A Self-Reliant Australia

Welfare Policy for the 21st Century

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Preface

On 4 November 2003, the Melbourne *Age* reported that the federal Opposition spokesman for Family and Community Services, Wayne Swan, had attacked the Commonwealth government for having spent one billion dollars less on family welfare benefits than it had budgeted for. The government expected to spend $12.8 billion on Family Tax Benefits and childcare benefits in 2002-03, but these payments 'only' cost $11.8 billion. Mr Swan complained that this amounted to 'a shortfall of more than $500 per family'.

When a government delivers all the welfare services it has promised to deliver at $1 billion less than expected, and is then criticised for not having spent enough money, then truly, we have all joined Alice down the rabbit hole. How are we ever to make progress on the debilitating problem of spiralling welfare spending and escalating welfare dependency if politicians still believe that the test of welfare policy is the amount of money that is spent, and that a reduction in the number of households receiving handouts is cause for alarm rather than celebration?

Forty years ago there were 22 workers paying taxes for every one person reliant mainly or wholly on welfare. Today the ratio is just five to one and this trend away from self-reliance and towards dependency on government handouts shows no sign of reversing. Indeed, it is a trend that feeds off itself, for the more welfare dependency grows, the higher becomes the level of taxation on those who remain in paid employment, and the lower become the incentives for them to find or remain in work. Over the last 40 years, even the lowest-paid workers have been sucked into the tax system to help pay the nation's welfare bills.

In this paper I suggest that the time has come to turn back the growth of this expensive, damaging, demeaning and largely unnecessary welfare state behemoth. I argue that in the 21st century we no longer need a mass welfare state, which originated in the 20th century to tackle what were essentially 19th century problems. We need to reduce welfare dependency by reforming the system of Income Support, by pushing forward on labour market reform (to create more jobs for people currently on welfare), by radical reform of personal taxation (to restore work incentives), and through savings reform (to reward and encourage self-reliance).

A Self-Reliant Australia arises out of work conducted in the Social Foundations programme at The Centre for Independent Studies. It is based on two recent conference papers. The first, 'Do We Still Need the Welfare State?', was delivered to the Australian Institute of Family Studies conference in Melbourne in February 2003. The second, 'Tax, Welfare and Jobs: A First Step to Reform' was delivered to the Second Economic and Social Outlook Conference, sponsored by the Melbourne Institute and *The Australian* newspaper and held in Melbourne in November 2003. I am grateful to Barry Maley for his comments on an earlier draft.

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Introduction

The demise of the welfare state

Nearly twenty years ago[1] I suggested that western, capitalist countries are in a long-term transition from what I called a *market mode of consumption* characteristic of the 19th century, through a *socialised mode of consumption* which lasted for much of the 20th, and towards a *privatised mode of consumption* emerging today. Seen in this way, the socialised mode, exemplified by the mass welfare state, is historically transitional, for the circumstances which brought it into being are now disappearing.

In the 19th century, people were expected to provide for their basic needs through market transactions and self-provision, and when these failed they relied on charity, philanthropy, mutual aid and a rudimentary system of official poor relief to get by. Industrialisation, urbanisation and democratisation eroded this market mode of consumption. Problems such as insanitary housing and an uneducated workforce, combined with competitive party bidding for the votes of a newly-enfranchised working class, led governments increasingly to assume responsibility for providing social necessities that many people at that time could ill afford to purchase for themselves.[2]

The socialised mode of consumption which developed as a result of this increased government activity rested on the idea that citizens should have a right to a range of basic services financed and/or provided by government. In 1950, T. H. Marshall identified these 'social rights' as one of the core principles of modern citizenship, along with legal and political rights.[3] In most countries, the extension of 'social rights' meant that governments ended up financing or directly providing education, healthcare, housing, retirement pensions, child support and insurance against periods of unemployment, sickness or other incapacity.

By the 1980s, however, it was clear that this system was in irreversible decline across the western world as a result of four factors:

- Escalating costs (or what Marxists of the time called the 'fiscal crisis of the state')[4] because of ever-rising levels of demand and low productivity increases in the labour-intensive welfare sector;
- Increasing affluence subsequent to sustained economic growth (ordinary people could now afford to buy services like housing and retirement pensions which had in earlier times been prohibitively expensive);
- Expanded popular aspirations for private ownership (as private solutions spread through the population, they increasingly became the norm to which most people aspired. As a result the convenience of car ownership displaced reliance on public transport, the autonomy of home ownership displaced public sector rental, the security of a retirement annuity displaced reliance on a state pension, and so on);
- The sheer momentum of change (the more people who moved from socialised to privatised provision, the more those they left behind wanted to follow them, thus reinforcing the stampede to exit the State system).

Consideration of these four factors led me to suggest that a new 'privatised' mode of consumption was emerging in place of the socialised welfare state. I emphasised, however, that this newly emerging 'privatised' system was not (despite the arguments of its critics) a return to 19th century 'laissez-faire', because having occupied such a central place in the life of modern societies during the 20th century, it was most unlikely that the democratic state would or could abdicate its social responsibilities in the 21st century—modern political expectations and civic sensibilities would simply never allow it. The role of government was therefore not so much receding as changing its form. In particular, government was shifting from provider to enabler.[5]

In the emerging privatised system, for example, subsidies and tax incentives are used to allow more people access to private healthcare, private schooling, home ownership or retirement saving schemes, at the same time as direct provision of the socialised alternatives is gradually wound down. The emergence of a privatised system involves tax reductions (to leave money in the hands of consumers who can then buy these services for themselves), but it also entails a change in the way government uses tax revenues, devoting more of its spending to boosting consumers' purchasing power rather than providing them directly with state services. We see this trend clearly in Australia in policies such as the federal government's subsidy of private schools, the use of tax incentives to encourage people to take out private medical insurance, the use of special payments such as the First Homebuyer's Grant to help people gain access to home ownership, and the Labor Party's recent proposal to establish 'nest-egg accounts' to support personal saving.

The overall level of government social expenditure should fall as a result of the transition to a privatised system (as more people buy what they need rather than relying on the government to provide it), but what changes even more dramatically is the *form* in which services are produced and consumed. Increasingly, property rights are vested, not in government authorities, but in the final consumers themselves—the purchasers of healthcare, the owners of housing, the stakeholders in the private pension funds. The implications of this for personal autonomy, and for the character of power relations between service providers, consumers and public sector politicians and bureaucrats, are profound.

Although this shift from a socialised to a privatised mode has been in progress for more than 20 years, it is still being fiercely resisted by many social affairs activists and professionals in our universities, voluntary organisations and media. In some cases, this resistance is born of self-interest, for social affairs professionals depend upon the socialised welfare system for their employment, and a shift to a privatised mode threatens to transfer power from them to those who currently consume the services they supply.[6] In other cases, resistance is the result of intellectual laziness or political habit, for supporting the welfare state has become totemic for many intellectuals, a sign of their membership of 'progressive' political and intellectual circles and a symbol of their 'compassion' and 'humanitarianism' (even though the experience of those at the receiving end of the welfare state is generally far from positive).[7]

But not all defenders of the socialised welfare system are motivated by self-interest or are guilty of laziness. Some genuinely believe that the mass welfare state still has a crucial role to play in modern society. Their argument takes one of two forms.

Some commentators say the welfare state is needed *economically*, to meet people's material needs and to keep them out of poverty. Others argue that it is needed *sociologically* to reinforce the cohesion of society by forging a bond between the more and less fortunate. Neither of these arguments is convincing, although both may have been true in earlier days. The transition from a socialised to a privatised mode of consumption that we are now witnessing is entirely consistent both with meeting people's needs and with maintaining a vibrant and functioning society. Indeed, the more we move away from the mass, bureaucratic welfare state model, the more these functions are likely to be fulfilled.

Part One

Do we need the welfare state to prevent poverty and provide for people's needs?

The politics of poverty

One of the ironies about contemporary Australian debates over poverty and welfare is that the most ardent defenders of the existing welfare system are among the first to argue that it has been grossly ineffective in achieving what it was set up to do. On one hand, they insist that a mass welfare state is needed to prevent poverty, but on the other, they continually claim that the mass welfare state has failed to prevent poverty from rising, and therefore even more needs to be done. As welfare spending has escalated over the last 40 or 50 years, so the welfare lobby's estimates of the number of people in poverty have also escalated. The more we spend, the worse the outcomes appear to become.

The explanation for this paradox is not hard to find. Those who want to defend and expand the welfare system need to demonstrate the continuing plight of 'the poor' in order to justify their demands. If they were to suggest that half a century of rising welfare expenditure had actually worked, and that poverty had to a large degree been eradicated, their case for stepping up welfare spending in the future would disappear. Activists therefore have to argue both that welfare works, and that it doesn't. By defending the welfare state by claiming that poverty is still widespread, they are caught on the horns of a logical dilemma of their own making. In this area of public policy, it seems, nothing succeeds like failure.

Throughout its history, the welfare state has been justified by the argument that it is needed to ameliorate or eradicate poverty. It is the existence of poverty that has given the welfare state its rationale and its popular legitimacy:

- In Britain, the early surveys of poverty by Charles Booth and Seebohm Rowntree helped shift government thinking and justified early welfare interventions such as non-contributory State old age pensions.
- Half a century later, the so-called 'rediscovery of poverty' in the United States (by Harrington), in the United Kingdom (by Townsend) and in Australia (by Henderson) again had a massive impact on governments, leading to the 'War on Poverty' and the 'Great Society' programme in America, to area-based positive discrimination initiatives in Britain, and to the Whitlam government's health and welfare reforms in Australia.[8]
- Today, nearly half a century after that, the same pattern is being played out again, only this time poverty research is being used defensively, to counter attempts by governments to restrain and reform their increasingly antiquated and costly welfare systems.[9]

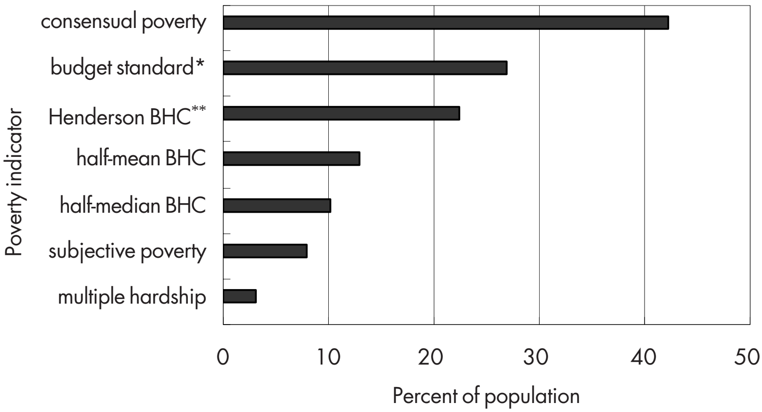
Without widespread poverty, the economic case for the mass welfare state begins to crumble. Poverty statistics are thus intimately bound up with the political battles over social policy. This is why, as the welfare state has come under increasing threat, the social policy establishment has responded with ever-more exaggerated claims about the extent and depth of the poverty problem.

- In Britain, where unemployment is at its lowest for 30 years and the economy has been booming, the Rowntree Foundation claims that more than one-quarter of adults now live in poverty, and that poverty rates are rising. Its latest survey, which claims to have defined and measured poverty 'scientifically', also takes seriously the finding that 17% of Britons believe they live below the United Nation's definition of absolute poverty.[10]
- In Australia, the key mouthpiece for the welfare lobby, the Australian Council of Social Service (ACOSS), insists that poverty affects around 22% of the population. This estimate rests on a poverty measure—the Henderson poverty line—which, in the course of the 1990s, rose in value at twice the rate of inflation and which now returns estimates much higher than most conventional measures.[11]

There are many different ways of defining and measuring 'poverty'. Figure 1 shows that published poverty estimates currently range from around 3% to over 40% of the Australian population. None of these is inherently 'right' or 'wrong', for 'poverty' is a highly emotive, inherently politicised and essentially contestable concept. There can be no 'true' rate of poverty, nor any authoritative definition of what the term means. This is why poverty statistics (and government inquiries into poverty) are popular with lobbyists, for the elasticity of the data allows them to be pressed into service to support almost any reform proposal they care to formulate.

Welfare lobbyists generally arm themselves with the most inflated (and arguably meaningless) poverty estimates they think they can get away with, hoping to convince us that the sorts of problems that led 19th century European governments to get involved in mass welfare provision in the first place still exist, and

Figure 1. Poverty rates estimated by 7 different measures



* estimated at an average of 1.2 times Henderson

**BHC = before housing costs.

Sources: Ann Harding, Rachel Lloyd and Harry Greenwell, *Financial Disadvantage in Australia 1990 to 2000* (Sydney: Smith Family 2001); Peter Saunders, *The Ends and Means of Welfare* (Sydney: Cambridge University Press, 2002); Peter Saunders, 'A New Poverty Line?', *SPRC Newsletter* No.69 (May 1998); Rob Bray, *Hardship in Australia,* Occasional Paper No.4 (Canberra: FaCS, 2001).

that a mass welfare intervention is still required. No matter how wealthy our society becomes, and how much the living standards at the lower end of the income distribution improve each year, the welfare lobby wants us to believe that we shall always need a huge, costly welfare state to care for millions of people who would otherwise be destitute.

Transitional (lifecycle) hardship

In reality, even social policy activists and intellectuals know that the world has changed dramatically since the welfare state first emerged. A modest rate of economic growth (say 3% per annum) sustained over an extended period doubles the real purchasing power of ordinary working people every 30 years or so, and this is precisely what has been happening across much of the western world since World War II. The unattainable luxuries of one generation have become commonplace in the next, and the widespread deprivation that brought the welfare state into existence has vanished. With it has gone the rationale for direct government provision on a mass scale.

This is not to say that all poverty and deprivation has disappeared from developed capitalist countries. Significant proportions of the population may still experience periods of relative hardship as they go through life—as students, when they start a family, when they buy their first home, when they are between jobs, and so on. These people figure prominently in poverty surveys. But in most cases, the periods of relative hardship that they experience do not last for long, and most of those who find the going tough at one time are on a trajectory which soon leads to a more comfortable situation. Throughout the western world, longitudinal income surveys consistently find that between half and two-thirds of those who appear under any given 'poverty line' in one year are no longer there just a year or two later.[12]

This means that many of those identified in surveys as 'poor' are actually in transition between periods of relative affluence. Over their whole lifetime, they will earn more than enough to get by on; it is just at certain short points in the life cycle that they struggle. The policy implications of this are crucial, as income shortfalls in these transitional periods could, in principle, be covered by savings and investments built up in more prosperous periods. With today's higher living standards, it should be possible for many more people to save for their retirement, to borrow to pay for higher education, or to insure themselves to provide an income during periods of sickness or unemployment, funding such provisions from earnings during the more affluent periods of their lives. Our grandparents could never have afforded such expenditures, but we could, if only we were not being taxed so much to pay the government to provide these things on our behalf.

Residual poverty and welfare dependency

What is true of the majority is not, of course, true for everybody. Although most of us could provide for our consumption needs perfectly adequately without the government doing it for us, not all of us could. Whether as a result of inability to work, lack of opportunity or personal deficiencies of one kind or another, there will always be a small minority of the population incapable of earning enough in the course of a lifetime to sustain themselves. Do we need a welfare state to support them?

Radical libertarians argue we do not. They suggest that needy and deserving cases will be supported informally (for example, by family and neighbourhood mutual aid, coupled with charitable support and philanthropy), while the lazy and the feckless can make their own decision whether to work or starve. As already noted, however, it is unrealistic to believe that any democratically elected government would stand aside and let people go without basic means of subsistence, even if they have brought their fate upon themselves. Like it or not, there will be no return to the 19th century market mode of consumption.

This means that some provision will always have to be made for that section of the working-age population who cannot or will not support themselves by working. The key question is, how many people fall into this category?

It is impossible to give an accurate answer to this question, but there are grounds for suggesting that it is probably somewhere between 3% and 5%.

One basis for this estimate is the level of welfare dependency in the past, when the welfare system was more tightly targeted on supporting those incapable of working. In Australia, the proportion of the working-age population receiving social security income support payments in 1965 was just 3.2%, and this figure remained below 5% right through to the Whitlam reforms of the mid-1970s.[13] This suggests that only a tiny fraction of the working age population is likely to be incapable of maintaining self-reliance.

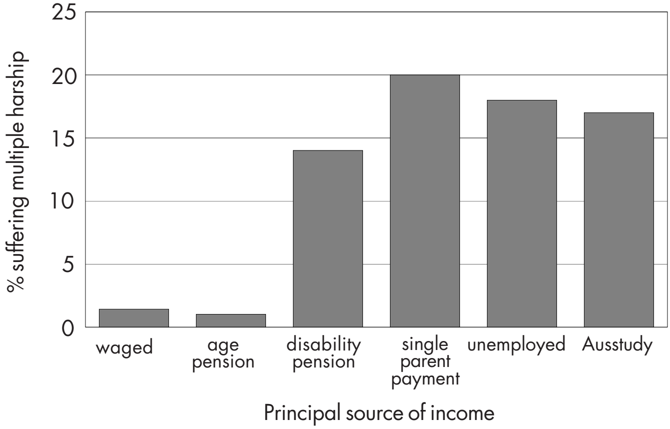
A different but complementary indicator of the likely size of the long-term dependent population may be the number of people who currently live in chronic 'poverty'. Again, an estimate of up to 5% of the population in countries like Britain and Australia seems appropriate:

- In Britain, the Rowntree poverty survey found that only 2.5% of adults (1 in 40) report having experienced long-term poverty and are currently 'deprived' on three or more lifestyle indicators;
- In Australia, Rob Bray finds that just 2.2% of the population reports income and spending levels that are lower than 50% of the respective median values in the whole population, the Social Policy Research Centre's (SPRC) Peter Saunders[14] identifies 5.9% of people as claiming to have insufficient income while also having a 'deprived' lifestyle, and Helen Hughes estimates that around 5% of Australians may qualify as 'poor' on a relative definition once income from the 'black economy' is taken into account.[15]

Of course, it could be argued that it is the existence of the welfare state that keeps these rates of chronic, long-term poverty so low. Against this, however, almost all commentators accept that 'chronic poverty' is rare in households where somebody has a full-time job. In other words, it is not the welfare state, but paid employment, that today keeps people out of chronic poverty.

There is widespread agreement in the literature that, no matter how it is defined, the principal cause of 'poverty' is joblessness. Using a fairly tight measure of poverty as 'multiple hardship' (defined as lack of money resulting in experience of two or more of the following in the previous year: missing a meal, going without

Figure 2. Principal source of household income and 'multiple deprivation'



Source: Based on Rob Bray, *Hardship in Australia,* Table 15.

heating, pawning or selling something and seeking help from a charity), Rob Bray estimates that just 3% of households overall suffer multiple hardship, but among unwaged households this rises as high as 20% (Figure 2). Similarly, despite using a much more generous definition of poverty generating an overall estimate of one in eight households below the 'poverty line', the Smith Family's 2001 report authored by Ann Harding, Rachel Lloyd and Harry Greenwell of the National Centre for Social and Economic Modelling (NATSEM),[16] found only 3% of waged households were in 'poverty' as compared with 31% of those relying on welfare.

Unlike the situation 100 years ago, therefore, regular, full-time employment has become almost a guarantee against poverty. It is not the welfare system but the labour market that offers the best security against poverty in the contemporary period. As the results of the 1996 welfare reform in America have shown, cutting the numbers of people reliant on welfare need not increase poverty—in America, it reduced it (the number of Americans on welfare has been reduced by 60%, yet child poverty is now at its lowest point since 1979).[17]

There will always be some people who for one reason or another are incapable of supporting themselves on a long-term basis. But their numbers are not so large as to require a welfare system on anything like the current scale to support them. The most effective way to reduce poverty is to ensure that (wherever appropriate) every household contains at least one adult who has a paid job. I shall consider later in this paper how this objective might be achieved.

The self-financing of welfare benefits

The welfare state does not only consist of cash transfer payments supporting the incomes of those who do not have paid work and are deemed to be in particular 'need' of help, it also consists of payments and services in kind which are commonly provided to the mass of the population. In particular, millions of people make use of the so-called 'universal' services such as schooling, healthcare and age pensions. What would happen to them if the welfare state were radically scaled back?

The answer is that most of them would be better off than before. The guilty secret of the contemporary welfare state is that it is inefficiently recycling our own money back to us. Most of us could afford to buy the services we need were it not for the fact that the State is forcing us through taxation to pay for the inferior services it thinks we should have.

The most expensive single item most people need during the course of their lives is housing, yet this is the one area of mass consumption where few commentators are any longer prepared to argue the need for a socialised solution. It is obvious why: social housing never took root as a mass tenure in the United States or Australia, where owner occupation has long been the norm and the aspiration, and in Britain, where state rental did become widespread between the 1920s and 1970s, its appeal and relevance has dimmed as its record has tarnished. In the 'Anglo' countries at least, the 'masses' have demonstrated a clear preference to buy rather than to rent from the state, and most of them do just that.[18] Any defence of socialised provision in this area appears archaic.

But when it comes to other (generally cheaper) services—health, education and income insurance—it is still commonly argued that government must provide them on a mass scale if people are to receive what they need and if 'social justice' is to be served. Yet this is no more true of these heartland areas of the welfare system than it is of housing. The proof of this lies in the distribution of tax payments and welfare benefits across the population—evidence that shows that most of us are already funding most or all of our welfare benefits.

Simultaneous churning and middle class welfare

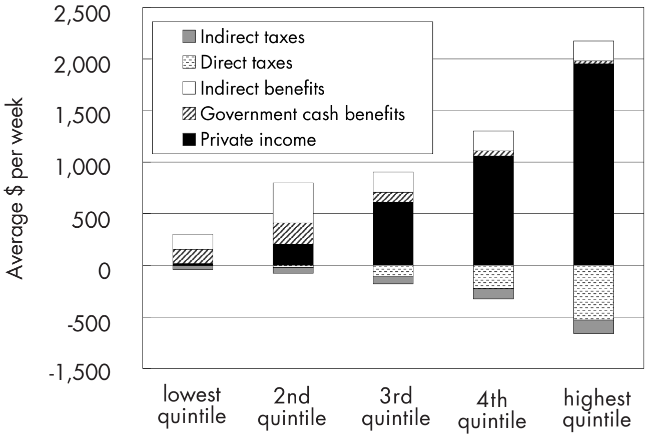
The image that most of us have of the welfare state is of a system that takes from those who can afford to pay and reallocates to those who are poor. The reality, however, is that as welfare spending has grown, it has had to be funded increasingly by taking money from all sections of society, not just the wealthy or high income earners. Many people now pay with one hand and receive the money (less overhead costs of the government bureaucracy) back with the other, and the majority of beneficiaries end up paying for most or all of what they receive. Indeed, the main reason many welfare recipients appear to need government assistance is that the government has taken so much of their income away in taxation, thereby pushing them into dependency.[19]

James Cox has analysed this process of *simultaneous churning*—the way people pay taxes only to receive the money back straight away in the form of welfare—in the context of New Zealand.[20] He estimates that the top 60% of New Zealand income tax payers receive in cash or in kind 46% of all social expenditure. They get more than their share (71%) of the money spent on public education, plus 55% of the health expenditure, 39% of income-tested benefits, 38% of family assistance and 25% of superannuation assistance. Echoing the public choice analysis of Anthony de Jasay, Cox argues that the government has over time boxed itself into a corner by constantly buying off different sections of the electorate with their own money.[21] The result is that today, many New Zealanders are paying high rates of tax to finance provisions which they could afford to buy for themselves if left to their own devices.

A similar pattern can be found in Australia. The heavy reliance on targeting and means-testing in the Australian income support system means that direct, cash benefits are steeply progressive (while the lowest income quintile receives 27%, the highest receives only 5%), but the distribution of benefits in kind, such as government education and health services, is much flatter and somewhat regressive (the lowest income quintile receives 15% by value as compared with 21% going to the highest quintile).[22] Putting direct and indirect benefits together, Des Moore calculates that the top quintile of income earners receives 14% of total government expenditure on health, education, housing and cash benefits—barely less than the 18% received by the lowest income quintile—and the ABS confirms that the highest gross income quintile receives almost as much on average each week in government payments and services as the lowest ($221 against $286).[23] This would appear to be confirmed by Figure 3.

Of course, even if higher earners take almost as much out of the system as lower earners do, it is still true that they put more in, so the system overall does redistribute money between them. The ABS calculates that the highest quintile in Australia pays an average of $661 per week in taxes into the welfare system (leaving this group with a net 'loss' on its welfare transactions of $439) while the lowest pays an average of just $40 (realising a net gain of $246). Nevertheless, Figure 3 makes clear that much of the money that goes into the welfare system is effectively returned to the same

Figure 3. Composition of final income (1998-99)



Source: Based on ABS, *Government Benefits, Taxes and Household Income,* Cat. No. 6537.0 (Canberra: ABS, 2001).

people, particularly in the middle income bands, and particularly when it comes to services in kind.

This scale of churning (paying tax with one hand and receiving benefits in cash or in kind with the other) is administratively wasteful, it has a damaging effect on work incentives, and it disempowers consumers because they are prevented from exercising effective choice over how best to spend their money. We have locked ourselves into a vicious circle from which we urgently need to escape.

Lifetime churning

The 'churning' of money through the welfare system is even more marked when we look at income flows over an individual's entire lifetime, rather than at just one point in time. In Britain and Australia, studies have attempted to calculate the total taxes paid, and total value of welfare services received, by different income groups over the course of their entire lives. These simulations divide the population into lifetime income deciles and then calculate how much each decile pays into the welfare system in tax over a full lifetime (assuming current tax rates), and how much it gets back in welfare payments and services (assuming the current system of entitlements). The results show that the modern welfare state operates more as a system of forced saving than as a mechanism of interpersonal income redistribution, as most of us pay in at one point in our lives only to get much of our own money back at another.

This pattern of lifetime churning is particularly marked in social insurance systems, where entitlement to income support is established through personal contributions. In the United Kingdom, John Hills and Karen Gardiner find that, while people with higher lifetime earnings pay more tax over a lifetime into the welfare system, the overall allocation of benefits (cash income from social security, plus the value of government health and education services) is remarkably flat. Every income decile receives more or less the same (around £133,000 at 1991 prices), and on average, £98,000 of this is self-financed:

> Nearly three-quarters of what the welfare state does looked at in this way is like a 'savings bank'; only a quarter is 'Robin Hood' redistribution between different people.[24]

Even those making up the lowest 10% of lifetime earnings self-finance half of what they receive, and the next decile up self-finances two-thirds of its receipts.

In Australia, where the government-financed income support system is more tightly targeted, and where eligibility for cash benefits is on the basis of 'need' rather than contributions paid, this pattern of lifetime churning is less marked. Peter Whiteford and Gregory Angenent[25] have pointed out that our flat-rate, means-tested, non-contributory welfare benefits system targets those in need more effectively than overseas insurance-based social security systems do. While we spend less in total on income support payments than most European countries do, the value of the net transfers made to the poorest 30% of Australian households is actually higher than in any other OECD country apart from Norway. Nevertheless, over a whole lifetime many people do still receive much of what they put in. As in Britain, there is evidence of substantial lifetime churning.

Taking 1986 as her base year, Ann Harding calculates the total lifetime value of direct federal taxes (but not indirect taxes) that people pay into the welfare state, and compares this with the total value of cash and education services (but not, initially, health services) that they receive back. She finds that:

> A significant proportion of income taxes paid during the lifetime are returned to the *same individuals* in the form of cash transfers during some other period of their lifecycle. Over the lifetime there is thus significant 'churning' as taxes paid to government at some point in the lifecycle are returned to the same individuals at some other point.[26]

Harding's calculations demonstrate that most of the inter-personal redistribution that does occur in the Australian welfare system takes place between men and women, rather than between higher and lower income earners *per se*, and this is mainly because women retire earlier and live longer (that is, they receive more in age pension payments) as well as benefiting from various family payments.

Taking men and women together, Harding calculates that the bottom income decile receives 21% of its entire lifetime income as welfare cash transfers. This poorest section of the population is therefore remarkably self-reliant, receiving only one-fifth of its lifetime income from government pensions and allowances. Even more surprising is the fact that this same group also pays 12% of its lifetime income to the government in income taxes. Of course, as Harding points out, not all of these taxes go towards welfare, and looking only at what she calls 'adjusted income tax' (that is, that portion of their tax devoted to welfare expenditure), she shows that they take much more cash out than they put in. What is most significant as regards future tax and welfare policy options, however, is that even at the very bottom of the lifetime income distribution, cash benefits account for only one-fifth of lifetime income, and half of this is cancelled out by income tax paid.

When we turn from cash benefits to welfare services in kind, Harding finds that lifetime churning is even more marked, and that richer individuals often end up taking more value out of government-funded services than poorer people do. For example, the highest decile of lifetime income earners receives $45,000 of taxpayer-funded schooling at 1986 prices, while the lowest decile takes only $38,600 (were it not for the fact that private schools attract lower levels of public subsidy than government schools, this pattern would be even more regressive). Similarly in healthcare,[27] although the bottom decile ends up receiving about twice the share of government spending on doctors, hospitals and drugs as the highest decile, this is due mainly to the willingness of wealthier groups to pay for private healthcare. Even the bottom decile still pays for $30,000 of its $86,000 lifetime health benefits, and on average, Australians end up paying in taxes for 73% of the government healthcare they receive.

The key role of the Australian welfare system for most citizens today is, therefore, that of a compulsory 'piggy bank'. By taking taxes away from us during the more prosperous periods of our lives and returning the money to us during the leaner years, the government is ensuring that we save enough to cover our lifetime needs. However, we exert precious little control over this process and the administrative cost of this churning is very high.

It is important that individuals should 'smooth out' their lifetime income flows, but using the welfare state to achieve this is a cumbersome solution to what is a very simple problem. As developments around the world have been demonstrating, the same outcome could be achieved more efficiently and equitably by developing instruments like Personal Savings or Investment Accounts which allow people to accumulate funds in their own personalised accounts and to play an active role in how they are managed.[28] The welfare state is a bureaucratic, costly, non-responsive and increasingly anachronistic way of forcing us to save. There are better ways of achieving the same outcome.

Part Two

Do we need the welfare state to hold our society together?

We no longer need the welfare state to ensure that people's basic consumption needs are met. There is, however, a longstanding assertion in the sociological literature which claims that this is not, or should not be seen as, the key role for the modern state welfare system to discharge. According to this argument, the welfare state is still needed sociologically, even if not economically, for its role is to bind our society together.

The argument takes two forms. First, there is the specific claim that the minority of the population that still needs help will be abandoned unless everybody else is forced into participating in a common, state-organised, welfare system. Second, there is the more general claim that market relations undermine social cohesion and solidarity and that the welfare state is needed to bring us all back together again. Both arguments are repeatedly heard, but once we analyse what they are saying, neither is convincing.

Middle class welfare as an insurance for the poor

The first argument was outlined by Julian Le Grand 20 years ago[29] and has recently been restated in Australia by the SPRC's Peter Saunders. He accepts the 'arithmetic' argument that many of us no longer need the welfare state to provide for us, but he rejects as 'naïve' the conclusion that our society could therefore get by without it:

> Neo-liberal critics of 'income churning' have argued that the net distributional impact could be achieved with a far smaller state sector . . . This is arithmetically accurate but politically naïve because it ignores the role of broadly-based programs in underpinning the support of the middle classes, without

> which the welfare state would founder politically . . . Middle class welfare is the lifeblood of the welfare state.[30]

It is being argued here that people have to be coerced into paying for a system they do not need to prevent the system from collapsing. There are a number of obvious points to make in response to this logic:

- The argument is tautological. It makes no sense to defend a universal, comprehensive system on the grounds that it would collapse if it were not universal and comprehensive. The system has become its own reason for existence. It is illogical to worry about how to keep people on board a system that has outlived its usefulness.
- The argument is ethically dubious. Essentially it endorses the idea that politicians should bribe electors with their own taxes. The argument rests on an assumption that people will only be willing to pay money to help others in need if they think that they will get something too. But this was never the rationale for a universal welfare system. If people have to be bribed to support it, then we are better off finding an alternative.
- The argument is historically blind. Before governments took over the responsibility to provide for people's consumption needs, ordinary people often organised such provisions for themselves. Thriving mutual aid arrangements emerged in Australia, Britain and the United States around the late 19th century, but these were undermined by the imposition of compulsory, tax-funded state systems. Historically, therefore, it makes little sense to say that universal systems are needed to protect lower income groups, because it was the emergence of universal systems that stopped lower income groups from organising their own arrangements in the first place.[31]
- The argument is also unnecessarily pessimistic. Before the welfare state evolved, more privileged sectors of society often recognised a social responsibility to support those who could not care for themselves, and even today, the State welfare system is complemented by hundreds of voluntary agencies dedicated to looking after those in need. Furthermore, public opinion surveys suggest that there is strong public support for policies designed

to help those who cannot be expected to help themselves.[32] All this suggests that higher income groups (and corporations) do not need to be forced or tricked into supporting fellow citizens who are needy and deserving. They have done it in the past, and despite the existence of a state system, many still do it to this day.

The argument that the welfare state holds society together

The broader sociological case for the welfare state is that society would fray and fragment without it. This is often taken as a self-evident truth by those who seek to defend and expand the socialised system. They think that an extensive welfare state is all that stands between us and an individualistic, atomised, fragmented and anomic society polarised between a privileged class barricaded behind 'gated communities' and a dispossessed, alienated and increasingly desperate underclass. The welfare state, in other words, is a *civilising* institution at the heart of contemporary capitalism, a source of civic altruism in a sea of competitive individualism.

This argument was implicit in T.H. Marshall's suggestion that welfare rights are an integral component of what it is to be a citizen, and it has been taken for granted ever since by social policy intellectuals and activists who demand that government increase welfare spending to head off impending social breakdown.[33] But the argument is almost totally groundless. I have discussed the issues that it raises in more detail elsewhere,[34] but essentially:

- It misunderstands the sources of social cohesion. As sociologists like Peter Berger have long argued, and as 'third way' revisionists like Mark Latham and Peter Botsman also recognise, cohesion develops from the bottom-up, not the top-down.[35] A sense of common identity and mutual empathy develops, not from state bureaucracies administering largesse from on high, but out of the 'little platoons' of families and neighbourhood associations coming together to solve common problems. To the extent that the welfare state has taken over responsibilities from these smaller agencies of civil society and left them with nothing to do for themselves, it is more likely to have eroded social cohesion than to have contributed to it.

- It misunderstands the social character of market-based relations. Market relationships and private property rights do not produce social disaggregation, but quite the reverse—they create the conditions in which an active civil society can flourish. As Michael Novak suggests, 'Markets draw individuals out of isolation and into reasoned, civil, voluntary interchange with their fellows.'[36] Classic sociological indicators of social malaise (divorce, crime, drug abuse, mental illness, and so on) were all much lower during the market mode of consumption in the late 19th century and increased as the welfare state expanded. Clearly, then, there is no inherent link between market-based social life and social atomism. Indeed, the capitalist market system has historically co-existed with both individualistic and communalistic cultures.[37]
- It misrepresents the lived reality (as against the ideology) of welfare state relations. The welfare exchange between donors and recipients is not one that builds trust and mutual recognition, and it is more likely to fragment than to unify. The experience of receiving aid from government welfare agencies is widely recognised as being alienating, stigmatising and disempowering. No matter how much state agencies try to change this (for example, by redefining recipients from 'claimants' through 'clients' to 'customers'), the relationship remains the same, because the welfare system is inherently impersonal, distant and bureaucratic. Similarly, the experience of paying into the system does not generally foster values of altruism, but rather creates suspicion of one's fellow citizens. The rhetoric of 'bludgers', which social policy intellectuals like to explain away as the product of media scare campaigns, is better understood as an expression of frustration and anger by people of modest means who look around their own immediate neighbourhood and (correctly or mistakenly) see others taking advantage of them.

The welfare state relationship between net donors and net recipients is not one that generates cohesion and solidarity. Far from binding us all together, the lived reality of the welfare state is that it ferments distrust, encourages dishonesty, undermines social responsibility and reinforces selfishness. Society would be stronger without it.

Part Three
First steps to reform

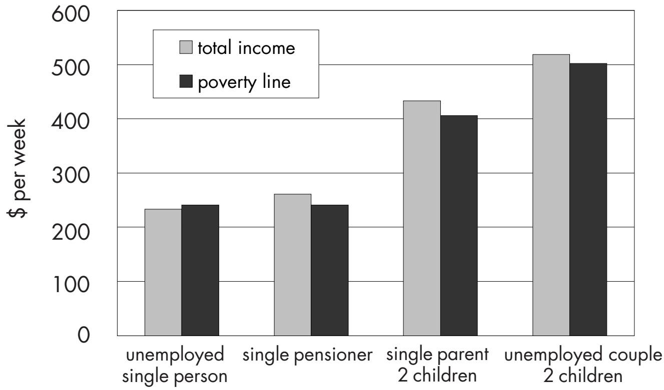
Why we must not raise benefit levels

When in a hole, stop digging. The first step towards reversing the welfare juggernaut is to resist the repeated calls for more spending. In particular, we must resist the pressure from the welfare lobby to raise the value of Income Support benefit payments.

We saw earlier that low income (or 'poor') households are overwhelmingly those where no adults of working age are employed. Welfare lobby groups characteristically respond to this by claiming it 'proves' that welfare benefits are too low and that an effective anti-poverty strategy requires that we raise the value of benefits. ACOSS, for example, has long demanded that the value of allowances be raised at least to match that of pensions.

But even when judged against an inflated and exaggerated measure of poverty such as the Henderson poverty line (the measure preferred by ACOSS), there is little evidence to support the contention that benefits are too low. We saw earlier that the Henderson poverty line now generates an absurdly high poverty rate in excess of 20% among Australian households. Since the early 1970s it has become increasingly generous because of the way it has been adjusted with inflation—today it would buy 37% more than it would have done in 1973. Yet despite its increasing generosity, calculations by the Melbourne Institute (Figure 4) indicate that the value of the benefits to which welfare claimants are entitled (the allowance or pension, plus partner's allowance, Family Tax Benefit and rent assistance) are still above the current Henderson poverty line in nearly every case.

Figure 4. Welfare payments compared with the Henderson poverty line



Source: Based on Melbourne Institute of Applied Economic and Social Research, *Poverty Lines: Australia* (March 2003). The value of the Henderson poverty line is slightly higher for employed households than for non-employed ones (this reflects the additional expenses incurred in going to work). ACOSS prefers to use this higher line when estimating poverty rates among those on unemployment benefits—this slightly increases the gap shown above for an unemployed single person. However, it should also be remembered that the estimated incomes shown above take no account of the value of concessions available to the unemployed and pensioners.

If we were to accede to the welfare lobby's persistent demands to make benefits more generous, the result would almost certainly be to increase 'poverty' or 'hardship' rather than reduce it. This is because higher benefits would further weaken the incentive of people on welfare to get a job while simultaneously increasing the tax burden on self-reliant workers. Already high Effective Marginal Tax Rates (EMTRs) would become even higher, more people would stay or end up on welfare, and 'poverty rates' caused by joblessness would expand even further. As noted earlier, one of the ironies of the last 40 years is precisely that welfare spending has been rising dramatically yet 'poverty' seems not to have been falling as a result. Welfare lobbyists keep pushing for higher social expenditure (and the higher taxes to fund it), despite clear evidence that higher welfare does not lead to lower poverty (and may actually do the opposite).

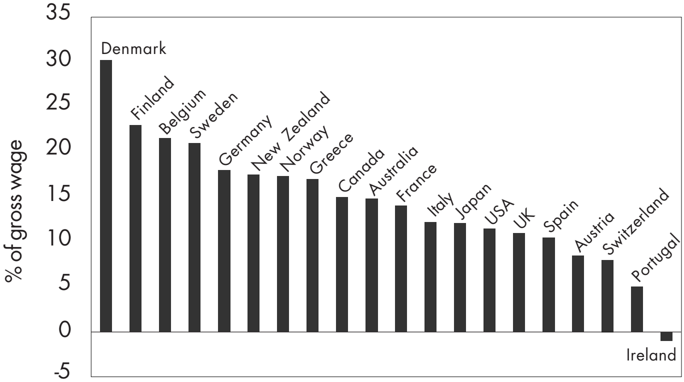
Rather than treating the symptom—the low living standards of some of those living on welfare—we should focus on the cause, that is, lack of full-time employment. This means we should not be looking for ways to increase the value (and hence the attractiveness) of benefits, but instead seeking to get as many people as possible off welfare and into paid employment.[38]

To achieve this, three things are required, and they must be done together. There must be radical **tax reform** (to encourage self-reliance), further **labour market reform** (to generate more jobs), and major **welfare reform** (to improve work incentives and reduce dependency rates). In addition, to encourage greater self-reliance across the whole population, we also need to **reform savings** so that people can more easily make provision for their own lifetime income needs rather than relying on the state to do it for them.

Tax reform to encourage self-reliance

Those who advocate higher government social expenditure and higher taxes point out that total taxation as a proportion of the country's GDP is lower in Australia than in most other OECD countries (31.5% as compared with an OECD average of over 37%). But this is mainly because our indirect taxes are lower. When we consider net taxation on earnings, Australia is around the middle of the international rankings. Figure 5 shows that a couple with two

Figure 5. Net income tax and social security deductions (after receipt of cash benefits), for family of two adults and two children on average wage, various countries



Source: Based on OECD, *Taxing Wages 2002* (Paris: OECD, 2003).

children living on one average wage loses 15% of their earnings net of all government taxes and transfers—a smaller net deduction than in New Zealand, Germany or Scandinavia, but bigger than Britain, the United States, Japan, Italy and even France. Australian workers are not under-taxed by international standards.

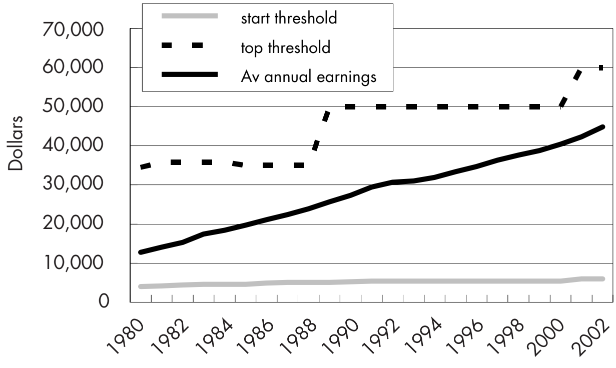
Bracket creep

Income tax rates in Australia have declined over the last 20 years, but the tax take has continued to rise because tax thresholds have not kept up with inflation. This is true of both higher and basic rate thresholds.

In 1980, workers did not start paying the top rate of tax (which was then 60%) until they earned $35,000, which at that time was approximately three times the average income. Today, workers start to pay the top rate (47%) on earnings just one-third higher than average earnings. There is widespread recognition of the need to raise (or abolish) this threshold to stop penalising middle-income families.

The erosion in the value of the base personal tax-free threshold has been even more marked. In 1980, workers did not pay any tax at all until they earned $4,041 per year (one-third of average earnings). Wages have gone up by 350% since then, but this tax-free earnings threshold has only risen by around 50%, to less than one-seventh of today's average earnings (Figure 6). Had the threshold kept up with wage inflation, it would today be worth over $14,000; as it stands, it is worth only $6,000.

Figure 6. Average earnings and tax thresholds 1980-2002



Source: Based on table in Bendzulla Actuarial Pty Ltd website (www.bendzulla.com.au).

The case for raising the personal tax-free threshold

There are two strong grounds for arguing that the personal tax-free threshold should at least be raised to a point above the minimum welfare floor.

The first is that workers should, as a matter of principle, be able to earn at least a basic subsistence income before the government starts taking their money away in direct taxes. Assuming that the welfare minimum is the government's own definition of a subsistence level income, nobody should be taxed until they have secured an income in excess of this welfare floor. This would mean, for example, that a single person should be allowed to earn more than $12,173 per annum (the current unemployment benefit plus rent assistance for a single adult) before being taxed; that a childless couple should between them be allowed to earn at least $19,893 (unemployment plus partner allowance plus rent assistance) before tax; and that a couple with two children should be allowed to earn $27,050 between them (unemployment plus partner allowance plus FTB Part A plus rent assistance) before tax.[39]

The second (more pragmatic) argument is that raising the personal tax-free threshold would allow us to reduce (or in principle even eliminate) the 'churning' of tax and welfare payments described earlier. This is because people on welfare would not pay tax, and those paying tax would not receive welfare. Anybody earning above the appropriate welfare minimum would pay less tax than they do now but would receive no income support top-ups.

We have seen that currently, many Australians pay taxes on their incomes while also receiving benefits in cash from the government (as well as additional benefits in kind). The extent of this 'churning' is less marked than in many other countries because we do not have a social insurance system that entitles higher earners to income-related benefits. However, churning is still a significant feature of our tax-benefit system, and it is the reason why people moving from welfare into work commonly experience dispiritingly high EMTRs. As original (earned) income rises, so workers find their taxes go up *and* their welfare benefits tail off sharply (the sharp reduction in benefits is precisely the mechanism which allows us to target benefits on the most needy so efficiently). The result is a massive work disincentive with EMTRs of 80 cents or more in every extra dollar earned.

Raise the threshold rather than introduce tax credits

Everybody agrees that something needs to be done to reduce these cripplingly high EMTRs. One solution that has been suggested is to follow the United States and the United Kingdom and introduce an earned income tax credit—that is, an additional cash transfer paid by the state through the wage packet to lower income earners to compensate them for the increased taxes they are called upon to pay and the reduced benefits they receive as their income rises. But as Kayoko Tsumori and I have recently argued,[40] this would be an undesirable move for a number of reasons.

Despite its name, an earned income tax credit is really just another welfare handout, and it would discourage personal initiative just as other welfare benefits do. If we go down this road, we will end up spending even more than we do currently on income support (the UK Labour government's spending on its various tax credits has grown alarmingly since 1997), and once granted, it is almost politically impossible to reverse a policy like this and claw the money back. Tax credits lock full-time workers into dependency on government handouts, thereby undermining their self-reliance. Former UK Labour Minister for Welfare Reform, Frank Field[41] estimates that 83% of UK families are now getting the new Working Families Tax Credit, and he points out that this has made it impossible for most people to work harder and escape welfare dependency. Like any other means-tested welfare transfer, these tax credits inevitably create new work disincentives, because their value tapers off as household incomes rise. This means that workers further up the income scale start to lose substantial proportions of any additional earnings they accrue, for as they pay more tax, so they also lose their tax credit. While encouraging unemployed people into work, this means tax credits discourage people from working longer hours or getting a higher-paid job, and they penalise second earners in low-to-middle income households who find it is simply not worth their while working.

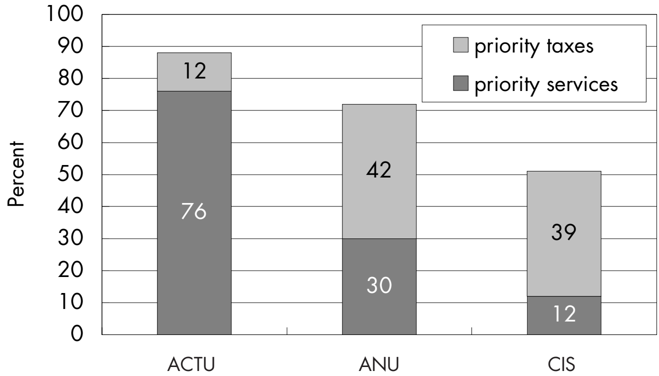
As ACOSS points out, tax credits also subsidise low-paying employers who can rely on the government to supplement inadequate wages. Indeed, the British experience has been that they encourage fraud, for employers collude with their workers to pay a proportion of the wage 'off the books' to maximise tax credit payments.

Rather than introduce yet another means-tested income transfer to counter the effects of all the other ones, the best solution to the problem of high EMTRs is to raise the personal tax-free threshold above the minimum welfare floor so that people paying tax do not receive welfare, and people receiving welfare do not pay tax.

Do workers want to pay less tax?

It seems a stupid question, but it is sometimes argued by those favouring higher taxes and higher welfare spending that most Australians do not want their taxes reduced. Recently, for example, an ACTU survey asked: *Would you prefer the Federal Government to (a) offer you an income tax cut or (b) spend the money on improving services like schools and hospitals?* Only 18% opted for the tax cut while 76% said the money should be spent on services (www.actu.asn.au).

Figure 7. Public preferences regarding taxes and social expenditure (as recorded in three different surveys)



Sources: ACTU website (www.actu.asn.au); Shaun Wilson and Trevor Breusch, 'Taxes and Social Spending', *Australian Journal of Social Issues* 38 (2003); First CIS ACNielsen survey (March 2003), see endnote 43.

The ACTU President recently used this survey to tell her conference that 76% of Australians wanted more public spending, but these respondents were never asked if they wanted the government to *increase* its spending. Other surveys which have asked people if they want government social spending increased have found nothing like three-quarters of the population in favour. A 2003 Australian National

University survey[42] for example, asked: *If the government had a choice between reducing taxes and spending more on social services, which do you think it should do?* It found 42% in favour of tax cuts while 30% said they wanted spending increased.

Change the question wording a little more and ask people if they are willing to pay *more* tax to achieve higher levels of spending, and public support for higher government spending dwindles even further. A recent poll carried out by ACNielsen on behalf of The Centre for Independent Studies asked: *Some people want the government to increase income tax and to spend the extra money on welfare and social services. Other people say we are already over-taxed and that the time has come to reduce taxes even if this means reducing total welfare spending. Which do you think the government should do?*[43] Thirty-nine percent opted for lower taxes and lower spending (much the same as in the ANU survey). But only 12% went for higher taxes and higher spending, far fewer than the ANU estimate, and a figure *six times smaller* than the 76% claimed by the ACTU.

In the same survey, we also asked at what level of earnings people thought income tax should begin. The results (Table 1) reveal strong support for raising the personal tax threshold above the minimum welfare floor.

Table 1. Public opinion and the personal tax-free threshold: *What level of annual earnings do you believe people should start to pay income tax?*

	Frequency	*Percent*
On every dollar they earn, right from the first dollar	217	3.8
On earnings above $6,000 per year (as now)	764	13.4
Not until they earn above the basic welfare benefits level	2,445	42.7
Not until they earn above the minimum award wage	2,014	35.2
People should not have to pay income tax at any level	230	4.0
Don't know/No opinion	51	0.9
Total	5,721	100

Source: First CIS ACNielsen survey (see endnote 43).

Labour market reform to create more jobs

Australia's unemployment rate recently fell below 6%. But New Zealand and the United Kingdom—two traditionally weak economies which are now enjoying the fruits of radical reforms introduced back in the 1980s—both have unemployment rates lower than Australia's. And although unemployment in the United States is today about the same as it is in Australia, this is only because the US economy has been going through a downturn. Over time, the 'structural' rate of unemployment in the United States is much lower than it is here and it is no cause for celebration that our unemployment rate has only begun to match theirs when their economy is in a downturn while ours is still strong.

Of particular concern is the number of people out of work for a year or more (so-called 'long-term unemployment'). The ABS Labour Force Survey, which asks unemployed people how long it has been since they started looking for work or since they last had a job lasting for two weeks or more, reported in May 2003 that 22% of all unemployed respondents had been out of work for a year or more. The Department of Family and Community Services records, however, suggest that the figure is much higher. As of June 2001 (the most recent available date), 57% of people claiming unemployment allowances (either Newstart or 'Youth Allowance Other') had been claiming benefits for more than one year and the average time spent on unemployment benefits was more than two years.

The welfare lobby tends to respond to the problem of unemployment by arguing for 'active labour market programmes,' but these policies are rarely effective. A review of **employment subsidies** in France, Germany and the Netherlands as well as the United States and the United Kingdom found that they 'tend not to be effective with harder-to-serve groups' such as the long-term unemployed,[44] and the OECD reports very substantial 'deadweight effects' and 'displacement effects'.[45] International evidence suggests that giving people work experience by employing them in newly-created **public sector jobs** likewise has a 'negligible' impact on their long-term job prospects and rarely provides them with the skills and experience that other employers are looking for.[46] The OECD concludes that such measures have 'been of little success in helping unemployed people get permanent jobs'.[47] In Australia, the Productivity Commission has concluded that active labour market programmes 'have variable, but usually small, effects on the employment and earnings of participants'.[48]

In previous CIS publications, Kayoko Tsumori has identified three key labour market changes which together could help create more jobs without government giving out subsidies to employers or creating more public sector jobs.

- First, although the **award system** has been scaled back in recent years, we still impose a one-size-fits-all uniformity of wages and conditions on one in five of all Australian workers (and many more are in practice covered by awards). This stifles job creation, particularly in companies facing higher than average costs or operating in the least advantageous locations, and there is a strong argument for reintroducing regional variability in awards and increasing the opportunity for employers to seek exemptions or to opt out altogether.[49]
- Secondly, the award system has given us an effective national **minimum wage** that is one of the highest in the OECD. Only France (with its 9.1% unemployment) has a higher minimum wage than we do. A high minimum wage means employers will not find it profitable to employ as many workers in low-skilled positions. If we were to raise the personal tax-free threshold, minimum wages for low-skilled jobs could be lowered without reducing workers' living standards.[50]
- A third factor is that we impose many onerous and often unnecessary regulations on companies, and particularly on small businesses. The **unfair dismissal laws** are a classic example, for they deter small companies from taking on new employees lest they are unable to get rid of them later. The Melbourne Institute has estimated that the unfair dismissal legislation alone is costing at least 70,000 new jobs in the small business sector.[51]

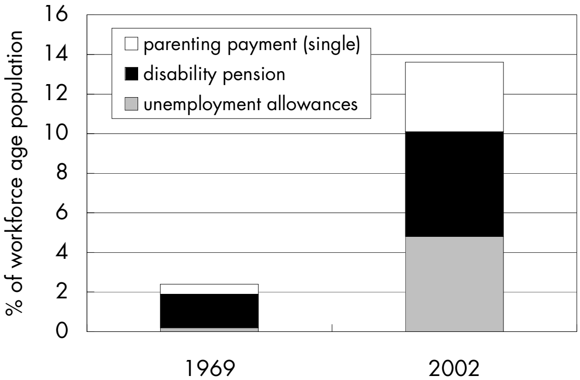
A more flexible award system, a lower minimum wage floor and reform of legislation which inhibits employers from taking on more workers would all help generate more job vacancies.

Welfare reform to reduce dependency

We saw earlier that in 1969, fewer than one in 20 adults below retirement age were drawing welfare payments. Today it is more than one in five, and one in six working-age adults are dependent on welfare for at least 90% of their income. Now there are just five workers paying income tax for every one person reliant wholly or mainly on welfare payments. In the mid-1960s there were 22.

This trend of an ever-increasing dependency ratio is clearly unsustainable (especially when linked to the forecast blow-out in age pension dependency among retired people which will occur as the population ages over the next 30 years). We are chasing our tails—the more people on welfare, the fewer people there are to support them and the greater becomes the disincentive to maintain self-reliance. Self-reliant, tax-paying workers are a wasting asset.

Figure 8. Proportion of working-age population receiving Unemployment, Disability and Single Parent payments in 1969 and 2002



Sources: Australian Bureau of Statistics, *Australian Social Trends 2001: Income and Expenditure, Income Support Among People of Workforce Age* (Canberra: ABS, 2002); ABS, *Year Book Australia 2003,* Cat. No. 1301.0 (Canberra: ABS, 2003).

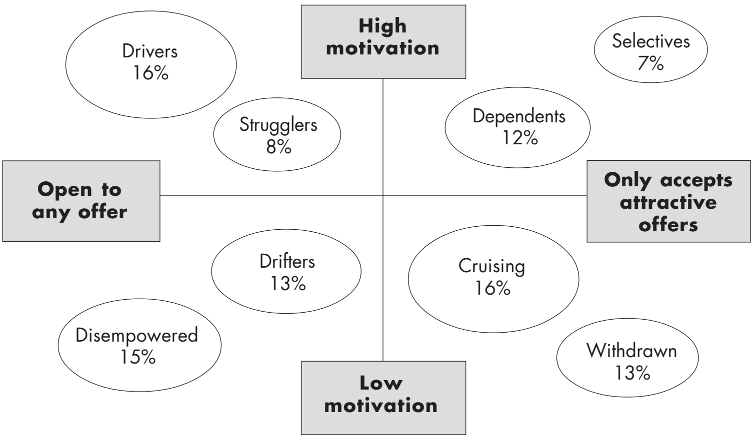
The increase in working-age welfare dependency has been concentrated in three main groups: the unemployed (benefits now cost $5 billion per year), people on disability support ($6.4 billion), and claimants of Parenting Payment Single ($5.6 billion). It is a key priority that we reduce dependency rates in all three.

Reforming unemployment benefits by introducing time limits

Half the people registering as unemployed find a job within eight weeks, but we have seen that half or more of those on unemployment allowances have been claiming benefits for more than a year. The longer a period of unemployment lasts, the weaker the motivation becomes to find a job. As time passes, people start to 'rationalise' their continued failure to find or keep a job, concluding that they are 'too old', or they 'cannot find suitable childcare', or employers 'discriminate' against them because of their race, or the jobs 'do not pay enough', or they are 'under-qualified' (or 'over-qualified'), or the job is 'dead-end' and demeaning, or they lack 'experience', or they are the 'victim' of a drug habit or some other 'barrier' that stops them from working. The expectation of failure becomes self-fulfilling. As Lawrence Mead puts it:

> Disadvantaged people without jobs find no end to reasons why working is impossible for them . . . They avoid personal responsibility and blame circumstances beyond their control . . . a mentality is at work that refuses to believe that opportunity exists, even when it does.[52]

Figure 9. Orientation to job search of people on unemployment allowances, 2002



Source: Colmar Brunton Social Research, *Job Seeker Attitudinal Segmentation: An Australian Model* (Canberra: DEWR, 2002); Labour Market Policy Group, *Job Seeker Attitudinal Segmentation* (Canberra: DEWR, May 2002).

In 2002 a report commissioned by the Department of Employment and Workplace Relations[53] found that about half of the unemployed could be said to exhibit low work motivation (Figure 9).

Elsewhere[54] I have argued that introduction of time limits on unemployment benefits would reduce long-term unemployment by strengthening what the Productivity Commission calls the 'compliance effect.' The Productivity Commission's *Independent Review of the Job Network* found that only 38% of people referred to Job Search Training (JST) in 1999 commenced with the programme.[55] Similarly only 68% of those referred to Intensive Assistance commenced. It seems that many people, when required to undertake these activities, leave welfare of their own accord (the Americans found much the same thing when they reformed welfare in 1996).

The Productivity Commission notes: '[C]ompulsory participation in programs can generate a *compliance* (or *motivation* or *deterrence*) *effect* whereby—to avoid having to participate in the program—some job seekers increase their job search activity and find employment, or those inappropriately claiming income support stop doing so because of their lack of availability for participation.' Work for the Dole (WFD) in particular has a very strong compliance effect—Dan Finn[56] reports that three-quarters of young people referred to 'Work for the Dole' schemes fail to attend the first session, preferring to leave welfare altogether rather than undertake part-time work.

Time limits linked to an extension of WFD could, therefore, be expected to have a substantial compliance effect, resulting in a significant reduction in the numbers of people unemployed for more than six months. The prospect of reverting to WFD at the end of six months would increase the sense of urgency among those looking for work and would drive out those whose commitment to finding a job is not serious as well as those who are currently defrauding the system. We might realistically expect a fall of up to 50% in the numbers of long-term unemployed under this proposal (more if the change were coupled with some of the labour market and tax reforms mentioned earlier in this paper). This adds up to nearly 200,000 claimants and an estimated net saving of around $2 billion dollars per year.

In August 2003, ACNielsen conducted a second opinion poll on behalf of CIS in which respondents were asked their views on the following proposal: *It has been suggested that unemployment benefits should be limited to a period of six months, after which people would be expected to participate full-time in a 'Work for the Dole' scheme until they find a job.*[57] Seventy percent agreed with the proposal (36.5% said it was a 'very good idea' and 33.5% thought it was a 'good idea'). Only 22% disagreed with it. Support was spread fairly evenly across all income groups and ages. It seems from this that time limits would meet with the approval of a large majority of Australians.

Reforming eligibility for Disability Support Pension (DSP)

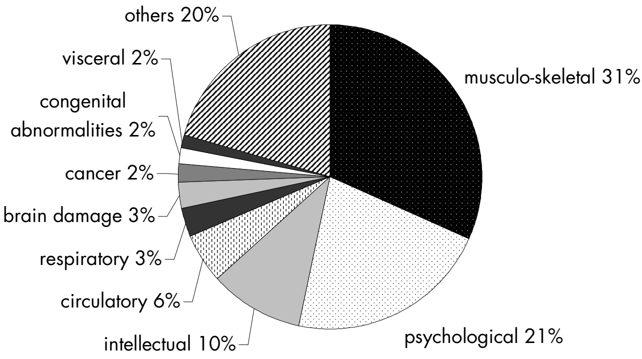
In 1980, just 2% of the working-age population was receiving a disability payment; today it is 5% (more than 625,000 people), and the proportion is still rising. The number of disability pensioners increased from 229,200 in 1980 to 602,300 in 2000.[58]

It has been shown that this increase has little to do with actual disability rates.[59]

Some disability pensioners suffer major impairments, but the most common conditions are 'musculo-skeletal' problems (for example, bad backs), which account for 32% of the total, and 'psychological/psychiatric' problems (not including intellectual and learning difficulties) covering another 22% (Figure 10). Such conditions can be debilitating, but they are rarely incapacitating. The OECD estimates that across western countries, only one-third of those on disability payments are suffering the sorts of 'severe disabilities' that make paid employment difficult or impossible.[60]

Australia's system of income support provides a strong incentive for unemployed people to have themselves reclassified as 'disabled'. People on Disability Pension are not currently subject to mutual obligation requirements as they receive their payments without having to undertake any activity tests or sign up to any participation agreements. They also receive a higher rate of payment than those on Newstart and are subject to a more lenient income test. Once on the Disability Pension, they normally stay there, undisturbed, until retirement (rates of exit from DSP other than through death or retirement are tiny).[61]

Figure 10. Main disability recorded for Disability Support Pension recipients aged 16-65



Source: Based on Australian Bureau of Statistics, *Australian Social Trends 2002: Income and Expenditure, Income Support, Trends in Disability Support* (Canberra: ABS, 2002).

Reviewing Centrelink file data, Bob Gregory has found that half of all disability pensioners in Australia are recruited directly from the unemployment rolls, and that the average time spent by these people on the Newstart Allowance before transferring to the Disability Pension is more than one year. This means that at least 300,000 of those claiming DSP have transferred out of long-term unemployment. Clearly, a significant proportion of those on DSP represent 'displaced unemployed' claimants, and it was in an attempt to reduce this flow of displacement that the federal government issued proposals to redefine 'inability to work' from its current 30 hours per week definition to 15 hours per week.

Such a move would certainly help stem the growth in DSP dependency, and it would be popular. In a CIS public opinion survey, respondents were told: *The proportion of working age people who are claiming Disability Pension has doubled to more than 600,000 in the last 20 years.* They were then asked whether or not they thought eligibility rules should be tightened (Table 2 overleaf). Nearly two-thirds thought they should and only one in five opposed it. Nevertheless, the government's proposal remains blocked in the Senate where the Opposition parties refuse to support it.

Table 2. Public opinion on tightening DSP eligibility rules:[62] *Do you agree or disagree that we should tighten up the rules for deciding whether somebody can claim Disability Pension?*

	Frequency	*Percent*
Strongly disagree	471	8.2
Disagree	772	13.5
Neither agree or disagree	747	13.1
Agree	2,022	35.3
Strongly agree	1,579	27.6
Don't know/No opinion	130	2.3
Total	5,721	100

Source: First CIS ACNielsen survey (see endnote 43).

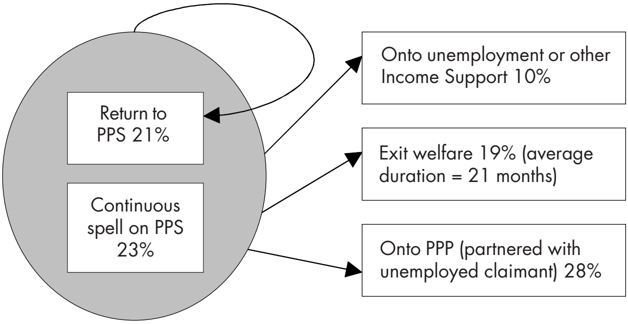
Reforming Parenting Payment

Parenting Payment is a welfare benefit paid as a wage supplement or replacement for a caring parent, single or partnered. It is not intended to cover the costs of raising children (parents get Family Tax Benefits and other allowances to help with this).

Australia is one of a very few western democratic countries that permits parents to remain on welfare benefits for as long as they have a child below the school-leaving age.[63] One in 10 of Australia's lone parents claim no government benefits at all, and another one in five rely on benefits for less than 20% of their total income. At the other extreme, however, one-third of lone parents have no income other than their welfare payment, and another 20% rely on welfare as their principal source of income.[64]

Bob Gregory has estimated that single parent claimants are spending an average of 12 years on benefits. His longitudinal research found that many lone parents who leave Parenting Payment Single do not leave welfare, but simply exchange one kind of benefit for another (Figure 11). Over a five year period, Gregory found that only one in five single parents went from welfare into financial self-reliance (either as a result of finding a job, or finding a new partner who was employed and who earned enough to support them).

Figure 11. What happened over the next 66 months to sole mothers on Parenting Payment in January 1995



Source: Based on Bob Gregory, Keynote Address to Australian Institute of Family Studies Conference (Melbourne, 2003).

For a single parent to stay at home, on benefits, for 12 years does no good either for the child or the parent. In the United States, researchers have found that children who grow up in welfare-dependent households probably do not suffer in early childhood, but as they approach adolescence, continued 'exposure' to welfare significantly damages their educational attainment.[65] As for the parents themselves, an extended period of welfare dependency means their skills and qualifications erode, their work-readiness decays, and their self-esteem plummets. It also means their income remains at a much lower level than would be the case if they were working, possibly at or below 'poverty level', depending on how that is defined. As Jocelyn Pech and Helen Innes suggest: 'The social security system might, under the guise of allowing women choice, be helping to entrench some in poverty and disadvantage.'[66]

If we were devising the welfare rules today, it would not occur to us to allow lone parents to stay on welfare for up to 15 years (or longer if they have more than one child), for it is now common for mothers to go to work once their children start school. Throughout most of the western world, sole parents are expected to return to the workforce once their children start school.

In a previous paper[67] I have argued that Parenting Payments (for sole parents and for coupled parents who claim Parenting Payment Partnered) should be payable in full only while a parent has responsibility for a child under the age of five. Once the youngest child starts school, the expectation should be that the parent will seek part-time work, and the rate of Parenting Payment should be adjusted accordingly. If these changes were introduced, even with no other reforms to the system, the annual saving on Parenting Payment Single alone would be over $1 billion.

As with the proposed changes to unemployment and disability payments, so too with Parenting Payments, a change like this would attract widespread support. Research on public attitudes conducted by SPRC finds that over half the population thinks it appropriate that sole parents should look for a part-time job once their youngest child starts school, and nearly half say sole parents should be expected to work full-time once their children reach 11 years of age.[68] A CIS opinion survey first told respondents: *Sole parents who look after a child and do not go out to work can currently claim Parenting Payment*, then asked when it is reasonable to expect a sole parent to work part-time. Table 3 shows that 84% thought sole parents should be expected to work at least part-time once their children have started school.

Table 3. Public opinion on reforming Parenting Payment Single: *When do you think it is reasonable to expect a sole parent to go out to work part time?*

	Frequency	*Percent*
By the time the youngest child reaches its first birthday	346	6.0
Once the youngest child is old enough for pre-school	1,906	33.3
Once the youngest child starts primary school	2,563	44.8
Once the youngest child goes to high school	488	8.5
Once the youngest child turns 16	354	6.2
Don't know/No opinion	64	1.1
Total	5,721	100

Source: First CIS ACNielsen survey [69]

Conclusion

The transition from a 20th century socialised mode of consumption to a 21st century privatised mode points to the need for linked innovations across five areas of public policy.

1. Labour market reform to get people into work

We have seen that the 'mass' problem of meeting people's basic consumption needs, which brought the welfare state into existence at the start of the 20th century, has now dwindled to become a minority, targetable problem. Despite the current size of our welfare rolls, probably no more than 5% of working-age adults should need long-term government aid and support, and they are people who, for one reason or another, cannot work or rely on others to support them. Poverty surveys exaggerate the size of the problem of necessary dependency by including people going through transitional periods of low income with those experiencing chronic long-term hardship. Sustained poverty is today almost entirely caused by lack of full-time paid employment, and the solution to it lies not in expanding welfare, but in getting more people who currently rely on welfare into the labour force. This means we have to ensure there are jobs for them to do—particularly lower-skilled, lower-paid jobs. The supply of lower-skilled jobs can only be expanded by further labour market reform (in particular, changing the award system and reforming the unfair dismissal laws).

2. Reform of the Income Support system

Although it sometimes seems to be forgotten, expanding welfare rolls are a sign of social policy failure, not success. The number of

Disability Pensioners has almost trebled in 30 years suggesting that 'disability' needs redefining. Numbers of single parent claimants have also escalated, and it would be in line with community expectations to reduce this number by expecting claimants to re-enter the labour force once their dependent children start school. Welfare rolls can also be cut by setting time limits on temporary assistance for unemployed claimants. American experience suggests that time limits, coupled with intensive one-to-one counselling, can dramatically reduce long-term welfare dependency rates, although there is also a strong case for government to be the job-provider-of-last-resort (that is, 'work for the dole') for those who exceed their welfare time limits.[70]

3. Reform universal services to end middle class welfare

Welfare services, such as public education and healthcare, benefit high and middle income earners almost as much as (and sometimes more than) low income earners. Many recipients do not need this help from government. Even under current arrangements, most 'middle income households' could afford to purchase their healthcare, education and retirement annuities from outside the state system, and many more could do so if government switched its funding from paying service producers to supporting service consumers. This could be achieved by phasing out direct provisioning in favour of subsidised purchases (for example, through tax allowances or vouchers to offset schooling costs).[71]

4. Tax reform to overcome simultaneous churning

The fundamental problem of Australia's means-tested, non-contributory income support system is that it inevitably creates 'welfare traps' and huge disincentive effects when recipients seek to improve their situation. Proposed tax credits for working households would exacerbate rather than resolve this problem. The solution lies in an increase in personal tax thresholds designed to bring us back to a position where low-paid workers pay no income tax and have no need for welfare top-ups. The present system of taking money with one hand and giving it back with the other has to be changed if high EMTRs are to be avoided. We currently start taxing workers at $6,000, yet this is well below the income required for self-reliance.

5. Savings reform to reduce lifetime churning

A large part of welfare expenditure involves intra- rather than inter-personal transfers as money is taken away at one point in the life cycle and returned at another. A more sensible and less costly alternative, which is consistent with the principles of the 'enabling state', would be to require or encourage wage earners to save and invest in their own personal accounts (which might be supplemented where necessary by means of 'matched savings', as in the United Kingdom and various experimental US schemes). The Australian compulsory superannuation scheme is a first step down this road, although this system needs reforming as well as expanding. In Singapore, personal accounts are now used to fund house purchases, education and new business formation as well as retirement, and in Chile, personal funds have recently been extended to provide unemployment insurance as well as retirement annuities.[72]

All five areas of policy change are important, but our immediate aim should be to reverse the rising trend in Income Support dependency by increasing self-reliance through employment wherever this is practicable. This suggests the following reforms as priorities:

a) First, there must be further **labour market** reform to increase the supply of jobs—*not* 'active labour market programmes' such as subsidies and an expansion of the public sector, for these either do not work or are very expensive, and they can end up destroying jobs in the real economy. Rather, an employment strategy designed to increase the availability of jobs for those at highest risk of long-term unemployment should seek to bring about:
   - A more flexible award system;
   - Reform to Unfair Dismissal laws and other job-destructive legislation;
   - A lower effective minimum wage (compensated by raised tax thresholds).

b) Second, we need to reform **income tax** to increase work incentives and rewards and reduce simultaneous tax/benefits churning and the high EMTRs that result from it. This is best achieved by:

   - Raising personal tax-free thresholds at least to the equivalent household welfare minimum levels so that (in principle) nobody who pays income tax receives welfare, and nobody on welfare pays income tax;[73]
   - Reducing punitive higher rates with a view (longer term) to establishing a flat rate income tax.

c) Third, we must radically reform the **Income Support system** to reduce long-term dependency rates. This can be done by:

   - Introducing time limits on unemployment benefits to increase the compliance effects of Work for the Dole (estimated 50% reduction in unemployment over 6 months duration);
   - Accepting tighter eligibility rules for DSP to stop displacement from unemployment into disability and to re-establish a clear distinction between those who are expected to work and those who are not (the target should be a return to the 1980 level of DSP claims—a reduction of 150%);
   - Expecting part-time work by parents with school-age children and adjusting the value of Parenting Payments accordingly (possible saving around $1 billion per annum).

The welfare state as it currently exists in Australia is an anachronism, designed to meet the needs of an age that has past, and increasingly doing more harm than good. To extricate ourselves from this institutional legacy, the first step must be to reverse the 40 year trend of growing expenditure and escalating dependency. After that, we can start developing innovative policies to restore self-reliance.

Endnotes

1 P. Saunders, *Social Theory and the Urban Question, Second Edition* (London: Hutchinson, 1986), ch. 8.

2 Although many working class people could and did make provision for themselves even then. See D. Green, *Mutual Aid or Welfare State* (Sydney: Allen & Unwin, 1984).

3 T. H. Marshall, 'Citizenship and Social Class', in *Citizenship and Social Class and Other Essays* (Cambridge: Cambridge University Press, 1950)

4 J. O'Connor, *The Fiscal Crisis of the State* (New York: St Martins Press, 1973).

5 This idea of the state as enabler has more recently been developed as part of a 'third way' political agenda. See, for example, P. Botsman and M. Latham (eds.), *The Enabling State* (Annandale: Pluto Press, 2001).

6 As Michael Duffy puts it: 'If the sheep can look after themselves, they will not need shepherds' (*The Australian,* 7 October 2002).

7 There is an unthinking tendency still to equate socialist ideas with personal morality. As David Green notes: 'For decades, capitalism has been characterized as callous and uncaring and socialism as humanitarian. The result is that it takes quite an effort for intellectuals to break with socialism because, at first, the choice seems to be as stark as that between good and evil'. See David Green, *Equalizing People* (London: IEA, 1990), p.3.

8 According to Michael Jones, 'In 1971, Australia had a minimal welfare state', *The Australian Welfare State Fourth Edition* (Sydney: Allen & Unwin, 1996), p.27. Henderson's crucially influential survey of poverty in Melbourne was published in 1970.

9 I have discussed some of the claims currently being made by the poverty lobby in Australia in P. Saunders and K. Tsumori, *Poverty in Australia: Beyond the Rhetoric* (Sydney: The Centre for Independent Studies, 2002).

10 See D. Gordon, 'Measuring Absolute and Overall Poverty', in D. Gordon and P. Townsend, *Breadline Europe* (Bristol: Polity Press, 2000); David Gordon, *Poverty and Social Exclusion in Britain* (York: Joseph Rowntree Foundation, 2000). The estimate of 26% of the population in poverty is based on the number of respondents who claimed to be unable to afford at least two from a list of 29 'socially necessary' items. The 17% of Britons who think they live below the United Nation's absolute poverty line apparently believe that they

suffer from life-threatening conditions such as unclean drinking water, lack of sanitation, shortage of food and absence of health and education services.

11 The Henderson line is regularly updated by the Melbourne Institute and latest poverty estimates are published on its website (www.melbourne institute.com/). For a discussion of issues regarding the method of updating, see H. Greenwell, R. Lloyd and A. Harding, 'An Introduction to Poverty Measurement Issues', NATSEM *Discussion Paper* No. 55 (Canberra: NATSEM, 2001).

12 C. Whelan, R. Layte, M. Maitre, B. Nolan. 'Persistent Income Poverty and Deprivation in the European Union', *European Panel Analysis Group Working Paper* No. 17 (Dublin: Economic and Social Reearch Institute, 2001). Australian data should become available shortly as the HILDA survey moves into successive waves.

13 Department of Family and Community Services, *Trends in Pension and Benefit Receipt,* Research FaCS Sheet No. 2 (Canberra: FaCS, 1999); P. Whiteford and G. Angement, *The Australian System of Social Protection: An Overview,* FaCS Occasional Paper No. 6, Second Edition (Canberra: FaCS, 2001).

14 There are two of us with the same name (but very different ideas) working on social policy issues in Australia. My namesake is Director of the Social Policy Research Centre (SPRC) at the University of New South Wales and is one of Australia's leading defenders of high levels of welfare provision.

15 R. Bray, 'Poverty Lines and Living Standards', Paper to FaCS seminar on 'Hardship in Australia' (Sydney, 2 September 2002); P. Saunders, *The Ends and Means of Welfare* (Melbourne: Cambridge University Press, 2002); H. Hughes, 'The Politics of Envy', *Policy* (Winter 2001).

16 A. Harding, R. Lloyd, H. Greenwell, *Financial Disadvantage in Australia 1990-2000* (Sydney: The Smith Family, 2000).

17 R. Haskins, 'The Poor Go to Work', *The American Enterprise* (April/May 2002), 41; also 'The Welfare Watershed', *Wall Street Journal* (13 May 2002).

18 I have analysed the desire to own in *A Nation of Home Owners* (UK:Unwin Hyman 1990). This does seem to be particularly marked in the 'Anglo' cultures, or what Esping Anderson calls the 'liberal' welfare state regimes.

19 See Lucy Sullivan *Taxing the Family* (Sydney: The Centre for Independent Studies, 2001). We are now in the absurd position where taxation begins at a level of income well below subsistence level, and individuals and families then have to be given support to bring them back up to this level. This, of course, is why modern governments are confronted with a seemingly insoluble problem of 'poverty traps' and 'welfare traps': if those on low incomes paid no tax, they would not need so much welfare support, and they would not then be penalized by high effective marginal tax rates when they start to earn more. I shall develop this point more fully later in this Paper.

20 J. Cox, *Middle Class Welfare* (Wellington: NZ Business Round Table, 2001).

21 A. de Jasay, *The State* (Indianapolis: Liberty Fund, 1998), ch. 4.

22 ABS, *Government Benefits, Taxes and Household Income 1998-99,* Cat. No. 6537.0 (Canberra: ABS, 2001).

[23] Des Moore, 'Election on Jobs a Good Wager', *The Australian Financial Review* (22 January 2003); ABS, *Government Benefits.*

[24] R. Hills and K. Gardiner, *The Future of Welfare* (York: Joseph Rowntree Foundation, 1997), p.19.

[25] *The Australian System of Social Protection—An Overview,* FaCS Occasional Paper No. 6, Second Edition (Canberra: FaCS, 2001).

[26] A. Harding, *Lifetime Income Distribution and Redistribution* (Amsterdam: North-Holland, 1993), p.168, emphasis in original. See also Harding, 'Lifetime Versus Annual Tax-Transfer Incidence', *The Economic Record* 69:205 (June 1993), p.179-91.

[27] Health is modelled in a later paper, see A. Harding, R. Percival, D. Schofield and A. Walker, 'The Lifetime Distributional Impact of Government Health Outlays', NATSEM *Discussion Paper* 47 (Canberra: NATSEM, February 2000).

[28] I have summarised some of these initiatives in P. Saunders, 'What Future for Welfare?', *Occasional Paper* No. 11 (Sandton, SA: Free Market Foundation, 2002).

[29] R. Goodin and J. LeGrand, *Not Only the Poor: The Middle Classes and the Welfare State* (London: Allen and Unwin, 1987).

[30] Saunders, *Ends and Means of Welfare,* p.59.

[31] In addition to David Green's work on Australia, see also: D. Green *Reinventing Civil Society* (London: IEA, 1993) and D. Beito *From Mutual Aid to the Welfare State* (Chapel Hill: University of North Carolina Press, 2000).

[32] Tony Eardley, Peter Saunders, Ceri Evans, *Community Attitudes Towards Unemployment, Activity Testing and Mutual Obligation,* SPRC Discussion Paper No.107 (Kensington: University of New South Wales, 2000).

[33] The latest example is from ACOSS, quoted in *The Australian*, 30 January 2003: 'Mr McCallum said it was up to the federal and state governments to try to redress the social divide. "We forget that good economic growth does not impact society equally," he said. "The consequences are that society pays one way or the other. We pay for it through social control or we pay for it through good social policies . . ."'

[34] See P. Saunders, *Capitalism: A Social Audit* (Buckingham: Open University Press, 1995), ch. 4; P. Saunders 'Citizenship in a Liberal Society', in B. Turner, *Citizenship and Social Theory* (London: Sage, 1993); Saunders and Tsumori, *Poverty in Australia*, ch. 4.

[35] P. Berger and R. Neuhaus, *To Empower People* (Washington: American Enterprise Institute, 1987); P. Botsman and M. Latham, *The Enabling State*.

[36] M. Novak, *Morality, Capitalism and Democracy* (London: IEA, 1990), p.13.

[37] N. Abercrombie et al, *Sovereign Individuals of Capitalism* (Sydney: Allen & Unwin, 1986).

[38] Some people, of course, are not capable of working and should not be expected to. This is recognised in our existing welfare system in the distinction between unemployment allowances and pensions, although we shall see that this distinction has become increasingly blurred and that many people on pensions

could and should arguably be expected to work. Responding to this blurring, the 2000 McClure Report recommended replacing the existing system of benefits with a single payment, but this would arguably make matters worse. See Peter Saunders, CIS submission to House of Representatives Inquiry into *Reform of Income Support for Working Age Australians*, available at www.cis.org.au.

39 One idea for how this might be achieved (see Barry Maley, *Family and Marriage in Australia* [Sydney: The Centre for Independent Studies, 2001]) is that all children should be given their own tax-free allowance (or a refundable tax credit) which could be claimed on their behalf by their parent/s and added to their own personal tax-free allowance/s. No other income supplements would be paid, and these child allowances would not be means-tested (thereby avoiding the problem of high EMTRs while increasing horizontal equity between households).

40 CIS Submission to the House of Representatives Standing Committee on Employment and Workplace Relations Inquiry into *Increasing Participation in Paid Work*, available at www.cis.org.au

41 Frank Field, *Welfare Titans,* (UK: Civitas, 2002).

42 Shaun Wilson & Trevor Breusch, 'Taxes and Social Spending', *Australian Journal of Social Issues* (2003).

43 The survey comprised 5,721 respondents taken from the Australian Internet User Survey in March 2003. The sample was weighted by gender, age, state of residence and annual income to bring it into line with population estimates by the Australian Bureau of Statistics and appears valid on tests of external validity (comparing with marital status and voting preferences). Further details available on request.

44 Martin Evans, *Welfare to Work and the Organization of Opportunity,* CASE Report No.15 (London: London School of Economics, 2001), p.49.

45 John Martin, 'Labour Market Programs' in Business Council of Australia, *New Directions: Rebuilding the Safety Net* (Melbourne: BCA, 2000), pp.94-7. Deadweight effects occur when jobs that would have been created anyway attract subsidies. Displacement effects occur when target groups get jobs as a result of a subsidy but displace other workers who would have gained employment had the subsidies not changed employers' selections.

46 John Martin, 'Labour Market Programs', p.100.

47 John Martin, 'What Works Among Active Labour Market Policies', *OECD Economic Studies* No. 30 (Paris: OECD, 2000/01), p.98.

48 Productivity Commission, *Independent Review of the Job Network* (Canberra: PC, 2002), p.1.3.

49 Kayoko Tsumori, *Poor Laws (3): How to Reform the Award System and Create More Jobs,* Issue Analysis No. 41 (Sydney: CIS, 2003).

50 Kayoko Tsumori, *Poor Laws (2) The Minimum Wage and Unemployment,* Issue Analysis No.28 (Sydney: CIS, 2002).

51 Kayoko Tsumori, *Poor Laws (1) The Unfair Dismissal Laws and Long-term Unemployment*, Issue Analysis No.26 (Sydney: CIS, 2002).

52 Lawrence Mead, *The New Politics of Poverty* (New York: Basic Books, 1992), pp.143-5.

53 Colmar Brunton, *Job Seeker Attitudinal Segmentation: An Australian Model* (Canberra: DEWR, 2002).

54 Peter Saunders, 'How to Reduce Long-term Unemployment', *Issue Analysis* No. 40 (Sydney: CIS, 2003).

55 Canberra, 2002, p.5.14.

56 Dan Finn, *A New Deal for Unemployed Australians?* (Melbourne: Dusseldorp Skills Forum, 2001).

57 This is a different survey from the one referred to earlier (see footnote 41). The target population of this second survey was 1,850 internet users, of whom 467 (25%) responded in August 2003. The sample appears representative of the Australian population as a whole when checked against national data on age, gender, income, state and region, and has not therefore been weighted

58 ABS, *Australian Social trends 2002: Income and Expenditure* (Canberra: ABS, 2002).

59 E. Healy, 'Disability or Disadvantage', *People and Place* 10 (2002), pp.68-83.

60 'Disability Programmes in Need of Reform', *OECD Policy Brief* (Paris: OECD, March 2003), p.2.

61 See John Landt and Jocelyn Pech, 'Work and Welfare in Australia', *Australian Social Policy* 2000/2 (Canberra: FaCS, 2000); also 'Why Has the Disability Program Grown So Much?', Report on seminar by Bob Gregory, *FaCS Research News* No.15 (Canberra: FaCS, March 2003), pp.13-14.

62 For survey details, see note 43.

63 The UK does not require lone parents to rejoin the labour force until their children reach school-leaving age, but most other countries have tighter expectations. In the US, 1988 legislation reduced from 6 to 3 the age of child at which lone parents were exempt from work requirements, and since 1996 this has been left to individual states to determine. Germany and the Netherlands have both extended labour force participation requirements for single parents to those with primary school age children, and in France, participation is assumed to occur once the youngest child reaches three. See Martin Evans, *Welfare to Work and the Organisation of Opportunity*, Case Report No.15 (London: London School of Economics, 2001). In Denmark, Sweden and Norway, it is expected that sole parents will actively seek paid employment once a child reaches three years of age. See Tony Eardley, Peter Saunders, Ceri Evans, *Community Attitudes Towards Unemployment, Activity Testing and Mutual Obligation,* SPRC Discussion Paper No.107 (Kensington: University of NSW, 2000), p.29. In contrast, the 'Australians Working Together' package introduced in September 2003 requires single parents with children of primary school age to attend one Centrelink interview per year, and those whose children are at senior school now have to undertake an average of six hours per week of some recognized activity such as community work or training.

64 Peter Whiteford and Gregory Angenent, *The Australian System of Social Protection: An Overview,* FaCS Occasional Paper No. 6, Second Edition (Canberra: FaCS, 2002), Table 9.

65 Inhoe Ku and Robert Plotnick, 'Do Children From Welfare Families Obtain Less Education?', *Demography* 40:1 (2003), 151-70.

66 FaCS, 'Women in the Australian Labour Market', *Social Security Journal* (1998/99), p.23.

67 Peter Saunders and Kayoko Tsumori, *The Tender Trap*, Issue Analysis No.36 (Sydney: CIS, 2003).

68 T. Eardley, P. Saunders and C. Evans, 'Community Attitudes Towards Unemployment, Activity Testing and Mutual Obligation', *SPRC Discussion Paper* No. 107 (Kensington: University of NSW, 2000).

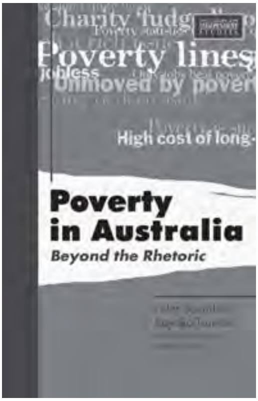
69 For survey details, see note 43.

70 On the case for government as employer of last resort, see D. Ellwood, *Poor Support: Poverty in the American Family* (New York: Basic Books, 1988); and D. Ellwood, 'The US Vision of Work-based Reform', in T. Eardley and B. Bradbury (eds), *Competing Visions,* SRC Report 1/02 (Sydney: SPRC, April 2002).

71 See, for example, J. Buckingham, *Families, Freedom and Education* (Sydney: CIS, 2001) on how schooling could better be funded by a system of tax allowances.

72 On American experience with personal savings initiatives, see M. Sherraden, 'From Research to Policy: Lessons From Individual Development Accounts', *Journal of Consumer Affairs* 34 (2000), pp.159-81, and M. Schreiner et al., *Savings and Asset Accumulation in IDAs* (Washington: Centre for Social Development, 2001). On recent UK initiatives, see HM Treasury, *Saving and Assets for All,* (London: HM Treasury, 2001). On recent developments in Chile, where individual investment accounts to cover retirement have now been extended to provide personal unemployment insurance as well, see W. Conerly, 'Chile Leads the Way with Individual Unemployment Accounts', *Brief Analysis* No.424, (Dallas: National Centre for Policy Analysis, November 2002).

73 As noted earlier, the details of how this would work have yet to be finalised, but a system of tax-free thresholds above the welfare level coupled with flat-rate allowances or credits for dependent children should be enough to ensure that all working families end up with an income above the welfare level, that no working family receives welfare other than a child allowance, and that the transition from welfare to work does not entail high EMTRs. A similar result might also be possible by setting a zero tax rate at low levels of income, and gradually increasing this rate as total income rises (CIS hopes to publish a paper on this alternative proposal early in 2004).



Poverty in Australia

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