Family Friendly?

Dr Justin Wolfers & Andrew Leigh

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When politics is dressed up as economics, the result is generally bad policy. Worse, John Howard's $1.2 billion "baby bonus" is likely to make for bad obstetrics.

Put simply, Howard wants to pay mum to stay at home to look after the kids. However, because conservative gender roles are out of step with the views of most young voters, the policy is not marketed as social engineering, but rather as a pragmatic response to an economic problem.

Many commentators have pointed to the inequities of such a system. The baby bonus is not uniform: a child born into a poor household is apparently worth only $500 annually, while children from high-earning households are worth $2,500. Single mothers - who have no other way to support their children - will go back to work, and hence miss out on most of the benefit. The biggest payout will go to couples where he earns enough to support the family for five years, and she made over $50,000 in the year before they had the baby.

Beyond equity, the details begin to reveal what a wayward policy this really is.

According to the Coalition, families suffer because "the arrival of a child generally leads to a large fluctuation in the family's income." Fluctuating income, in turn, leads to higher taxes because the tax-free threshold may not be fully utilized in the leaner years. In each of the five years after childbirth, Howard's new policy allows women to claim back to $2,500 of the taxes they paid in the year of their pregnancy - ensuring that their tax-free threshold is not "wasted" when looking after the kids.

In practice, this means that the way in which women will maximise their benefit is by boosting their earnings in the year prior to childbirth, and then not working for the next five years.

Such a policy creates some quite bizarre incentives. When deciding how hard to work, people typically consider how much of each extra dollar that is earned will be pocketed by the tax office. For most of us, this is about one-third. By contrast, during the year leading up to childbirth, these women will be facing potential tax rates of zero.

What would you do if John Howard offered you one year of tax-free earnings? If you're like most people, you'd probably work more overtime, put in extra hours in the hope of getting a promotion, or perhaps even take a second job. Many would sacrifice some sleep, and those doing piece-work might even take a few more risks on the job.

For pregnant women, this is a recipe for disaster. Countless studies show that work stress raises rates of premature birth, foetal anxiety, and infant illness.

Do we really want to be using the tax system to encourage sixty-hour work weeks, second jobs, and greater exposure to workplace hazards among women who will soon give birth?

But this is only part of the story. After junior enters the world, Howard's baby bonus acts as a disincentive to work. Not only would these women have to pay tax, but they would also be missing out on up to $2500 of baby bonus annually. In effect, they are faced with a double disincentive preventing them from returning to the workforce.

As a result, some couples will likely respond to this double disincentive by cramming their child-bearing into this five year window. Not surprisingly, decisions on the timing of pregnancies depend on individual circumstances and are best informed by a trusted doctor rather than tax incentives. Indeed, medical research shows that the tight child spacing induced by this policy may increase the incidence of problems ranging from low birth weight to schizophrenia.

While the law of unintended consequences is no stranger to economics and politics, in this instance political expediency comes full circle, transforming family-friendly intentions into pregnancy-unfriendly consequences. This is not a policy for which the babies of the future are likely to thank the Coalition.

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