

March 2006

Rt Hon Gordon Brown MP
Chancellor of the Exchequer
1 Horse Guards Road
London
SW1A 2HQ

Dear Gordon,

I write ahead of the budget to let you know what the Child Poverty Action Group (CPAG) believes is needed in order to make the further and faster progress urgently needed to achieve the ambition to eradicate child poverty. As I write, we await the publication of the reporting data for the first milestone in the reduction of child poverty. We recognise the progress the Government has made to date. However, since last year's results were disappointing, we fear the first target will be narrowly missed or only just achieved. This will send out a clear signal that policy needs to push much faster and harder toward 2010 and to get ahead of the target. CPAG remains strongly supportive of the existence and centrality of this target: the budget and the comprehensive spending review offer the opportunity to make significant further progress and, if necessary, to get back on track.

To this end, this letter draws on research conducted by the University of Bath and funded by the Joseph Rowntree Foundation due to be published later in the year.¹ CPAG and One Parent Families asked the Rowntree Foundation to fund the investigators from Bath to explore how current policies would perform for certain model families, each with a child born in the first milestone year of 2005. The Lifetime Opportunity and Incentives Simulation (LOIS) model used by the researchers allowed the examination of profiles over time of the relationship between family income and the poverty line based on assumptions drawn either from official publications (such as the Tax and Benefit model tables), on recent history (in the 1997-2005 period) or on widely held research presumptions (such as around likely growth of median incomes). It is on families like those investigated that policy must focus if the 2010 and, ultimately, 2020 commitments are to be met.

The LOIS project fits within a wider Rowntree Foundation stream of work, a final report of which is to be published in July 2006. The Rowntree work which, alongside the LOIS and significant policy analysis, contains micro-simulation of policy options for tackling child poverty conducted by the Institute for Fiscal Studies. LOIS adopts a specific method – modelling policy impacts over the life course – but the multi-strand approach adopted by the Rowntree project confirms the scale of the challenge LOIS suggests. The

¹ Evans, M and Scarborough, J, 2006 forthcoming, 2020 Vision: Child Poverty and Future Policy, Joseph Rowntree Foundation.

LOIS findings offer a mixed interpretation of policy, showing what is working well and what will need to be done to improve the policy mix towards 2010. The conclusions suggest that since policy to date has helped those easiest to help, much more will be needed to make further progress.

- **Wage levels.** CPAG supports the government's conviction that increasing the employment rate for those able to work is crucial to reducing child poverty. Clearly also significant effort has gone in to improving the incomes of low wage employees through both the minimum wage and tax credits. However in 2003/04 52 per cent of the poor child population had at least one parent in paid employment: work is not therefore always a route out of poverty. LOIS reveals that currently a couple with two children working at the minimum wage level, would need to work a combined total of 58 hours a week on the before housing cost basis and 74 hours a week after housing costs (assuming a relatively low – local authority - level of rent) just to obtain an income above the poverty line – we emphasize that not all families are in a position where this is possible or reasonable. The position for lone parents is better but both examples illustrate the need to address the current levels of in-work support and wage rates (through the national minimum wage and investment in skills) if work is to truly provide a secure route out of poverty.
- **High costs.** Not only does the median income rise but within general inflation there are specific areas of high costs: the LOIS project picks out housing, council tax, childcare and transport in particular, each rising above the rate of price inflation. Recent concern has also focused on fuel costs, rising rapidly and above the rate of price inflation. These costs affect poorer families disproportionately and risk undermining both work incentives and broader anti-poverty gains. For example the LOIS research reveals the negative impact that housing costs had on work incentives (due to reduced housing benefit and higher taxes). For two lone parents, both in paid work at the minimum wage – one with low and one with high rent (based on Department for Work and Pensions' assumptions from the 'Tax and Benefit model tables'), it reveals that the lone parent facing high rent would have to work 76 hours for marginal tax rates to fall below 90 per cent (that is to be able to keep more than 10p for each pound earned). Although the lone parent with low rent still faced a high rate of marginal taxation, this was lower: beyond 28 hours of work this fell to 70 per cent (allowing 30p in the pound to be kept). With this in mind it is very worrying that rents are rising faster than price inflation, thereby worsening this poverty trap. High housing costs reduce work incentives and suggest the need for greater focus and investment in the supply of housing to restrict rent increases, rather than through the housing benefit system.
- **Poverty gaps.** Currently for many families the combined level of out of work benefits which should provide a financial safety net, leaves their children below the poverty line. The LOIS report indicates for a couple with two children a poverty gap of 20 per cent (that is the safety net paying 20 per cent less than is needed to lift people out of poverty) on a before housing cost measure, and 31 per cent after housing costs. Closing gaps

in the safety net - which means not only improving child payments but also increasing the real value of income support payments for their parents – is crucial if financial security is to be provided for those who are unable to work, or who suffer unemployment. If the safety net provides less than the poverty line, child poverty cannot be truly eradicated.

- **Uprating of benefits and tax credits.** In order to keep up with rising societal norms and the relative nature of the poverty line, benefits and tax credits (including both rates and thresholds) need to increase at or above the growth in median incomes to reduce the extent of poverty gaps in the safety net. The welcome linking of the child element of child tax credit to earnings growth stands out amongst other elements of family incomes – such as income support - which are prices linked, or those - such as the family element of child tax credit - which have been frozen and have therefore lost considerable real value. We would particularly draw your attention to the role of child benefit which plays a significant role in getting income through to poorer families and does not suffer the same non-take up or marginal tax rate problems of means tested benefits. The last above price- inflation increase to child benefit came in 1999 – now seven years ago - and applied only to the first child rate only. Recent concern over poverty in larger families should focus policy attention on the subsequent child rate of child benefit – CPAG would like to see the subsequent rate to rise significantly in real value. Since it is widely expected that median income growth will outstrip prices towards 2020, price uprating of benefits will significantly undermine efforts to reduce child poverty. To reduce and eradicate child poverty on a sustainable basis, the value of the safety net (both child benefits and adult ones) need to rise above the level of price inflation.
- **Child support.** The LOIS findings illustrate the potential impact of parental separation on the incomes of households containing children. The shock is sudden, considerable, and may also be linked the parent with care leaving work to spend more time with children. On this basis we welcome the Henshaw review of child support policy and urge that this review be driven by the need to deliver financial security for children. Although the LOIS findings suggest that the payment of maintenance does provide a protective effect against poverty, its impact is limited by a combination of a widespread failure to pay maintenance and -where it is – of lost benefit entitlement. The current £10 child maintenance disregard is welcome and should be received by all families, rather than just those on the new scheme. However, if this disregard were larger it would also have a greater impact in reducing child poverty. A system whereby the state guaranteed payment of maintenance whilst also enforcing its collection from non-resident parents, would protect those children for whom maintenance is currently not being paid.
- **Measurement of child poverty.** The LOIS research highlights that different definitions of relative income poverty – before and after housing costs – give very different profiles of poverty towards 2020. Since the before housing cost measure – now to be adopted in official statistics –

includes housing benefit as income it produces some perverse results which do not match the experience of poverty (for instance high rents – with housing benefit in payment – apparently lifting people out of poverty without changing living standards and actually worsening work incentives). With this in mind it is critical that the proposed material deprivation Public Service Agreement target picks up aspects such as the impact of high housing costs. Otherwise it will fail to provide a true impression of the impact, and effectiveness, of policy for children.

In conclusion, CPAG congratulates you on the progress made thus far in reducing child poverty. Nevertheless I hope this letter makes clear the scale of the problem and our expectation that much more will be done to develop policy ahead of the 2010 target. Without more effort we do not believe the milestones will be met. We urge the government to use both the budget and the comprehensive spending review to ensure we are fully on track in eradicating child poverty.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Kate Green', with a long, sweeping underline that extends to the right.

Kate Green
Chief Executive