family off Housing Benefit, so housing tenure makes no substantial impact here).

There has been a debate in the UK as to whether these changes in financial incentives will cause people to change their behaviour. Blundell et al (2000), simulate the impact of the introduction of the WFTC (so they compared the WFTC system of October 1999 to the system in April 1999) using a structural labour supply model. They predict that the WFTC will reduce workless households with children by just under 60,000 (affecting around 100,000 children). They also suggest that there will be some offsetting reduction of labour supply by women with working husbands.[11] The UK Government's estimates are that the total package of reforms will encourage around 80,000 extra parents to enter work, a little more than twice the estimate in Blundell et al (2000) for the WFTC alone (HMT, 2000b). These estimates use elasticities derived from data on labour market transitions using the methodology laid out in Gregg et al (1999). Comparisons for the WFTC alone suggest the two methodologies give very similar results (Blundell and Reed, 2000).

4. Lone parents' employment change: Early evidence

The WFTC has been in operation for thirty months now, and the first evidence of its impact is beginning to emerge. As of November 2001, there were 1.3 million claims for WFTC—430,000 more than for its predecessor in summer 1999—whilst the numbers of children covered by these claims rose by 870,000 (see Table 3). The numbers of children of lone parents supported by the WFTC was 1.1 million in November 2001, over 400,000 more than under the previous regime. So, by November 2001 the numbers supported through in-work tax credits was almost equal to those supported by out-of-work welfare payments. However, the numbers of children for whom support through in-work tax credits were claimed was also rising prior to 1999, especially among single parents. These numbers do not necessarily imply falling out-of-work welfare dependency. But the number of children for whom out-of-work welfare payments are claimed has itself fallen, by around 730,000 since the peak at the end of 1995, with children of lone parents accounting for nearly half of this fall (290,000).

Table 3: Numbers of children for whom payments are made by type of welfare benefit and tax credit, 1995-2001

So, there has been a sustained decline in the number of children supported by welfare payments and this was well established prior to the advent of WFTC. Amongst lone parents, though, the rate of decline has been faster since August 1999 (the last date prior to the advent of the WFTC) than before, and faster than the decline in the number of children in all families claiming out-of-work benefits since the summer of 1999 (DWP, 2002d; and earlier editions). These differences are encouraging on their face. But since they are modest and take no account of changing population demographics or the state of the economic cycle, they yield no clear conclusion about the impact of the WFTC.

In search of a more definitive conclusion, Table 4 explores the evidence for lone parents more formally, using a simple difference in difference methodology. Lone parents in the UK have long had very low employment rates. From the mid 1980s to the early 1990s, employment rates for lone mothers were broadly stable at just above 40 percent, even though over the same period, employment among mothers with working husbands rose sharply (Desai et al., 1999; Blundell and Hoynes, 2001). But in 1993 the employment of lone parents started to rise. Table 4 compares the annual changes in this rate for 1996-1999 (before the advent of WFTC) and 1999-2001 (after its introduction). Splitting the data in this way (see the raw annual changes in column 2 of Table 4) supports the suggestion in the administrative caseload data of Table 3 of a modest increase in the rate of growth of lone parent employment post-1999, although the difference between the two periods is not statistically significant.

Table 4: Annual changes in employment rates among live-alone lone parents, 1996-99 and 1999-2001

In any case, raw differences do not take account of the strong employment recovery over the last few years in the UK, which slowed after 1999 and stopped entirely in 2001. To account for the state of the economic cycle and the differing performance of different age and skill groups in the recovery, we compared the raw changes in column 2 of Table 4 with those of single (live-alone) adults without children of similar age and education—a natural comparison group as they were unaffected by the policy shift and have similar household circumstances apart from the presence of children. We also adjusted for differences in age of the children of the lone parents. The results are shown in column 3 of Table 4.

The difference between the pre- and post-reform periods is more marked, and on the borderline of statistical significance. These results suggest that the buoyant labour market drove the bulk of the improving employment rates of lone parents between 1996 and 1999. They also suggest, however, that since 1999 there has been an acceleration in employment growth for lone parents that is higher than employment growth among childless individuals with similar characteristics. Hence, it tentatively appears that

[11] The authors have benchmarked this model against labor supply estimates derived from past reforms to in-work benefits in the UK (Blundell, 2000 reviews this evidence) and believe it to be consistent.

lone parents have had an exceptional increase in employment rates over this period, which could reflect a behavioural response to the financial incentives and other aspects of welfare reform since 1999.

Future Directions

All three of the main areas of policy development described earlier—raising direct financial support for families with children, reducing the numbers of workless households, and mitigating the scarring factors of childhood deprivation—are continuing to develop. Two current policy proposals in particular—for expanded case management and greater system integration—would profoundly change the picture of the UK welfare system.

Job Centre Plus, and the Expansion of Case Management in the Welfare System

Job Centre Plus is a tag used by the Government to describe the unification of administration systems for different out-of-work working-age benefits. In practice, this means that, over time, all benefit claimants will get regular contact with a personal advisor (case manager), with the frequency of the contact depending on the specific benefit. Under the New Deal programmes this has been compulsory for the unemployed but voluntary for disabled workers and lone parents. This is in the process of changing. In the future all claimants will have a compulsory "work-focused interview" at regular intervals, with a personal advisor asking about a person's desire to work and the inhibiting factors. Claimant groups will have different job-search requirements, but similar support systems will be available to all, whatever benefit they are on, if they want them.

This reform places work at the heart of the welfare administration process for all groups, whereas in the past the unemployed were clearly given a higher priority for job placement efforts. It also means that benefit advisors will not have implicit incentives to push people onto other benefits. All groups will have readily available job-search support systems. The case management will not just help with job search, but will cover issues of transition in the benefit system and access to care services for dependants as well.

This development follows from the New Deal framework of contacting a wide range of benefit groups to discuss, promote, and support a transition into employment (see Chapter 6 for discussion). The main difference is that it will be embedded routinely in the benefit administration and attending the "work focused interview" will be compulsory. It falls a long way short, though, of compulsory job search or time limits on welfare receipt.

Integration of Child Support Payments

The integration of all child support payments is another unifying reform, but one affecting the tax and benefit system rather than the administration regime. The aim is to pull together all the financial support for children (outlined in Figure 5 earlier in the chapter) that is currently paid through welfare payments, in-work benefits and tax credits into a single instrument, with the same rules and administration. This proposed Child Tax Credit has many more similarities with the Canadian Child Tax Benefit than with the US system. It will remain nominally distinct from the universal Child Benefit, but in most practical terms—such as who receives the payment, and how it is paid—the two will be identical. Payments in respect of adults in Income Support and the WFTC will remain outside this system. And, at the same time as the switch to the child tax credit, in-work support will be extended to adults without children (with restrictions to full-time employment and a minimum age of 25) in something called the Working Tax Credit.

There will be few immediate changes in family incomes as a result of the child tax credit: the emphasis is on a structural change to how payments to families with children are delivered, rather than how much is paid.[12] The new features are as follows. First, all payments in respect of children will be paid to the mother or the main care-giver. Under the current system, who gets the payment depends on which benefit is being paid and even how the payment is being made. Second, income uncertainty at the time of transitions into and out of work will be reduced. This is because there will be a stable platform of financial support for children across the welfare-to-work divide, rather than the uncertainly (and possible delay) of moving from out-of-work benefits to in-work benefits. Third, as almost all families will be able to receive some support, take-up rates for the Child Tax Credit may be substantially higher than for the WFTC. Fourth, payments will be assessed against family income throughout. This represents the most significant step towards joint assessment for families with children since income tax became individualized in 1990.

Although the new tax credits will notionally depend upon annual income, they will not be a retrospective annual system like the EITC. The aim is to operate an annual system (and so minimise hassle for families whose circumstances are stable) but also to provide some protection for families whose income falls. In practice, this means that awards will depend upon either the previous fiscal year's annual income or expected annual income in the current fiscal year. A novel feature is that year-on-year income rise of under £2,500 will be ignored by the tax credit system. The impact of this, which will lower the short-run effective marginal tax

[12] Writing some time before the final details had been announced, some authors noted that a unified and integrated child tax credit would require either benefit increases for families on out-of-work benefits or benefit cuts for those on in-work benefits (see Brewer, Myck and Reed, 2001): in the end, the Government chose the former and phased these in gradually in the years leading up to the new tax credits so that most families with children will see almost no change in incomes in April 2003 (the main exceptions are better-off families with children, some of whom will qualify for the child tax credit but not the children's tax credit, and some the other way round).

rates for some families with children, is hard to predict (Inland Revenue, 2001; HM Treasury, 2002; for the development of official policy; Brewer, Clark and Myck, 2001; for more details of the background to the reform).

Conclusion and Assessment

While the UK Government's strategy contains many of the main elements of US welfare to work agenda—such as increased financial incentives and case management of the welfare caseload to support transition into work—it also has substantial differences. The most striking factors that are different in the UK are:

- Levels of welfare support for those not in work—as well as those in work—are rising substantially.

- There is no time limiting of welfare support or requirement to seek work for lone mothers. (Sanctions only apply to those claiming unemployment benefits who do not meet their responsibilities to look for work and accept appropriate job offers.)

- There is a strong emphasis on tackling poverty and its consequences for children.

The objectives which underlie welfare development in the UK are primarily the economic circumstances for families with children and the outcomes achieved by the poorest of those children. Reducing welfare rolls and reducing expenditure are clearly secondary priorities. Hence, from a British perspective, welfare to work is a policy success if and only if it results in reduced deprivation for the child. It is also clear that the reform process is far from over. The second round of reform currently underway has been more about the structures of welfare systems and caseload management than payment generosity, although support levels are still rising. This reflects in part the difficulty of quick implementation of fundamental reform to institutions.

Whilst the objective in general is clear, the more specific target is not. At some stage the government will have to declare its position on what it means by elimination of child poverty. Elimination of poverty on a high relative income measure is almost impossible. The most successful European Union countries (Sweden, Denmark and Norway) have child poverty rates (on a 50 percent of mean income before housing costs basis) of a little under 5 percent (Bradbury and Janie, 1999). Measurement error and lumpiness of income over the short windows commonly used to assess income in the UK data will always leave some people below such a benchmark. The longer term financial position may be a better guide to the financial situation that actually matters to children's well-being and development.

The Government has a number of sensible ways forward. It could assert that such imprecise data means that an estimated child relative poverty rate of 5 percent—or higher—is consistent with its intention to eliminate child poverty. Alternatively it could focus on the measurement of material deprivation or some combination of a relative income and material deprivation measure, as used by the Irish government. A reliance on relative income will require large resources to be committed to supporting children, and child support systems to rise in line with median incomes thereafter. This is difficult but not impossible. Indeed one crucial new announcement in the April 2002 Budget was that the per child payments in the new child tax credit will be automatically linked to earnings rather than prices, ensuring the relative value of these payments. It is clear from Government publications, however, that the intended target is larger than a simple financial measure. As a result, it is likely that the measures ultimately adopted to assess success will include some indicators of material well-being.

The strategy is clear, however, even if the target is not. The Government has substantially raised financial support for families with children. Increased payments have been focused on low-income families, whether or not they are working, but all families with children have gained something under the Government's package of reforms. Work incentives have risen, especially for full-time work, and those lifted out of poverty to date are much more likely to be working. Increasing the financial rewards for work at low wages is part of a wider strategy to reduce the number of children living in workless households. This part of the strategy would appear vital if the costs of eliminating childhood poverty are not to prove prohibitive. Here there are some early signs of improvement, with the number of children in workless households down from 19.4 percent in 1996 to 15.3 percent in spring 2001. There have also been substantial reforms to the way welfare is administered to support transitions into work. The most important is the development of a case management approach, with all claimants having a personal advisor. The final part of the strategy is to reduce the extent to which children from the poorest households and communities underachieve in terms of development and education. This involves a mixture of extra resources and focusing the machinery of government and service delivery on out-turns among the poorest children. All elements of this strategy are evolving, and further steps have already been announced or proposed.

The intention is commendable, and the strategy coherent, but the scale of the task so large that many argue it is unachievable. Some cynics even suggest the Government has little intention of achieving it. The central problem is maintaining political and public support for the large financial transfers required to reduce poverty on a relative income basis, especially if recent reductions in worklessness do not continue. The increased work incentives are certainly not substantial enough alone to drastically reduce the numbers in such workless households; hence the strategy relies heavily on the reforms to welfare administration and increased childcare availability to facilitate moves back to work. Increased generosity of support in and out of work may actually reduce the desire for work, as life without work becomes more tolerable at these higher income levels. Increased generosity of support will also mean that the high withdrawal rates cover an ever-expanding section of the population. This could be reduced by greater use of the universal, or near universal, parts of the child support system, but at a large extra cost.

In addition, there are problems in establishing exactly what the impacts of financial resources are on child development outcomes, and even more problems in designing and implementing successful interventions. In mainstream policy areas, Britain has not developed as strong an experimental and evaluation culture as the US. Nor has it developed systematic mechanisms by which evidence can influence policy delivery on the ground. This becomes all the more difficult where policy allows for significant local inputs and choices. On a more up-beat note, if interventions and reduced financial distress lead to fewer people with very low levels of literacy, for example, then fewer parents in the next generation will suffer as acute problems earning and supporting their families. This intergenerational transmission aspect of deprivation is very important in government thinking.

The ambition of this program will be perhaps surprise American readers, and it seems unlikely to us that such ambition would be ever attempted in the US. It is interesting, however, to think about whether it should be and what form supporting federal and state policy might take.

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Table 1. Distribution of marginal deduction rates faced by employees with children before and after the reforms

Marginal Deduction Rate	Percentage of Employees with Children	
	1997-8	2002/3
more than 100%	0.1	0.0
more than 90%	3.7	1.4
more than 80%	4.7	3.9
more than 70%	8.4	4.3
more than 60%	8.9	15.4
more than 50%	8.9	19.1
more than 40%	27.3	30.9
more than 30%	73.2	80.4
more than 20%	91.6	89.7
more than 10%	94.0	92.2
more than 0%	94.4	92.4
All	100	100

Notes: A marginal deduction rate is the percentage of the marginal pound of earnings that is lost in taxes and withdrawn benefits or tax credits. Calculations are performed on employees only, assuming full participation in all means-tested benefits and tax credits. 1997/8 values calculated using FRS 1997/8 and the tax and benefit system as of April 1997; 2002/3 figures estimated using FRS 1999/0 with earnings adjusted for two years of average growth, and the tax and benefit system as of April 2002. There were around 7.5 million employees with children in both years.

Table 2. The effect of the reforms on the financial gain to work for parents with children

	Gain to work (£)			
	16 hours		35 hours	
	1997	**2001**	**1997**	**2001**
Not on HB:				
Lone parent	63	71	107	130
Primary earner in a couple with children	26	50	79	99
Single person, no children	13	13	72	79
With HB:				
Lone parent	43	43	65	80
Primary earner in a couple with children	20	21	42	49
Single person, no children	2	8	2	31
With childcare of £50/week when in work:				
Lone parent	13	56	92	115
Second earner in a couple with children:				
No childcare costs, first earner on £300 a week	67	30	127	93

Notes: Table measures difference between zero-income benefit income and income after taxes and benefits in work. Assumes 2 children under 11 and full take-up of all entitled benefits, hourly wage of £4.20, rent of £50 a week where indicates, in-work childcare costs of £50 a week where indicated (slightly more than the average of those lone parents currently claiming the Childcare Tax Credit). All values expressed in 2002 prices.
Source: Authors' calculations based on TAXBEN model.

Table 3: Numbers of children for whom payments are made by type of welfare benefit and tax credit, 1995-2001

	Number of Children (thousands)							
	Nov 95	**Nov 96**	**Nov 97**	**Nov 98**	**Aug 99**	**Nov 99**	**Nov 00**	**Nov 01**
Welfare Benefits for Workless Families								
Unemployed	633	510	382	341	325	298	251	201
Sick & disabled	628	633	656	646	658	649	666	671
Lone parents	1,884	1,853	1,795	1,718	1,731	1,704	1,643	1,593
Other	111	93	90	83	77	78	66	61
Total	3256	3089	2923	2788	2797	2729	2626	2526
Tax Credits for Working Families								
	Family Credit					WFTC		
	Nov 95	**Nov 96**	**Nov 97**	**Nov 98**	**Aug 99**	**Nov 99**	**Nov 00**	**Nov 01**
Couple	788	882	901	885	871	1000	1208	1330
Single	450	520	580	647	663	761	935	1071
Total	1238	1402	1481	1532	1534	1761	2143	2401

Note: The Working Families Tax Credit replaced Family Credit in October 1999.
Source: Office for National Statistics (2001).

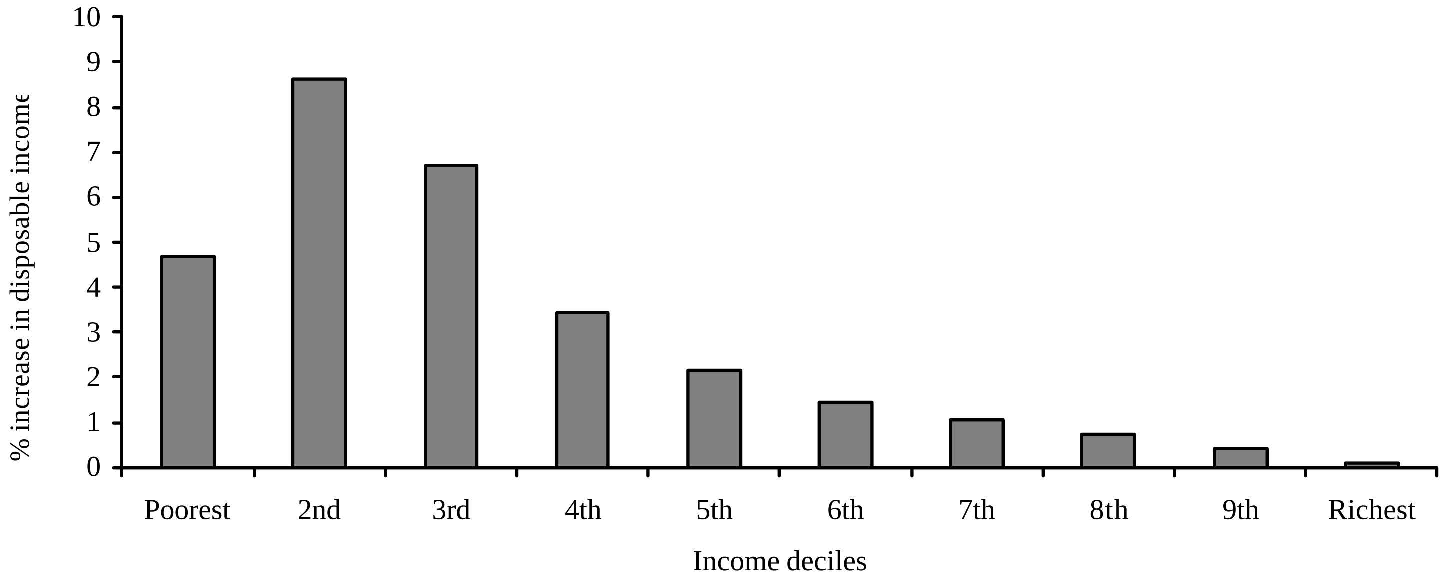
Table 4: Annual changes in employment rates among live-alone lone parents, 1996-99 and 1999-2001

Period	Raw Annual Changes	Adjusted to control for parenthood and age of youngest child
1996-1999	1.82	0.16
1999-2001	2.40	1.20
Difference	0.58	1.04

Note: Column 3 is the difference in employment growth rates between comparable lone parents and single adults with in the two periods. They have been estimated from probit equations of employment status controlling for year, age 18-24, 25-34, 35-44 (45+ as the base), qualifications of degree level or equivalent, a level but below degree, O level or equivalent and below O level (the base). Gender and gender and age, qualification interactions and interactions of gender, age and qualifications with time are also included. As are dummies for age of youngest child being 0-1, 2-4, 5-10 and 11+ (5-10 as the base) which are not interacted with time. The marginal effects reported are the transformed coefficients on a year/lone parent interaction for the two periods.

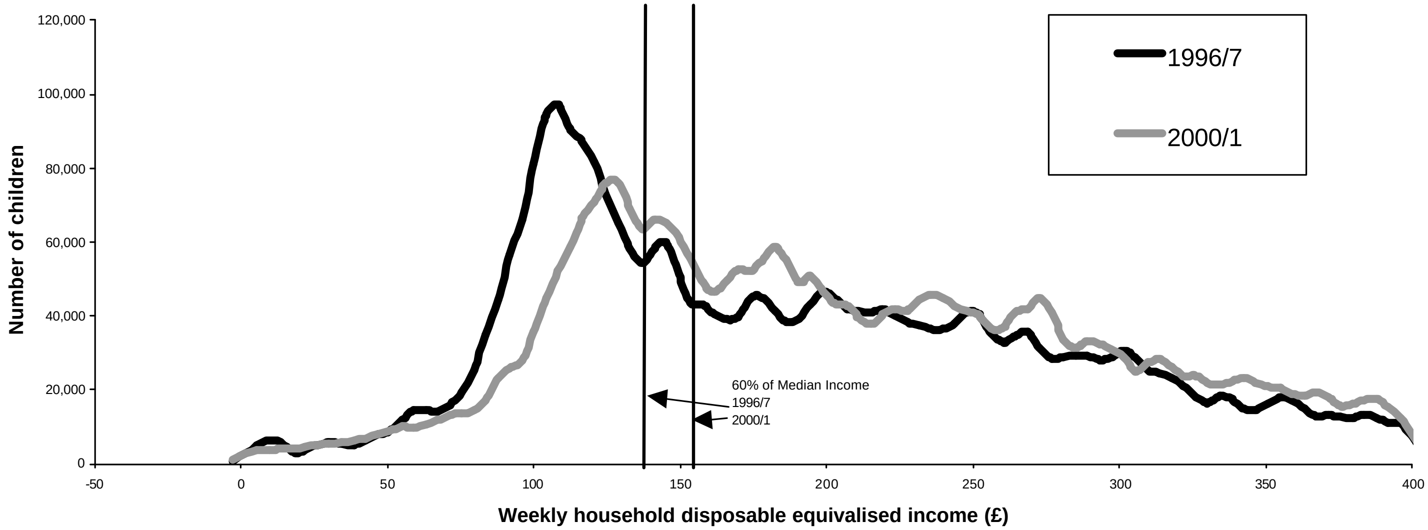
Source: Labour Force Survey.

Figure 1: Estimated income gains for families with children from increases to child support, 1997-2002



Notes: Income deciles are derived by dividing all families (with and without children) into 10 equally sized groups according to income adjusted for family size using the McClements equivalence scale. This graph shows the effect on families with children only. For example, the reforms will increase incomes of working-age families with children in the poorest tenth of the population by 4.7 percent. Assumes full participation in all income-related transfer programmes.
Source: The IFS tax and benefit model, TAXBEN, based on 1999/00 Family Resources Survey.

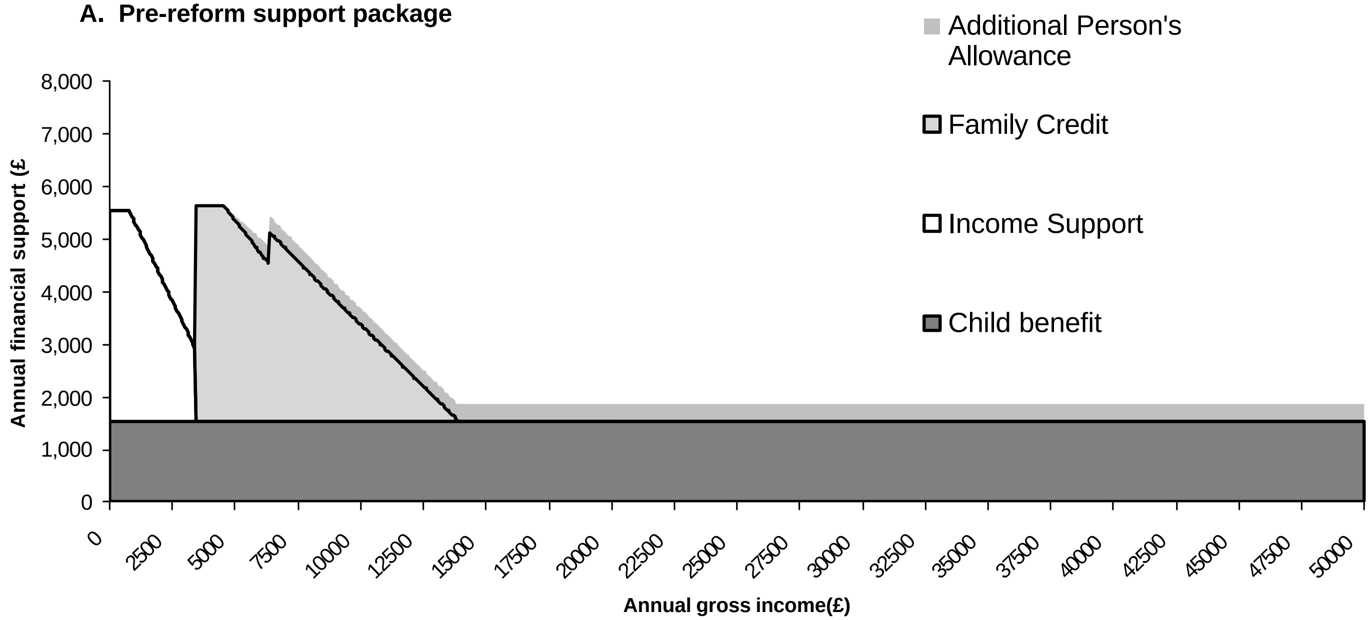
Figure 2: The changing real income distribution for children in low-income households



Source: from Brewer, Clark and Goodman, 2002, and calculated using data from Family Resources Survey.
Note: Figure shows estimated distribution of equivalised weekly disposable household income for children in households below £400/wk (in 2000/1 prices). The proportion of children living in such households was respectively 88% and 84% in 1996/7 and 2000/1; 60 percent of median income on this definition was, respectively, £139 and £153 in 1996/7 and 2000/1.

Figure 3: Total financial support by gross income, before and after reform

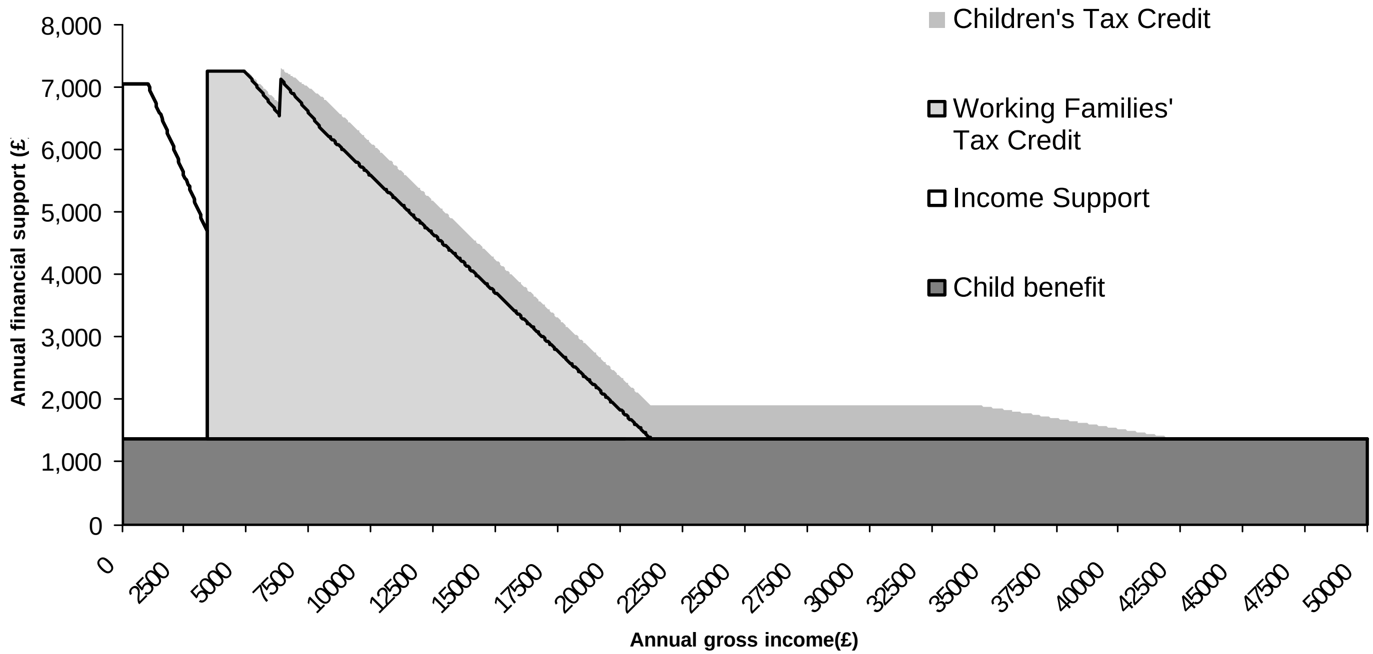
A. Pre-reform support package



Note: Assumes live-alone lone parent, 2 children under 11, no housing costs or childcare costs. Entitlement for WFTC reached at £3,400, or 16 hours work/week at the minimum wage. Values uprated to April 2002 prices.

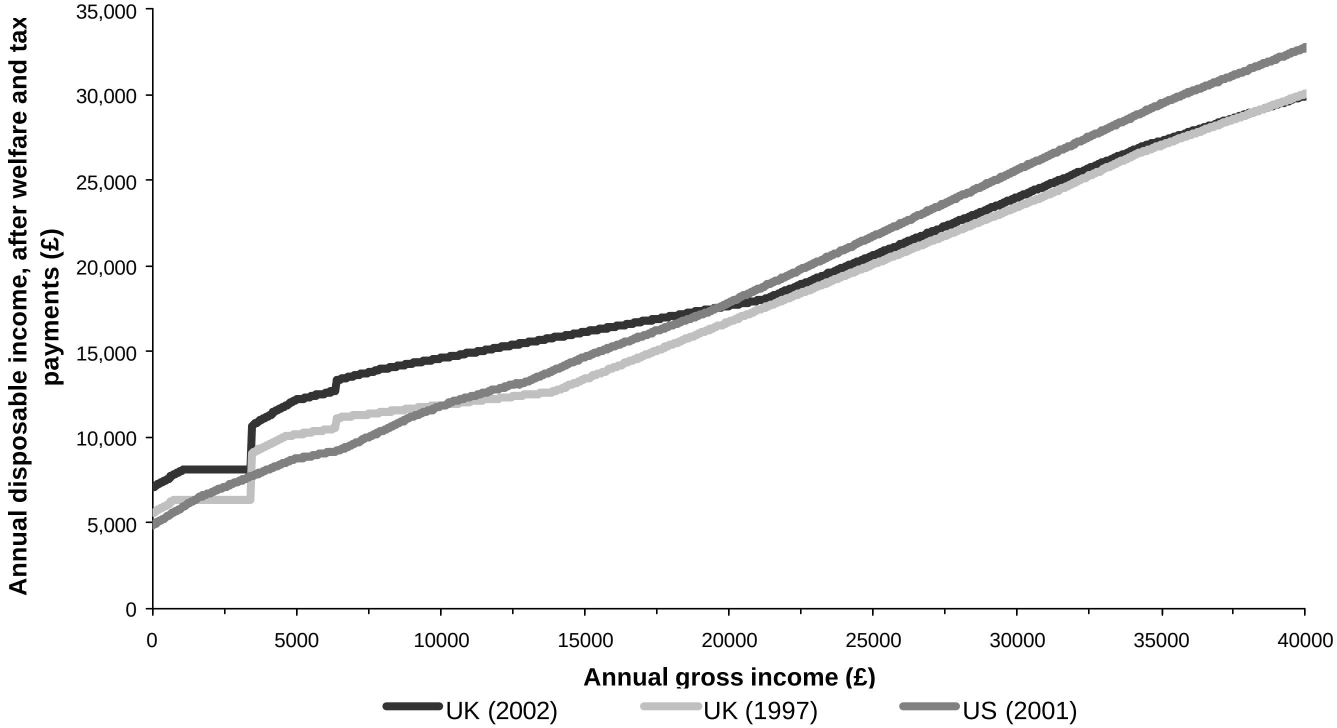
(Figure 3, Continued)

B. Post-reform support package



Note: Assumes live-alone lone parent, 2 children under 11, no housing costs or childcare costs. Entitlement for WFTC reached at £3,400, or 16 hours work/week at the minimum wage. Values uprated to April 2002 prices.

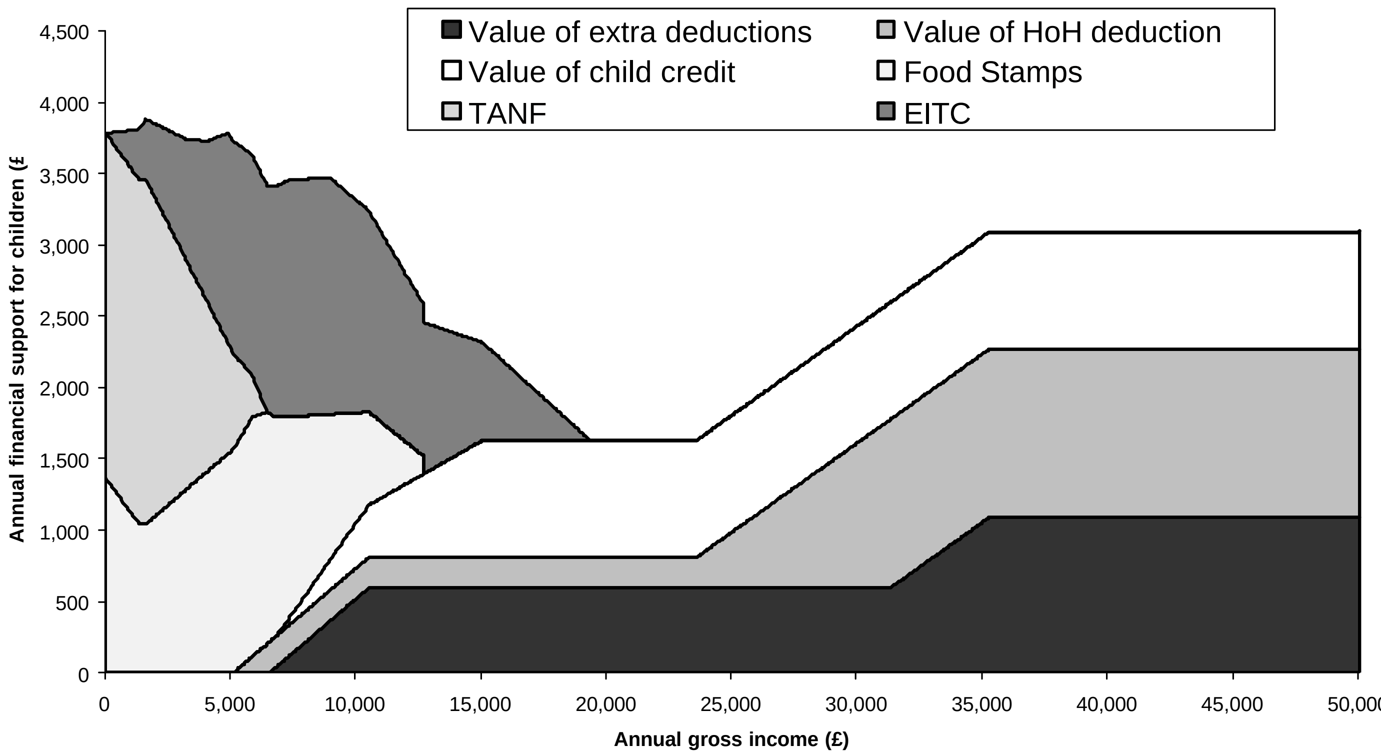
Figure 4: Disposable income after welfare and tax payments, by gross income, UK before and after reform, and US in 2001



Note: Assumes live-alone lone parent, 2 children under 11. Does not include housing or childcare support or costs.

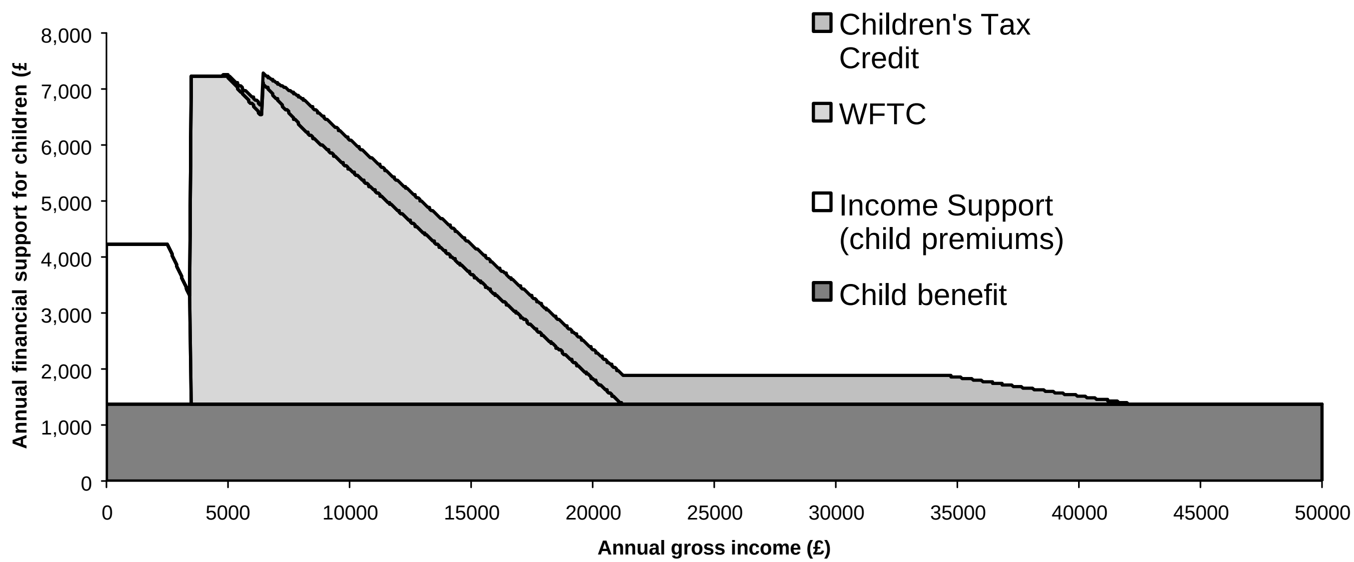
Figure 5: Financial support for children, by gross income, UK and US

A. US



(Figure 5, Continued)

B. UK



Note: Assumes live-alone lone parent, 2 children under 11. Entitlement for WFTC reached at £3,400, or 16 hours work/week at the minimum wage. Values uprated to April 2002 prices.