The Universal Welfare State

incorporating proposals for a Universal Basic Income

by Keith Rankin

A. THE WELFARE STATE

The universal welfare state in New Zealand is in its death throes. The case presented against it has been a *fait accompli*, bought with little thought about what a welfare state really is. The impression given by the many participants in the current debate is that the welfare state is a costly item of public consumption; a form of discretionary social expenditure that distorts otherwise efficient market mechanisms.

A welfare state is basically a means of sharing resources. It comprises four interlocking systems: an insurance "safety net" against individual misfortune, a system of economic stabilisation, a system of human investment and a system of income distribution. None of those are inherently expensive; rather they all involve negative opportunity costs. That is, it costs society more to *not* have these systems in place than to have them.

Massey University's David Thomson, in his 1991 book *Selfish Generations?*, sees the Welfare State as being an income-smoothing scheme to which people of certain ages contribute and people of other ages draw on; a system of redistributing income between generations. In contrast, I believe that income redistribution has not been the most important component of the twentieth century welfare state.

1. The Safety Net Function

The welfare state provides compensation to people who, through misfortune, are prevented from earning a living for themselves and their families. The main forms of misfortune covered are sickness, incapacity through accident or illness, and unemployment. Much of the cost of the public hospital system comes into this category. So, indirectly, does much of the cost of law enforcement. The payment of social insurance premiums through ordinary taxation minimises administration and collection costs, and makes it easy to adjust premiums according to people's ability to pay.

The cost of this function of the welfare state is directly related to the level of distress in the community. If the cost is too great, it is because the levels of unemployment, accidents, mental illness, crime and other forms of distress are much greater than they need be. It therefore follows that, to reduce the cost, we as a society must stop pursuing economic policies which use the threat of poverty and redundancy as a spur to individual competitiveness. "New Right" philosophies assume that, for some people to be efficient producers, others must become casualties; that the economy is like a game of musical chairs.

It is true that in a free society, misfortune can only be minimised, never eliminated; there has to be an ambulance at the bottom of the cliff. That is the role of the welfare safety net. I believe, however, that it is appropriate to reduce the cost of social insurance by ensuring that the number of casualties is kept to a minimum, and not by reducing the level of compensation to each claimant as the number of claimants rises.

An important factor to note about the insurance aspect of social welfare is that nobody wants to receive any of its "benefits". As in life insurance, those who do not qualify for claims are the winners. We are better off being healthy, employed, or voluntarily out of the workforce than being on a targeted benefit. We experience higher levels of welfare by not suffering misfortune than by being compensated for misfortune. A generation of people who pay more through taxes in the operation of the safety net than they receive in claims should be regarded as a fortunate generation, not an exploited generation.

2. Economic Stabilisation.

The level of social insurance payments automatically rises in a recession, and falls during a period of recovery. The ensuing budget imbalance acts to limit the extent of both recessions and booms. Benefit payments rise as earnings fall, and *vice versa*, ensuring a stable and predictable pattern of consumer demand. Thus, the efficient operation of the welfare state in itself acts as a source of the business confidence needed to keep unemployment down.

If the welfare state is scaled down during a recession, the recession can easily become a depression. In such circumstances banks become risk-averse; their conservative perceptions of future profitability can hinder the expansion of investment needed for recovery. Who would lend money to a retailer in a town with high unemployment if unemployment benefits are being cut and more tightly targeted? In the depression of the 1930s, countries with comprehensive unemployment insurance, such as Britain and Sweden, recovered quickest.

3. Human Investment

The main forms of human investment are involved in physical reproduction and education; ensuring that there are enough young people born to perpetuate their society and to collectively support their elders, and ensuring that children are cared for and educated in such a way so that their lives will, on balance, make a positive net contribution to their society's future. Thus, most forms of social spending on the young fall into the category of social investment; education, maternity and primary health care, family support, domestic purposes benefit. Other social programmes, such as housing assistance, also fit this category of social investment. So does basic social and scientific research.

A generous family benefit structure is appropriate in a society with insufficient numbers of children being born to support their elders in following decades, a problem that was addressed in New Zealand in the late 1930s. Once again, social policies favouring a moderately high birth rate remain an obvious means to ensure that there will be enough young adults to support next century's elderly.

The provision of public education for both children and people of working age is a critical component of human investment. Most adults will pay a dividend to society if society invests in the upgrading of their technical, critical and communicative skills. Indeed, adults are often more receptive to learning than are school leavers, and, already having invested in their communities, are less likely to take their new-found skills overseas.

Appropriate human investment, like other kinds of investment, pays a dividend in the form of economic growth. It is costly for society to forego such investment. At present, such investment is cheaper than it has been for 60 years, because New Zealand has over a quarter of a million working-age people whose productive potential is being stifled. Social investment requires few foreign exchange earnings. The cost of using unemployed resources to add to future productivity is, at most, nil.

4. Income Distribution.

This category covers progressive taxation and retirement pensions, although pensions also count as human investment. Healthy retired people are productive people. By paying them pensions we free them from the discipline of the marketplace, allowing them to be productive to the extent that they see fit and in the activities of their choice. For example, they can play a key role in the voluntary sector, in the household sector providing services to their parents, adult children and grandchildren, and in the research sector, writing books and embarking on other socially desirable projects that they did not have time to fulfil in their period of formal employment. And they can be employers.

Much of society's income derives from non-labour resources; eg natural resources over which we hold collective sovereignty, capital equipment such as buildings and machinery, and human capital, all of which go to raise the productivity of people. Much of this valuable capital is the result of past social investment. The result is that a society can have high levels of *per capita* income without everyone needing to work hard all their lives. With *per capita* economic growth, an increasing share of a nation's income comes in the form of profits, rent and interest (returns to capital) rather than as wages (returns to labour).

Much of the economic return on natural endowments and social investments is initially registered as private income; for example to road users, electricity users, and employers of publicly educated workers. This is really collective income - a social wage or dividend - that should be distributed equitably to all members of society. Progressive taxation - the former system of taxing people of high incomes at higher average rates - and transfer payments (eg benefits) therefore constitute income distribution, not income appropriation for redistribution.

Collective income, like company profits, can be split between future investment (retained profits) and current consumption (dividends). What constitutes an equitable division is a political decision. In this case, retained profits enable investment in public infrastructure; in social overhead capital. Most societies regard the distribution of dividends to the elderly for consumption as equitable, not simply as a recognition of past contributions but also as a form of retirement insurance premium for people in the workforce.

As electronic technology gradually raises the productivity of work in service occupations, the mechanism of a universal welfare state should be used to develop forms of income distribution which facilitate reduced market-driven workforce participation. The income distribution function of the welfare state needs to be extended in the future, not cut back. National Superannuation, as originally implemented, was, I believe, a foretaste of a truly modern welfare state. It was a form of universal basic income. It simply required an appropriate income tax regime to make it work.

B. THE UNIVERSAL BASIC INCOME

In the second part of this paper, I propose a form of universal income distribution and taxation that is diametrically opposed to the tightly targeted system being implemented in New Zealand; a system that, with full-employment becoming an unrealistic goal, could well become the basis of twenty-first century welfare provision. The suggested system is simple to understand, and requires very little bureaucracy to administer. It is equitable, contains no poverty traps, no means tests and is not inflationary. A poverty trap is the situation which makes it very difficult for targeted beneficiaries to help themselves, because for every action they take to raise their incomes, the government responds by taking away most of that additional income. In technical language, the problem is one of high *effective marginal tax rates*. A marginal tax rate of 50% means that half of one's *additional* income is taxed; a rate of 100% means that all additional income is taxed.

The National Government's targeted welfare "reforms", although driven by a philosophy claiming to espouse individual freedom and minimal government, impose the heavy hand of government on the day-to-day lives of all but the richest New Zealanders. The government is implementing a system in which the majority, controlled by a combination of market forces and government action, effectively serve the interests of the most privileged members of society. It is a system that acts to keep people poor once they have become poor.

The system I am proposing seeks to enhance the freedom of *all* individuals - in the sense intended by the Royal Commission on Social Policy - while fully maintaining the marketplace as a means of allocating resources. It is based on a universal tax credit/rebate available to every adult - the universal basic income (UBI) - and a moderately high flat tax rate. By combining the two elements, the result is an elegant system of income distribution based on progressively higher average tax rates. A benefit structure, a pension structure, a student allowance structure, and a family support structure all emerge from the system. Basic income systems already exist in New Zealand with respect to retired people and children; they are called "ational Superannuation" and "Family Support".[1]

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[1] Another system also exists in New Zealand, the "Gross Minimum Family Income" (GMFI). This system is often confused with the universal tax credit system. The GMFI is in fact a highly targeted system - like the Speenhamland system tried in England last century - which uses a subsidy to top up low wages. The GMFI yields family marginal tax rates of 100% - that is, additional private earnings of any family member are effectively taxed at 100% where the total income remains lower than the gross minimum. The system can be abused as it eliminates the incentive of low-paid workers to seek better wages. Finance Minister Douglas proposed to expand the use of the GMFI in the ill-fated mini-budget of December 17, 1987.

The amounts I have in mind for New Zealand at the present would be a universal tax credit of $6,000 *per annum* (20% of gross domestic product per adult) or $115 per week, and a flat tax rate of 48%. In addition, some people would qualify for a "pension", which would be an additional credit of $4,000 ($77 a week). This pension would be abated at 14 cents in the dollar. (Another way of putting this would be to say that pensioners would receive a total tax credit of $10,000 and pay tax at a rate of 62%.) Eligible pensioners would be anyone over a certain age (such as age 60), anyone who would today qualify for an invalids benefit, and the highest income earner in any household containing children. Company tax would be set just below the personal rate, at 45%.

I would define adults as anyone who is aged over 18, or who has completed four years at secondary school, or who is legally married. Anyone else is a child. A separate income tax scale would apply to children, say $3,000 *per annum* of tax-free earnings with remaining income taxed at the pensioner rate (62%). This should allow for children's legitimate employment, such as newspaper delivery work and limited school holiday employment, but also operate as a means of dissuading young people from entering the full-time workforce.[2] The $3,000 is *not* a tax credit; it is tax-free income.

The basic income and pension replaces all mainline benefits, including family support and student allowances. A few specific benefits could be retained, such as assistance for disabled children, legal aid, and accommodation benefits. The system of payments as outlined is sufficiently conservative to allow for a largely free education and health-care system. Any user part-charges for these services, where they exist, should be the same for everybody.

The basic income would be regarded as a dividend, not a hand-out, and should be indexed. It would normally be adjusted in line with forecasts of *per capita* GNP (gross national product) and not indexed to consumer prices. That is, it would be set as a percentage of GNP *per capita*. It would constitute a guaranteed share of national income rather than a guaranteed level of income. The percentage of GNP could be changed as a budgetary response to changed circumstances. For example, the introduction of labour-saving technology would be a reason to raise the tax credit, making the tax scale more progressive. On the other hand, an expansion of demand for labour-intensive services such as nursing, teaching or research might be a reason to advocate a lower tax rate.[3] At election time, one could imagine centre-right political parties promising to lower taxes while centre-left parties would be promising to raise the tax credit.

It is not possible to categorically determine how well off people would be under the system I am proposing compared to the present system, because the new system contains a different incentive structure. Marginal tax rates of 48% and 62%, which are not excessive by past standards, would become transparent. Under the present system, people on low incomes

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[2] In depressions, such as that of the 1930s, while some children stayed on at school longer because of the lack of work, many children - especially girls - were forced to leave school either to save money on school-related expenses, to perform unpaid labour in the home or family business, or to earn wages which would help support their parents and siblings. It is characteristic of depressions - as distinct from recessions - that teenagers make up a greater proportion of the employed workforce than they do in normal times.

[3] In general, the existence of involuntary unemployment would indicate that the basic income was too low, and the presence of labour shortages would suggest that basic income levels and tax rates were too high.

effectively pay tax rates of up to 100% on additional income, through the workings of the gross minimum family income (GMFI), the imposition of means-tested user charges and the abatement of family support and benefits. Nevertheless, costings of the proposals can be made, and have been made at the end of this paper. Such comparisons show the proposed system to be no more generous overall than the present system. The main effects are to transfer welfare from people on higher incomes to those on lower incomes, and from breadwinners to family caregivers.

Most present beneficiaries would be worse off under the proposed system unless they act to raise their private incomes. By such action, they both raise their own welfare and ease the net contribution made by the rest of society to their welfare. For example, unemployed people over 25 would appear to be better off under the present benefit, but by only losing 48 cents on each dollar of income, they would be much more inclined to seek additional income.

The system acts as an efficient automatic stabiliser. Nearly half of any additional aggregate private income - economic growth - would flow into Treasury, although this would be offset by annual increments to the basic income and pension. Fiscal surpluses would occur whenever the economy threatened to become overheated, and self-limiting deficits would prevent recessions from becoming depressions. This automatic tendency to macroeconomic equilibrium would ensure that planned investment expenditure by firms would not experience the excessive fluctuations we have become used to, and that, for most of the time, those who wished to be employed as wage/salary earners would be able to receive a reasonable job at a reasonable wage. The basic income would confer a degree of additional bargaining power on employees, giving them the option of leaving a job in which working conditions are unsatisfactory.

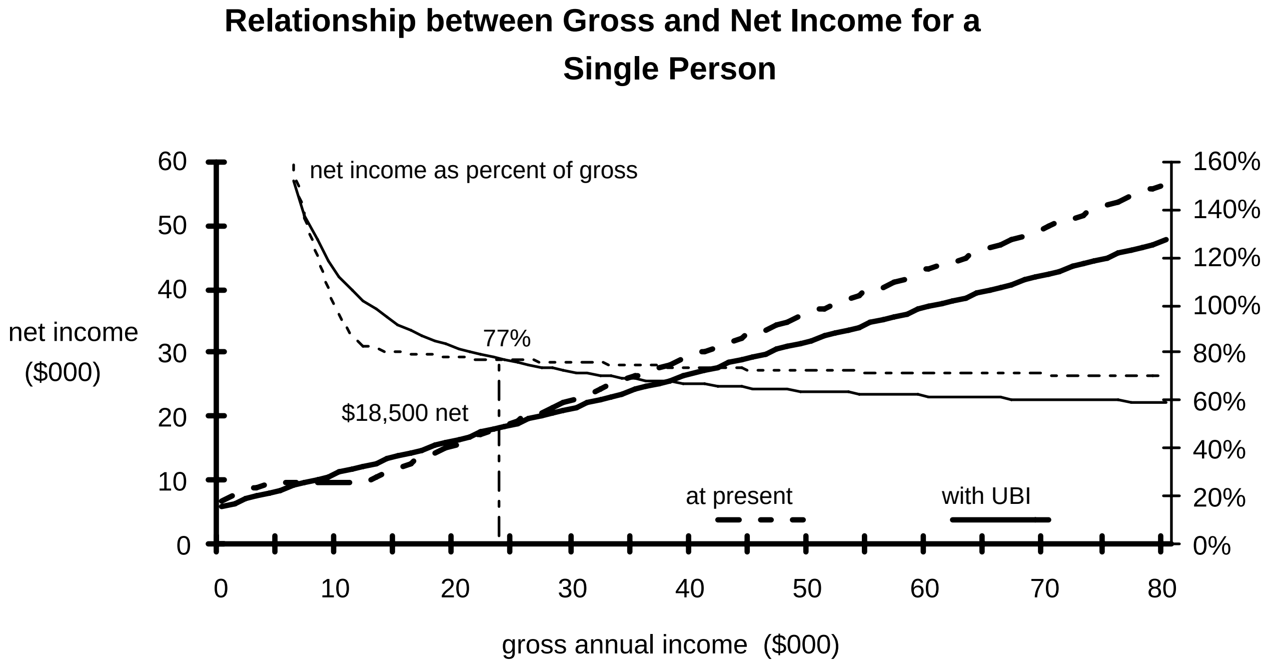
SINGLE ADULTS

People who do not qualify as pensioners would be better off under the proposed system only if their private incomes fall in the $7,000 to $24,000 range. Otherwise they would make a greater net tax contribution. Individuals would be net taxpayers if their income exceeds $12,500 ($240 per week), which is approximately the minimum adult full-time wage. All full-time employees would pay PAYE tax as at present, and receive no credit payments.

TABLE 1 ANNUAL PRIVATE INCOMES: SINGLE ADULTS						
gross private income	present net income	effective marginal tax rate	ave. tax rate	proposed net income	effective marginal tax rate	ave. tax rate
$0	$6,770	15%		*$6,000*	48%	
$5,000	$9,520	98%		*$8,600*	48%	
$10,000	$9,620	98%	4%	*$11,200*	48%	
$15,000	$12,040	28%	20%	*$13,800*	48%	8%
$20,000	$15,630	28%	22%	*$16,400*	48%	18%
$30,000	$22,840	28%	24%	*$21,600*	48%	28%
$50,000	$36,280	33%	27%	*$32,000*	48%	36%
$70,000	$49,680	33%	29%	*$42,400*	48%	39%
$100,000	$69,780	33%	30%	*$58,000*	48%	42%

In table 1 and figure 1, it is assumed that, under the present system, the earner is over 25 and would be an unemployment beneficiary unless the level of private income ceased to make it worth while to be so. Thus, at present, for incomes between $5,000 and $11,000, such a person loses 98 cents of each dollar of additional income. Married individuals without children would each face the above tax rates. Thus, a household in which a woman earns $100,000 and her husband receives $50,000 would contribute $16,000 more than at present to the public welfare pool.

Fig. 1



TWO PARENT FAMILIES

In the proposed system, all households with children would be eligible to receive one pension, on application. Households with a breadwinner earning more than $29,000 would have their pension fully abated. The pension would be assessed against the highest income earner in the household, although it would be paid to the designated caregivers of the children. The Statistics Department definition of households would pertain; namely all people living at a single address. Families at present on a benefit and with private incomes between $1,500 and $5,000 would be slightly worse off, as would single-income families receiving more than $62,000. *All* non-earning homemakers would receive a personal tax credit of $6,000 *per annum*, or $10,000 if sole parents.

TABLE 2 ANNUAL PRIVATE INCOMES: SINGLE INCOME FAMILIES

gross private income	present net income	effective marginal tax rate	ave. tax rate	proposed net income	effective marginal tax rate	ave. tax rate
$0	$15,330	28%		*$16,000*	62%	
$5,000	$17,930	98%		*$17,900*	62%	
$10,000	$17,710	100%		*$19,800*	62%	
$15,000	$17,710	100%		*$21,700*	62%	
$20,000	$18,520	46%	7%	*$23,600*	62%	
$30,000	$23,560	58%	22%	*$27,600*	48%	8%
$50,000	$36,280	33%	27%	*$38,000*	48%	24%
$70,000	$49,680	33%	29%	*$48,400*	48%	31%
$100,000	$69,780	33%	30%	*$64,000*	48%	36%

Table 2 and figure 2 assume that, under the present system, the breadwinner would be an unemployment beneficiary at incomes below $10,000. Incomes from $10,000 to $18,500 are topped up to $18,500 through the GMFI provisions. Single income families would not become net taxpayers until breadwinners' incomes reach $26,000.

Fig. 2

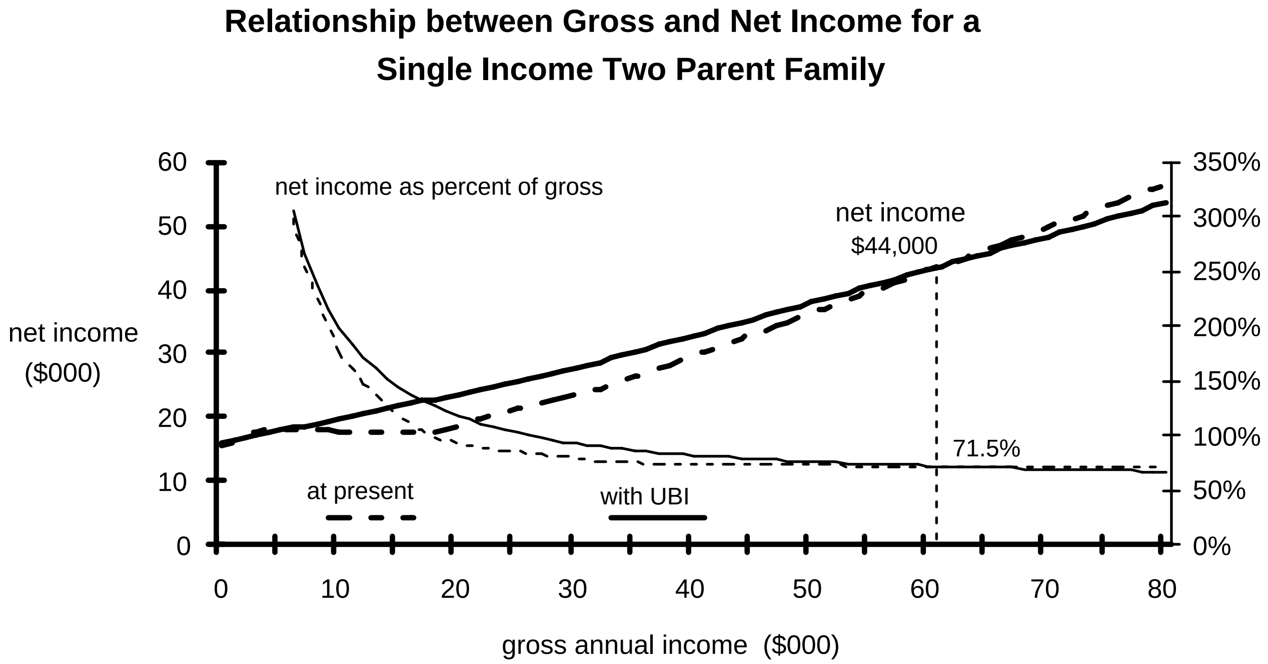


TABLE 3 ANNUAL PRIVATE INCOMES: DOUBLE INCOME FAMILIES

gross private income	present net income	effective marginal tax rate	ave. tax rate	proposed net income	effective marginal tax rate	ave. tax rate
$0	$15,330	22%		*$16,000*	55%	
$5,000	$18,260	92%		*$18,250*	55%	
$10,000	$18,360	94%		*$20,500*	55%	
$15,000	$18,690	94%		*$22,750*	55%	
$20,000	$19,760	46%	1%	*$25,000*	55%	
$30,000	$24,800	58%	17%	*$29,500*	55%	2%
$50,000	$38,470	28%	23%	*$38,500*	55%	23%
$70,000	$52,460	33%	25%	*$48,400*	48%	31%
$100,000	$72,560	33%	27%	*$64,000*	48%	36%

For two-income families, it is assumed for Table 3 that each adult has the same private income as the other; eg they share a job. With a total family income below $58,000, one parent would have a marginal tax rate of 62% and the other 48%. Thus, the effective family marginal tax rate is 55%. Once individual incomes exceed $25,000 the family becomes less well off than under the present system. Families with two equal incomes totalling $50,000 pay the same average tax rates under both systems. It is assumed that, under the present system, the family receives the unemployment benefit at incomes below $10,000 and the GMFI at incomes from $10,000 to $18,500.

Most two parent families come between the extremes of Tables 2 and 3, with one parent earning more than the other. In low income families, it would usually be the mother who would face the lower marginal tax rate. Thus, my proposals encourage female workforce participation and shared parenting. To further facilitate this, and to assist sole parents, I would like to see a 100% subsidy for up to 15 hours a week of quality childcare available for all children aged between one and five, with full market rates being charged for additional hours.

Using Treasury figures, Simon Collins (*New Zealand Herald*, 29 July, 1991) showed that 40% of two-parent families had gross incomes in excess of $50,000. Allowing for the fact that some families receiving benefits would become less well off, 35-40% of two parent families would make a greater net contribution to the welfare pool than they do at present.

RETIRED PEOPLE

In the proposed system, the basic pension is the same as the present National Superannuation for single people who receive the living-alone allowance. The abatement is slightly harsher than at present, but considerably less harsh that the clawback contained in the 1991 Budget. The proposed basic entitlement is not reduced for people who are married or not living alone. Two pensioners living in the same household, regardless of marital status or gender, would each receive a full pension. The system seeks to encourage people to make efficient use of housing and other resources. Pensions would be fully abated when pensioners earn $29,000 or more, leaving just the basic income of $6,000 in addition to private income.

In the proposed system, I would advocate that tax on interest be payable on real (ie inflation adjusted) income,[4] and that there would be an exemption on the first $1,000 of interest received. This would help protect pensioners' investment incomes.

TABLE 4 ANNUAL INCOMES: RETIRED PEOPLE

private income	*proposed net income* $	at present alone	at present married
$0	*10,000*	9,740	7,500
$5,000	*11,900*	13,130	10,710
$10,000	*13,800*	15,480	13,060
$15,000	*15,700*	17,830	15,410
$20,000	*17,600*	20,130	17,760
$30,000	*21,600*	24,330	22,880
$50,000	*32,000*	36,280	
$70,000	*42,400*	49,680	
$100,000	*58,000*	69,780	

Figure 3 shows the differences between the new National Superannuation and the proposed pension for single retired people, while figure 4 contrasts the two schemes for married pensioners. Table 4 summarises the information.

[4] Note that, if prices fell by 2% in the tax year, money deposited at 10% interest would be assessed at 12%.

Fig. 3

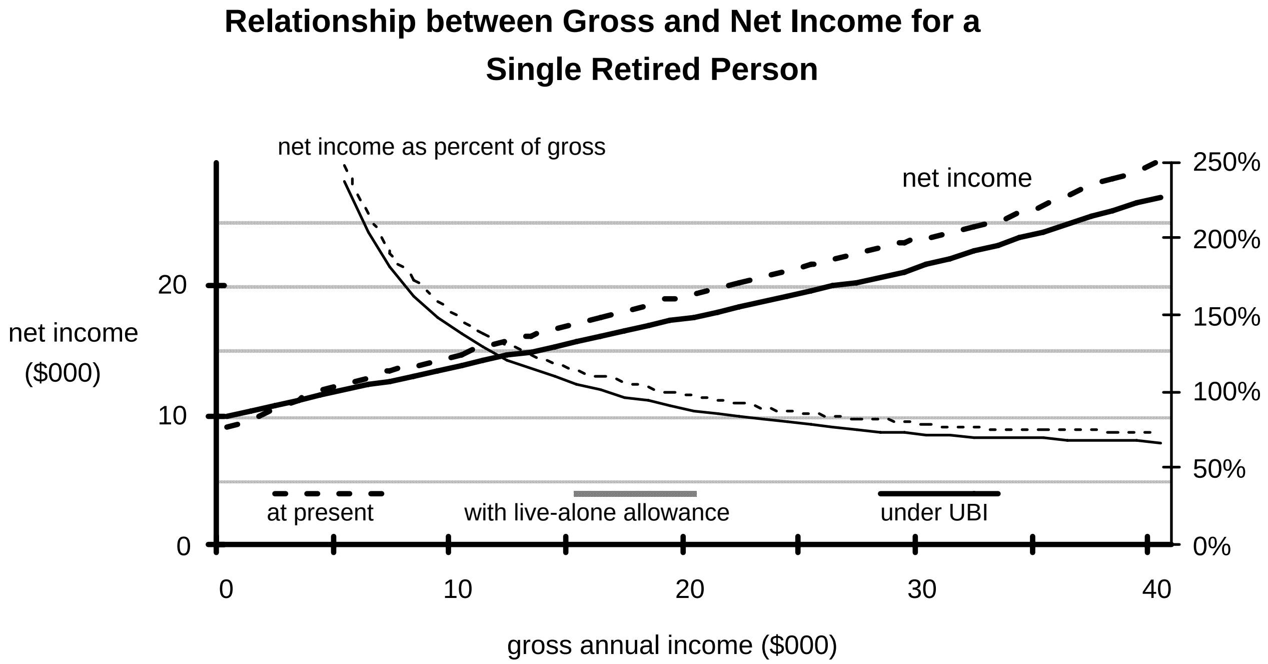
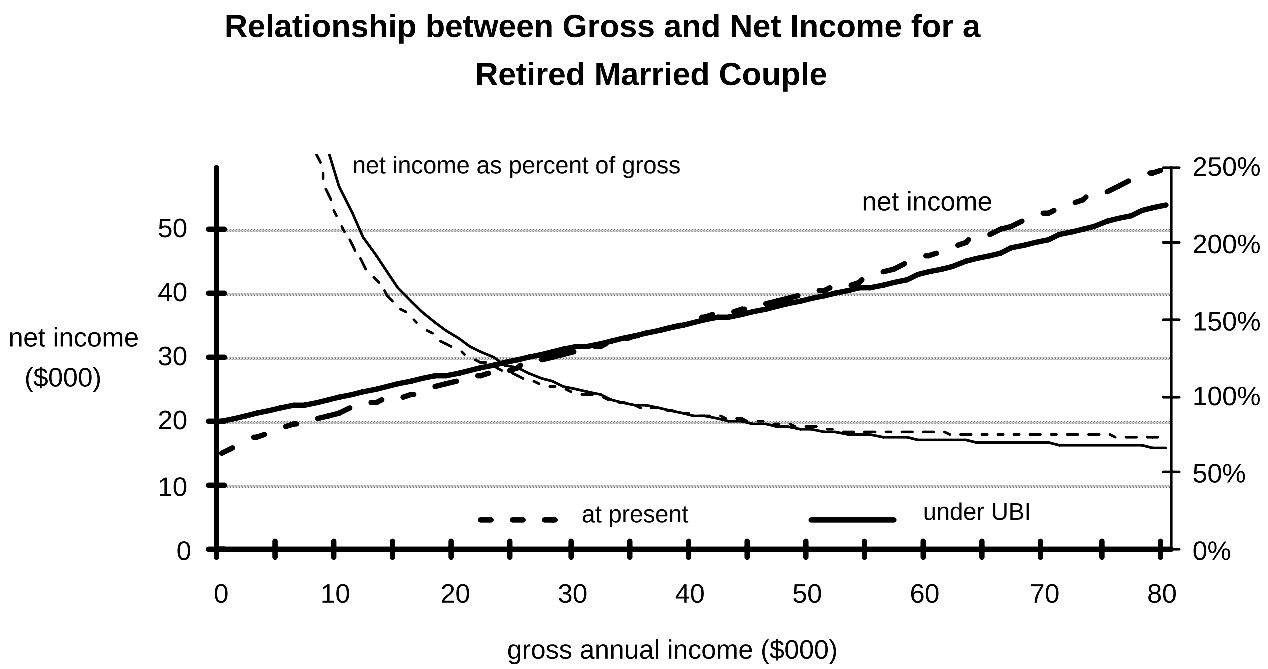


Fig.4



It should be noted that it was the introduction of the 33% tax rate for higher income earners that has made the existing scheme generous for high income recipients. Before 1988, they were paying tax rates comparable with those I am now proposing. That was also true before the tax surcharge was introduced by the fourth Labour Government. In the nine years following the introduction of National Superannuation in 1976, marginal tax rates on higher incomes exceeded 50%, reaching 66% in 1982.

SINGLE PARENT FAMILIES

A sole parent in a one-adult household would receive the pension in lieu of the present domestic purposes benefit and family support. The amount is less than the present benefit. The advantages are that anyone, such as a new partner, could live with such a parent without compromising their financial independence.

The system encourages rather than penalises shared living, making no value judgements about conventional or non-conventional families. (A communal household of ten adults and at least one child would receive $64,000 without any private income.) In the proposed system, adult members of a household are regarded alike whether or not they share the same bed. Thus, a household composed of two mothers each with one child, would claim one pension (payment would be split equally if both designated themselves as care-givers), exactly the same as for a conventional two-parent family. Together they would receive $16,000 plus any taxable private income. In addition, I would advocate that maintenance, where applicable, should be deducted from the gross income of the non-custodial parent and added to the taxable income of the custodial parent.

STUDENTS

Full-time tertiary students without children would receive the same as similarly placed unemployed people - $6,000 per annum - or $10,000 if pensioners. One possible innovation would be to grant pensioner status to students with proven academic success. That would be equivalent to an "A bursary". Such undergraduate students would be expected to work as research assistants within their universities, repaying part of their extra allowance through a 62% effective tax rate.

THE AGE OF AUTOMATIC ENTITLEMENT TO A PENSION

While the proposal should initially be costed with 60 as being the pensionable age, automatic entitlement to pensioner status could commence at age 40. This would reflect the fact that 40 is now the age that many employers, when hiring, regard as too old. Pensioner status would confer dignity on older unemployed people, and give them more alternatives about how to run the rest of their lives. The average wage/salary of people over 40 is likely to be well above the national average of about $29,000, so probably over half of the people aged between 40 and 60 would not become pensioners, and would pay more tax on their present incomes.

Two 40 year-olds without dependents living together, could collect a total of $20,000 without working. This is not a lot of money, bearing in mind that, when both are working, that couple could expect to be receiving over $50,000 net. The consequences of unemployment can be much more severe for people in middle-age than for people in their twenties, because they will have typically taken on more financial commitments. The benefit levels proposed are sufficiently low to not discourage many people from working.

There are important economic advantages as well, in having a pension entitlement at 40. While pensioner status would not be attractive to people who are fully satisfied with their careers, it would constitute a way out for the many people of middle age who are becoming aware that they need a career change if they are to best use their acquired skills to their own and their society's long term advantage. The era in which people were expected to follow a single career is already over, yet present policies make it very difficult for middle-aged people to retrain, to gain the educational skills needed to complement skills acquired in early adulthood. For some, a career switch would mean starting new businesses and becoming employers. As children grow up, marriages can become business partnerships. The pension would become an effective source of capital, a means of buying time, of helping to maintain fledgling entrepreneurs until their enterprises start to yield an adequate return. Entitlement to a pension would thus reduce the downside of entrepreneurial risk-taking, giving those who try to make it on their own a soft-landing if they don't succeed the first time. When successful, such people would not remain pensioners, and they might never again need to become pensioners, because their businesses would remain their sources of income.

Another way of regarding a pension for people aged 40-60 is to see it as a scholarship or fellowship. As such, it would be clearly seen as a form of human investment, available on application. Recipients could be asked to state what they plan to use the money for. Examples might vary from the need to support teenage children, to attending university, to devoting time to a political organisation that attracts little corporate funding, or to writing a novel.

The entitlement could perhaps be abused by "subsidised surfers" (to use a recent expression of the Minister of Finance) who have no intention of making any contribution to their society. But a benefit of between $0 and $4,000 per year is not going to excite the dishonest any more than do present benefits, and the incentive to not declare private income would be lower than for today's beneficiaries. I think that we have to assume - as they do in Sweden[5] - that universal benefits are not generally abused. They convey an element of mutual trust that underpins most social and economic life. Most people want to make a contribution to the welfare of others. The evidence of New Zealanders' willingness to make charitable donations is testament to that view.

Being eligible for a pension at 40 would open up the career options for women. One popular strategy might be for a woman to develop a professional career as a salary earner until her early 30s, then to have her family. About when her last child starts school, she would become a pensioner for a few years while developing business and technical skills at an educational institution, and while retaining the time flexibility to cope with school-age children.[6] She might subsequently work on a free-lance basis.

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5 According to Gosta Esping-Andersen, keynote speaker at *Policy for our Times, an International Conference on Policy Options for the 1990s* sponsored by the social policy research centre at Massey University (July 17-19, 1991), Swedish adults can claim benefits virtually on demand.

6 It should also be noted that women in the 40-60 age range often find themselves having to cope with the special needs of elderly parents. The availability of a pension at age 40 would make it easier for them to cope, saving resources in the public health system.

People who move out of unsatisfying jobs at age 40 make way for younger people to become employed. One of the great tragedies of New Zealand at present is the large number of young people who have become virtually unemployable because their society has been reluctant to provide opportunities for them at the critical time of their graduation into adulthood; a time when they should be becoming economically independent and their society should be actively soliciting their contribution.

Another advantage of having pension eligibility at 40 is that it discourages people from thinking of 60 or 65 as an automatic retiring age. There would no longer be a sharp division by age of who is in the workforce and who is not. Some people receiving pensions while in their 40s would not receive a pension again until well into their 70s. Indeed, it is possible that pension eligibility at age 40 would eventually place less pressure on public finances than at age 60. A few years of pensioner status while in middle-age would facilitate a career progression from wage earner to entrepreneur and eventually to *rentier*.[7]

Finally, it should be noted that at times of high unemployment, when many more people than usual can expect to be seeking pensions, it is quite appropriate for these "scholarships" to be funded through increased government deficit financing, just as state housing and works schemes were funded in New Zealand in the 1930s. Genuine investment expenditure - whether public or private investment - can legitimately be financed through monetary expansion. By taking this expansionary approach, the universal basic income could be introduced today at a lower tax rate; eg rates of 46% and 60% for pensioners would add $1,000 million to the deficit.

EFFECTS ON LABOUR SUPPLY

In the short term, the introduction of a universal basic income would be likely to see an increase in labour supply as people now on benefits (excluding GRI) and parents with partners who receive the GMFI would find their effective marginal tax rate halved. They would largely seek the kind of part-time or temporary employment which today's economy is providing relatively more of. Such jobs may have quite low implicit hourly wage rates but would be attractive if they provided non-remunerative (including altruistic) benefits. Many mothers, at present in part-time work, pay effective marginal tax rates of 46 or 58%, so their labour supply would be largely unaffected. It is also true that many sole parents choose to work at present rather than become beneficiaries. They work despite implicit tax rates in excess of 62%.

People on higher incomes would experience a reversal of the effects faced in 1988. A higher marginal tax rate favours a reduction in their labour supply, but a higher average tax rate induces an *income effect* which encourages them to raise their work effort.

In the long term, increases in overall economic wellbeing could occur through normal economic growth - increased *per capita* incomes and consumption - or through reduced labour supply. With historical rates of productivity growth being about 2% *per annum*, we could each consume 2% more each year, or each reduce our work effort by 2%. The present system seems to have has a bias towards increased output rather than leisure; the length of a

7 A *rentier* is a person self-sufficient on investment income, including rents. An established example of such progression is from farm worker to sharemilker, to farm owner in partnership with a younger sharemilker.

full-time work week remains at 40 hours, the same as in the 1930s. With a universal basic income, many people may find it easier to negotiate employment contracts favouring flexibility over security. If that flexibility leads to a big reduction in the length of the average working week and negative economic growth it need not be a problem; it would simply be an expression in favour of preference for leisure or non-market work at the income margin. The real value of the tax credit would fall in line with falling average incomes. The UBI doesn't guarantee a "green" future, but it does at least make such a future possible.

NOTE ON OVERALL COSTING OF THE PROPOSALS

There are two ways to check the overall financial viability of the proposed universal basic income. The first is by comparing different categories of the adult population under the present and proposed systems (assuming a pensionable age of 60, and assuming nobody changes their circumstances); the second through recourse to the 1991 budget for an estimate of the tax base and existing income maintenance costs.

The population can be classed into five overlapping categories; workforce participants, two-parent families with children, retired people, students, and beneficiaries. Under my proposals, about 60-65% of two-parent families with children would be better off. Of remaining employed people, the clear majority earn over $24,000 so perhaps only 35-40% would become better off. Pensioners would on average be about as well off than under the present GRI, as would students who would pay more tax on earnings than at present. People receiving unemployment, domestic purposes, sickness and widow's benefits would mostly become less well off, but those on invalid's benefits would become better off.

Turning to the aggregate approach, New Zealand has about 2.5 million adults, 30% of which might be classed as pensioners. If each abated pension averages $2,000 then the average tax credit for all adults would be $6,600. That comes to $16,500m. In the 1991-92 estimates, $20,000m is required for non-benefit expenditure; about $12,750m to be funded by sources of revenue (including borrowing) other than income tax. Savings in student allowances and administrative costs would bring this down to $19,750m. That means that $23,500 is required from income taxation, including company tax. The 1991 Budget estimates the income tax base to be $51,500m for 1991-92, including $8,330m of company income. Employees' wages would be taxed at 48%, yielding $15,500m. Tax on interest and dividends should yield $1,250m, with the $1,000 personal exemption negating the impact of the higher 48% rate. Self-employment income and fringe benefits would yield $3,000m. Company tax, set at slightly less than the personal rate (45%) to encourage investment, would bring in $3,750m.

Paying pensions on demand to 40-60 year-olds should add about 200,000 to the number of pensioners, which, at $2,00 each, would raise the amount of revenue required by $400m. This could be financed by additional spending resulting from increased consumer confidence - eg from increased money in the hands of modest-income families - which would, among other things, raise GST receipts and the profits of State Owned Enterprises.

Table 5 compares the existing budget estimates with those that could be expected to prevail under a universal basic income with 60 as the pensionable age. Note that about 1.25

million New Zealanders would not actually receive the UBI, because it would be deducted from PAYE or provisional tax payments. Thus, both the tax take as estimated above and the required revenue should each be adjusted downwards (column 2 of Table 5) by $7,500 million, leaving net government expenditure and income a little lower than in the present budget estimates. The net result would be an income tax base of $51,500m taxed at 31%.

TABLE 5: BUDGET ESTIMATES FOR 1991-92

$ million	with UBI (gross)	with UBI (net)	at present
Govt. Expenditure	36,250	28,750	29,250
benefits / UBI	16,500	9,000	9,250
other	19,750	19,750	20,000
Govt. Revenue	35,000	27,500	28,000
PAYE	15,500	9,000	10,000
other personal tax	3,000	2,000	3,000
company tax	3,750	3,750	2,250
interest/dividend tax	1,250	1,250	1,250
total income tax	23,500	16,000	16,500
other revenue, incl. GST	11,500	11,500	11,500

A cut in the proposed tax rate to 46% - the current marginal tax rate faced by modest income families - would provide additional stimulus to the economy by adding $1,000m to the estimated budget deficit of $1,250m.

C. SUMMARY

The welfare state is not about transferring resources between generations; it is about providing all individuals with an adequate share of a nation’s income, and about investing in future economic growth. If wider socio-economic factors mean that some generations prove to be more fortunate than others then so be it. Their greater fortune means they have less need to make claims on the component of the welfare state that is causing problems with the government's budget at present; the safety net function. And their greater fortune makes it possible for them to make a greater contribution to the welfare pool through progressive taxation.

All four basic features of the welfare state are essentially forms of cost saving. The costs of not insuring against misfortune, of allowing recessions to become depressions, of not investing in people, or of not allowing retired or incapacitated people to fully share in society’s collective well-being are prohibitive but unquantifiable.

The provision of a universal basic income financed by a moderately high flat tax is an effective means of distributing incomes in a modern industrialised society. Effective marginal tax rates are made constant across the income spectrum, at the same rate that prevailed in 1987. The UBI acts as a tax rebate to employed people, making the tax scale progressive. For other adults it acts as a benefit; a kind of benefit which does not distinguish between the deserving and the undeserving. The system advocated is a logical extension of welfare provisions introduced in the 1970s, 1980s and 1990: national superannuation as originally conceived, family support, and the generic "universal" benefit. The continuation of welfare reform in this direction was fatally compromised by the introduction and subsequent non-negotiability of the low 33% tax rate for higher income recipients; a rate which made targeting necessary.

The universal basic income is fair, it is administratively efficient, it encourages enterprise, freedom of choice, and personal responsibility. It is an old idea whose time has arrived.

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