

The impact of tax credits on mothers' employment

Findings
Informing change

October 2007

Child Tax Credit (CTC) and Working Tax Credit (WTC) were introduced in April 2003 to support families with children, reduce child poverty and make work pay for those on low incomes. These new credits are central to the Government's ambitious policy of reducing and eventually abolishing child poverty. This research investigated their impact on labour-market participation and the working hours of women with children. It also explored reasons for non-take-up of the tax credits among those eligible.

Key points

- The estimated employment rates of lone parents who were receiving CTC were around 11 percentage points lower than those of eligible non-recipients with similar characteristics.
- The employment rate of mothers in couple families (i.e. with partners) who were getting CTC was 8 percentage points lower, on average, than that of comparable non-recipients.
- CTC decreased the probability of moving into work for women who had not been working in 2002-03 and were not in receipt of WTC at any of the two subsequent FACS interviews.
- Lone parents receiving WTC worked around four hours fewer, on average, than comparable non-recipients.
- Getting WTC did not make any difference to the number of hours that women in couple families worked.
- Neither WTC nor CTC affected the working hours of mothers who already worked 16 or more hours a week, in both 2003-04 and 2004-05, and were eligible for WTC (and CTC) in 2004-05.
- Lone parents were most likely to receive either CTC on its own or in conjunction with WTC, in comparison with mothers in couple families.
- In 2004-05, families in the lowest income quintile were only half as likely to be in receipt of WTC as those in the second quintile. Those in the third, fourth and fifth quintiles had successively lower chances of receiving WTC than those in the second quintile.
- Families in the London area who were eligible for CTC/WTC were about half as likely to be receiving tax credit as those in the North of England.

The research

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Background

The context for this study was the Government's aim to halve child poverty by 2010 and abolish it by 2020. However, the Government failed to lift a quarter of children out of poverty by 2005. Recent research has shown that these ambitious aims will not be met unless further progress is made in encouraging women with children – both lone parents and those with partners – into the labour market. High take-up rates of Child Tax Credit and Working Tax Credit, which were introduced in April 2003, will also be needed.

Using information from the Families and Children Study 2002-03 to 2004-05, the two main objectives of this study were to:

- analyse the impact of CTC and WTC on labour-market participation and the working hours of women with children;
- explore reasons for non-take-up of these tax credits.

Take-up of CTC and WTC

The study's best estimate of take-up in 2004-05 suggested that a quarter of CTC-eligible families were not receiving the tax credit, and that two-fifths of families eligible for WTC were not getting it. However, the take-up rates produced using the Families and Children Study were lower than the 2004-05 take-up rates estimated by HM Revenue and Customs using a combination of survey and administrative data. Matched administrative data and survey data tend to produce more accurate estimates of take-up than survey data alone.

According to FACS, among families eligible for CTC, lone parents were much more likely to be in receipt of the tax credit than mothers with partners. Among families eligible for WTC, lone parents were also more likely to take up the tax credit. In 2004-05, families in the lowest income quintile were only half as likely to be in receipt of WTC as those in the second quintile, which is potentially worrying and needs to be explored further. Those in the third, fourth and fifth quintiles had successively lower likelihood of receiving WTC than those in the second quintile, all else being equal. This suggests that families with higher incomes and, hence, lower perceived entitlement are less likely to claim their tax credits, as would be expected. Families who had received Working Families Tax Credit in 2002-03 and, therefore, would have been aware of the new tax credits that replaced it, were almost twice as likely to receive CTC and almost three times as likely to claim WTC in 2004-05, all else equal. Families in the London area who were eligible for CTC were about half as likely to be receiving the tax credit as those in the North of England, all else being equal. Similarly, WTC-eligible families in the London area were about half as likely to be getting the tax credit as those in the North of England, on average, despite high child poverty rates in London.

The impact of CTC on mothers' labour-market participation

In 2004-05, the estimated employment rates of lone parents who were receiving CTC were around 11 percentage points lower than those of eligible non-recipients with a similar chance of receiving CTC. Mothers in couple families who were in receipt of CTC had an 8 percentage points lower employment rate, on average, than comparable non-recipients.

From a dynamic perspective looking at changes over time, CTC had no significant effect on the likelihood of being in work in 2003-04 or 2004-05. This may have been because the positive effect of WTC, which the study did not control for, balanced out the negative effect of CTC. This analysis also accounted for individual characteristics about which information was not available in the dataset, but which were stable over time ('unobserved individual effects').

However, when yearly changes in activity status were analysed, CTC decreased the chances of moving into work for those who had not been working in 2002-03 and were not in receipt of WTC at either of the two subsequent FACS interviews. This negative effect of CTC on the probability of moving into work was larger in magnitude for lone parents.

CTC also increased the chances of moving out of work for lone parents who had been working at the time of the 2002-03 FACS interview and were not in receipt of WTC at either of the two subsequent interviews. However, it decreased the probability of moving out of work for mothers with partners. Among CTC recipients, mothers with partners were substantially less likely to move out of work than lone parents, although there was no difference by family type among CTC non-recipients.

An important omission from the study due to data limitations was not being able to look at the impact of WTC on the labour-market participation of women with children, which should be positive for lone parents and negative for second earners in couples.

The impact of WTC and CTC on mothers' working hours

In 2004-05, lone parents who were receiving WTC worked around four hours fewer, on average, than comparable eligible non-recipients. Women in receipt of WTC with employed partners worked a similar number of hours, on average, to comparable non-recipients.

When the study examined changes in working hours over time, neither WTC nor CTC affected the working hours of mothers who already worked 16 or more hours a week in both 2003-04 and 2004-05, and were eligible for WTC (and CTC) in 2004-05. This analysis also accounted for individual characteristics about which information was not available in the dataset, but which were stable over time ('unobserved individual effects').

For mothers eligible for WTC and CTC in 2004-05, neither tax credit had a significant effect on the probability of moving from full-time work (30 or more hours a week) in 2002-03 to part-time work (between 16 and 29 hours) in any of the two subsequent years. Similarly, neither tax credit increased the chances of moving from part-time to full-time work among those who worked 16-29 hours a week in 2002-03.

In the context of the finding that CTC decreased the labour-market participation of women with children, especially lone parents, it may seem surprising that the tax credits had little effect on working hours. However, only those who were working 16 or more hours a week before and after the introduction of the tax credits were examined in the working hours analysis. Nevertheless, CTC seemed to do a relatively poor job of moving non-participating mothers into work – though, of course, this is not what CTC is supposed to do. For those who were already working and eligible for WTC, neither CTC nor WTC produced substantial changes in their hours of work.

About the project

The project analysed the most recent three waves of the Families and Children Study 2002-03 to 2004-05. FACS is a longitudinal survey containing a representative sample of all families with dependent children in Britain. The analysis involved propensity score matching techniques, panel regression, event history modelling and simple descriptive methods.

For further information

The full report, **The impact of tax credits on mothers' employment** by Yekaterina Chzhen and Sue Middleton, is published by the Joseph Rowntree Foundation.

You can download this report free from www.jrf.org.uk

Published by the Joseph Rowntree Foundation, The Homestead, 40 Water End, York YO30 6WP. This project is part of the JRF's research and development programme. These findings, however, are those of the authors and not necessarily those of the Foundation. ISSN 0958-3084

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