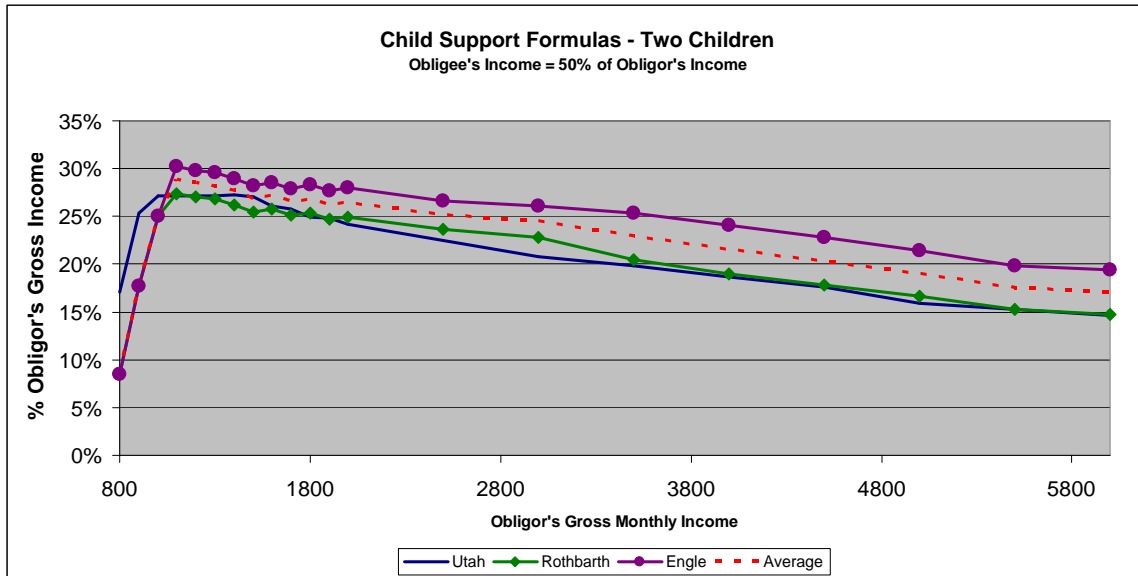


# Examining the Basis of the Child Support Increase

The motivation to increase Utah's child support is mainly due to a **report from Policy Studies Inc.** that shows a **comparison of economic models and current Utah child support amounts**. The report was commissioned by the Utah Advisory Committee and was completed in the fall of 2003. It is a federal requirement to review child support guidelines every four years, and Utah contracted with PSI to produce this report as a result of that requirement.



The several graphs included in the PSI report show two economic models (Betson – Engle and Betson – Rothbarth) that attempt to estimate the costs of raising children for families at different income levels and different numbers of children. The report states that “economists believe the Engle measurements overstate actual child-rearing costs” and “economists believe the Rothbarth measurements understate actual child-rearing costs”. The graph also includes an average of the two models (labeled as average in the above graph), represented as a line halfway between the high and low models. The current Utah child support amounts are also included in the graph. The highest model charted higher than the current Utah support guidelines by as much as 70%. The Utah Advisory Committee determined to raise child support using the average line (red dotted line in the chart above) on all income levels for all numbers of children resulting in increases of as much as 57%. Senate Bill 23 caps the increase at 25%.

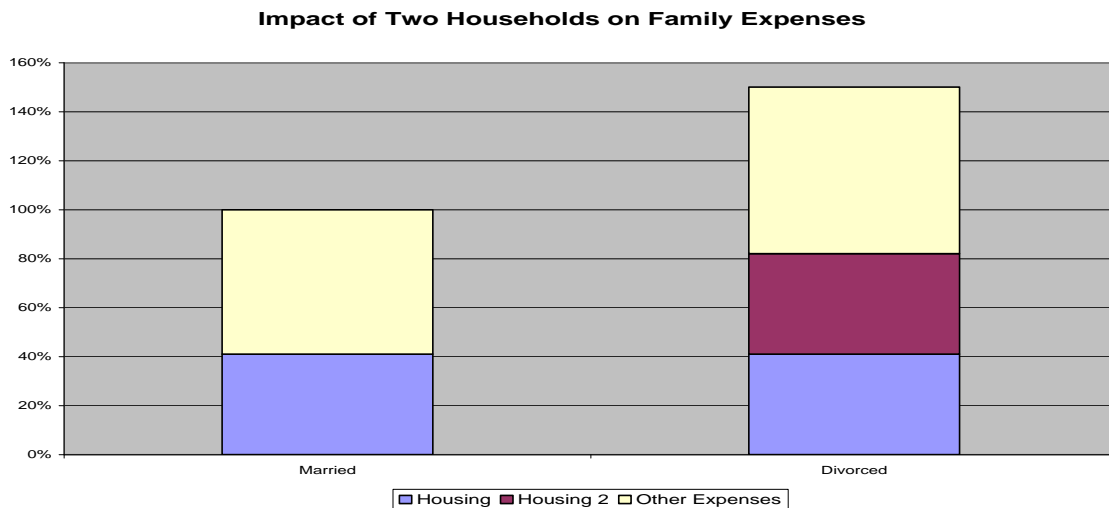
This all sounds reasonable on the surface, but I propose we dig a little deeper into the origin of these lines on the graph that is motivating such a drastic increase. It is easy to look at a graph and say one line is lower than the other, but what do these lines represent in the real world? How do these economic models relate to the financial state of a divorced family? That is the question that really matters here, because if they don't relate to reality then their use in comparison is pointless. I will show that the models do not

equate to reality in divorced homes. The reason they are so far from reality is they ignore some of the basic financial facts that confront a divorced family.

## Child Expenses for Divorced Family are Based on an Intact Home

The two models used in the PSI report are both Income Shares models which derive their estimate of child rearing costs on the costs of an intact home with parents and children living together under one roof<sup>1</sup>. This **ignores the biggest single financial impact on the divorced family**, the increased costs of maintaining the family in two households, with duplicated rent or mortgage payments, duplicate utilities and phone, increased transportation costs, etc. As these costs nearly double, **the available income to spend on child-rearing is greatly reduced**. The models are aware of this fact but explicitly ignore it<sup>2</sup>.

Below is a graphic example of what happens to expenses when an intact family is divided into two households. The bar labeled “Intact” shows the expenses of an intact family, the bar labeled “Divorced” shows the expenses of a two household family. Under Income Shares methodology the family must maintain the same standard of living of an intact home. This has the effect of increasing the costs by roughly 150%<sup>3</sup> over what the family can afford with the current income level.



Sometimes, after a few years receiving cost of living increases and promotions, the noncustodial parent reaches a level of income that actually provides enough resources to meet the increased costs of the duplicate housing. Unfortunately, more often than not, he

<sup>1</sup> “the Income Shares Model ... seeks to apportion the child-rearing expenditures between the parents based on what the parents would have spent if the household was intact.” Jane C. Venohr, *PSI Report on Improving Michigan’s Child Support Formula*, Policy Studies, Inc. (PSI), Denver, CO, (April 12, 2002), page 17.

<sup>2</sup> “the Income Shares model assumes the child should be entitled to the same standard of living the child would receive if the parents lived together. In contrast, the Cost Shares model recognizes that the same standard of living the parents are able to afford when they live together, cannot be achieved when there are two households.” Venohr (2002), page 108.

<sup>3</sup> Duplicate costs of rent, utilities, phone, and other household costs plus increased costs of transportation, food, and other expenses require an increase of roughly 150% if the divorced family were to maintain the same standard of living present before the divorce. David M. Betson, *Composition of Expenditures for Average Family CEX (1996-99)*, (2001), Exhibit 5-3, Two Children.

is then taken back to court to have his support increased. He is now required to provide support at a higher level for an intact household which inflates his two household expenses once again.

The requirement to maintain the pre-divorce standard of living assumes that there is “phantom income<sup>4</sup>” to meet these significantly higher expenses. This overestimate of costs is blatant, counterintuitive, and is one of the major reasons these models produce child-rearing costs that are so high.

## Models Ignore Huge Disparity in Taxes

The child support amounts provided in the PSI report include the assumption that the noncustodial parent receives no tax deductions<sup>5</sup>. They also suggest that both the child support amount and the day care amounts should be divided by ability to pay, which is equated to the gross income ratio of the parents. Because the custodial parent is entitled to the Head of Household filing status, Earned Income Tax Credit, Child and Dependent Care Tax Credit, and Day Care Flex Spending Accounts (none of which are available to the noncustodial parent) there is a substantial difference in before and after tax income between the two parents.

The example in Table 1 illustrates this point. It shows the tax effect on divorced parents with equal gross income, which when combined is equal to the Utah 2005 median income. The table uses 2005 tax rules and a two child family with monthly daycare costs of \$500. Medical insurance is included due to the fact that it is a pre tax deduction, and is based on actual 2005 medical insurance costs for a Utah employer. The custodial parent receives no tax deductions, thus matching the assumptions of the PSI models.

Table 1 - Effect of Taxes 2005 Utah Median Income Custodial Income = Noncustodial Income (monthly amounts)		
	Custodial	Noncustodial
Gross Income (relative percent)	\$2275 (50%)	\$2275 (50%)
Health Insurance	-\$58	-\$158
Taxable Income	\$2217	\$2117
Social Security & Medicaid	-\$170	-\$162
Federal Income Tax	\$318 (credit)	-\$185
Utah Income Tax	-\$50	-\$89
<b>After Tax Income (relative percent)</b>	<b>\$2315 (58%)</b>	<b>\$1681 (42%)</b>

<sup>4</sup> “It falsely assumes that there is additional income when a child is added to the family: additional income that would raise the family’s presumed standard of living to what it would be without children.” *Ohio’s Child Support Guidelines Council Report*, Ohio Job and Family Services, Columbus, Ohio, (March 1, 2005), page 16.

<sup>5</sup> Recall, that the proposed schedule assumes the noncustodial parent earns all income and is a single tax payer who claims no dependents as tax exemptions. *Utah Child Support Guidelines, PSI*, Denver, Colorado (Sept 25, 2003), page 33.

As you can see the noncustodial parent is left with only 42% of the after tax income when the models' assumptions are applied. Since the models use gross income to measure ability to pay, child support and daycare costs are assigned to the noncustodial parent at the 50% rate.

The PSI report recognized that the noncustodial parent may be awarded tax deductions by court order. A full 20 pages of the report are devoted to analyzing how the child support amount should be increased if the noncustodial parent receives one or more tax deductions stating "When the noncustodial parent's taxes are reduced— say, through claiming the children as dependents for tax purposes— then the noncustodial parent has more income available to spend on the children."<sup>6</sup>

## **Models Ignore Noncustodial Home**

The models make the assumption that all costs for the children are in the custodial home. This precludes normal Utah minimum parent time with the children, which calls for the children to be with the noncustodial parent from 25-28% of the time. It not only overstates the costs of the custodial parent slightly (due to the 25% time the children are absent from the custodial home), but completely ignores the cost to the noncustodial parent for housing and other child related costs in the noncustodial home. It is definitely not in the best interest of the child to implement a financial system where their time with the noncustodial parent is completely written out of the budget.

According to Utah law the fixed costs of raising a child (for rent, utilities, etc) are 50% of the calculated child support amount<sup>7</sup>. That means that the noncustodial parent is spending a significant amount to house the children, in addition to the food and other variable expenses for the children where they spend 25% of their lives. None of these costs are considered, and when the child support amounts are applied with taxes, daycare and other mandated child expenses, many noncustodial parents are taken below the poverty level that would include at least the fixed costs of the children.

## **Litmus Test**

One test suggested by an economist to determine the accuracy of a model's presumptions would be to apply the model to parents of equal income. If the model is accurate the parents should have the same standard of living, with the custodial parent having a higher measure for the standard of living, due to the presence of the children for the greater amount of time. The government often uses the poverty guideline to determine a relative standard of living, and this is the measure used in Tables 2, 3, and 4 below. The tables are based on the same family used in Table 1, median 2005 Utah income, two children, with equal gross incomes. All three models (i.e. the two models and the compromise line which Senate Bill 23 is based on) were used in this comparison. Since daycare costs are based on gross income they remain unchanged in the comparison (\$500 month for two children divided equally between the parents).

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<sup>6</sup> Utah Child Support Guidelines, PSI, Denver, Colorado (Sept 25, 2003), page 33-52.

<sup>7</sup> Utah Code 78-45-7.11

Table 2 - Effect of Betson-Rothbarth Model 2005 Utah Median Income Custodial Income = Noncustodial Income (monthly amounts)		
	Custodial	Noncustodial
After Tax Income (relative percent)	\$2315 (58%)	\$1681 (42%)
Daycare expense	-\$250	-\$250
Child Support	\$467	-\$467
<b>Disposable Income (relative percent)</b>	<b>\$2533 (72%)</b>	<b>\$964 (28%)</b>
<b>Percent of Poverty Guideline<sup>8</sup></b>	<b>183%</b>	<b>88%</b>

Table 3 - Effect of Average of two Models 2005 Utah Median Income Custodial Income = Noncustodial Income (monthly amounts)		
	Custodial	Noncustodial
After Tax Income (relative percent)	\$2315 (58%)	\$1681 (42%)
Daycare expense	-\$250	-\$250
Child Support	\$507	-\$507
<b>Disposable Income (relative percent)</b>	<b>\$2572 (74%)</b>	<b>\$924 (26%)</b>
<b>Percent of Poverty Guideline</b>	<b>186%</b>	<b>84%</b>

Table 4 - Effect of Betson-Engle Model 2005 Utah Median Income Custodial Income = Noncustodial Income (monthly amounts)		
	Custodial	Noncustodial
After Tax Income (relative percent)	\$2315 (58%)	\$1681 (42%)
Daycare expense	-\$250	-\$250
Child Support	\$547	-\$547
<b>Disposable Income (relative percent)</b>	<b>\$2612 (75%)</b>	<b>\$884 (25%)</b>
<b>Percent of Poverty Guideline</b>	<b>189%</b>	<b>80%</b>

In every case the custodial standard of living as measured by the poverty level is more than double the noncustodial standard of living. This shows how the models completely ignore the noncustodial home.

<sup>8</sup> The poverty guideline used for the custodial parent is based on a family size of three, which is slightly overstated due to the absence of the children from the home 25% of the time. This yields a lower than actual poverty percentage for the custodial home. The poverty guideline used for the noncustodial home is a family size of two, which includes the fixed costs for two children at 50% of the total cost to cover housing and other fixed costs. This guideline is slightly understated due to the presence of the children 25% of the time which would increase food and other variable costs. This yields a higher than actual poverty percentage for the noncustodial home.

If the goal of the child support guidelines is truly the best interests of the child, the models used by PSI undermine that goal by ignoring the true divorce financial picture and making it difficult for the noncustodial parent to provide for the children, or even for himself, in the noncustodial home. The PSI models do not reflect the financial realities of the divorce by requiring the expenditures of an intact family from a divorced family, ignoring the tax disparity between the homes, and ignoring the noncustodial home altogether. These models should not be used to determine an increase in child support.

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