#### **INTRODUCTION**

Over much of the developed world and an increasing part of the developing world, governments provide support to families with children. The extent of such support and whether it is provided directly through income supports or indirectly through the tax code or through public services can vary enormously in accordance with a country's wealth and its tradition of social policy. However, most countries provide some cash payments to assist families with the costs of raising children and Ireland is certainly no exception. The most significant of these child income support (CIS) payments are delivered through the social welfare system: Child Benefit (CB), QCIs (increases for qualified children to primary social welfare payments), Family Income Supplement (FIS), Back to School, Clothing and Footwear Allowance (BtSCFA) and the now defunct Early Childcare Supplement (ECS)¹. Total spending on these supports is very significant, both in social welfare spending and in macro-fiscal terms, amounting to around €3.3 billion or 2 per cent of GDP in 2010.

Until now CIS policy has not been the subject of a policy and value-for-money (VfM) review, despite being the primary subject matter in many reports over the last thirty years. As part of the government's ongoing programme of spending reviews, the Department of Social Protection (DSP) initiated, in 2009, a review covering policy around the CB, QCIs and FIS payments as well as aspects of the BtSCFA and ECS payments. The review was undertaken over a period of 18 months in 2009/10 by the DSP under the supervision of a Steering Group established by the Secretary General of the DSP and chaired by an external chairperson. This report presents the analysis, conclusions and recommendations of that review; it outlines the approach taken and key themes emerging within specific chapters. In line with the overall approach of the expenditure review process, conclusions reached in the review do not necessarily represent Government policy in this area but are expected to play a role in informing future policy development particularly directed at securing more coherent, effective and efficient spending of public money on families with children.

# **OBJECTIVES OF POLICY AND PROGRAMMES**

The policy that underpins spending on child income support payments has evolved over a long period of time. Nonetheless, there is still no single statement of the objectives of this

<sup>&</sup>lt;sup>1</sup> The Early Childcare Supplement was replaced in January 2010 by the Early Childhood Care and Education Scheme.

spending. In effect, overall CIS policy has tended to reflect the sum of its component parts and has evolved in line with their relative importance and shape. Although some child-related payments predate it, the introduction in 1944 and progressive extension of the Children's Allowance payment can be identified as one of the first key developments. It was followed by the progressive extension and convergence of targeted payments such as QCIs (formerly Child Dependant Additions) in the 1960s and 1970s and the introduction of FIS in the 1980s. Although these separate payments with their different target groups and conditionality still determine the policy landscape, a greater coherence in the overall policy approach began to emerge from the 1980s onwards and it has been possible since then to provide a coherent narrative of the evolution of CIS policy trends and the policy motivation behind them.

In order to define current policy objectives around CIS policy and place them in their historical context, the review first of all considered the specific objectives underlying each CIS payment and used their common features to derive two primary policy objectives and a number of secondary objectives:

- Primary objectives: Child income support payments provide (i) universal assistance
  with the cost of child-raising to all families ("horizontal redistribution") and (ii)
  targeted child-related assistance to families who are at risk of poverty ("vertical
  redistribution").
- Secondary objectives: The evolution of policy has also seen other objectives emerge
  over time with varying significance. These include: the reduction of financial
  disincentives for parents to take up work; financial assistance with specific costs
  such as the cost of paid childcare and the provision of an independent income
  source for women in the home. Given the association between parental
  employment and poverty, the first of these is particularly significant for the current
  review.

An understanding of the two primary objectives is the key to an analysis of the overall structure and level of spending on these programmes. CB (and for a time the ECS payment) is associated with the "horizontal redistribution" objective while QCI's and FIS, targeted as they are at poorer families, are associated with the "vertical redistribution" objective. However, CB has a unique role in the structure of income supports insofar as it is currently the only universal payment made and thus does not add to labour market disincentives. A review of relevant policy documents confirms that these primary objectives remain valid<sup>2</sup> as well as the secondary objective of retaining employment incentives. Nonetheless, the economic and fiscal crisis has focused attention on the *balance between universal and targeted instruments* rather than undermining the continued existence of the spending

<sup>&</sup>lt;sup>2</sup> The current economic and fiscal situation, however, precludes the attainment of targets in relation to universal payments and most notably the CB payment.

programmes themselves. This balance and the appropriate payment structure required to provide it coherently, effectively and efficiently lie at the heart of the review.

#### SPENDING TRENDS AND DRIVERS

The review conducted an analysis of spending trends and the key drivers underlying them. Spending on Child Income Supports<sup>3</sup> rose almost continuously over the period of the review (resulting in a rise from 1 per cent of GDP in 1999 to 2.1 per cent in 2009) before falling back to around 2 per cent in 2010. CB is by far the largest spending programme reflecting its universal application and rapid increases in payment rates over much of the review period. The proportion of total CIS spending spent on universal payments (CB plus ECS) reached a peak in 2006 (85 per cent) before falling back to 71 per cent in 2010. QCIs are the next largest component at around 20 per cent of CIS spending while FIS and BtSCFA account for the remaining 7 per cent and 2 per cent respectively. The increase in spending was largely driven by increased payment rates for CB (well over 300 per cent). Demographic factors also played a significant role: the total number of children (0-19 years) increased at around an annual average of 0.2 per cent a year (from 1.19 million in 1997 to 1.22 million in 2009) with the rate of increase accelerating towards the latter part of the period. Annual births rose from almost 53,000 in 1997 to 75,000 in 2008. As a result, the number of younger children (0-14) increased rapidly compared with the older age group (15-19) which actually fell by 1.7 per cent a year over the period.

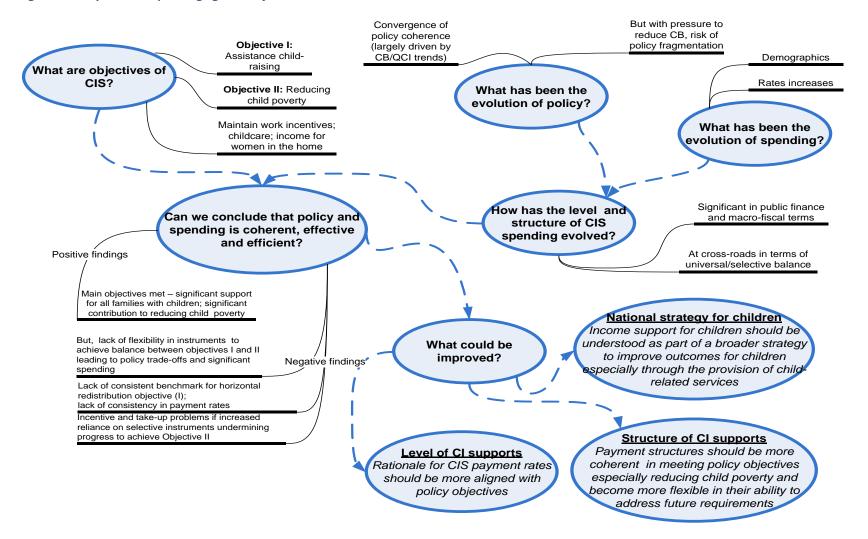
# COHERENCE, EFFECTIVENESS AND EFFICIENCY OF CIS POLICY

In the absence of a specific target for how much assistance should be provided to all families (horizontal redistribution), the review examined the evolution of the CB payment against a number of relevant indicators and found that the level of assistance increased significantly both in real and relative terms. However, the extent to which this can be objectively assessed is hampered by a lack of clear policy targets on how much assistance should be provided. The analysis did not consider in detail the objective of addressing childcare costs but rather treated this as an aspect of the cost of child-raising generally. The review also undertook an examination of the effectiveness of payments in reducing child poverty (vertical redistribution) and its impact on employment incentive indicators. This included specific analyses in order to assess how well objectives were being achieved: comparison of child income support payment rates with income indicators; household income simulation to determine the impact on poverty and on work incentives of programmes; and calculating the static effectiveness and efficiency of CIS payments on poverty outcomes. A summary overview of the conclusions from this analysis is presented in Figure 1.

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<sup>&</sup>lt;sup>3</sup> CB, QCIs, FIS, BtSCFA and ECS.

Figure 1: Analysis of CIS spending against objectives



Combined spending on CIS programmes has increased considerably, especially in universal payments, over the period of the review and this has allowed for significant increases in the value of support to families with children. This has allowed both primary policy objectives (horizontal and vertical distribution) to be met in a way which limited the trade-off between targeting poor households and minimising work disincentives from income support. While child poverty rates remain higher than adult equivalent rates, the key child poverty indicators have fallen by more than adult poverty indicators over the period of the review – and notably so in recent years. Spending on child income supports contributed to this positive development, although it is difficult to get a clear picture of the exact size of this contribution because of data limitations and because of the effect of indirect factors on employment incentives. These positive effects arose because of the value of the CIS package kept pace with the rising poverty line, the universal nature avoided potential problems with selective instruments (such as disincentives and non take up) and the CIS package was moderately efficient at targeting resources at the lower half of the income distribution despite the dominance of CB and ECS spending. More specifically, the review concludes that:

- In relation to horizontal redistribution, the value of the Child Benefit payment has increased significantly in real and relative terms over the period of the review. It is likely that a greater proportion of child-related costs are being met by the taxpayer. However, in the absence of an explicit official benchmark on the cost of a child and of the extent to which the state should provide help to all families, the review was not in a position to formally evaluate how well this objective was met.
- In relation to *vertical distribution*, child poverty did fall over the period of the review particularly at times when the level of (largely) universal support was increased. Child income support spending clearly contributed to the reduction in child poverty over the period of the review. However, it is difficult to be specific about the size of this contribution given the range of factors around both the measurement and the drivers of child poverty. While these confirmed a positive impact of the level and structure of child income supports on poverty and incentives, they also confirmed the earlier conclusion that such supports could play only a partial role in addressing child poverty and that other factors including increased employment and family structures were important in addressing child poverty.

How were these outcomes achieved? Over much of the review period, the policy target around the CB plus QCI package was to achieve a value of 33-35 per cent of the adult social welfare rate. This target was attained despite very significant real increases in the value of adult payments and this was clearly important in maintaining the value of incomes in poorer households with children. Another particularly significant development over the period of the review was the evolution in the **policy mix** (that is, the balance of support between universal and selective instruments in general and between CB against QCIs in particular). At the beginning of the review period, the policy mix could be described as 'mainly selective'

(with QCIs accounting for around three-quarters of the income support package for a child). In the mid-to late 2000s, major increases in the value of CB and the introduction of the ECS led to a policy package that could be described as 'mainly universal'. Changes since the onset of the economic and fiscal crisis has led the policy back to what could be described as a 'mixed approach' where the values of CB and QCIs are similar.

An increased reliance on universal payments may have meant a higher programme cost than strictly necessary to reduce poverty given the possibility of some deadweight or efficiency costs. While universal supports did provide additional resources to households in the bottom half of the income distribution, it did also provide additional resources (albeit not as great) to households in the sixth and seventh income deciles. Furthermore, the largest increases went to households in the fourth and fifth income deciles compared with relatively modest increases in the bottom decile suggesting some degree of problems with targeting the selective instruments. The question of how these shortcomings might be addressed is considered later in the review.

#### WIDER AND LONGER-TERM IMPACTS

CIS policy cannot be considered in isolation from other public policy programmes for children. Instead CIS payments should be understood as part of the broader strategy to improve outcomes for children and specifically child well-being. The National Children's Strategy focuses on these wider outcomes and CIS payments contribute to at least one of the positive outcomes for children identified within that strategy (*economic security and well-being*); they can also complement programmes that focus on producing other positive impact on children's lives such as educational attainment and health status. The provision of child-related services (particularly education and childcare facilities) is also important for parental employment and can facilitate a route out of poverty for some families and their children. In terms of the longer term impact of spending, children living in low-income households are more likely to have a low income when they reach adulthood. The consequences of the intergenerational transmission of poverty can have a limiting effect on children's opportunities later in life and thus on the long-term effectiveness of CIS payments.

### LESSONS FROM OTHER COUNTRIES

In order to place child income supports in Ireland in a broader context, the review also considered what happens in other countries. Child income support systems vary enormously across countries in terms of their absolute value to families, the degree of targeting/universalism and mode of delivery (e.g. the income support or the taxation systems). However, while differences can be discerned across countries, similarities in policy objectives can also be observed: alleviation of poverty amongst families, improving child well-being as a whole and reconciliation of family life with participation in the labour

market. While most OECD countries operate a universal system at some level of payment, many countries also place an emphasis on targeted payments (notably the UK, United States and Australia, all of whom operate forms of tax credit systems). Indications are that measures internationally to reform child income support systems tend to move in the direction of targeting and trying to improve labour market outcomes for parents.

The review also considered the effectiveness of expenditure on child income support against child poverty outcomes. In the mid-2000s, the poverty rate in Ireland was higher than the OECD average despite significantly higher levels of spending on cash benefits. Furthermore, some countries, such as the UK and Australia, achieve better child poverty outcomes from a similar level of spending as Ireland. Other countries, mainly Nordic, achieve lower poverty rates with lower levels of spending on cash benefits but with significantly higher levels of spending on services for children, particularly on supports, such as parental leave and childcare, for families with young children.

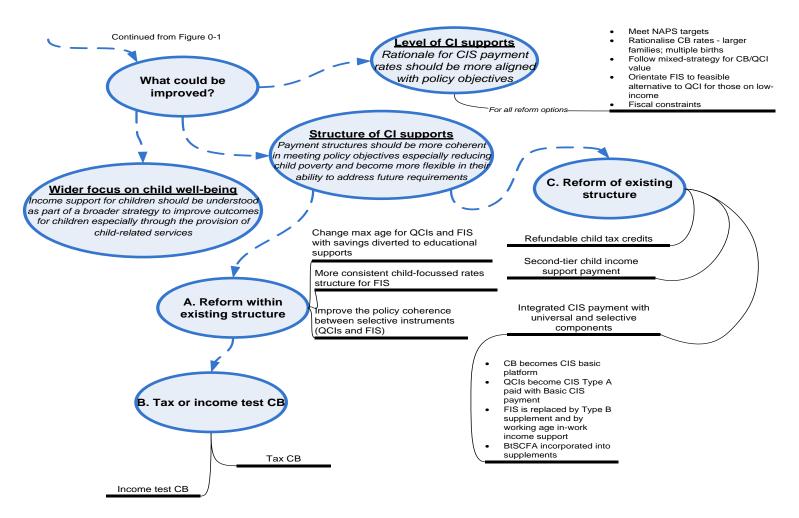
#### **CONSULTATION PROCESS**

A consultation exercise was conducted as part of the review process. This consisted, firstly, of an invitation for written submissions from the social partners and community and voluntary groups and, secondly, an invitation to policy experts to make an input into the process. With regard to the written submissions, there was a general acceptance that both the horizontal and vertical redistribution objectives of CIS should be maintained. However, there was less agreement as to the appropriate level of CIS payments to be devoted to the horizontal redistribution objective. With regard to the vertical redistribution objective, there was a general view that CIS was not wholly effective in tackling child poverty. To improve this effectiveness, submissions in the main identified remedies to the current CIS structures, particularly with regard to FIS, and some suggested the development of a targeted second tier payment as an alternative policy approach. While similar themes were also addressed in the contributions from the policy experts, alternative approaches to improving the effectiveness of CIS included the development of an integrated and taxable child benefit system. The issue of work incentives and the effect of in-work benefits, such as FIS, were also identified as areas that should be considered in the context of the review.

# IMPROVING OUTCOMES THROUGH GREATER RATES COHERENCE AND STRUCTURAL REFORM

A summary overview of how the earlier analysis links with the case for reform and the options available for reform is provided in Figure 2. The review considered change under a number of areas: a wider focus on child well-being; changes to the level of supports; and changes to the structure of supports.

Figure 2: Link between analysis and conclusions



#### WIDER FOCUS ON CHILD WELL-BEING

The review recognised that overall spending on child income supports needs to be seen as part of the wider effort by governments to improve outcomes for children and their families. Well-designed child-related spending can have largely positive outcomes, particularly in relation to material well-being and economic security - one of the high level outcome goals in the National Children's Strategy. However, in order to improve child well-being, many other interventions may be necessary, most notably in the provision of child-related services. Given that the balance between income supports and services are acknowledged to be out of line with the experience of other countries with better outcomes for children, it may be possible to secure better outcomes by shifting some financial resources from income support towards services taking account budgetary constraints. The nature of those interventions would have to be carefully identified and it is noteworthy that issues similar to those considered in this review for cash payments may also arise for such service interventions (such as the choice of universal or targeted provision, forms of targeting etc). The NESC, in its report on the Developmental Welfare State, outlined its vision of 'tailored universalism' as a system where "high quality services are provided through universal access for the means of access are tailored to individuals' specific circumstances" . 4 Decisions on these means of access will depend on the nature of the intervention and its programme logic and may go beyond the operation of the child income support system and indeed the social welfare system. The clearest example of this in recent years has been the decision to abolish the universal early childcare supplement in favour of the Early Childhood Care and Education scheme. In the future, similar issues may arise and will play a part in the preparation of a new National Children's Strategy.

#### LEVEL AND CONSISTENCY OF SUPPORT

Taking account of the two primary objectives and the policy trade-offs contained within the payment structure, the review considered the question of support levels **between** universal and selective components and **within** each of those components.

The analysis suggests that a **mixed strategy** where universal and selective elements are roughly equivalent in value may have considerable advantages over alternative approaches. Rough parity between the value of CB and targeted instruments can provide both traction in tackling child poverty and meeting horizontal objectives. This is because it provides both an employment/income-neutral <u>platform</u> and <u>supplements</u> for poorer families. A mixed strategy also avoids the possibility of stigmatising payments and provides considerable administrative and delivery advantages. The review recommends that where it is possible

<sup>&</sup>lt;sup>4</sup> The Developmental Welfare State, National Economic and Social Council (Dublin, 2005).

given fiscal circumstances, a mixed strategy should be pursued in the future rather than moving in the direction of greater selectivity or universality.

The review also considered the question of greater coherence and consistency **within** both universal and selective instruments:

Coherence of CB payment structure: The level of universal assistance should be determined by (a) the objective costs of raising children and (b) the societal and political consensus on how much of these costs should be shared between the state and the household. While the latter is ultimately a decision for the policy process itself, an understanding of the former would be improved by more regular monitoring of the cost of a child and of transparency and coherence within CB payment structures. For this reason, the review felt that it would be worthwhile in the future to regularly monitor child-related costs. Economies of scale related to the number of children in a family might also be examined in this context, since different payments address this matter in different ways. For instance, CB pays more for larger families, whereas FIS has a bias towards smaller families and can pay less. Furthermore, as the rationale around higher payments for larger families is often linked to poverty objectives (i.e. larger families tend to be poorer), a mixed strategy where poverty reduction was pursued through selective instruments could justify the gradual reduction and eventual abolition of the higher CB rate with savings diverted to selective instruments, subject to budgetary constraints. Microsimulation analysis documented in the review suggests that this is likely to have a positive impact on poverty reduction as well as rationalising the CB structure itself. Another area requiring further analysis was the actual costs to families associated with multiple births and the ages at which these costs occur. This is in order to objectively justify the current CB payment structure that provides a large financial bonus to multiple births.

Coherence of selective instruments: It was clear from the analysis that there were a number of areas, particularly in relation to FIS, where selective instruments did not operate coherently and consistently. For instance, QCIs are paid with the FIS payment for some households but not with others; and the rate of FIS per child varies widely depending on family size and income. Some steps have been taken to ensure greater coherence in selective payments over the period of the review. These included bringing QCIs to a single payment rate and reducing the extent of divergence in the FIS payment per child through successive annual increases to the income limits for larger families since 2006. Nonetheless, the coherence of policy would benefit from a common approach to the level of support to be provided across all low income families, regardless of the employment status of the parents. The degree to which this could be achieved without fundamental reform of FIS is limited. This is because of the dual role of FIS (employment and child income support) and reform in this area would have to take account of broader reform in working age payments (addressed in Chapter 9).

# STRUCTURE OF SUPPORT

The review also addressed the issue of the structure of child income supports (eligibility for and design of payments) in order to be more effective in reducing child poverty by targeting resources coherently and consistently. Views on the balance between universal and selective supports will evolve over time as they have done over the period of the review. The ultimate objective of a reformed CIS structure should be to provide future policy makers with instruments that are sufficiently flexible to meet policy objectives effectively and efficiently. The review identified a number of reform strategies in order to achieve this flexibility: some within the existing payments structures and some implying significant structural reform of payments.

The extent to which structural changes can improve coherence and effectiveness within existing structures (that is, maintaining the broad conditions underlying CB, QCIs and FIS as they currently stand) is limited by the existence of overlaps, different target groups and the interaction between benefits and income. However, the system could be improved somewhat through:

- Aligning some of the main determining conditions for payments, most notably the
  age requirements for selective payments. In principle, this would mean aligning the
  upper age for all payments to 18 years which could allow for resources thus saved to
  be put into appropriate educational supports;
- Reforming CB through taxation or income testing. While a CB based strategy would have some potential to make overall spending more targeted it would suffer from considerable policy, legal and administrative difficulties without any guarantee of improved outcomes or coherence of policy instruments;
- Reconsidering the specific conditions for FIS in order to make it more efficient as a child income support payment. In addition to aligning the thresholds to provide greater consistency between payments per child for families on similar incomes, reform could focus on eliminating overlaps between QCIs and FIS, reviewing the minimum hours of work requirement and taking further administrative measures to improve take-up of FIS. However, as noted earlier, the extent to which FIS can be reformed to produce better child-related outcomes is constrained by the extent to which FIS has alternative employment support objectives. FIS needs to be more fundamentally reformed if it is to achieve both employment and child income support objectives.

The review therefore considered a number of other approaches centred on **structural reform** of the system of child income supports:

- Refundable child tax credits;
- Second-tier child income support payment;
- Rebalanced and integrated child income support payment.

Each of these options implied a greater degree of integration with tax administration or increased use of income data in the delivery of support than is the case in the existing system. The strongest degree of integration would arise with refundable child tax credits: such credits are delivered through the tax system as in other countries (UK, US). While such an approach could not be ruled out at some stage in the future and indeed has been suggested as a possible alternative to FIS by the recent Commission on Taxation, it is unlikely to be a feasible option in the short to medium term. Furthermore, it would result in a reduction in the visibility of income support for children as it would be delivered in the main through pay packets rather than through a specific child-related payment. A second-tier child income support payment has been suggested as a possible alternative to replace QCIs and FIS but administrative and technical difficulties indicate that it would take some considerable time to achieve it.

The review identified a third approach (rebalanced and integrated child income support payment) that would rely as much as possible on the positive features within the current system but would rebalance their relative levels and interaction so as to make the overall system more coherent and effective. Such a payment could combine the following components in one single payment per child: a universal component (to replace CB); plus a selective supplement delivered where entitlement to a primary social welfare payment was in payment (to replace QCIs) or as an income tested supplement (to replace FIS).

Such a system would differ from the current system in a number of ways. Families would receive a single integrated payment per child. For all families this would comprise of a basic payment while some (low income) families would receive a supplement based either on their social welfare status or by virtue of low income. Unlike the current situation where both FIS and QCIs could be paid, only one supplement per low-income child would apply. This approach would allow for the **incremental** alignment of CB, QCIs and FIS into a single child income support payment that would provide some support to all families and deliver

additional targeted support to all low income families across the welfare-to-work divide. In common with other approaches to structural reform, this would have a number of advantages over both the current structure and the alternative of means testing or taxing child benefit:

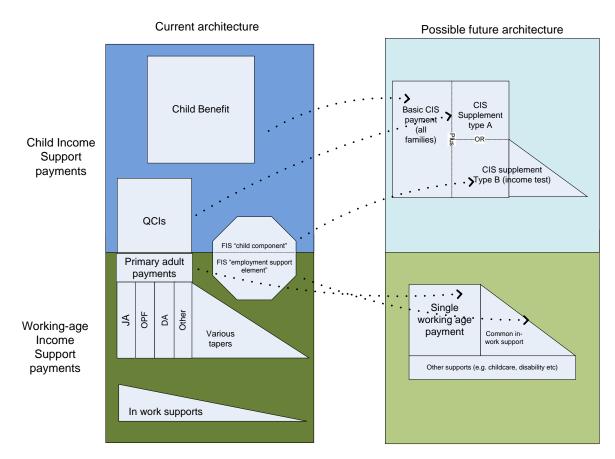
- It would address horizontal and vertical redistribution objectives in a single instrument making it more visible and easier to assess if it was meeting governmental objectives;
- The various elements would be more transparent to families with children and inconsistencies could be avoided;
- It would be easier to cross the welfare-to-work divide while minimising work disincentives.

The main advantage of the integrated and rebalanced CIS payment approach over other structural approaches is in terms of its medium-term feasibility. It does not assume that data on current household income from either the current taxation or social welfare system will be more readily available than is currently the case. While it would constitute a major project of reform, it would build incrementally on the positive features within the existing system of child income supports to provide a more coherent payment structure allowing support to all families with children while at the same time applying a consistent level of support to low-income families without weakening employment incentives. The expenditure review identifies the main steps of such a reform process but the overall feasibility of this approach would have to be examined in greater detail if it is to be progressed. For instance, reform of FIS would not only have an impact on supports for children but also for working age payments. The review therefore recommends that the DSP undertake a more detailed assessment of the policy and operational feasibility of such an approach, particularly for the FIS payment given that changes to FIS would have both employment support and child income support implications. The possible future of working age payments is currently being considered as part of another report by the DSP.5 An overview of how the high-level architecture of such a new integrated payment could be structured and connected is shown in Figure 3.

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<sup>&</sup>lt;sup>5</sup> Report on the desirability and feasibility of introducing a single social assistance payment for people of working age, Department of Social Protection (2010).

Figure 3: Architecture of Child Income Support and Working Age payments - current and possible future



The review also identified a number of performance indicators around which the future effectiveness and efficiency of the child income support spending can be monitored and evaluated. These centre on the two primary objectives as well as maintaining work incentives.

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