Submission on

NZ Productivity Commission

Interim Report

A fair chance for all

Breaking the cycle of persistent disadvantage

Submission by:

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Prologue

Once upon a time there was a country whose noble Ruler wanted only the best for their subjects, especially the poorest and neediest ones. The Ruler was in possession of a large stock of gold coins to give out, but unfortunately both Ruler and coins were located a long way away from the citizenry at large.

Thus, the coins needed to be transported by a rather large army of the Ruler's retainers, called civils, through an expanse of difficult country known as Bureau Bog. And throughout the long journey, the civils would be assailed by hordes of holders-of-stakes, each waving their stake threateningly or beguilingly in efforts to distract and influence the civils to hand over gold to them or to their favoured group.

The ardours and expenses of the trek through Bureau Bog were such that one gold coin in three never made it through to the citizens, and it was not clear that those who were lucky were always the needy ones; nor that there were none of the truly needy missing out getting any gold at all, nor that neediness was not actually encouraged by the prospect of thereby procuring pieces of gold.

The good-hearted Ruler was worried about the state of affairs and called on a wise old savant called Ec to give counsel. The Ruler explained: 'You see I have this unusual problem – the gold just floods in to my vaults; more and more each year -- I don't know why -- but I have the devilish difficulty in disposing of it, given that, as you know, I am not one of those despicable Rulers who like to siphon off gold for their own venal benefit.

'No you aren't, Excellency, thank goodness,' says Ec, 'But you do know where your gold comes from, don't you?'

'Isn't it from "taxes"?' the Ruler suggests.

'Yes it is, Excellency' agrees Ec. 'So you tithe your subjects for gold and then give it back to them, though rather depleted by the rigours of crossing Bureau Bog.'

The Ruler's eyes light up as though experiencing an epiphany. 'So I could simply cut the income tax rate and not send out the gold at all! What a brilliant idea one has just had!'

Ec coughs apologetically: 'A very brilliant idea, Excellency, but there is a small catch. You are most concerned with the lot of the poorest and neediest of your subjects, is that not so?'

'Absolutely that is so,' says the Ruler, now looking very solemn and sincere. 'Oh, I do see the problem. Most of the income tax is paid by the people with the largest incomes – the ones I least need to help. But isn't there a tax that everyone pays and so all would benefit if I cut it? What about the 'GST' – the Goods & Services Tax – even I have to pay that, don't I, and so too do my poorest subjects?'

‘True, Excellency,’ replies Ec. ‘But we have still the same difficulty: the rich spend the most and so would capture most of the benefit from eliminating GST.’

The Ruler looks wistful. ‘If only there was a way we could give all my subjects the same benefit. I know that wouldn’t solve everybody’s problems but it absolutely would be better overall than the present system, wouldn’t it?’

‘Another brilliant idea from you, Excellency,’ says Ec. *Equal* benefits is, hmm, absolutely the key here. You see, there is a wonderful new invention that you should know about: it’s called “Internet banking”. It does away with gold completely. You just need to press a button on the computer and the money flows instantly into everyone’s bank accounts! And because everyone gets the same, what that same amount is the single thing you need to decide on.’

The Ruler risks showing some excitement. ‘So we could forget about having to battle across Bureau Bog, and all those civils could be released to find more socially useful employment, and so too all those pesky holders-of-stakes. Brilliant!’

‘Brilliant, brilliant!’ agrees Ec. ‘And Excellency will be pleased to learn that we have already taken the liberty of trying out the system on some of your more expendable subjects: the oldsters. It’s how we’ve been giving them their pension. And it works perfectly. No fuss at all, and no complaints.’

‘No complaints…’, says the Ruler, rather wistfully. ‘Well, I shouldn’t really say this, but if the boomers can handle it, then surely so can Gen X and so on. But can I really afford to give everyone a benefit?

‘Excellency,’ responds Ec, ‘So costly and wasteful is the present system, that eliminating it would pay for a universal benefit of one thousand dollars a month to every adult citizen of our country with no increase in taxation.’

So the Ruler implemented the Universal Basic Income, and everyone lived happily ever after.

Disclaimer: this fable is fictional. Any resemblance to actual living people and events is purely wishful thinking.

The present welfare system and the Productivity Commission's proposal.

As a preamble, my view of the Productivity Commission's *Interim Report* is that it certainly is well-meaning, and that, within its conceptual limits, it is well written, well drafted and well organised (but not quite so well researched). However, those conceptual limits are serious, and as such damaging to the usefulness of the document in providing guidance to government in the important matter of 'breaking the cycle of persistent disadvantage'.

Our present system

In New Zealand, as in other 'welfare states', the central government spends large sums of taxpayers' money on what are called social welfare programs: hospitals, schools, and cash payments not for service -- these often known as 'benefits' or, more generally, 'transfer payments'.

How large? I will use data for the 2017 fiscal year. Why? Because in this year total central government expenditure totalled almost exactly $100 billion [GDP was $270 billion], so that figures for any particular expense item can be simply read off as a percentage of the total.

(In 2022 or 2023, all the numbers are, or will be, considerably larger, due to economic 'growth', inflation, demographic changes, and, currently, special Covid-related expenditure.)

By 'functional classification', the social welfare budget was about $30 billion, and health and education expenditure each around half that amount. 'Economic and industrial services' had a budget of $7.5 billion – much, perhaps most, of this was 'corporate welfare' – handouts of free or subsidised services or actual cash grants to the private sector. Sundry other transfer payments -- perhaps a billion or two – are buried in other classified expenses.

The processes of getting money from the taxpayer to the beneficiary (sometimes the same person) can be complex and unwieldy. Decisions to spend made at the Cabinet or Ministerial level work their way down through the civil service departments to eventually be implemented by front line staff, these mostly (but not all) in the Ministry of Social Development (MSD) in the case of personal transfers, and the Ministry of Business, Innovation and Enterprise (MBIE) and other agencies for transfers to companies and corporate entities.

In only one major case is money handed out automatically, with no strings attached (including no means-testing). This is the pension paid to citizens over the age of 64 – 'NZ Superannuation' – which is by far the largest single transfer payment, at around $13 billion in total, in 2017. Other programs require qualification checks before and during periods of payments, including means testing, and often the acceptance by the beneficiary of helpful advice from civil servants or designated community 'providers'.

The Commission's proposal

The essence of the Productivity Commission's *Interim Report's* recommendations is that these processes be made yet more complex and unwieldy, in two main dimensions.

First, the Commission criticises what they call the 'silo mentality' restricting the design and delivery of social services. Specialists in healthcare, education, social services, housing and so on devise and direct policies and programs in their own field of expertise with no (or little) attempt to coordinate policies and programs with those being operated within the other silos.

The Commission repeats some anecdotes or stories about lack of coordination between front-line welfare agencies[1], but does not give any evidence at all that silos at a higher level are in fact a problem; nor any cohesive plan for eliminating them with their proposed 'systems' approach.

I suggest that the latter (cohesive plan) is unnecessary (which is a relief, because it would be diabolically difficult to specify and implement), because there is not in fact a first-order problem generated by siloed decision-making, for a reason that the Commission would recognise: namely that there are in general positive spillovers between the good effects of siloed policies and programs, such that a desirable outcome in one silo is likely to be beneficial, not harmful, for outcomes generated in neighbouring silos.

In other policy fields this may not always be the case. For example, a policy to change the speed limit will have opposing effects on two worthy social goals: road safety and travel time. But a policy, say, that improves housing conditions (dryer, warmer) will have health benefits, which will have benefits for student performance in school, which will have benefits for incomes and other desirable outcomes in later life, which will enable people to further improve their housing, and so on.

It could be an interesting policy research exercise to try to pin down the size of these positive spill-overs, which could assist in prioritising expenditures between the different activities, and it might well turn out that the direct income transfers that I will recommend in this Submission would do very well in such an exercise, but, as far as I am aware, we do not yet have such research to guide us.

The second accretion of complexity proposed by the Commission is in essence to add a whole new layer of intermediaries between the government and the beneficiaries of social welfare policies and programs: these being various 'community' organisations

[1] For example, the Commission (page 63) quotes a School Principal: 'Those families have sometimes got seven, eight agencies involved independently. There's no collaboration. There's a big gap, it's very siloed'. It would be unreasonable to expect the Commission to have exercised due diligence in checking out all the submissions and claims that it has received or referenced, but perhaps notes of scepticism here and there would be appropriate.

or other ‘stakeholders’ -- many of whom made submissions to the Commission, and were generous with their advice and offers to help spend the taxpayers’ funds.

‘Communities’ are of course of immense social and cultural importance, including their importance in providing informal care and oversight to individuals and families. But administrative capacity and political legitimacy in Aotearoa NZ at the sub-local authority level is very sketchy – some lightly-elected local boards or ward committees -- and quite probably should remain so.

Political, moral, social, philosophical justifications for the involvement of community-level intermediaries in the distribution of large sums of public funds are not documented in the Commission’s *Interim Report*; nor do we get anything like a blueprint, or even just a set of principles, that could in general guide the involvement of third parties in transactions between our government and the citizens who elect it.

The Commission in its Table 5.2 (page 64) lists as one of the ‘Constraints (symptoms)’ of ‘Risk aversion and power imbalances constrain[ing] the breakdown of government silos’:

> Government reluctance to genuinely decentralise funding and decision making to communities

I applaud government’s reluctance here, and hope it remains staunch in this matter.

I do also applaud the Commission’s criticisms, on page 63 and elsewhere, of the evil effects of the neoliberal (my choice of word) ‘New Public Management’ imposition in the 1980s and 90s of ‘Key Performance Indicator’ (KPI) oversight of managers in the public sector. However, restoring trust in the people who lead our ministries and departments does not in itself justify hopes that these leaders be more ‘collaborative’ with each other. The negative metaphor of ‘silos’ could, in my view, be better replaced by the positive metaphors of ‘sticking to your knitting’, or ‘doing good where you know what you are doing’.

So, no change, please? Not at all. Indeed, in its proposal that agency in social welfare policy be somehow extended to ‘communities’, the Commission gets tantalisingly close to making a conceptual breakthrough that would completely upset the status quo. Why stop with communities? Why go there at all? Why not bypass communities and give agency in this matter *directly* to the individuals and families who are – as we all agree, don’t we? – the sole legitimate ultimate beneficiaries of public social welfare policies and programs? Give the money to the people, with no qualifying conditions and helpful administrative guidance, and trust them to make what use of it they will.

So where do I spot an inkling of this idea in the *Interim Report*? In just two passages.

> The welfare reforms of the early 1990s and mid-2010s in Aotearoa New Zealand provide an example of how government became more paternalistic. In

> the 1980s, it was assumed that beneficiaries would behave in a way conducive to bettering their own lives. By the mid-2010s, these assumptions had changed to reflect a more paternalistic system of welfare that was underpinned by the following assumptions: the poor were incompetent and suffered from behavioural deficiencies… and people were to be case managed in the welfare system through a mix of help and hassle to find work. (page73)

Whether or not this passage is historically accurate, it does seem to imply a willingness by the Commission to entertain the idea that beneficiaries could indeed be trusted to act competently in their own best interests, even if this is in contradiction to their murmurings about allowing 'communities' to decide on those interests.

The second potentially supportive passage is with reference to devolution of beneficiary spending decisions:

> Evidence from Fry (2022) demonstrates that persistent disadvantage is often more responsive to devolved services. Devolution is a continuum from individuals being budget-holders with the flexibility to purchases the services they consider will best meet their needs *from a pre-approved list* [emphasis added]…through to the "navigator" approach recommended in the 'More effective social services' report (NZPC, 2015), to central government entering into contracts with providers to achieve specified outcomes for a set fee (which is the main approach to commissioning services at the moment). (page 100)

So just drop the 'pre-approved list' and give individuals full discretion in their spending choices.

Now, this could seem like "Welfare State-Lite", with all or most of the existing benefits and transfer payments remaining in place – in their silos, if you will -- but with simplified and streamlined access to and use of them. But I will now suggest that the logic behind devolution leads naturally to universalism: to extending similar, non-conditional (in particular, not means-tested) access to cash benefits to all adult citizens. Full devolution; full freedom must mean dismantling the 'paternalistic' welfare state structures and institutions that have been making the choices and imposing the limitations on access to and use of public funds.

In more familiar terms: why should only old people get state superannuation (universal; not means-tested, in NZ)? Simplify and extend the pension to all adults in good standing, and let them get on with it.

The birth and bloat of the Welfare State

The social and political system we call the Welfare State has, to put it politely, somewhat outgrown its origins in New Zealand and Britain. Those origins were indeed a legitimate – even, rather splendid – response to the conditions of their time -

- after forty years of World Wars and economic slump -- but those times have fundamentally changed, even as the Welfare State has remorselessly expanded; becoming by now a hugely expensive anomaly.

Three generations down the line, the welfare state has lost its simple purity. It began as a universal safety net – really a national insurance system. It was intended to be available to everyone, but used only by the unlucky few in destitution or sickness. Now it is not just insurance against exceptional misfortune. In the 2013 NZ Census, more than one million benefits were received, by the 3.1 million reporting respondents over the age of 15 – a lot more than needed just for people *in extremis*.[2] For a huge number, being a beneficiary has become – whether wished for or not – a way of life.

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By July 1945, when Clement Attlee's Labour party swept into power in Britain, two successive generations of young men had been decimated by war and demoralised by economic depression. The survivors of 1914-18 had, in Britain, come home as hopeful heroes to a bleak economic landscape of almost instant mass unemployment. In America and New Zealand and other countries, the 1920s were a decade of brittle boom, to implode spectacularly in the 1929 Wall Street stock market collapse, triggering a decade of Economic Depression around the world. In this setting, Hitler had fanned the flames of Fascism and provoked the second cataclysm. It must not happen again. What to do? To many intellectuals and politicians, it seemed that the logical -- perhaps inevitable – path to the future lay with socialism. The most successful economy in the middle third of the twentieth century, in seemingly sharp contrast to the ineptitude of the capitalist democracies, was a socialist dictatorship – Soviet Russia. Russia had industrialised its economy and sailed through the 1930s without a Depression, and, of course, had made a huge and heroic contribution to beating Hitler.

The English economists John Maynard Keynes and William Beveridge wanted to save what they called liberal capitalism from socialism, but they recognised that compromise was needed. The state was the only institution capable of effectively intervening against the obvious and abject failures of laissez-faire market economics. Keynes himself had provided a big part of the remedy with what would come to be called Keynesian stabilisation policy -- using the spending and taxing power of central government to lean against the apparently incorrigible inconstancy of private sector investment and spending. And just stabilising paid employment at a high level would in itself make a huge contribution to abolishing want.

But, by 1946, Keynes was dead and his policies as yet unproven in peacetime. The risks of market life were still there. Beveridge and Attlee wanted to do more. Really, what they wanted was what New Zealand had done eight years earlier, in 1938, when

[2] The percentage of benefits to total population was 37%, but this does over-estimate the proportion of the adult population receiving benefits, because some tap into more than one benefit source.

the First Labour Government under its legendary leader Michael Joseph Savage (1872-1940) inaugurated the world's first full Welfare State, with comprehensive unemployment benefits, universal free health care, universal superannuation and a state housing program, supplementing free universal education legislation dating back to 1877, and of course the world's first extension of the vote to women, in 1893.

So, if we ask: were the welfare states as put in place three quarters of a century ago properly designed for the conditions of their day: I think the answer is that yes, they were. Those were in reaction to terribly troubled times of war and economic Depression. There was mass fear, worry, material want, misery. How bad was it? William Beveridge in his *Full Employment in a Free Society* (1944) passes on many affecting stories of distressed social conditions and personal demoralisation in Britain in the slump of the 1930s. Here is one of the lighter ones:

> One young mother told how, when her husband got the offer of a job, she had immediately to go and get him a pair of heavy working boots and pay them up by instalments. He thought the job would last at least a fortnight, and with two week's pay she could manage to pay them up in full. The job lasted four days. It took her many weeks to return to her planned budget. (p246)

If the definition of a bourgeois is "He who has reserves", then after a decade of Depression many middle class people were in danger of falling out of the bourgeoisie, and most working class folk never had reserves to start with, even to buy a pair of work boots.

The War gave everybody a paid job and actually demonstrated in fact the truth of Keynes' theory. Thanks, Herr Hitler! But the generation who rebuilt the world after 1945 -- the parents of my baby boomer generation – had grown up in the slump and survived total war. They wanted above all security for themselves and their children. And so they created the Welfare State, and good for them.

But we should not shy away from the good news: the bad stuff feared by Attlee and Beveridge, and Savage and his Finance Minister Walter Nash, didn't actually happen. The Social Insurance policy never had to pay out. Largely due to the success of the inter- and intra-national coordination of economic policies planned by Keynes, the first thirty or so years – from the 1940s to the 1970s was a period – throughout the Western world – of unprecedented economic growth and prosperity.

So, the NZ Official Year-Book for 1951-52 reports (page 868):

> The number of disengaged [unemployed and seeking work] persons still enrolled for placement by the National Employment Service reached its lowest level (12) at the end of March, 1951. It has usually been found that a considerable proportion of those concerned [*five? seven?*] were suffering from some form of disability, making placement in suitable employment a matter of some difficulty

And we had what informally was termed 'the wage earner's welfare state':

> The basic wage for adult male workers is required to be fixed at a weekly sum which will, in the opinion of the [Arbitration] Court, be sufficient to maintain a man, wife, and three children in a fair and reasonable state of comfort.' (*ibid, page 822)*

So, shouldn't the official Welfare State have withered away for lack of use – at least with respect to transfer payments to working-age adults? Well, it didn't.

In New Zealand in September 2022, with a total population three times larger than in 1951, there were 170,037 people receiving job-seeker benefits, of whom 98,934 were 'work ready' and 71,103 had a 'health condition or disability' issue – the latter still a 'considerable proportion' of a now vastly larger number of unemployed workers. Overall, after adjusting for inflation, I calculate that the cost of our welfare state now, per person, is around five to six times higher in 2022 than in 1952.

The great growth period for targeted transfers in New Zealand was the quarter century from 1975 to the millennium. Over this time, the numbers of people on invalid benefits increased from about 10,000 to more than 50,000; on sickness benefits from 5,000 to 30,000. Were people sicker or more indisposed than before? Probably not. Numbers receiving the domestic purposes benefit shot up from a few thousand to more than one hundred thousand. Were more women having babies outside of relationships, or in relationships that didn't last? Quite possibly, yes, for various reasons, including the availability of the DPB.

What happened? In the nature of things, it is easy to see how it could get out of hand. You've got these gigantic, swelling torrents of cash pouring into the public coffers with little fuss or effort – what could be more natural than that the governments of the day should assume it to be their right, or even their duty, to find things to spend the money on, rather than consider the possibility that some of the money might better be returned to private households. And then, on the expenditure side of the ledger, the great bulk of the 40 percent of national income reallocated by the state is simply given away for nothing: on services such as free education and free hospitals, and on transfer payments such as pensions and benefits for which no useful work is required in return. Of course when it doesn't cost you anything you are going to be putting pressure on politicians to supply more free stuff and more free money.

Basically, targeted benefits are paying people to not deal with whatever problem the benefit is targeted at – or to not avoid developing the problem in the first place – with this disincentive intensified by the poverty trap clawing back of the benefit when the beneficiary finds paid work.

So it surely is reasonable to take a critical, open-minded look at the system. Put it this way: if we were starting in the third decade of the 21st Century with a clean sheet of paper, would we -- people of goodwill and sensibility – *want* to design a welfare state just as we have inherited from our parents and grandparents?

Costing the modern Welfare State

In the 2017 NZ Budget, there were 82 separate rows of social assistance and related payments, ranging from $13 billion for National Super down to $3,000 for 'Transitional Assistance'. The total paid out was $26.2 billion[3]. Add in other transfers, including $1.5 billion in net student loans paid out, and around $8.5 billion in another lolly-scramble of handouts to business (businesses are by far the largest beneficiary class by total payments, after pensioners). Include the above-the-line administration costs – salaries etc of civil servants and subcontractors: at least $3 billion/year. Subtract income tax paid by superannuitants who work[4] and add in what might be a similar amount that would be paid if beneficiaries were in paid employment.

And there's more! The superstar Harvard lawyer Cass Sunstein -- co-inventor with the Nobel-winning behavioural economist Richard Thaler of the 'nudge' – has come up with 'sludge' as a name for the paperwork and other chores that a would-be beneficiary has to trudge through on their path to securing their entitlement to social security payments under the present system. Sunstein tells us[5] that the number of hours put in filling in forms, etc, just for Federal government programs in the US, added up in 2015 to nearly 10 billion, valued at more than $US250 billion in peoples' time. If New Zealand is similar, our beneficiaries put in about $2 billion worth of tedious effort each year to establish that they are entitled to what they are indeed entitled too. On top of this are the psychological costs (worry, frustration, perhaps stigma and humiliation), travel and other financial costs of applying, waiting in queues, and spending time sitting on the other side of all those civil servant's desks.

An absolutely inevitable consequence of all these transaction costs, as economists call them, is that alarmingly large numbers of income etc programs for the poor don't actually reach the poor – the sludge is too deep for them to wade through. Sunstein reports as typical, participation rates in the 30-60 per cent range, and even the well designed and highly user-friendly Earned Income Tax Credit (EITC) misses one in five of the people eligible to receive it –that's about 5 million missing families, in the US.[6]

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[3] Less than the $30 billion 'expenditure' figure mentioned above, because some expenditure is not paid out – it goes in administration costs,

[4] An undated printout in my files gives Statistics NZ as source of the figure that 24 percent of older people still work – up from just 9 percent 30 years ago.

[5] In his Review in the *New York Review of Books* (April 4, 2019) of *Administrative Burden: Policymaking by Other Means*, by Pamela Herd and Donald P. Moynihan (Russell Sage Foundation).

[6] Calsamiglia and Flamand, *( )*, pp 652-4, give a useful round-up of the international evidence on non-take-up of transfer payment benefits. Linos *et al.* (*American Economic Journal: Economic Policy,* 2022 14(4): 432-452 find experimentally that clever nudges are not able to affect take up of the EITC – not able to 'overcome the barriers faced by low-income households' in filing returns

Below-the-line costs are important and should be accounted for in social policy The great founder of economics, Adam Smith, gave guidance here nearly two and a half centuries ago, as part of the fourth of his elegant principles for the levying and collecting of taxes:

> [B]y subjecting the people to the frequent visits, and the odious examination of the tax-gatherers, it may expose them to much unnecessary trouble, vexation, and oppression, and though vexation is not, strictly speaking, expence, *it is certainly equivalent to the expence at which every man would be willing to redeem himself from it.* [emphasis added]

Smith's is probably the first, and possibly still the best exposition of the concept of willingness-to-pay for a non-marketed service (or to be free of the burden of this service)[7], which has become central to cost-benefit analysis and economic policy evaluation in general.

I have not found (and nor, apparently, have the Productivity Commission) evidence or research into the extent and magnitude of 'sludge' in New Zealand, but my intuition is that it would be reasonable to expect this to be at least of similar magnitude to the audited above-the-line administration costs of welfare transfer programs.

Policy admin costs are always a worry, though often neglected in political and other discourse. About one half of the $26 billion social security income transfer outlays is superannuation payments, which are very cheap to administer. When I applied for the pension all it took was a short meeting with a pleasant MSD employee, and the money has been coming in every fortnight ever since. So simple! This, of course, is because National Super is not means- or needs-tested, so after basic eligibility is easily established, you're in for the rest of your life.

So if the private plus public costs of administering the other $13 billion came to, say, $6 billion, then it is currently costing about 45 cents to deliver each dollar of transfers to beneficiaries. That is quite a lot! Not all of this is book-keeping costs – ascertaining and monitoring eligibility/applying for a benefit – but a lot of it is. Some is more pastoral --- assisting people to find jobs or deal with landlords. But even then the question must be: is pastoral care best dealt out by central government agencies, with their huge desk-bound staffs and superstructures of high-paid 'managers', or would, on balance, these matters be better handled by the people themselves, assisted where needed by the on-the-ground (voluntary) support of friends, family, whanau, charities and perhaps local authorities?[8] Financial support for community organisations would be 'bottom-up', rather than 'top-down'. Such is indeed how churches are financed.[9]

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[7] Adam Smith, An Inquiry into the Nature and Causes of the Wealth of Nations (1776): pp453-4 of Oxford World Classics Selected Edition, Kathryn Sutherland , editor, 1993

[8] As of course people do often rely on help from friends etc now. "Heard about it from a friend or relative" is a far more common explanation of how people find a new job than "The MSD found it for me".

[9] With the qualification that churches are (why?) tax-exempt, so there is indeed top-down support for organised religion by the tax payer.

So let us ask: if we eliminated the whole present social welfare system, how much money would thereby be liberated to fund its replacement? A quite conservative tally would give us a total of $40 billion (in 2017) to spend elsewhere. What could we buy with this?

The UBI (Universal Basic Income/Trust Dividend Alternative

The proposal for a general transfer payment -- to young and old – is usually now labelled the 'Universal Basic Income', or UBI, though I will later rename it the 'Trust Dividend', because I see it, not as a transfer payment, but as a just return for living as a trustworthy citizen in society. The UBI idea has been around for a very long time, and gets support from both the Right and the Left, politically -- even, from the extremes of Right and Left.[10] It seems always on the threshold of breaking through into practical politics, but the day of 'free' money never quite arrives. Perhaps its bi-partisan appeal is actually the problem: Party Y mistrusts a policy approved of by Party X, and vice versa.

Could it be done? Should it? Take the 'could' first. The key to a fiscally manageable UBI is that it must be not enough. That is, not enough to live comfortably on, by itself. Let us take a figure that has been often suggested by its more practical enthusiasts, which is about $400, tax-free, per fortnight, or about $10,000/year (perhaps $450/fortnight or around $12,000/year in 2023). Limit access to adults – say, eighteen years or older, and apply the same number to the required minimum number of years of tax residency (cumulative, not necessarily continuous) in New Zealand[11], and require too that you be a permanent tax resident in this country (whether or not you are actually currently paying taxes – you might be full-time having babies or bringing up children, or retired). I've done the sums (for 2017) and I calculate that about 3 million of our then 4.8 million residents would qualify for the Trust Dividend on this basis. That's $30 billion a year. And where can we find $30 billion lying around? Well, we found it in the previous section – actually about $40 billion to be saved by slashing the expensive tangle of transfers to businesses, households, individuals and the civil servants doling out the funds. There's enough and probably more to replace the 82 line budget items, etc, with a single, universal, untaxed, non-means-tested or need-tested basic income or trust dividend.[12]

It still doesn't seem to add up, though. In March, 2018 there were about 750,000 of us collecting Superannuation, at an annual average gross pay-out of a bit more than

[10] A good survey article is Caterina Calsamiglia and Sabine Flamand, 'A Review of Basic Income', *Journal of Economic Literature*, 57(3), September 2019, pp644-658.
[11] The current requirement to receive National Superannuation in NZ is just ten years of residency, which seems a bit too generous.
[12] Because old people who are still working pay income tax on their Superannuation benefit, the net fiscal cost to the government of replacing Super with an untaxed Trust Dividend would exceed current gross outlays.

$18,000 each, and 270,000 on one of the three 'main benefits' – unemployment, solo parent, living support --- receiving annual sums in the $14-19 thousand range. That's 'only' a million people – well short of the three million who would receive the UBI or Trust Dividend. Well, the difference is made up for in four parts: (1) $10,000 is less than what the main benefits pay out (though of course people would be getting it throughout their adult life, so much more in total); (2) there is about $3 billion in total doled out in smaller per person amounts for various special needs[13]; (3) huge amounts are gobbled up by businesses with their hands out for handouts, and (4) about $5-6 billion in administration cost, and sludge. So it does add up fiscally – quite easily.

What about the politics? The American's EITC is the successor to a more robust universal income program attempted in 1972 by Republican President Richard Nixon, an absolute policy wonk, whose economic views, John Lanchester writes[14], were 'closer to Alexandria Ocasio-Cortez than to those of today's Republican Party.' Nixon's proposal passed in Congress, but was rebuffed by the Democrat-controlled Senate. He lacked a Lyndon Johnson (with whom Nixon had been on generally good terms) to push it through.

Nixon was influenced by the conservative economist Milton Friedman's proposal for a negative income tax, which was supported by a 1968 petition signed by 1200 American economists of all political persuasions. Friedman, in his turn, was preceded on the Right by Friedrich Hayek – the neoliberals' hero -- who in the *The Road to Serfdom* firmly argued for the 'certainty of a given minimum of sustenance for all' as non-negotiable in a prosperous, civilised society.[15]

You might think that progressives on the Left would welcome the chance to make common cause on such a key issue, but, mostly, they don't. They are suspicious of a hidden agenda of neoliberals to destroy the welfare state, even though no-one at all is proposing dismantling its other two pillars: free schools and free hospitals -- are they?

Some on the extreme left go for what John Lanchester calls a 'full-fat' UBI, simply added on to all the existing means-tested benefits. Of course this would require substantial additional taxes, for which left-wing folk are only too happy to come up with schemes: closing tax loopholes, limiting allowable deductions, raising the income tax rate for the very rich, and so on.

Well, maybe such taxes are a good idea in themselves, though I am with Keynes in the camp that believes that the overall tax burden needs to be reduced, not increased – even if I am realistic, and expect Keynes would be too, if we had a chance to explain it

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[13] And many beneficiaries aren't on the books for a full year – for example, unemployed people mostly find another job within twelve months.

[14] In his excellent and well referenced survey essay on the UBI: 'Good New Idea'; in the *London Review of Books*, Vol 41 No.14, 18 July 2019. Lanchester writes that the Left are desperately short of a new idea, and that the UBI is the only candidate so far to surface.

[15] Frederick A. Hayek, *The Road to Serfdom*, University of Chicago Press, 1st US edition, 1944, page 120. For an ecumenical essay on Hayek, read Bruce Caldwell, '*The Road to Serfdom* after 75 years', *Journal of Economic Literature*, September 2020, 58(3), 720-48.

to him, that, given especially the seemingly inexorable inflation in healthcare costs, there is no desirable way to reduce the government's share of GDP to the 20 percent or so last observed in the 1960s. However, I do believe – on the numbers given above – that our tattered and piecemeal package of targeted and means-tested social security programs could be replaced by a Universal Basic Income at, if anything, a somewhat lower total cost to the taxpayers.

But *should* it? What is so great about a UBI? Quite a lot. There's no social stigma attached, because everybody gets it. There's no humiliating and time wasting 'sludge' of interviews and monitoring by officials -- if you pass the eighteen years residency threshold, you are automatically enrolled, and so long as you stay out of jail, don't join a criminal organisation and don't fall behind on your childcare payments, you will be enrolled forever.

Some people worry that a fiscally responsible UBI is, indeed, 'not enough'. Most households will need to supplement it with wage income, most of the time. Well, I am fine with that. If your household plans to get through its days and years without ever sending someone out into the working world to reciprocate all the work other people are doing to feed, clothe and shelter you – ok, you might get away with it, but we should not run a hugely expensive welfare state system to enable you to do so

Others have the opposite concern: that the UBI will dilute other peoples' incentives to work outside the home -- not that this is really any of their business. In any case, the Finnish and other pilot studies find that both paid and unpaid outside work is, if anything, encouraged by receiving a basic income – paid work in particular because the poverty trap is done away with – you don't lose part or all of the benefit if you take a job.

A particularly useful recent study – useful because it covers an entire political jurisdiction, not just an experimental sample – is of the impact of the 'Alaska Permanent Fund', which since 1982 has annually distributed natural resource revenues to every resident, amounting recently to around USD3,900 per family.[16] The researchers found a macroeconomic spending effect from the additional income. This would not be a factor in a NZ UBI which just transferred spending from other social welfare programs. At the microeconomic level, they found no significant decrease in people taking on paid jobs.

Perhaps best of all, having the UBI as an absolutely secure backstop takes a lot of bad risk out of life. An American survey by the Federal Reserve found that nearly one half of US households could not meet a sudden expense of just $400 – a car repair, replacing the broken fridge, a healthcare emergency, even, buying work boots and clothing -- without going into debt or selling assets – or simply going without, if they

[16] Damon Jones and Ioana Marinescu (2022), 'The Labor Market Impacts of Universal and Permanent Cash Transfers: Evidence from the Alaska Permanent Fund', *American Economic Journal: Economic Policy*, 14(2): 315-340.

had no assets or credit. With the UBI or Trust Dividend, even a single-adult household would never be more than fourteen days away from an automatic $400 plopping into their piggy bank; two adults never more than a week away.

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$400/fortnight may not seem like a lot of money. Well, it isn't. But, capitalise it. Absent the UBI, how large a lump sum would be needed to generate an income flow after tax of about $10,000/year? Lacking access to the preferential investment opportunities available to the wealthy, most of us just have to make do with the retail money market – 5% returns pre-tax is about the best we can hope for. So, depending on what income tax bracket you are in, we'd need to put aside around $250-300 thousand of capital to match the UBI in 2017: more now.

That is, the capital value of receiving the UBI is quite a tidy sum -- certainly more than the current net assets of most New Zealanders. And with assured steady access to this income stream people could turn down bad jobs; challenge bad employers; leave safe but boring jobs to retool to pursue some vocation they had always dreamed of; create a nest-egg for retirement or to fund a small start-up business. It's a basic risk-free asset that will free people to take other, creative, risks in their lives in the famous new gig economy. It will be a bulwark of personal and family economic autonomy.

Getting to the parts that other policies don't reach

Defenders of the myriad of targeted benefits that make up the old Welfare State tend to be worriers about the chronic losers in society -- those who are too weak, or sick, or disabled, or dim-witted to look after themselves, economically. At least now, they say, there is something to save the day for everyone whose misfortune is such that they cannot provide a decent market income for themselves or their children.

Well, yes, there is a saviour, on paper, if the benefits hit their target. But – due to 'sludge' and other factors, in practice a lot of people get missed, as noted above, in the US case. And even signed-up beneficiaries are hardly doing well financially, and are discouraged from doing better by the welfare trap of super-high marginal income taxes. After all, the premise -- which is quite well documented – of the Productivity Commission's Report is that there is indeed a problem --- a 'cycle of persistent disadvantage'.

The leading researcher into poverty in New Zealand is Bryan Perry, who produces regular reports into the incidence of poverty or 'material hardship' in New Zealand. Weighing up various measures, Perry found that, in 2008, 13% of New Zealanders could reasonably be said to be living in serious hardship, with incidence for older people particularly low (4%), and for children quite high (19%). Particularly high hardship rates were found in sole parent families (39%) -- ie families receiving the domestic purpose benefit, or eligible to do so -- and in beneficiary families with dependent children (50%), in contrast to working families with children (11%). The welfare state, sadly, never has succeeded in abolishing want in New Zealand.

While these numbers would probably be worse without the targeted benefits, they are still unacceptably high, and therefore there is a possibility that a quite different income support scheme such as a UBI would do better. In particular, we could see a sort of 1st World version of the 'demographic transition', whereby when girls and young women gain access to education and decent jobs they delay marriage and childbirth, with resulting boost to their own and their country's prosperity, and a reduction in material hardship. In NZ, the jobs for women are there – though these often relatively low-paid jobs – but the surety of receiving a UBI could encourage life-changing hopes and aspirations, transforming the futures of young people in general.

I and many others believe that the UBI is not just a cute little scheme for policy wonks, but really is *the* Big Idea of our age. It is key to reimagining the role of government and public policy in enabling the flourishing of responsible autonomy that the Millennial young, especially, yearn for and need, in our shifty, globalized world.

However, even though support is politically widespread, it is by no means unanimous amongst economists, including amongst the dissenters the MIT economist Daron Acemoglu, who is one of the three or four of my fellow economists -- along with Emmanuel Saez, and the great Joe Stiglitz and the great Angus Deaton – whose contributions as public intellectuals I value most. After calculating that funding a UBI in America on top of existing social programs would be hugely expensive (and it would), Acemoglu explodes:

> Sacrificing all other social programs for the sake of a UBI is a terrible idea. Such programs exist to address specific problems, such as the vulnerability of the elderly, children, and disabled people. Imagine living in a society where children still go hungry, and where those with severe health conditions are deprived of adequate care, because all the tax revenue has gone to sending monthly checks to every citizen, millionaires and billionaires included.[17]

I truly hate to resort to sarcasm in the presence of Daron Acemoglu – though could he himself actually be being sarcastic here? -- but the name of a country in which 'children still go hungry, and where those with severe health conditions are deprived of adequate care' is the United States of America, right here and now. And, Aotearoa New Zealand.

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[17] Daron Acemoglu, 'Why Universal Basic Income Is a Bad Idea', *Project Syndicate*, June 7, 2019. Acemoglu supports the related but fundamentally different 'Guaranteed Basic Income', to be paid in full only to people with no other income source, and reduced, eventually to zero, as the size of such other sources increases. Thus, this program suffers from the same welfare trap problem as do existing targeted benefits. The idea should be to encourage people to get good jobs, not to punish them for it.

Why we deserve it: the UBI as Trust Dividend

The second 'but' -- this usually from the Right side of the political spectrum – is: but why should *anyone* get 'something for nothing'? This seems to be an increasing concern of the Trumpists of America and the world – disaffected working class people whose resentments are directed not – surprisingly, to me – up at the rich, whom they rather admire for 'getting away with it', but sideways at the non-working poor: the beneficiary class. Having universality must take some of the sting out of this grudge, but it can still be held: *why don't they go out and get a shitty job like I have to do*?

Part of the answer is that jobs won't be so shitty if workers are empowered by the UBI to stick up for their rights and higher wages. But the fundamental reason, which has been totally overlooked by the orthodox pro-UBI community with their focus on 'transfer' payments, is that the legitimate claimants to a share of the nation's material prosperity include not just the wage workers; not just the landlords, not just the capitalists, but also the public at large, who make productive work and profitable investment possible, basically, by living their lives – in particular their dealings with other people; in particular with strangers (ie, not just kith & kin) – with predictability, trust and trustworthiness. You do this at work, of course, but also as a client, as a customer, as a citizen keeping the peace in the streets, as a homemaker, and most importantly of all as a parent or mentor training the next generation how to behave in the civilised economy.

Put it another way – as indeed did Daron Acemoglu and James Robinson in their terrific book, *Why Nations Fail* – in a low-trust society, no-one can get rich or even moderately prosperous without engaging in criminal violence, and, conversely, none of the rather numerous cadre of non-violent and non-criminal rich and prosperous persons in New Zealand now did it without relying extensively on social trust.

I and others have quite recently documented the importance of generalised trust (trust in strangers) to economic prosperity as well as other dimensions of well-being[18], but, as usual, we find that Adam Smith thought of it first:

> In civilised society [man] stands at all times in need of the co-operation and assistance of great multitudes, while his whole life is scarce sufficient to gain the friendship of a few persons.[19]

Why are the multitudes needed? Because of the division of labour, which in this period just before the industrial revolution, was the prime source of prosperity (along with still-uncrowded land). Smith carries on to his more famous passage:

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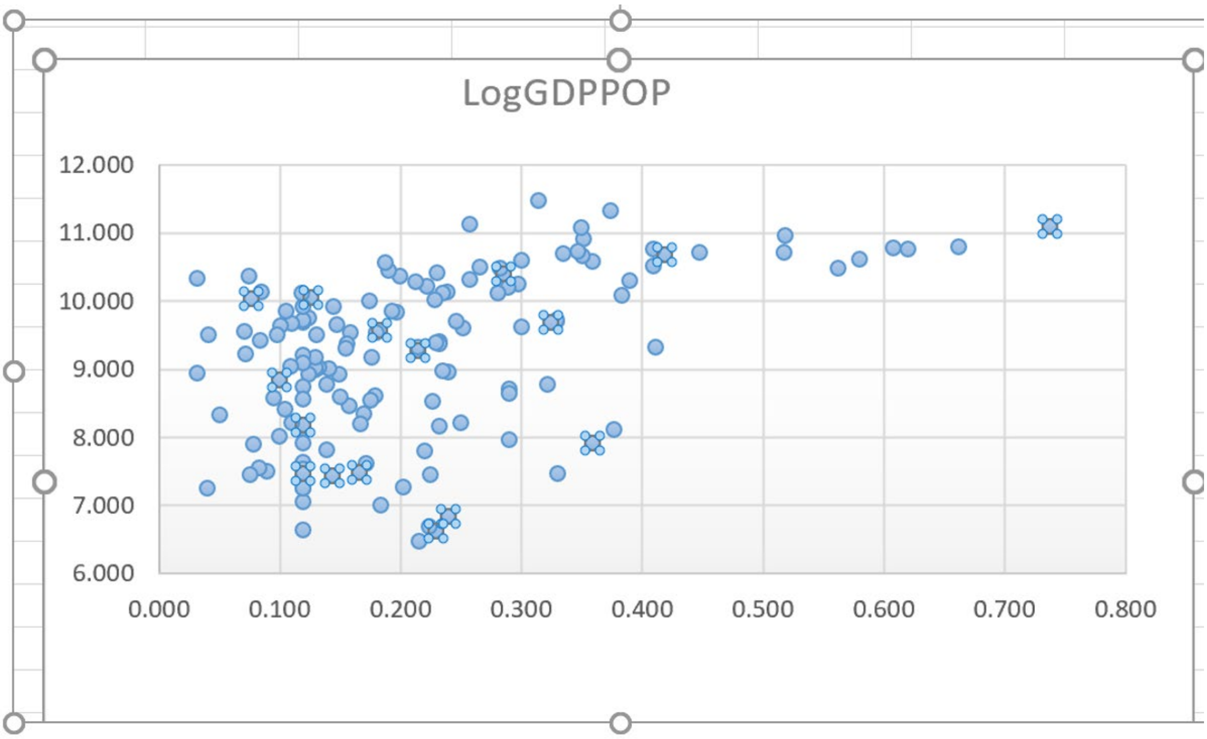
[18] For results and references, see Tim Hazledine (2022) 'Trust, Deep Trust, Productivity and Well-being in 136 Countries', *International Productivity Monitor*, No. 42, June.

[19] Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, 1776 [1998], p22.

It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of their advantages.[20]

But Adam Smith -- a moral philosopher by trade -- was well aware of the importance of 'humanity' to civilised life, including civilised economic life. All those strangers upon whom each 'man' depends: with no ties of kinship or friendship, what is to stop them cheating, robbing, neglecting, even injuring or killing the lonely butcher, etc, in the pursuit of their self-love?

A simple scatter diagram of per capita GDP and trust[21] reveals that, though trust is not the only thing that matters for prosperity, it is indeed a factor. All the high-trust countries are high-income, and if countries are ranked from highest to lowest average trust scores, all first-world countries are in the upper half of the ranked distribution.[22]



[20] *Ibid.*
[21] The trust variable is the average proportion of the population of each country answering 'yes' to the survey question: "Generally speaking, do you think people can be trusted?".
[22] The least trusting rich country is France, for which the trust score is right at the mid-point of the rankings.

Adam Smith again:

> The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state.

Smith would not, I believe, have any trouble in extending this classic justification for the rich to pay more taxes than the poor to the idea that taxation, and its subsequent redistribution to all members of society is the proper return to the protection afforded the well-off by civil society in general: by people behaving well (including paying their taxes): it could be called the returns to our moral capital.

I would expect that these returns are easily large enough to justify a 'trust dividend' of $12,000/year in 2023: not as a welfare benefit; not as guilt money from the better off; but as fair and reasonable return for living a life of responsible adulthood in society.

Whether you want to call it the Trust Dividend or just stay with the conventional rationales for a Universal Basic Income, you are buying in to the one Big Idea – apart from the urgent need to cut back carbon emissions – on which sensible members of the political left and right find themselves in agreement, and as such this really needs to be taken up by our governments. The Welfare State has not eliminated mass poverty, to which the conventional response has been: "We need more welfare state". I am suggesting that we need something quite different, not more of what doesn't work any more.