The Welfare State: Foundations & Alternatives

Social Welfare Research Program

Michael James (ed.) • David Band • Charles Murray • David Willetts • Alan Woodfield • James Cox • Susan St John • Suzie Kerr • John Logan • Peter Swan

The Welfare State

Foundations and Alternatives

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The Welfare State

Foundations and Alternatives

edited by Michael James

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PANEL DISCUSSIONS

Editorial Note

This book records the combined proceedings of two conferences held in November 1987: the first in Wellington, the second in Sydney.

The papers by Michael James, David Band, Charles Murray, David Willetts, and Alan Woodfield were given at both conferences. James Cox, Susan St John and Susie Kerr presented papers at the Wellington conference, where Hugh High commentated at the first session and Claudia Scott at the second. In Sydney, where the commentators were Martin Krygier and James Cox, papers were given by John Logan and Peter Swan.

Charles Murray and David Willetts were panel members at both conferences. Edited versions of the two panel discussions are reproduced separately at the end of volume.

I am grateful to all the participants for their cooperation in expediting this record of the conference proceedings. Above all I wish to thank Garth Nix for his assistance — indeed his dogged persistence — in reducing the multifarious conference materials to a coherent and readable form.

Michael James

Introduction

Michael James

In recent years, political pressure to reduce tax burdens and to encourage faster economic growth has led several Western countries to undertake reviews of their social security systems. Australia and New Zealand have been no exception. New Zealand's Royal Commission on Social Policy submitted its final report in 1988; in Australia, the Social Security Review established within the Department of Social Security has been issuing a continuous stream of studies since mid-1986. The UK and the US are likewise in the process of revising their social policies in the light of systematic and comprehensive policy reviews.

These official policy reviews have proceeded from the assumption that the welfare state should continue to exist but should be made more efficient; hence the widespread shift recently (very marked in Australia, less so in New Zealand) towards selective, means-tested benefits rather than universal ones, and towards replacing automatic unemployment benefits, especially for the long-term unemployed, with training schemes and other devices for encouraging re-entry into the workforce. The US and, to a lesser extent, the UK, have also begun to change the moral basis of their welfare systems by insisting that welfare recipients should, where possible, undertake work or training as a way of repaying their debts to the society that provides for them.

The CIS Social Welfare Research Program seeks to widen the terms of the debate by examining the intellectual foundations of the welfare state and by canvassing alternatives to state welfare that remain outside the scope of the official policy reviews. Some of the papers in this volume reflect the rationale behaind current policy changes and go on to recommend that they be extended more widely. Other papers, however, raise the question of whether the welfare state can in principle be reformed. The phenomena of 'dependency' (the creation of incentives to behave so as to qualify for benefits) and of 'political capture' (whereby influential lobbies manipulate the redistributive process to their own advantage) may be ineradicable features of all state welfare systems and may in the long run erode the fiscal gains that flow from attempts to target benefits to the genuinely needy. Even more fundamental are the moral issues raised by the tax-transfer system. Can it ever be acceptable for the state to make compulsory levies on some citizens and to redistribute the proceeds to others? Conversely, is it morally right to distribute benefits in a way that may deprive individuals of the personal challenges that give meaning to their lives? (This last question is the special concern of Charles Murray, whose book *Losing Ground* has, since it was published in 1984, transformed the welfare debate in the US and profoundly affected it elsewhere in the West.)

The possibility that the welfare state may suffer from insoluble efficiency problems and may rest on morally flawed foundations has led some of its critics to look favourable on voluntary and private income transfers and insurance systems as alternatives to state welfare programs. Much of this volume is devoted to exploring reforms of this kind that would restore to individuals greater control over their own incomes and eliminate much of the coercion that is a necessary feature of political processes. Crucial to this approach is the evidence (some of which is cited in this volume) that state welfare is not so much a necessary supplement to voluntary effort as a hindrance to its expansion.

The emphasis of the volume is thus on questioning the means employed by the welfare state rather than the goals it officially serves. In some ways this approach is more difficult to canvass in Australia and New Zealand than in some comparable countries with similar welfare systems. Although both countries have long enjoyed vigorous networks of voluntary welfare provision, their political traditions have always accorded primary responsibility for welfare to the state. By the turn of the 20th century Australia and New Zealand had taken the lead among the English-speaking countries in establishing compulsory state insurance schemes of the kind already pioneered by Germany. In addition, they gave the state a crucial role in determining the 'primary' distribution of income by such means as centralised wage-fixing. In 1930, Sir Keith Hancock, in his book *Australia*, characterised Australia's dominant political philosophy thus: 'Australian democracy has come to look upon the State as a vast public utility, whose duty it is to provide the greatest happiness for the greatest number'. The British philosophy of utilitarianism, which has always faced a measure of competition on its home ground from the liberal tradition, established a virtual monopoly in Britain's antipodean colonies.

In the 1980s this has begun to change. Australia and New Zealand have again attracted international attention, this time by demonstrating how far Labor governments can go in freeing their economies from state control. Policy-makers and the general public have accepted that government intervention does not necessarily improve on the outcomes of voluntary action.

This more realistic appraisal of governments' capacity to do good is beginning to call into question the state's near monopoly of expenditure on social welfare. It is to be hoped that the 1990s will witness not only a renewed appreciation of existing non-state forms of welfare provision but also the discovery and development of fresh ones.

Welfare, Coercion and Reciprocity

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Welfare, Coercion and Reciprocity

Michael James

I. INTRODUCTION

In their recent efforts to cope with their fiscal crises, Western governments have been careful to cut welfare spending in ways acceptable to public opinion. The means- testing of previously universal benefits such as the family allowance reflects a growing public demand that welfare should be targeted to the worst-off. The withdrawal of unemployment benefits for teenagers eligible to remain at school implies acceptance of the widespread belief that those benefits actually discourage young people from either finding work or preparing themselves for working careers. Governments have also responded to public fears of growing tax evasion and welfare fraud. The Australian government's abortive attempt in 1987 to introduce a national identity card system explicitly assumed that these problems were together worth about $1 billion annually. True, the proposed card was deeply unpopular, but none of its opponents denied the existence of the problem it was intended to solve.

Behind the common complaints about the misallocation of welfare benefits and the dependency and petty criminality they encourage lies a disillusionment with the welfare state and an uncertainty about its legitimacy. When the welfare state was being constructed in the decades following World War II, it was sustained by an enthusiastic and idealistic consensus around its three major goals. These were: the reduction of social and economic inequality; the satisfaction of certain basic individual needs as of right; and the expression and encouragement of compassionate and communitarian relationships between citizens. But the welfare state has, by common consent, failed to live up to expectations. Socio-economic inequality remains undiminished and may even be increasing. Some people still live impoverished and disadvantaged lives because certain basic needs go unattended. Interpersonal relationships are not noticeably more marked than previously by neighbourly concern; on the contrary, the welfare state has become a focus of increased social divisiveness.

What then has gone wrong? A major problem at the intellectual level has been an almost exclusive concern with the ends of the welfare state as opposed to the means it employs. Its architects thought that once a consensus on the goals of the welfare state had been created, the democratic state would implement them virtually automatically. We now know better. We know that individuals do not necessarily behave so as to fulfil the official purposes of the welfare state, but to some degree adapt their behaviour to the pattern of incentives that the welfare state creates.

The welfare state generates two broad kinds of counterproductive incentives. First, many welfare programs encourage individuals to adjust their behaviour so as to qualify for the benefits they bestow. Second, the political process, which gives temporary legislative majorities unconstrained powers to tax and redistribute, encourages pressure groups to organise and lobby for welfare policies that favour them. These incentives would not have mattered very much had the welfare state succeeded in fostering the altruism and sense of mutual obligation that its founders believed it would. But their effect has been the opposite. The widely observed phenomena of middle class welfare on the one hand and welfare dependency on the other should therefore be seen, not as aberrations to be corrected by policy adjustments, but as systematically predictable outcomes of the modern welfare state.

In Section II of this paper I criticise the standard case for the welfare state by reference not to its goals but to its misleading assumptions about the contrast between political processes and voluntary processes. In Section III, I support this criticism by arguing that the modern welfare state shows no signs of realising its own ideal of equality, and that recent attempts by some defenders of the welfare state to come to terms with 'middle-class welfare' are likely to be self-defeating. In Section IV, I examine the scope for a revival of voluntary welfare provision by private individuals. Such provision is often described rather disparagingly as 'charity'. My concern is to promote the idea of 'reciprocity', which includes some kinds of charity as well as other non-market activities that promote welfare. Not only has Australia, along with other countries, enjoyed a long tradition of effective voluntary mutual aid organisations, but recent studies of reciprocity have indicated its important continuing role, actual and potential, in welfare provision.

I should stress that I am not arguing that the state should have no role at all in welfare provision, or even that such a role should be limited to last-resort relief of destitution. The means employed by the welfare state ensure that any putative consensus about its goals will be eroded over time by behavioural adaptations and ordinary democratic politics. But the welfare state has also raised legitimate expectations that must be respected by the political system. The attraction of voluntary welfare is precisely that it offers a way of meeting those expectations that avoids the tensions induced by the welfare state's collectivist decision-making procedures. Voluntary welfare provision is therefore likely to grow in response to the welfare state's crisis of legitimacy. One of our tasks is to find ways of handling the transition so that the benefits of voluntary systems of welfare delivery become available as quickly and as widely as possible. In the concluding section I suggest some policy principles that may help achieve this.

II. THE CITIZENSHIP THEORY OF THE WELFARE STATE

The Three Goals of Citizenship Theory

The traditional case for the modern welfare state amounts to what one of its most recent defenders, David Harris, has called the 'citizenship theory'. This theory holds that 'the welfare state is rooted in a conception of what it is to be a full member of a community and the social rights that are necessary to protect and reinforce that membership' (Harris, 1987:27). Citizenship theorists defend the welfare state by reference to a wide range of policy goals, but the leading ones, as indicated in the Introduction, are equality, altruism, and the satisfaction of needs-based welfare rights.

Equality is arguably the central policy goal of the welfare state, but the degree of state intervention thought necessary to achieve equality has steadily declined over time. In his book *Equality*, first published in 1931, R. H. Tawney elaborated a 'strategy of equality' involving three kinds of intervention: first, progressive taxation and income redistribution; second, industrial regulation; and third, public enterprise (1961:126).

More than 40 years later, this strategy was updated by Anthony Crosland, a leading British socialist intellectual. Crosland argued that the welfare state should promote equality in the widest possible sense, going far beyond equality of opportunity and 'embracing the distribution of property, the educational system, social class relationships, power and privilege in industry' (1975:2). But he thought that this could be done without extensive public ownership, since the economic growth generated by the post-war mixed economy could be relied upon indefinitely to finance painless redistribution.

Most recently, Raymond Plant, a leading member of the British school of 'market socialism', has argued that the state should promote 'the central redistribution of resources produced within the market sector so as to secure greater equality of outcome as well as initial economic conditions'. But he wants this redistribution to be done by way of statutory rights rather than administrative discretion, and, where possible, to take the form of cash grants rather than benefits in kind. 'This', he writes, 'puts power into the hands of citizens rather than bureaucracies and welfare professionals, and makes bureaucracies more accountable to democratic machinery' (Plant, 1987:15).

The second goal that supporters of state welfare believe it promotes is altruism. The best-known defender of state welfare from this standpoint is Richard Titmuss. In his book *The Gift Relationship* (1974), Titmuss celebrates the voluntary donation of blood as the archetypal act of compassion and the symbol of what the welfare state stands for. This is not so much because blood is freely given rather than sold for profit, but because the gift is a unilateral transfer to a 'stranger', and not performed in recognition of any reciprocal rights and obligations of the kind that bind together people related by particular ties. The anonymity and impersonality of the gift enable the donor to give without being condescending, and the recipient to receive without feeling dependent or stigmatised. Titmuss is not trying to tap our altruism so that it generates the maximum amount of welfare; rather, he wants social policy to be based on gift relationships so that it promotes altruism and improves us morally.

Titmuss's case for the welfare state has been a popular one, and has given currency to the view that the degree of compassion in a community is measured by the level of its public spending on welfare. But some members of the citizenship school argue that Titmuss's approach fails to provide an adequate guarantee that the individual's welfare needs will be recognised, precisely because it relies exclusively on the rather risky factor of the spontaneous generosity of anonymous donors (Watson, 1980:157).

The argument that the citizen has a right to welfare that the community is strictly obliged to provide forms the third major justificatory foundation of the welfare state. T. H. Marshall, a leading member of the citizenship school, argues that individuals have social rights in the sense that the community has an obligation to ensure that their basic welfare needs are satisfied. The content of those needs depends on the prevailing standards of citizenship: as community standards rise, our needs expand and our social rights multiply. 'The modern rights to education and health are not merely recognised by all as being social in origin, but are part of the mechanism by which the individual is absorbed into society (not isolated from it) and simultaneously draws upon and contributes to its collective welfare' (Marshall, 1981:91).

More recently, some defenders of citizenship theory against its liberal critics have attempted to put the link between needs and rights on a more secure philosophical footing. Raymond Plant argues that we all have needs that are basic in the sense of being the necessary conditions of moral action; these conditions include physical survival and autonomy, i.e. freedom from arbitrary coercion and security against illness and ignorance (Plant et al.

1980:51). The obligation to satisfy these basic needs must be recognised by the members of any moral community. If we assume that individuals are moral beings and can incur moral obligations, we are committed logically to ensuring that they have the means to fulfil those obligations. In that sense, we each have an entitlement to welfare (Plant et al, 1980: 93-4).

The Market vs. the State

The citizenship school has devoted most of its intellectual effort to identifying and elaborating the goals that the welfare state should serve. But the ideological heart of the case for the welfare state lies in a set of underlying assumptions that are not always completely articulated or defended. These assumptions are, first, that the goals of the welfare state cannot be achieved by non-state mechanisms, and second, that the welfare state can achieve them. In practice, this amounts to claiming that the welfare state is needed to remedy the defects of the market. The arguments are familiar: the market causes economic inequality that can be rectified only through government services and tax-transfer systems; the market makes people selfish, whereas the welfare state embodies and promotes altruism; the market responds to wants rather than needs and so can leave some basic needs unsatisfied. 'Citizenship writers looked to the state as an instrument to correct the inadequacies of the market and to realize values which market relations could not exemplify' (Harris, 1987:27).

These assumptions, which have penetrated very deeply into the way we think about public policy, stem from the critique of *laissez-faire* that gained currency towards the end of the 19th century and paved the way for the emergence of big government and the welfare state in the twentieth. One obvious source of them is Marxism. Marx presented an immensely powerful image of the free market not only as the source of growing poverty and inequality but also as a wasteful and irrational system, doomed to give way to a collectively and rationally planned social order. But a more precise statement of the citizenship school's basic assumptions is to be found in the work of J. S. Mill. In *Principles of Political Economy*, first published in 1848, Mill posited a significant difference between the production and the distribution of wealth. Production was governed by inexorable and unalterable laws that resembled 'physical truths'; no amount of human will or desire could increase the national product beyond the level made possible by the existing amount of capital, skill and technology (Mill, 1970:349-50). Distribution was a different matter:

> That is a matter of human institution only. The things once there, mankind, individually or collectively, can do with them as they like.

> They can place them at the disposal of whomsoever they please, and on whatever terms. Further, in the social state any disposal whatever of them can only take place by the consent of society, or rather of those who dispose of its active force. Even what a person has produced by his individual toil, unaided by any one, he cannot keep, unless by the permission of society. (1970:350)

This distinction reflects the origins of Mill's thought in utilitarianism, which requires the state to redistribute income and property so as to produce the greatest amount of human welfare. It was continued by Mill's successors such as T. H. Green, and the later school of 'new liberalism', which had a profound influence in legitimising state welfare in Britain in the early years of this century. The separation between production and distribution appears also in the more overtly socialist movements that began to flourish around the same time, such as the Fabian Society in Britain and the 'revisionist' school of evolutionary socialism in the German Social Democratic Party. These thinkers rejected the strict Marxist view that inequality in distribution was one of the laws of capitalist production, and so could not be remedied until the capitalist system as a whole had been swept away. Instead, they aimed to come to power through peaceful democratic methods and then to use the power of the state to construct a rational and just social order by whatever interventions were necessary for the purpose.

This strong contrast between the quasi-physical laws that govern production and the changeable human institutions that govern distribution underlies the common view that economics is a world of necessity whereas politics is a world of freedom: that the market rewards or penalises us according to its own remorseless and coercive logic, whereas the state expresses our collective will to fashion our lives according to our own ideals. This is why the idea of citizenship is so important in the traditional defence of the welfare state: as economic beings we may win or lose in ways that we cannot control, but as citizens we can all be winners together.

It is precisely at the level of its most basic assumptions that citizenship theory is most vulnerable to criticism. The view that the state is the community's instrument for implementing its freely determined solutions to the problems created by the market leads both to the misinterpretation of those problems and to utopianism in policy responses. A good example of this in Australia in recent years has been unemployment, and especially unemployment among youth, which is about twice the national average. The standard response has been to treat unemployment as evidence of market failure, and then to devise appropriate policy responses to cure it, such as maintaining aggregate demand, job creation and training schemes, and so on. These have not been a notable success. The problem is that 'market failure' (or, more crudely, 'the capitalist system') is not really an explanation but rather an ideological substitute for one. It serves to allow policy makers to concentrate on looking for interventionist solutions, since it is already assumed that such solutions **must** exist if only we try hard enough to find them. But it is now widely accepted that unemployment is very largely an unintended consequence of previous interventions, such as the centralised wage-fixing system, unemployment benefits for school-age teenagers, inappropriate curricula in the state schools, and so on. The real issue that faces the policy-makers is whether those earlier policy errors can be rectified in the teeth of opposition from the many special interests that benefit from them. Curing market failure nowadays looks much easier than curing government failure.

Voluntary vs. Coercive Redistribution

The conception of politics as a realm of free self-determination stems from the fallacy of treating collective decisions as merely individual decisions writ large. Take Richard Titmuss's view that the welfare state is based on the 'gift relationship' between strangers. Central to that relationship is the unconstrained spirit of freedom in which the gift is donated. But in what sense can a welfare state make 'free' transfers? Why does Titmuss ignore the obvious fact that taxpayers, unlike blood donors, are compelled to make transfers? Presumably because he thinks that collectively determined choices are as unconstrained as individually determined ones. But this analogy does not hold. Social choice theory has demonstrated that there exists no mechanism that automatically combines individual preferences into unambiguous collective ones; while public choice theory has shown that democratic processes are subject to agenda manipulation by politicians and pressure from organised lobbies that can override underlying public preferences. The legitimacy crisis of the welfare state springs precisely from a belief that some transfers are being made **without** the taxpayers' consent, and that some transfers to which they would consent are not being made. A political decision could theoretically spring from a genuinely 'collective' determination to make 'gifts' of the kind that Titmuss admires; but this would require constraints (e.g. a reinforced majority) far stricter than those that apply in normal democratic decision-making.

The voluntary nature of the gift relationship surely suggests a more natural and obvious analogy with private welfare provision. But as this phenomenon falls outside the market-state dichotomy it plays only a shadowy role in citizenship theory. Some private welfare is regarded as obviously desirable and provides the rationale for welfare programs (e.g. child endowments are supposed to help parents look after their children).

Other kinds may be resisted because they are thought to foster undesirable relationships (e.g. some kinds of private charity may humiliate the recipients). The general citizenship school opinion is that voluntary welfare is inadequate: 'it has to be accepted that neither family or private charity is likely to catch all cases of unmet need' (Harris, 1987:21).

However, citizenship theory has done a disservice to voluntary welfare provision, in two ways. First, its emphasis on state welfare has distracted attention from the many forms that voluntary provision takes, and therefore from its real importance in most people's lives. Between the intimate realm of family and friendship on the one hand and impersonal charities on the other there exist numerous neighbourhood and community organisations that reflect a wide range of citizen concerns and employ a wide variety of methods of delivering welfare. In Section IV, I examine the argument that the voluntary sector has been largely crowded out by the welfare state but is potentially a superior alternative to it. To the extent that these claims are valid they challenge the conventional wisdom that the welfare state is needed to make up the inevitable deficiencies of private provision.

Secondly, the state-market dichotomy at the heart of citizenship theory masks the affinities and continuities between voluntary welfare provision and the market. As noted, the market appears in citizenship theory as a coercive realm that we overcome collectively in our roles as citizens. But, for reasons we have already seen, ordinary political processes are themselves coercive, since they result in decisions from which some gain at the expense of others. In contrast, the market normally operates by way of exchanges that are freely undertaken (subject to constraints) and that improve the welfare of all the parties involved. However, I am not suggesting that we should simply invert the market-state distinction employed by citizenship theory. The market is within the realm of freedom, but it does not exhaust that realm, which also includes the transactions involved in what we call 'voluntary' welfare provision. The crucial distinction is therefore between **coerced** transfers and **free** transfers. Whereas ordinary political processes divide society between winners and losers, voluntary processes make winners of us all, not only as parties to market exchanges, but also as donors and recipients of gifts and other non-market forms of assistance.

Those citizenship theorists who, like Raymond Plant, call themselves 'market socialists' recognise the welfare-enhancing effects of the free market. But, as noted above, so far they have shown little interest in the potential of non-market forms of private welfare provision. The underlying reason for this, I think, is that they see no role for non-state forms of welfare delivery in promoting equality. From a citizenship theorist's point of view, private welfare provision could be useful in encouraging altruism, and may even go a long way towards satisfying welfare rights; but there is no reason to expect the uncoordinated and unpredictable voluntary efforts of private citizens to lead systematically to a more equal distribution of income.

The central role of state welfare in citizenship theory thus depends crucially on its playing an indispensable role in promoting equality. Yet it is precisely on this point that the citizenship school is currently having to face its most serious challenge, since the evidence increasingly suggests that the welfare state has been captured by the middle classes. This is one of the main reasons for the current shift of public opinion towards selective rather than universal welfare provision. The next section examines this evidence and comments on recent responses to it by defenders of state welfare.

III. CAN THE WELFARE STATE PROMOTE EQUALITY?

Measuring Redistribution

Claims about the redistributive impact of the welfare state presuppose that that impact can be calculated. But this task is complicated by several factors, such as the variety of methods of delivering welfare, the number of welfare programs, and the distribution of the heavy burden of taxation imposed by the welfare state. In recent years, a technique of measurement known as the 'standard method' has been developed to deal with these complexities. This method is not without its own problems, including a certain conceptual and terminological bias that reflects and reinforces the ideological assumptions of citizenship theory.

In a detailed recent study of the Western welfare states, Stein Ringen explains that the standard method of analysis 'is to compare the distributions of income "before" and "after" transfers and taxes and to take the difference between these distributions as a measure of the direction and degree of redistribution'. The standard method employs four main income concepts: market income (the sum of all private income); gross income (market income plus direct transfers); disposable income (gross income minus direct taxes); and final income (disposable income plus indirect transfers, minus indirect taxes) (Ringen, 1987:171-2). Research based on the standard method has found the following: that cash transfers are the most effective mechanism of redistribution; that indirect transfers are only mildly redistributive and in some cases are mildly regressive; and that any redistributive impact of direct taxes tends to be offset by the regressive effects of indirect taxation (Ringen, 1987:174-5).

However, the standard method suffers from certain methodological problems, the most serious of which concerns the concept of 'market' income that provides the base line from which the redistributive impact of the tax-transfer system is measured. Market income is, conceptually, the income that would have existed in the absence of taxes and transfers. But the distribution of market income is itself partly determined by public policy. It is heavily influenced by government regulations and by public sector employment practices. It also reflects welfare policy to the extent that individuals adjust their behaviour in response to taxes and transfers. Market income is therefore, in Ringen's words, a 'statistical' rather than a 'real' base line for measuring welfare state redistribution. Thus, we cannot simply assume that households that have little or no market income would be completely destitute in the absence of the welfare state, since in that case they would have to acquire some market income from earnings, savings, or charity. It follows that the standard method, by incorporating an unrealistically inegalitarian base line, exaggerates the redistributive impact of the welfare state (Ringen, 1987:243-5).

Despite these problems, the standard method is still regarded as the best available method for analysing redistribution. It is employed, for example, by the Luxembourg Income Study, a major research project started in 1983 for the purpose of international comparative analysis of income distribution and redistribution. The defenders of the approach have responded to its methodological problems by developing more refined statistical comparisons between welfare systems involving, for example, different mechanisms and levels of redistribution (Ringen, 1987:181-91). But why not concentrate directly on the causes of inequality revealed by the analysis of market income? The problem is that the standard method reflects the citizenship school's ideological assumption that inequality is caused by 'the market' and has to be cured by 'the state'. That is why the term 'market' is still used to describe the income distribution that the welfare state is supposed to correct even when it is admitted that government intervention is itself partly responsible for the inequality of that distribution. The standard method thus incorporates a conceptual bias towards an ever-expanding welfare state. The inequality generated by government intervention reappears statistically in 'market income' and so demands correction by further intervention. Government is assumed to be benign both when it causes inequality and when it cures it.

If the citizenship school's attachment to the market-state dichotomy is dropped, then an alternative interpretation of the welfare state suggests itself. The central point is that the inequality generated by government is frequently not a regrettable side effect of its otherwise beneficial interventions but rather their very rationale. The compression of youth wage rates by the centralised wage system is designed to reduce downward pressure on adult wage levels. Import tariffs survive because they redistribute from consumers to protected producers. In other cases inequality and disadvantage are unintentional but persist because of the political barriers to curing them: for example, the state school system performs generally worse than private schools, but teacher unions resist reform. From this point of view, the welfare state's function is to mop up the damage done by discriminatory intervention. It compensates the victims not so much of market failure but of inequalities and inefficiencies generated by government itself. Conversely, if government intervention were more constrained by the rule of law and went less against the grain of the market, then there would be less for the welfare state to do. But this approach to reducing inequality is masked by the conceptual apparatus of citizenship theory in general and the 'standard method' in particular.

The Middle Class Capture of the Welfare State

The foregoing analysis of the 'standard method' of measuring income distribution suggests that whereas the **overall** redistributive impact of government is uncertain (since the 'pre-intervention' distribution must remain unknowable), we do know the **direction** of the impact, direct and indirect, of particular interventions. This makes it possible to test the claim that the welfare state unduly benefits the middle classes.

Ironically, the most substantial evidence of the middle class plunder of the welfare state has been provided by a member of the citizenship school, Julian Le Grand. In *The Strategy of Equality*, Le Grand examines the distributive impact of the four major social services in the UK: health care, education, housing and transport. He finds that public spending on these services 'systematically favours the better-off, and thereby contributes to inequality in final income'. He doubts whether higher public spending can offset these effects, and argues instead for policies that redistribute income directly rather than indirectly through universal services (Le Grand, 1982:137).

Le Grand has since developed his explanation of the middle-class capture of the welfare state by reference to some of its unintended political and behavioural consequences. In a brief study of recent welfare spending cuts in Britain, he finds that those services from which the middle classes most benefit (whether as recipients or as employees) have fared relatively well and may even have been expanded. The services that have been most severely cut back or privatised have few middle-class beneficiaries or producers to defend them. On the other hand, unemployment benefits and last-resort social security benefits have been maintained: Le Grand speculates that this reflects a middle-class selectivist sentiment that favours benefits for the poor (1984:386).

Most recently, Le Grand has joined forces with Robert Goodin, another prominent citizenship theorist, and tested a number of theories explaining middle-class infiltration of means-tested welfare programs. The data are derived from three nominally selective Australian programs that gradually became 'universalised' in the years following World War II. Between 1945 and 1981, the proportion of old people receiving the age pension rose from one third to three quarters. In the same period, the proportion of invalids qualifying for the invalid pension rose from less than half to almost nine tenths. The number of widows receiving the widow's pension remained less than half, but rose from 29.8 per cent in 1971 to 40.6 per cent ten years later. This occurred despite a gradual **reduction** in the percentage of average income that individuals could receive and remain eligible for benefits. This last detail leads Goodin and Le Grand to reject three explanations of the phenomenon, namely, 'boundary' problems (difficulties in unambiguously defining the characteristics of those the programs are intended to help), bureaucratic empire-building, and political pressure from the middle classes. If these factors had been significant, they would have led to a gradual relaxation of the means tests. The fact that the opposite happened leads Goodin and Le Grand to suggest that the explanation was behavioural: 'the non-poor responded to the imposition of a means test by re-arranging their affairs, legitimately or illegitimately, so as to pass the test' (Goodin & Le Grand, 1987:124).

Middle-Class Welfare and Citizenship Theory

The outcome of this research seems quite serious for citizenship theory. If Le Grand is correct, then neither universal services like health care and education nor selective cash transfers targeted towards the poor can be relied on to reduce inequality, since the middle classes find ways of turning both kinds of welfare program to their own advantage. But the citizenship school's response has been to reconstruct the case for universal welfare provision. Michael O'Higgins, for instance, has recently revived Anthony Crosland's claim that government services promote equality in 'non-differentiation' rather than in distribution: even if some citizens do better out of them than others, they help break down social class barriers and generate a communal ethos. O'Higgins himself argues that universal provision may actually be more egalitarian even in a distributive sense: Where universal services are of a high standard, the middle classes make use of them and support them rather than opting for private alternatives, whereas selective provision spurs the growth of private services and renders the programs on which the poor depend vulnerable to middle-class pressure for tax cuts (O'Higgins, 1987:13-14).

This line of reasoning is adopted by Peter Saunders to explain why the Australian welfare state is less redistributive, despite being more selective, than its Western European counterparts (though it should be noted that Saunders bases this claim entirely on a comparison between market income and gross income as defined by the standard method, and thus ignores any redistributive impact of taxes and indirect transfers). Saunders claims that selective welfare in Australia has failed to promote more equality than has universal welfare elsewhere because it has resulted in a relatively low overall level of expenditure on welfare transfers:

> The willingness of taxpayers to finance the activities of government and thus to provide their political support for them, is not independent of the form that those activities take. Australia's emphasis on social security targeting — unlike the universalist, contributory, social insurance approach — has undermined broad-based support for social security and thus led to a lower level of social security expenditure than elsewhere ... the level of resources available to governments depends crucially on public perceptions of, and political support for, those activities for which governments wish to acquire these resources in the first place. (Saunders, 1987:36, 37)

The idea, then, is that any middle-class capture of the welfare state is in the interests of the poor because it generates strong political pressure for relatively high benefits; whereas if welfare is selectively targeted to the poor, the non-poor majority will use their political influence to reduce welfare expenditures.

This argument unintentionally subverts the citizenship school's claim that the welfare state promotes altruism. It says that the middle classes are so selfish that they will support only those welfare programs from which they directly gain, and that the only way to protect the poor is to mobilise that selfishness into supporting universal services and benefits. Whether any such implicit alliance between rich and poor is at work in the welfare state is doubtful. Much of the middle-class capture of the welfare state can of course be attributed to selfishness. But this will not help the poor if it redistributes limited resources to the middle classes from everyone else. For example, student unions oppose the reimposition of tuition fees, even though tertiary education expenditures disproportionately favour the middle classes. This is a clear case where user charges would help the poor both by easing the tax burden and by enabling universities and colleges to increase their enrolments.

The real weakness of the new case for universal welfare is that it misinterprets the current pressure for lower taxes and selective benefits, which is not fundamentally a matter of selfishness versus altruism but of freedom versus coercion. Taxpayers by and large seem willing to finance welfare for the needy and deserving, partly, no doubt, because they fear they may one day fall into those categories themselves. But they are also compelled to finance programs whose beneficiaries are often neither needy nor deserving. In addition, they have to finance government services like health care and education over which they can exercise little control as consumers. The middle classes then either use their political influence to secure better government services for themselves or buy private alternatives that remain beyond the reach of the worse-off. This is turn helps legitimise 'selfish' behavioural responses like avoiding and evading tax and maximising welfare entitlements.

The upshot of this is that no approach to state welfare delivery — selective, universal, or some combination of the two — can be relied on ultimately to realise the citizenship theory's ideal of equality. Any initial movement towards equality tends to be reversed over time by behavioural adaptation and political opportunism. This in turn leads to steadily rising burdens of welfare expenditure that have to be dealt with by regular rounds of spending cuts and increasingly rigorous eligibility criteria. But while the failure of the strategy of equality has discredited citizenship theory and the tax-transfer system it has created, it has also generated a mass of conflicting vested interests in the status quo. This is the dilemma that prompts us to look to voluntary welfare provision as a possible solution.

IV. ALTRUISM, RECIPROCITY, AND VOLUNTARY WELFARE PROVISION

Does the Welfare State Crowd Out Voluntary Provision?

Opponents of the citizenship theory generally believe that voluntary welfare provision has declined in response to the rise of the welfare state. Some anarchists believe that intervention in all its forms causes our spontaneous altruism to wither away. Michael Taylor, for instance, argues:

> In the presence of a strong state, the individual may cease to care for, or even think about, those in his community who need help ... he may come to feel that his 'responsibility' to society has been discharged as soon as he has paid his taxes. Under the state there is no practice of cooperation and no growth of a sense of the interdependence on which cooperation depends; there are fewer opportunities for the spontaneous expression of direct altruism and there are therefore fewer altruistic acts to be observed, with the result that there is no growth of the feeling of assurance that others around one are altruistic or at least willing to behave cooperatively — an assurance that one will not be let down if one tries unilaterally to cooperate. (Taylor, 1976:135-6)

Taylor cites Titmuss's argument that altruistic behaviour is imitative and tends to spread throughout society by the force of example. But whereas Titmuss thinks the welfare state encourages altruism, Taylor believes the opposite: that the state stifles the spontaneous, altruistic cooperation that, if allowed to flourish, would take care of all our needs.

The crowding-out argument has received substantial empirical backing. Jeffrey Obler, for example, found that the level of charitable donations was much higher in the US than in the UK; in 1973 it was seven times higher, even though American per capita income was only twice as high as the British. Given that Britain's welfare state is much more developed than America's, this seems to confirm Taylor's thesis and to refute Titmuss's. However, the American tax system is specifically designed to encourage charitable giving, and this must account for some of the difference between the two countries (Obler, 1981:27-31).

Obler's work is important also because of some interesting additional evidence that voluntary effort is not entirely crowded out where the state is active, and is to some extent **diverted** into areas ignored by the state. Obler found that, in the English village of Penridge, while 'unilateral personal' giving had declined, 'unilateral impersonal' giving had continued in the form of a few charities whose services often overlapped with those provided by the state. But the moving force behind this kind of giving appeared to be the opportunities it provided for social gatherings rather than a direct concern for its beneficiaries. Where the state was wholly absent, as in the provision of recreational services, the villagers were highly active in looking after themselves through voluntary action (Obler, 1981:36).

Is Altruism a Public Good?

Obler's findings, as well as generally supporting the crowding-out thesis, also suggest that voluntary activity could emerge to take over supplying any welfare services withdrawn by the state. Nevertheless, most supporters of the crowding-out hypothesis believe that some state involvement is essential. Several classical liberals argue that the benefits of private charity are a public good and may therefore be undersupplied unless the state makes up the deficiency. Milton Friedman justifies the negative income tax on these grounds. He argues thus:

> I am distressed by the sight of poverty; I am benefited by its alleviation; but I am benefited equally whether I or someone else pays for its alleviation; the benefits of other people's charity therefore partly accrues to me. To put it differently, we might all of us be willing to contribute to the relief of poverty, **provided** everyone else did. We might not be willing to contribute the same amount without such assurance. In small

communities, public pressure can suffice to realize the proviso even with private charity. In the large impersonal communities that are increasingly coming to dominate our society, it is much more difficult for it to do so. (Friedman, 1962:191)

Friedman advocates a much smaller welfare role for the state than does the citizenship school, and treats this role as an adjunct not merely to the market but to the voluntary sector as a whole. He assumes that the transfer mechanisms of the negative income tax will be much less divisive than political processes typically are, since they will be giving effect to the community's underlying altruistic preferences.

This entire line of reasoning has been challenged most effectively in recent years by Robert Sugden, who points out that it fails to explain why any voluntary giving occurs at all. Friedman's theory assumes that, since altruists benefit from the poverty alleviating effects of other people's charity, it is strictly rational for them to free ride on the efforts of others: my donation alone is insufficient to alleviate poverty, whereas if others donate, my contribution will not be missed. Yet, as we all know, some charities are very successful: Britain's Royal National Lifeboat Institution, for example, survives on voluntary contributions, even though it will rescue contributors and non-contributors alike. So why does anyone contribute? (Sugden, 1986:4).

Sugden's answer is that people are concerned not only with the overall effect of voluntary giving but with their own individual gifts as well: 'The act of giving has a moral significance over and above the significance of its direct consequences' (Sugden, 1983:28). Sugden interprets the individual gift as the fulfilment of a duty to give. It is crucial for Sugden's theory that this duty not be confused with altruistic concern, which can be satisfied by other people's gifts. Sugden himself believes that a good deal of unselfish behaviour stems from a 'principle of reciprocity', a principle that obliges us morally to make contributions only when other people do the same (Sugden, 1983:30).

A moment's reflection will confirm Sugden's claim that unselfish behaviour need not always be strictly altruistic. People often do things such as taking lost property to the police station, not cheating when it would be easy to do so, etc., out of a sense of moral duty rather than concern for the interests of the beneficiaries of those actions. No doubt some people give to charities in order to assuage their guilt at being well-off. Voluntary donations can also spring from strictly selfish motives, such as moral exhibitionism or (as Obler found) love of the social life that charities provide for their supporters. The possibility that altruism may not be enough to ensure unselfish behaviour seems to lie behind the misgivings some leading citizenship theorists have about Titmuss's defence of the welfare state. As noted in Section II, T. H. Marshall and Raymond Plant argue that the individual has a **right** to welfare that the community is strictly obliged to satisfy whether or not it feels the pure altruism that inspires the 'gift relationship'. But this still leaves open the question whether those obligations have to be performed by way of coercive transfers or whether they can be left to the voluntary efforts of private citizens.

It doesn't follow from Sugden's analysis that voluntary donors are not altruists: the point is that altruism would not explain their behaviour. But if so, then it's quite possible that many altruists fail to act unselfishly because they lack a sufficient motive to do so (such as recognising a reciprocal obligation). Where state provision is followed by a drop in voluntary provision, the explanation may be, not that citizens have become selfish, but that they think their taxes relieve them of the obligation to contribute further. This is consistent with Obler's evidence that voluntary welfare provision flourishes in areas untouched by state welfare. Would it flourish in areas from which the state withdrew? Sugden's analysis of reciprocity suggests one way in which this could happen. But first we need to be clear about the meaning of reciprocity.

Reciprocity and Voluntary Welfare Provision

Broadly conceived, reciprocity has two defining characteristics. First, reciprocal acts are acts whose performance is mutually conditional: I will do such-and-such only if you do such-and-such. Second, reciprocal acts are unselfish, even though the **system** of reciprocity benefits all actors. These characteristics allow a wide variety of actions to be defined as reciprocal, such as mutual aid, sharing, and voluntary cooperation.

Two important kinds of voluntary action fall outside the definition: market exchanges (which are normally self-interested) and unilateral, impersonal giving (which, as Titmuss defines it, is wholly unconditional and creates no obligation on the recipient's part, nor any expectation on the donor's part, of reciprocation). Nevertheless, both the market and unconditional giving share some of the properties of reciprocity. Market exchanges, contrary to the impression given in some of the citizenship literature, are normally accompanied by the mutual trust and goodwill that attend strictly reciprocal acts. Unconditional gifts resemble gifts whose reciprocal aspects are indeterminate and weakly felt (e.g. sending Christmas cards). Thus, while the concept of reciprocity does not cover the entire range of voluntary relationships, it does highlight some of their common characteristics and underline their fundamental difference from coercive relationships.

Sugden's most recent work on reciprocity forms part of his study of the evolution of the 'spontaneous order' of society, a subject to which he applies the insights of modern game theory and sociobiology. He speculates that evolution favours conventions of reciprocity because reciprocators fare better than non-reciprocators. But how does reciprocity emerge among people who initially have no reason to trust one another? Sugden distinguishes between 'brave reciprocators' (who are prepared to run the risk of making the first cooperative move) and 'cautious reciprocators' (who are willing to cooperate but only if others make the first move). Over time, people learn that cautious reciprocity is a better strategy than non-cooperation, since it is a risk-free way of reaping the benefits of reciprocity. Eventually, some brave reciprocators emerge and elicit the cooperation of their cautious counterparts; their success attracts the cooperation of almost everyone else, leaving stubborn non-reciprocators to die out (1986:104-21). Sugden's hypothesis would explain the tendency, noted by Taylor and Titmuss, for 'altruistic' behaviour to spread through imitation.

The greatest problem for Sugden's hypothesis is how to cope with free riders. Sugden notes the success of the mutual aid form of reciprocity, which typically takes the form of clubs that can confine their benefits to contributing members and punish defectors by withholding those benefits from them. But some benefits of cooperation are public goods and so can be consumed by free riders. This brings Sugden back to the British lifeboat service: this is maintained by a minority of its potential beneficiaries who cooperate because they feel an obligation to contribute to it (1986:122-44).

This last point is evidence of what Sugden calls 'the morality of cooperation'. He argues that the conventions of reciprocity, coordination and property (which together make up the spontaneous order of society) are sustained by moral sentiments that make us feel obliged to observe conventions from which we benefit, and justified in demanding similar behaviour from others. These sentiments help ensure that we behave cooperatively even when it is in our immediate interests to free ride on others' efforts. Sugden is at pains to stress that he is not saying that the morality of cooperation is something we ought to observe. His point rather is that the moral beliefs we actually have are largely a matter of convention, and for that reason are resistant to the efforts of moral reformers (1986:166-77).

If Sugden's speculations are sound, they should increase our confidence in the effectiveness of voluntary provision. Any 'morality of cooperation' that prompts individuals spontaneously to provide welfare in areas that the state currently ignores would spread into areas from which the state withdrew. Sugden's stress on the past and present success of welfare clubs is especially relevant. The appeal of citizenship theory rests in part on the myth that, before the present century, the masses were deprived of the most basic forms of welfare. Countless historians tell us that the welfare state emerged to deliver services that 'the market' had failed to supply. But, as Green and Cromwell point out, it is likely that during the 19th century 'throughout Australian towns 80-90 per cent of manual workers were members of friendly societies' (1984:xv). These mutual aid organisations, which provided sickness, unemployment and other benefits, were gradually reduced to the status of health funds by the rise of state welfare and other factors. But there are signs of a modern revival of the mutual aid principle, not only in the growth of health maintenance organisations in the US, but also in the emergence of bodies like Alcoholics Anonymous and neighbourhood watch committees. This, along with the growth of private **substitutes** for existing state services (such as education), renders the entire welfare agenda of government controversial and provisional, and suggests that public policy should begin to take seriously, and adapt itself to, the likely continuing growth of the voluntary welfare sector.

V. CONCLUSION

The welfare state is suffering from a legitimacy crisis because it imposes a uniform system of taxes and transfers that cannot possibly reflect the great variety of individual preferences (both selfish and unselfish) with regard to welfare. This mechanism has failed to realise the goals of citizenship theory; instead it has created a system permanently ridden by political conflict and from which the only escape is to start devolving welfare decision-making to the voluntary sector.

Governments faced with international debt burdens have every incentive to move in this direction. Several of the devices for beginning such a move have been on the fringes of policy debate for some time. One is to expand the role of private charities by handing over to them the administration of more state welfare programs and by encouraging private donations to them through more generous tax concessions. Another involves allowing citizens to opt out of government services (education, health care, unemployment insurance) by means of vouchers and tax credits. Other techniques could be developed, such as government grants to finance start-up costs for new charities and mutual aid clubs (thus encouraging 'brave' and 'cautious' reciprocators to get together). Revenues from public asset sales would be better employed in such ways than in artificially reducing the current costs of existing welfare programs. And, of course, further deregulation and tax reform would encourage economic growth and eliminate much intervention-induced inequality, and in this way both reduce pressure on the existing welfare state and ease the transition to more voluntary provision.

What is needed is a set of policy **principles** on the basis of which politicians can start offering leadership and building up support for fresh policy directions. Three such principles are suggested here. First, any shift from state to voluntary welfare should as far as possible be a matter of individual rather than collective choice. This means that existing government services in health care, education and so on would be retained to the extent that their consumers really preferred them to private alternatives. There seems no good reason to close down state schools that perform well and are supported by local parents. However, it would be consistent with this principle to start charging (on a means-tested basis) consumers of government services, in order both to promote rational choices between state and private services and to encourage competition between the two. Subsequent public expenditure savings should as far as possible then be reflected in tax cuts or vouchers. Second, welfare benefits (direct and indirect) for people living below the poverty line should be maintained at present levels for those who continued to claim them. This commitment would protect the worst-off from any loss of benefits resulting from a high level of opting-out of government services by the middle classes. Third, entitlements based on past contributions to insurance-type welfare programs should continue to be recognised on a pro rata basis. Observation of these principles would ensure that any movement away from the welfare state could proceed without violating the moral rights bound up in the status quo.

No one could predict in any detail what kinds of voluntary welfare systems would emerge, how quickly they would appear, or how popular they would be in comparison with state welfare. Those aspects of the state system that did survive would be based very largely on individual rather than collective choices, and so would more accurately reflect underlying preferences. More fundamentally, a commitment to allowing a greater role for voluntary welfare provision would indicate a rejection of the social engineering approach of the citizenship school and a recognition that individuals can tend to their own and one another's needs without having to cooperate in realising some social end-state, egalitarian or otherwise.

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Unintended Consequences and Unthinkable Solutions

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Unintended Consequences and Unthinkable Solutions

David Band

I. INTRODUCTION

'Welfare state' is one of those handy plasticine terms that can be stretched or contracted to suit the user's purpose. Most of the meanings it is made to bear are valid in different contexts, but the central requirement upon the user of the term is to be clear and consistent in that use. I believe the term is used most accurately when it incorporates all beneficiaries of government action. This would include not only the most obvious recipients of direct transfer payments, but also any enterprise that, thanks to some action on the part of government, gains an advantage over, or protection from, a competitor. According to this use of the term, a person who receives unemployment benefits has the same status as, say, American aeronautics companies, British electronics manufacturers or Australian steel producers. In each case the beneficiary receives a short-term financial benefit from the decisions of government. Whether or not the benefit extends to the long term is a question I shall put aside for the moment.

I prefer this use of the term 'welfare state' because it shows how widespread the supplicant mentality is in the West today. It shows too how ingrained our confidence in the efficacy of government action has become, notwithstanding overwhelming evidence to the contrary. Although this is my preferred definition, however, I shall not use it in this paper because the term has two more popular uses.

In the first and broader of these, income security, community services (assistance to the disabled, the homeless, etc.), health, education, and public housing measures constitute the 'welfare state'. This is the definition that most 'small government' opponents of the welfare state use because it allows them to focus on such things as the poor quality of health services, falling educational standards, and the inevitability of rent control hurting the poor.

In each area, because they are dealing with years of government control or monopoly, these critics have a fund of horror stories from which they can draw market-oriented lessons. However, they rarely question government's proper role of providing a safety net for the 'genuinely needy'. They may criticise how that role is performed in individual cases, but not the appropriateness (or necessity) of government's performing it.

It is precisely that appropriateness or necessity that I propose to question, using the term 'welfare state' in the second and narrower of its popular definitions, namely, referring exclusively to government provision of income security and community services as described above. The comments that follow can be applied to areas such as health, education and housing, but I shall not address those areas directly. The rest of this paper will examine the usual reasons for concern over the welfare state; why those reasons are either relatively unimportant or ill-founded; what ought to be our central points of focus in discussing the problems of the welfare state; and the first intellectual steps we need to take in order to address those problems.

II. THE WELFARE STATE DEBATE THUS FAR

The last few years have witnessed unprecedented debate over the welfare state, even in the narrow sense in which I am using the term. Why has there been such concern expressed in recent times about the direction in which it is heading? Two sources of that concern predominate.

The Financial Problem

The first concern has to do with the growing financial cost of state welfare. In brief, the argument is that, because Western economies generally enjoy slower growth rates than they did 20 years ago, because of various demographic trends, and because today there is a wider range of benefits available than existed 20 years ago, it is going to be increasingly difficult to sustain the welfare state's current share of GDP.

This is not just a wrong-headed concern about state welfare: it is a dangerous one. It leads to one of two assertions, the first of which runs thus: 'Don't worry about the proportion of GDP that welfare expenditures represent — just take steps that will dramatically increase the rate of growth of GDP'. This is an argument of beautiful circularity. One of the surest ways of dramatically increasing a nation's welfare is dramatically to reduce its levels of taxation and government regulation.

The second line of thought arising out of the growing financial cost of state welfare is more often implied than asserted, but is no less troubling for that. It goes something like this: 'As we reduce state welfare expenditures as a proportion of GDP, so the problem of the welfare state recedes'. This is where an **exclusively** fiscal concern with state welfare becomes dangerous. This line of thought creates incentives for politicians, bureaucrats and social commentators to invent more punitive or discriminatory ways of disbursing welfare benefits. These almost always involve new layers of intrusiveness and discretionary judgment by unaccountable officials. (This is a theme to which I shall return.)

The financial side of the welfare state is a problem inasmuch as it relates to taxation. And the real problem with a tax-based welfare system is not that there are fewer and fewer citizens out of whom more and more resources have to be squeezed, but that such a system does indeed depend on squeezing — on coercion rather than voluntary relationships freely entered into by fellow citizens.

The 'Dependency' Problem

The second source of concern about the direction of the welfare state is the fear that our kind of system of state welfare is creating (or has already created) an underclass of permanently dependent citizens — people who would be unable to live outside the system of state support; who have neither the ability nor the incentive to take responsibility for their own lives; people who are creations of the very system that supports them.

In fact, any student of economics could predict that our state welfare systems would create this kind of dependency. If the price of a 'good' — dropping out of school, or having a child out of wedlock, or not working — is made low enough, demand for that 'good' will rise: the lower the price, the higher the demand. Suppressing that price across generations creates exactly the kind of dependency outlined above. If it is objected that this is mere theory, we can point to Charles Murray and others who have produced data showing that we are indeed creating an underclass of this kind.

We are, however, in danger of learning the wrong lessons from these findings. I want to argue that the usual lament about the existence of this underclass either misses the central point or heads off in dangerous directions. Let us begin with the question: What exactly is wrong with this dependency?

Surely we do not mean to say that dependency as such is bad or wrong or socially destructive. Most of us find nothing particularly worrying about a child's dependence on his parents or an elderly parent's dependence on his children. Indeed, most critics of 'welfare state dependency' would probably argue for more dependency of this kind, although they would probably use phrases like 'greater assumption of family responsibilities'.

It seems to me that a great deal of the agitation over 'welfare state dependency' is of a social engineering kind. These critics seem to believe that it is in some way harmful for one person to be dependent upon others, and that, the greater the number of such dependent persons, the greater the harm to society as a whole. This belief leads logically to a concern about 'unemployable' or 'useless' citizens. As the perception grows of a 'crisis' in the funding of the welfare state, I believe there is a danger that this combination of concerns will create a situation tailor-made for demagoguery and absolutism.

As my familial examples show, people have always been dependent upon one another, just as people are born and have always been unequal in varying ways. It is as futile for the anti-collectivist to be concerned about dependency as such as it is for the collectivist to be concerned about inequality. Indeed, it is not just as futile, it is as dangerous — both are expressions of social engineering. Each is saying 'I don't like society looking like X — I want it to look like Y'. The history of attempts to give political and bureaucratic form to the egalitarian ethos shows that once a single step is taken down that path, it turns instantly into a slippery slope. Still, as Hegel tells us, we learn from history that we do not learn from history.

Just as there is a spectrum of political societies ranging from the liberal to the absolutist, so there is within liberal societies a spectrum of political philosophies ranging from the libertarian to the collectivist. The key to the different positions occupied at various points on either spectrum is not, as is often claimed, that the unit of analysis or concern varies from the individual to the community. The key is that, the closer one comes to the liberal end of either spectrum, the more one is focussing on a voluntary rather than a coercive set of relations between citizens and between individual citizens and society as a whole. Thus Western liberal democracies have put such voluntary relationships under the protection of the rule of law to a far greater degree than have, say, the dictatorships of Eastern Europe or the Third World.

In any society, no matter how coercive or voluntarist, some citizens will be dependent upon other citizens. Ron might be financially dependent on George, but George could at the same time be intellectually dependent on Ron. They might both be socially dependent on Bob. And so on: the argument is remarkably similar to the familiar anti-egalitarian one of cross-cutting inequalities in wealth, beauty, speed, strength, etc.

By way of illustration, let me take you to the republic of Voluntaria. This mist-shrouded island, somewhere off the east coast of Scotland, was founded in the 18th century and has only recently been rediscovered. Its inhabitants have been blithely ignorant of all the social and political 'developments' of the last two centuries. Their society is characterised by a remarkable absence of constraint and control of citizens by government. In fact, there is barely a 'government' worthy of the name. No taxes are collected — the citizens merely pay a voluntary membership fee against the day that the country might be forced to join something like the EEC or the United Nations. There is no police force — the unfettered exchange of private property within a legal system allegedly inspired by the work of Thomas Hobbes has made it unnecessary. There is no licensing of purveyors of medical or legal services, who are therefore forced to compete with each other in both price and quality in order to make a living. It is all quite barbaric.

And yet, strangely enough, even in this backward society, people are still dependent upon one another in a myriad of overlapping and inconsistent (in Voluntaria, they say 'balancing') ways. Even in Voluntaria, if a child is born incurably blind, no matter how successful he is through life in overcoming this disability, he is still going to have to rely on others to varying extents. They put a peculiar construction on this kind of relationship in Voluntaria. They say that not only is there nothing wrong with such dependency — it is wholly admirable. One citizen's needs are met, and because they are met by the voluntary actions of others, everyone gains. There is, they say, no moral cost to the meeting of those needs.

Visiting teams of social anthropologists have even found on Voluntaria examples of dole-bludging, or at least, since there is no dole, donor-bludging. Here is one such case. Smith, a middle-aged citizen of average means, decided two years ago, for reasons that he has chosen not to divulge, to provide financial support to one Fergusson, then aged 18 years. So generous has Smith's beneficence been that Fergusson has not felt constrained, either financially or culturally, to seek employment.

Researchers interviewed Hume, Fergusson's neighbour, to gauge his reaction to this state of affairs. They found his opinion repeated elsewhere in relation to similar cases: 'Well I don't like it. I believe strongly in the value of work, and I have a strong moral objection to any able-bodied individual choosing not to seek work. I've tried in vain to convince them of the correctness of my views. But I'm certainly not going to force them to adopt my opinions. A fool and his money are soon parted. If Smith is prepared to spend his resources in this way, and to live with its consequences for Fergusson, that's entirely his and Fergusson's business.

'It's possible, of course, that Fergusson will have a change of heart about the life he's leading, or that Smith will see the harmful effect he's having on a young man's life. But once again, in either case, that would be a matter for the two of them only. I see no reason why the rest of us should be dragged into their private relationship and implicated in their transactions. You seem to think that we are all involved anyway, because Smith and Fergusson are denying the rest of us an extra able body. But we think that that is a small price to pay for maintaining the largest practical sphere of private and voluntary action. The implication of what you're suggesting is that we should all pay into a central fund out of which monies would be paid to … well, to whom? To whoever shouts loudest, I suppose. And then we'd need people to administer the fund, and pretty soon we'd be doing what they told us. What sort of society would that be?'

The moral is that the problem with 'dependency' in today's welfare state is not so much that it involves the dependence of one upon others, but that it is fed by the proceeds of coercion and expropriation. Unlike the citizens of Voluntaria, if some of us don't like dependency or don't like dependency so based, **there is nothing we can do about it.** We certainly cannot withdraw our financial support for it and hope to escape prosecution, no matter how thorough we might be in denying ourselves any of the other government 'services' that are so based. We have no choice.

The only avenue seemingly left open to us — and this, I think, is part of the explanation for the kind of 'social engineering' attack on the welfare state that I have already mentioned — is to fall back on demands for punitive and highly discretionary ways of disbursing welfare monies. Such 'solutions', as I shall argue later, are immensely worse than the perceived 'problem' that they are thought to address.

III. THINKING THE UNTHINKABLE: THE REAL PROBLEMS WITH STATE WELFARE

I have dwelt at some length on the dependency issue because I believe all the evidence shows that it, combined with the question of financial cost, will unfortunately dominate the welfare state debate for the foreseeable future. In this section, I want to utter a small counter-plea, and to suggest that the state provision of welfare creates far more fundamental problems than the participants in that debate are apparently prepared to acknowledge. Those problems are:

- The confusion of objectives.
- The ethics of distributing the proceeds of coercion and expropriation.
- The consequent erosion of feelings of mutuality and obligation between citizens.
- The difficulty with giving a delivery task to the public sector.

The Confusion over Objectives

It is important to realise that a confusion exists between the objective of making the poor richer, and the objective of all members of society becoming more equal. The more vigorous are the state's attempts to achieve the latter, the less likely is it that the former will be realised.

Let me address the second objective first. The argument for equality has long since been dispatched to its deserved intellectual oblivion. Suffice to say that, until our gene-splicing friends get the upper hand over the rest of us, we and our descendants will go on being wonderfully different — each of us a unique mixture of strengths and weaknesses, talent and mediocrity. As Thackeray has it in *Pendennis*: 'A distinct universe walks about under your hat and under mine ... you and I are but a pair of infinite isolations, with some fellow islands a little more or less near to us'. So the attempt to make us all equal is doomed — mercifully, since a society of perfect equals is, to the extent that it is imaginable, a perfectly ghastly vision, best left to the subterranean excesses of the worst science fiction.

None of this, however, prevents many people in positions of influence being moved (in rhetoric, if not in deed) by the egalitarian chimera. For such people, there is simply something 'wrong' or 'unfair' about Jones being more successful than, being wealthier than, achieving more than, Smith, and a large part of the point of government is to right this wrong. Thus has the notion of 'redistributive justice' arisen — taxation, especially progressive income taxation, exists for government to redistribute its revenues to those in the weakest financial positions. In this way, government will create a more equal society.

Now, there is an obvious ethical question here: why is a society of material equals morally preferable to a society in which no individual has the fruits of his talents and energies expropriated by the government? This question is rarely raised and even less frequently answered, but I shall put it to one side for the moment. My main point in dealing with this objective for the welfare state is this: if the reason for the state's involvement in giving monies to the poor is to create a more equal society, then let us be clear that that is the objective, as opposed to, say, making the worst-off better-off in any meaningful long-term sense.

As our post-war history shows, the more that taxes are raised or created to provide the revenue for redistribution, the more the pace of wealth-creation slows. As that pace slows there is less and less wealth for all members of society, but especially its poorest members, to share in. We have, then, a choice. We can pursue a society in which, up to a point, we are all more materially equal than we were at the start of the process. (That point, of course, is the point at which taxes and regulations slow the river of wealth-creation to the faintest trickle.) This is the course that we have adopted for at least the past century. Or we can pursue a society in which there are no artificial restraints put on the creation of wealth, and in which therefore the poorest citizens will be much better off than their counterparts in a society of the first kind.

Let it be understood that in a society of this second kind, the gap between the richest and the poorest may well be much wider than it is in a typical Western welfare state in the 1980s. If we cannot accept that, let us be honest and say so. But let us acknowledge that, by taking that position, we shall be condemning our poorest fellow citizens and their descendants not only to a life of literally immeasurably greater discomfort, but also to one of many fewer opportunities to move from a relatively poorer stratum of society to a relatively richer one.

The state has only one source of income — its citizens' wealth. The more it takes wealth from one set of citizens and gives it to another set, the more it condemns the latter. But it does, up to a point, make them all more equal. If that is the real purpose of the state's involvement in the people's 'welfare', let us at least be clear about it.

The Morality of the Welfare State

The welfare state has been constructed on very shaky ethical foundations. We have given ourselves a moral problem of great proportions, and we cannot begin to deal sensibly with 'the welfare state problem' until we acknowledge that fact. Here I want to do no more than make a plea for that acknowledgment: let us at least gain a measure of agreement about the dimensions of this moral problem before we begin the task of trying to extricate ourselves from it.

To repeat, we have acquiesced in the construction of a set of social arrangements that assumes that it is ethically preferable to expropriate the fruits of each individual's talents and energies than to allow him to enjoy and deploy them as he sees fit. We have done this in the name of constructing a fairer or more equal society. We have not allowed ourselves to be detained by the question of why a society characterised by widespread coercion and expropriation is fairer, more just or in any other way more attractive than one characterised by the absence of those phenomena.

In order to illustrate how much moral damage we have done, let me briefly consider two possible answers to that question. (Note, incidentally, that a defender of the welfare state cannot put forward both of these answers, since they are based on antithetical views of human nature.) The first might run along the following lines: 'The state's disbursing monies to the poor is simply a more efficient, more comprehensive way of delivering charity. We like to see the poor made better off, and we also like to give expression to our charitable instincts. But without the state stepping in to take over that role, the effects of our charitable behaviour would be patchy. People in like circumstances would receive widely differing benefits in different parts of the community. So we consent to handing over part of our resources to the state so that those resources can be spread evenly among the needy'.

This answer is unsatisfactory, for a number of reasons. First, as I explain at greater length below, to suggest that government is more efficient at delivery services than are people is to ignore all the key elements of public sector managerial and employment practices. Second, this is a distortion of the concept of 'charity', which is by its very nature a deliberate, voluntary act and not a matter of tacit consent. Third, the 'consent' thesis is both of a morally objectionable 'Nuremberg' stripe ('You didn't object, therefore you must have been a supporter') and objectively inaccurate — otherwise politicians would not feel compelled to offer tax cuts. Finally, the argument attempts to claim that evenly distributing the proceeds of expropriation is morally superior to not expropriating at all. The claim is its own rebuttal.

A second possible ethical defence of state welfare might run thus: 'It is morally unacceptable to allow poor people to starve to death, and if the state did not assume responsibility for preventing that outcome, it would happen. There is no guarantee that, were the state to be completely removed from welfare provision, enough people would be sufficiently philanthropic to prevent the undesirable social outcomes that the state prevents'.

Again, this argument is defective or disturbing on several levels. First, it paints a particularly bleak picture of human nature, one that assumes that we are not (or not sufficiently) concerned with one another's distress, nor sufficiently motivated to relieve it. I happen to reject this view of human nature, and I believe that the historical evidence supports me. But I acknowledge that one person's view of the human psyche is just as valid as another's, therefore I would not want to impose the implications of my view on the rest of society.

The trouble is, of course, that such an imposition is precisely what has occurred. The panoply of the welfare state apparatus has been imposed on us because, over time, the policy-makers have felt it necessary to act on their pessimistic assumptions about how, left to our own devices, the rest of us would behave towards each other. Moreover, this view ignores the possibility that there may exist a wide range of motives for the relatively better-off to assist the relatively worse-off. These might include: plain unselfish generosity, egoism (making oneself feel better about oneself for giving), desire for esteem in the eyes of others, and so on.

But let us assume that the governors' view of human nature is accurate. Let us assume as well that it is morally acceptable to impose upon society the logical consequences of a particular view of human nature. Would it not follow also that such implications should be drawn for and imposed on all our relationships with each other?

As a matter of fact, of course, we do not do that — at least not yet. We go about our daily rounds engaging in an intercourse with each other that is based on a trust of one another. Smith and Jones agree to meet for lunch next Tuesday. Each does so on the assumption that the other will keep the appointment. The penalty for the failure to do so without good reason will be the potentially very heavy one of social disapprobation. Similarly, you have come to this conference expecting to hear a set of papers based on at least some evidence of hard work and analytical endeavour. We speakers have come here expecting to be given a courteous hearing. Neither side of the transaction has needed a third party to assume that these are unrealistic expectations and thus to impose a coercive set of behavioural patterns upon us.

The point is: our governors have been highly inconsistent in their assumptions about human nature and/or in the application of the implications arising from them. What are the rules for drawing a line between the private voluntary sphere and the coercive sphere? All of this, then, constitutes the first objection to this ethical defence of state welfare: its view of, and its imposition of a view of, human nature.

The second objection relates to the 'no guarantees' argument, which ignores the other side of the same coin. Defenders of state welfare argue that there is no guarantee that people by themselves would be philanthropic enough to prevent, say, poor people from starving, or other socially undesirable outcomes; but by the same token there is no guarantee that the present outcomes of the state's involvement in welfare are those that an uncoerced people would produce or would want to produce. If we were each subject to only minimal levels of expropriation, we would each enjoy a much greater capacity to expend our resources as we saw fit. Who is to say, in such circumstances, which 'beneficiaries' of state welfare would be beneficiaries of welfare voluntarily given? We simply do not know if, in such a marketplace of opinion and free action, the unemployed, the homeless, the single parent, etc., would tend to be defined more or less widely or rewarded more or less generously than at present.

But we do know that, in such a society, Brown's identification of Jones as warranting Brown's assistance would be a matter of Brown's exercising his free judgment, which may or may not differ from Black's or White's or Green's. Once again, the 'no guarantees' argument imposes a single moral universe on a society of individuals of diverse moral views. Maybe in an uncoerced society there would be no voluntary versions of the dole or single parent's benefit. Maybe there would be much more generous versions of them. The real point is: the lower the level of expropriation, the freer will be the relations between citizens and the closer we will come to a dynamic set of social arrangements that truly reflects the objectives and values of the people, rather than those of the bureaucrats and politicians. In the end, the 'no guarantees' argument is, to take Tawney's words, 'like using the impossibility of absolute cleanliness as a pretext for rolling in a manure heap'.

The final objection to the second attempt at a moral defence of state welfare is that it ignores objective evidence to the contrary. A large body of econometric scholarship now exists demonstrating that reducing personal income through taxation also reduces personal charitable giving (a number of examples of that scholarship are included in the selected references at the end of this paper). As Russell Roberts observes from his analysis of altruistic behaviour:

> ..., the model ... predicts that private charity first became negligible when government first intervened in a significant way in the charity market. Significant government intervention began in the 1930s and has continued to grow over time. (Roberts, 1984:142)

Roberts concludes:

> Current data and evidence from the Depression yield support to the crowding-out result. The huge growth in public transfers in the 1930s crowded out private antipoverty efforts and fundamentally changed the nature of private charity. Current data also support this conclusion. (Roberts, 1984:147)

There is abundant negative evidence from similar research, which, on reflection, is unsurprising. Regrettably, since recorded history has so few examples of sustained reductions in levels of net taxation, positive evidence is scantier. An interesting exception in recent times has been Britain. Since the early 1980s, that country has enjoyed reductions in both personal taxation and inflation. At the same time, according to the UK Charities Aid Foundation, voluntary giving to independent charities which stood at £7 billion in 1981, had risen by 70 per cent in real terms by 1987.

The End of Mutuality?

The cross-national evidence shows, unsurprisingly, that taxation reduces our financial capacity to give to those whom we perceive to be in greater need than ourselves.

There is a great danger that taxpayers will become resentful of those in even greater need whose income consists exclusively or overwhelmingly of tax-based benefits. This resentment can take two forms. The aggrieved taxpayer may feel, 'They're not really in need. They're getting my money under false pretences. Part of the reason for my financial struggle is that such undeserving people are getting money that is rightly mine'. Or he may feel, 'I've already had a substantial part of my income taken from me in order to pay for large government bureaucracies that look after the needy. I've already contributed to the needy. I'm not going to contribute any more. I can't afford it anyway'.

For societies like ours, the development of such sentiments has serious potential consequences. They threaten the fabric of mutuality that has always been shared by fellow citizens of liberal societies. They threaten too the sense of obligation and responsibility that the relatively better off have always felt towards the relatively worse off. History contains many hideous examples of the consequences of the rise of resentment and the breakdown of mutuality between citizens.

It may be further objected at this point that, while such sentiments would indeed be very dangerous in the way that I have described, there is little evidence that they are gaining currency. In fact, unfortunately, the evidence that they are is all around us. Tax evasion is the most obvious example. There are, of course, many reasons why people seek to evade tax. But we cannot deny that resentment at some of the destinations of our taxes is one of the reasons, perhaps a major one. The more strongly that taxpayers object to some of the uses to which their taxes are put, the more likely are they to try and minimise their tax burden or avoid it altogether. Certainly, if governments such as the present Australian one are to be believed, tax evasion is widespread. Let us consider our reactions to tax evasion and what implications they may hold for a liberal society. In general, those reactions have taken one of two forms.

The tax mix. The more sensible but less popular response is that, since income tax is hard to collect, it should be made a less important element of the general tax 'mix', and that indirect taxes, which are much harder to avoid should be made more important. This response is usually rejected on three grounds. The first is that such taxes would be inflationary. The second is that indirect taxes are more obvious to the taxpayer than direct taxes and so would cause much more (politically dangerous) resentment. The third is that consumption taxes would hurt the poorest members of society hardest.

The first two arguments are easily answered. The first is entirely disingenuous since, if governments were truly concerned about inflation, they would do away with its single greatest cause — government debasement of the currency. The second is an outrageous and paternalistic insult to the intelligence of one's fellow citizens. Apart from claiming that one's fellows cannot be trusted with greater freedom of decision, it also claims that, while they may be too stupid to understand that income tax deprives them of such freedom, they are sufficiently stupid to vote for a politician who believes they are so stupid.

The third argument puts defenders of state welfare into a difficult position. According to the first of the possible ethical defences of the welfare state, the main reason for the state's involvement in welfare is that only the state has the capacity to see where the greatest needs lie and to distribute tax revenues evenly to meet those needs. Let us suppose that a government found that its income tax take was declining in real terms. If it is true that only government can identify needs (whatever their cause) and meet them equitably, then this government would be logically required to abandon its income tax and replace it with a consumption tax, since a welfare state based on an unavoidable tax would produce much more revenue for the government to distribute. This would allow it to define 'needy' more broadly. If it is objected that no good is served by taking money from people only to give it back to them in another form, I can only agree. But what do we abolish first? Medicare? State education systems? The New Zealand Arts Council? The Australian Sports Commission?

Getting tough. The more prevalent response to tax evasion has been to demand tougher measures to deal with, and preferably to prevent, such evasion. Indeed, many governments have tried to close legislative loopholes, have employed greatly increased numbers of taxation officials, installed more advanced data processing systems, and so on, through to (in Australia) the failed attempt to introduce a universal ID system.

We may say two things about such efforts. First, for the reasons outlined in the following section, they are doomed. They simply will not meet the objective of preventing income tax evasion. Second, there is a real danger that they may create problems much greater than those they are supposed to solve. There is disturbing anecdotal evidence from both Australia and the US that tax officials in both countries are becoming laws unto themselves.

I have dwelt on taxation because I believe it is directly relevant to the erosion of feelings of mutual obligation between citizens. Moreover, the 'catch the tax cheats' mentality is of the same order as the 'bash the welfare cheats' mentality. Both focus on the consequences of perfectly predictable government failure. Both propose to compound the problem by adding more layers of equally predictable government failure. In Australia, the failed ID card proposal may have the unintended benefit of making people realise that it is the perfectly logical, if frightening, outcome of years of reliance on and trust in government.

One of the major arguments for the ID card was that it would somehow identify and prevent welfare 'cheating' — a term that only muddies the issue. Let me simply ask: who are we trying to catch? People exploiting loopholes in the rules (or the incompetence or sympathy of bureaucrats) in order to gain welfare benefits they are not technically entitled to? Or people who are seduced by their technically legal benefits into socially undesirable behaviour?

If it is the first, then this is the inevitable product of any attempt at a universal, comprehensive system. The one sure way to make the problem worse is to add yet more layers of rules and requirements containing yet more loopholes. There is no reason to think that governments, after such a long record of failure, are the best means of correcting those failures.

If, however, we are trying to change 'undesirable' behaviour, then we are on much more dangerous ground. The growing demands for 'workfare'-type schemes for those receiving unemployment benefits are stark evidence of the increasing 'welfare resentment' in societies such as ours. Having already lost (in fact, never having had) control over that part of their resources going to such people, many individuals have no other avenue for their resentment than venting a desire to make such people at least change their behaviour and do things they would not otherwise do. To this extent, workfare is merely the late 20th century's version of Bentham's Panopticon, or the late 1980s version of Malcolm Bradbury's 'sado-monetarism'. Moreover, since a government's meeting such demands would not give the demanders a jot more control over what should be their own resources, there is no guarantee that they would not soon demand new and harsher patterns of behaviour modification.

In an important respect, demands for 'workfare' schemes are also an example of the assumption that only government action can cure government failure. They can only lead to yet more layers of intrusion into people's lives, yet more varieties of discretionary judgments by officials (hence yet more erosion of the rule of law), and yet more power for the unaccountable. They will also require many more unaccountable positions to be created and filled.

All of this can only reinforce the frustration and resentment felt by all citizens against the system. It can only lead to a further collapse of the sense of obligation of one to another, and to the creation of yet more barriers between us. It will benefit only one class — the operators of the barriers. As E.M. Forster puts it in *Two Cheers for Democracy*, 'Love and loyalty to an individual can run counter to the claims of the State. When they do — down with the State, say I, which means that the State would down me'.

I'm from the Government and I'm Here to Help You

To this point in the paper, I have been concentrating on the ethical dimension of the welfare state. I have quite deliberately not focused on the welfare state's 'beneficiaries'. In this section I want to compensate for that omission.

If we want something delivered effectively, quickly and with greatest cost-efficiency, then, all of us know better than to ask the government to deliver it. And if government is incompetent at delivering things, a government monopoly is even less competent. If this holds for telecommunications, for airline services, for shipbuilding, for the maintenance and supply of clean water, and so on, why should it be any less true of transfer payments? There is no defence in logic for saying: 'Yes, I know from experience that government is inevitably incompetent at delivery, but of course transfer payments are the sole exception to that rule'. Let me now try and elaborate on that 'inevitably'.

There are many inherent structural reasons why — good as it may be at generating policies — the public sector cannot be effective at implementing them. Perhaps the central difference between the public sector and the rest of the world can be found in the word **control**. It may be said that responsibility for control over government resides in us the citizens, in the politicians we elect, or in the civil service managers who theoretically report to them; but no matter in which direction we sheet home that responsibility, it is virtually impossible to exercise it. Why is this?

Inconsistent goals. First, because government sets up performance measures that tend to be inconsistent with each other. A commercial enterprise sets itself very simple and clear goals, universally shared and objective, against which its leadership can be judged. Even a non-profit voluntary organisation must have clear and public goals, for if it does not it will have a hard time attracting support. Government's goals — to the extent that they exist — enjoy not one of these characteristics.

Large commercial enterprises face the discipline of the capital market. A poorly managed enterprise will attract no buyers for its shares, save those with an interest in taking over the company because it is poorly managed. Any such successful bidder will then take whatever steps he deems necessary — usually including dismissing the management — in order to see the enterprise's performance, and its share price, improve. He and the firm's other shareholders then benefit financially from the company's superior managerial performance. A smaller-scale commercial enterprise usually faces the disciplines imposed by the fact that the manager is also the owner.

Government departments have to cope with no such disciplines. In theory, of course, they are run by electors. If Susan Smith, elector of New Plymouth, doesn't like the way Fletcher Challenge is being run, she can choose not to buy its shares. In that way, if she is right, she will suffer no penalty for any errors committed by Fletcher Challenge's management. But as an elector the only thing she can do about the performance of the senior management of the New Zealand Social Welfare Department is to vote against the party of the Minister for Social Welfare who has refused to take action against (or who has denied) the incompetence (as Susan Smith sees it) of his officials. Her vote is unlikely to be decisive.

Sheer size. The second major reason that it is impossible to control government relates to its sheer size. Now, it may be true that there is no inherent reason why government must inevitably be large. But the plain fact is that no nation in today's world practices 'small government' in any meaningful sense of the term.

What are the implications of government's size for those who seek to control it? In static terms, there is simply too much of it for one head of government, or one set of elected officials, or one body of citizens even to *see* it all, let alone to restrain it. In dynamic terms, as in the animal kingdom, the larger the beast the slower its movements. Even if we manage to convince the beast to move in some new direction (or to move at all), it can do so at a painfully slow speed at best. The chances of achieving radical behaviour modification in such circumstances are slim.

Anarchy. The third factor that makes it impossible to control government is, paradoxically, its anarchic nature. For governments do not engage in only one kind of activity; they do not formulate only one kind of idea for action; they do not follow only one method of carrying out their ideas. Rather, there is seemingly no limit to the areas of life in which government takes an interest. There is no predictability about the 'rules' government will follow in determining what action it will take. And there is no clearly explained, publicly understood set of procedures that government follows in taking such action, even within one program or bureau.

None of this would matter greatly if government were but one agency among many competing for our attention and custom, and if it were able to exercise no coercive powers over us beyond those necessary to maintain physical security in the Hobbesian sense. When, however, it enjoys monopoly coercive status, and follows no rules of consistency, our chances of controlling it are slim indeed. But so too are its chances of exercising effective self-control, so long as rules and procedures are allowed to shift and change:

> Because it very often has to act upon very diffuse goals and programs — which are a product of multiple political compromises — public administration often lacks the basic prerequisites of internal control: no demands on behaviour and thus, no yardsticks for the examination and evaluation of that behaviour are available... If no practical and manifest results are sought by administrative action, the question of control is more or less redundant: it

> is difficult to address non-decision making as an objective of internal control. (Grunow, 1986:648)

There is a further difficulty with government enjoying monopoly status in a delivery area. Like the rest of us, government cannot possess a monopoly of information. This is, of course, just as well, when government enjoys such coercive power. But, from the client's point of view, the essential job of government's formulating and carrying out delivery tasks is inevitably hampered by the inadequacy of appropriate data. This goes a long way towards explaining why — and, again, this is a phenomenon of which we have all had personal experience — government cannot see things from the point of view of those whom it purportedly serves, thus making control so much more difficult. Indeed, as one writer puts it, public sector bureaucracies have

> emerged as major power centers of their own, exercising authority independently of the elected branches and being relatively uncontrolled by them. Consequently, in the modern administrative state, holding the elected accountable does not guarantee that government as a whole will be accountable. (Rosenbloom, 1979:69)

Process vs. outcome. There is, however, one kind of managerial control in which government does interest itself: the control of process. One of the great distinguishing characteristics of the public sector is its concern for **process** at the expense of **outcome**. Public sector committees spend less time trying to find the right outcome than they do deciding the right way to make a decision about an outcome. The issues of who should be consulted, at what levels, at what stages, with what frequency and by whom, are dominant in public sector decision-making. This is the triumph of process. It is also an unconscious admission that process is the only thing over which some semblance of control might be exercised.

No wonder, then, that 'It is a commonplace observation that a government official may take foolish and ineffective decisions all his life without retribution, provided he takes them **properly**, according to due form' (Dunsire, 1986:338). One noted public administration scholar, drawing on a mass of international data, concludes that essential managerial qualifications in senior civil servants are 'underdeveloped' and that, critically, this is an effect of '**the low autonomy for managerial decisions**' (Grunow, 1986:658). In other words, why should I develop the managerial skills essential for the effective implementation of my decisions, when no 'decision' is ever really 'mine'? In taking any 'decision', I must be careful to consider its perceived implications for those above and below me and hence to involve them in that 'decision'. In this way can we all disclaim responsibility for it. The triumph of process, again. The central point, however, is not so much that this is so, but that it must be so.

In societies such as ours, where the democratic ethos still prevails, senior actors in government entities necessarily try to please all of the (internal) people all of the time. This orientation leads to a mass of inconsistencies, which in turn give rise to widespread and cross-cutting hostility, suspicion and resentment. In such circumstances, an entity's capacity for effective long-term action is close to zero. And the larger the entity, the closer to zero is that capacity.

Who benefits most? There is one other crucial effect of the democratic ethos on government. It is a distinguishing feature of the public sector, and yet another constraint on public sector effectiveness. Anyone who has ever tried to renew a passport, or tried to find out from a British Rail ticket collector when the 5.50 for Colchester will actually be departing, or chased a government-owned bus in Sydney, knows that the public sector is different: it exists for the employee, not the customer or client. As a consequence,

> It is almost impossible to 'enforce' proposals for improving performance ... staff members with tenure positions are almost 'immune' from the effects of control ... [T]op officials in public administration complain that they cannot motivate their subordinates because they have no extra qualifications to offer. The regular (and regularly increasing) income is somehow taken for granted; it does not promote attempts to control and improve performance of public administration. (Grunow, 1986:658)

In such a context it is particularly worrying that, the more discretion the bureaucrat has, the greater his potential power over the client (Gummer, 1979:215). 'In the eyes of the poor the law and its officials cause more problems than they solve, and therefore it is better to stay as far away as possible' (Bruinsma, 1980:359).

The lessons from all this should be obvious; the difficulty is in applying them. First, there is the usual 'public choice' problem that the major class to benefit from government welfare delivery is the governing class. The political members of that class are understandably addicted to the idea that they are there 'to do things for people', and they derive great psychological gratification from doing so. They are egoistically incapable of imagining that people could cope without them. There can have been few social welfare Ministers who have not taken real pleasure from announcing increases in the age pension or single parent's benefit. The administrative members of the governing class have an enormous territory to defend against any attempt at reform. They are also the official advisers to the official decision-makers.

The second obstacle lying in the path of necessary change is the attitude of many non-government defenders of the welfare state. An alarming number of such people, it seems to me, when discussing 'the welfare state', are apparently more interested in the state than in welfare. This attitude constitutes a serious impediment to the development of a richer (in all senses) life for the disadvantaged. It ignores Schiller's dictum: 'See that you mistake not the welfare of the Government for Justice'.

I have outlined the difficulties facing reform in this area. I do not have a strategy for overcoming them. I know only that, the greater the element of decentralisation and choice in delivery services, the more powerful will be the voice and the actual position of those who should matter most — the receivers, not the senders (Young, 1971:429ff). I began this section by speaking of 'control'. In the end, the only worthwhile control is that exercised by the client or consumer (Lancaster, 1979:21f). It would be hard to imagine a delivery system less attuned to the welfare of the client than the one in whose unmanaged growth we have acquiesced.

IV. SOME FIRST TENTATIVE STEPS

As with other forms of addiction, our first efforts to free ourselves from the social engineering drip-feed needs to be based on a clear understanding of the problem. This paper has been an attempt to help formulate that understanding. As part of that attempt, I have been concerned to show as well what is not part of the problem, and hence why some apparently 'thinkable' solutions would be terrible mistakes. Above all, if there is to be 'a way out', it cannot involve the compounding of past or existing errors. In particular, we must reject demands for the imposition of more and more layers of discretionary judgment by unaccountable officials. These demands are already coming from a seemingly paradoxical alliance between the governors and the more unthinking opponents of the welfare state.

In fact, that alliance is not especially strange, composed as it is of those who, despite all the evidence to the contrary, think that only government can or should solve problems, even those caused by government. Our first concern should be the possibility that this authoritarian sentiment may be held by the majority of citizens in countries like ours. Our efforts should be directed towards the educative process of helping to encourage a new majority. If we fail, we may be sure that the outcome will be the erection of more barriers between citizens. While we will all be the poorer for this, those who will suffer most will be those least able to make the effort of scaling such barriers.

Second, we need to recognise that government is inherently inefficient at delivery tasks. Moreover, the closer its responsibility for such tasks moves towards monopoly, the more dangerously inefficient it becomes. Of course, there must be delivery agencies, but let them be voluntary, local, even — dare it be suggested? — competitive. Let them be operated by people who feel, and are, closest to those who benefit from their existence: people whose very passion and commitment will do much more to provide them with the necessary disciplines of effectiveness than could ever be found in the management wasteland of the public sector.

Third, and even more important, in order to allow this trust in people to work, we need to understand the necessity of reversing the process of expropriation and coercion. The key to this understanding is the recognition that taxation is at the core of the welfare state 'problem'. This core has two elements. The first is that the more that taxes are reduced, the more wealth will be created, and the richer will all members of society become. The second is this: a society that can sustain its less fortunate members only by distributing the proceeds of expropriation and coercion is morally bankrupt. It is a society whose governors have said to its members, 'You are not sentient, rational beings capable of making judgments about each other. And even if you are, it is not acceptable for you to employ your own resources on the basis of those judgments'. To return to the point about addiction, the very first step, I believe, is to recognise that this is a fact about our society. If we find this morally acceptable — if we concur in the implicit judgment that hordes of civil servants in Whitehall or Washington or Woden Valley are inherently more sentient, more rational and more trustworthy than the rest of us — then we deserve every new tax, every new scheme for handing out benefits by duress, and every new personal identification system thrust upon us.

Fourth, a word about mechanics. My perspective is that of the voluntarist who wants us each to enjoy the greatest practicable sphere of personal freedom and so wishes to see as little interference as possible with people's lives. 'People's lives' includes their spheres of opportunity. I am not suggesting that we should instantly abolish both state provision of welfare and the taxation on which it is based — even if we could. For that would be to interfere in innocent people's lives just as unacceptably as does our present system. To cite an obvious example, we must protect the 55-year-old who is five years from a taxpayer-provided pension that he has been led to expect and around which he has long been making his financial plans.

The nature of our reversal from the present situation must be consistent with our moral revulsion towards it. It may well involve setting long-term but firm and agreed objectives for gradually achieving greater control over the deployment of our own resources and determining for ourselves how we behave towards each other. (And, incidentally, it is 'us': he who waits for the politicians to initiate these changes will die disappointed.)

The lover of freedom, he who wishes to see genuine, long-term improvement in the lot of his least fortunate fellows, or even he who knows that the position of the least fortunate is not improving but hasn't yet realised why — none of these people has reasons for optimism. From the perspective of late 1987, it is hard to see how the entrenched governing interests could be overthrown. But let us at least try and explain the true nature of the issue before us. Notwithstanding many 'free-market' claims to the contrary, there is no 'welfare problem' in societies like ours. There is an absolutely central, and quite frightening, problem with the welfare state.

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Comments on Michael James & David Band

Comments on Michael James & David Band

Martin Krygier

The papers by Michael James and David Band cover a wide range of issues. I concentrate on some of the ethical questions they raise. Others discuss questions of cost, efficiency and effectiveness. I have no expertise in such matters. In any event I will suggest that there is a sense in which such concerns, which dominate public debate, only become relevant once a number of underlying moral questions have been resolved. And since no one has peculiar expertise in ethics, anyone can talk about them.

Moral appraisal of goal-directed schemes of governance — such as the welfare state — can occur at several different levels. I identify four. The deepest such level has to do with the underlying goals themselves. If one considers that the welfare state has been instituted to serve goals that are pernicious or unjustifiable **in principle** then one can reject it in principle, irrespective of how these goals are to be or come to be implemented; irrespective, indeed, of how or whether the scheme achieves them. Such in-principle rejection of a scheme of governance might have issued, for example, from an enlightened reading of *Mein Kampf* or, more controversially, *The Communist Manifesto*, well before anyone had attempted to put either into any sort of practice. Given such an appraisal, unless the scheme has managed to confound its founders' intentions and do more good than harm, enough has been said. If, on the other hand, one supports the goals of the scheme, enough has not been said.

A second level of appraisal has to do not with goals *per se* but with means necessarily presupposed by such goals. Thus if all sides acknowledge that the welfare state can only operate on the basis of compulsory progressive taxation, and one believes such taxation is immoral, then again one needn't

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worry about how it works. Those who criticize the welfare state for inefficiency or ineffectiveness are not operating at this level, but at a less fundamentally critical one. After all, if it is immoral to attempt to equalize through state coercion, and if that is what the welfare state necessarily involves, then it would be no better if it turned out to be effective. On the contrary, it would be worse. All in all, an incompetent burglar is to be preferred to a competent one though their intentions are similar.

Some participants in welfare state debates, however, argue neither about the in-principle justifiability of its professed goals nor of the means it necessarily presupposes. They debate at the third level of appraisal, which concerns the the actual — foreseeable or unforeseeable — consequences of its operations and mechanisms of operation. Does it or doesn't it reduce economic growth? Does it really help those who need help or are its resources soaked up by bureaucrats and the bourgeoisie? And so on.

Fourthy, and often linked to the third level, one can debate the feasibility of alternative ways of approaching the same ends, alternatives sought either on the principle of despair — nothing could be worse than what we have — or more responsibly, by matching and balancing costs and consequences.

Disillusionment at this third or fourth level might well feed back to deeper levels of dissatisfaction, as it did for those for whom the communist 'God' came to fail: having become disillusioned with the Soviet Union they came to reject communism altogether. And unless one can suggest ways to pursue valued ends, other than those ways one rejects, then either one's commitment to the ends or rejection of the means must be suspect. But there is at least analytical point in considering these levels separately. Too often discussion at one level is automatically taken to pre-empt discussion at every other: one is either for the welfare state or against it *tout court*. Arguably the appropriate questions are more complex than that, and so should be the appropriate answers.

David Band and Michael James both favour roughly the same sorts of proposals: welfare should be voluntary not coerced; private not state-enforced or administered. Yet their papers are very different and, notwithstanding considerable overlap, they operate primarily at different levels. Band is above all concerned with the first two levels; James with the second two.

In truth David Band objects to the welfare state at every level, but particularly at the deeper two. When he invited me to comment on these papers, I protested that I am no expert on the welfare state. He replied cheerfully that that was OK, there were too many of them anyway. At the time I took him simply to be side-stepping resistance in order to tie down his programme. I now know that he meant quite literally what he said.

Dr Band's article is fuelled by outrage. For him it is the ethical faults of the welfare state, not its financial cost, inefficiency or ineffectiveness (about which he has some insightful things to say) that matters fundamentally.

According to Dr Band the welfare state is not merely inept at doing good. What it does is wrong: morally wrong and greatly wrong. It is wrong in its ends and it is wrong in its means.

Dr Band has no time for the ends of the welfare state, at least for those pursued by its contemporary proponents. These are taken to add up to a crude Procrustean egalitarianism, envious of individual variations and ignorant of the futility of combatting them. Partisans of the welfare state are deluded by 'the egalitarian chimera'(p.33). They will fail to equalize, since this cannot be done, but in the attempt they do incalculable harm, particularly to liberty; for "The history of attempts to give political and bureaucratic form to the egalitarian ethos, shows that once a single step is taken down that path it turns instantly into a slippery slope'(p.30)

Even if the ends of the welfare state were tolerable, its means are not — not merely in practice but in principle. For these evil means — progressive taxation above all — involve 'coercion' and 'expropriation'. It is these authoritarian evils which must be exposed and which are often ignored, even by opponents of the welfare state.

Throughout the paper this ethical theme is stressed. Thus the welfare state relies on 'squeezing — on coercion rather than voluntary relationships freely entered into by fellow citizens' (p.29); the problem with 'dependency' in today's welfare state is not that it involves the dependence of some upon others — for that is universal — but that dependence in a welfare state stems from the proceeds of coercion and expropriation. The consequences of this coercion are bad for its alleged beneficiaries, among whom is bred 'the supplicant mentality'(p.27), and for its victims who resent their exactions, and among whom consequently is threatened 'the sense of obligation and responsibility that the relatively better off have always felt towards the relatively worse off'(p.38). Overall we are in pretty bad shape.

It is important to emphasize these ethical themes, both because Dr Band himself stresses their centrality in his argument and because, if they are as telling as he believes, then we needn't go any further. He says a lot about the inefficiency of government provision of services as opposed to those provided by the market, particularly toward the end of his paper. Strictly speaking, however, that is just insurance. If you are with him on goals and means, you can stop reading early. I have to confess that I am not with him on these matters and had to read to the end.

There is not space to discuss the many ways in which the goals of the welfare state have been and might be defended. All I would say is that there is no direct line from one such defence, based on the Kantian insistence that members of a human community have a right as persons to be treated with equal respect, to the demand that everyone get the same or the even more fatuous (and despotical) claim that we are or should all be (or should be made to be) identical. The latter are denials of individual difference. The former is a claim of right to be treated as the possessor of 'equal dignity' with others, in the sense explained by Pettit:

> To enjoy dignity is to be such that one does not have to curry favour or demean oneself in order to be assured of a reasonable existence: that is, reasonable by the standards of the society. This benefit is the product in significant part of the goods at one's disposal and so the equalization of dignity would have implications too for social distribution. (Pettit, 1986:65-66)

There have, of course, been tyrannical egalitarians, but there have been, equally of course, non-tyrannical ones, not to mention non-egalitarian tyrants. To be monomaniacally egalitarian is to be, well, maniacal; but one does not have to be a maniac to assert the right of all to be treated with equal dignity.

Respecting people's dignity involves respecting their liberty, not treating them as pawns to be moved around at will to satisfy some Procrustean fantasy. In that I agree emphatically with David Band. But I do not agree that moral egalitarianism or the welfare state necessarily must involve anything of the sort that he derides and, if I may say so, caricatures. There are many such egalitarians who are as committed to liberty as any of us. As one of them — Neil MacCormick — has written:

> My contention is that legal right and civil liberty indeed matter ... for they are indeed essential conditions of respect for persons. But I deny that the protection of civil liberty adequately justifies the inequalities of fortune which a **merely** libertarian legal order facilitates. I assert a debt of justice owed by the haves to the have-nots, a debt payable by redistribution of assets to the latter to secure to them adequate worth for their legal liberties. But there are practical limits on such distribution, bounded by the moral imperative against schemes productive of tyranny. (MacCormick, 1982:15)

It is worth emphasizing that, following MacCormick, I am speaking of welfare — at least for 'those whose economic means are too small to endow legal liberty with any substantial practical worth against those whose means are larger' — not as a claim on charity but of justice. And it further needs emphasis that requiring people to do their duty as citizens — whether by taxing them or for that matter, conscripting them in time of war — is not to treat them as Soviet or Chinese leaders treat their subjects. Abstract words such as 'coercion' and 'expropriation' blur the moral distinctions and hide the moral gulf that separate the way that liberal democracies treat their right-and-duty bearing citizens from the way Soviet and Chinese leaders have treated their rightless subjects. So does talk of a 'slippery slope'. Communist despotism is not the result of a slide down such a slope — it has its own sources which have more to do with the ruthless exercise of power in a misconceived (where not bogus) quest for 'liberation' than with equality. Nor has anything like the ghastly tyranny which communist states have brought to the world ever issued from a welfare state on the slide. Russia was not such a state; nor were China, North Korea, Vietnam or Cambodia.

So I believe that the aims of and means of extracting revenue for the welfare state can in principle be justified. But that does not tell us if any existing welfare state can be justified or even whether it should be preferred to non-state mechanisms for serving the same ends. The questions here become whether the welfare state actually **operates** in a morally just way or in a manner preferable to other ways of pursuing similar goals. This brings us to my third and fourth levels about which David Band has something to say, and on which Michael James concentrates.

Dr James does not, in this paper at any rate, reject the goals of the welfare state. At the very least he is prepared to tolerate their pursuit in order to meet the legitimate expectations that the welfare state itself has raised. Nor does it appear that he rejects state provision of welfare in principle. He argues indeed that far too much attention has been lavished on goals at the expense of an informed assessment of the means chosen to accomplish them. He believes — as does Band — that the welfare state cannot achieve the goals set for it, that many of its activities sabotage those very goals — and threaten other values as well — and that non-state, voluntary arrangements can achieve them in a way that is better, both practically and morally.

There is nothing in a commitment to the justice of welfare that requires that the state should administer or provide it. More particularly there is nothing that requires that the state should have a monopoly in doing so. Belief that certain citizens have welfare rights does require that the state make sure they are protected but not that it take sole responsibility for satisfaction of them. Whether it should do so depends on an assessment of the evidence in light of the values one seeks to achieve and the costs in terms of other values which might be affected by what one does.

It is a deep, and at times tragic, conceit of ideological politics to believe that decent ends naturally spawn the means to achieve them and that these can be used without cost to other important values. There is no reason in principle or experience to believe that. A prudent investor would believe the opposite. At least he would hedge. Yet many optimists about the welfare state, let alone more ambitious rivals on the left, rested with just that questionable assumption. The state has been the repository of many questionable dreams. One strain of socialism, for example, simply couldn't take the state seriously in world-historical terms. It was to be 'smashed' and replaced by an altogether simple machine which, after clearing the ground and burying the bodies, would have little to do and would 'wither away'. Sadly, as the world knows, it is still busy, still burying and shows few signs of withering (cf. Kamenka & Krygier, 1979; Krygier, 1985). Other strains, including — as Dr James observes — the promoters of the welfare state, were confident that, once captured, the state would work like a perfect, frictionless machine to attain the ends for which it was designed. Nowadays such optimism seems a little quaint.

One further argument, raised by Hayek but not mentioned by either Band or James, is that by its effects on law the welfare state endangers the very function that liberals most want the state to perform: protect liberty. The argument goes that the welfare state transforms the nature of law, from being an abstract goal-independent protector of individual rights and immunities to an increasingly intrusive, goal-oriented and unreliable arm of centralised bureaucratic purposes. I am not persuaded that this last development is as comprehensive, dangerous or uncontrollable as some fear. That is partly because I remain profoundly impressed by the differences between societies like our own where law counts as a restraint on power and others with which I have some familiarity, where it doesn't. Nevertheless the transformation in much of law is an important one and the results and long-term implications are not all in.

If these criticisms are borne out they point to heavy costs involved in implementing the welfare state primarily through the state. Whether the costs are worth bearing depends in part on the shortfall between what was sought and what was achieved. But on its own such a shortfall is not decisive. Disappointed optimism is a predicament not confined to the welfare state. One would want to know the answers to at least three other questions:

1. How the benefits actually and justly received from the welfare state compare with what had been available to those with morally and materially comparable claims before it was introduced.

2. To what extent can the welfare state be praised or blamed for the difference? This is a complicated question. It involves not simply 'before and after' comparisons but filtering out a host of other potential contributors — economic change, technological, medical and other advances, etc. — to whatever differences are found, and an attempt to answer what would have happened — and what would not have happened —if what we know as the welfare state had not materialised. This is a question which I have no competence whatsoever to answer.

3. How the benefits justly received from the welfare state compare with what might be justly made available by alternative measures. Here, at my fourth and last level, I find much of interest in Dr James's argument. For whether or not it can be shown that the welfare state has 'crowded out' voluntary provision of welfare and aid, it seems indubitable that optimism about the former has crowded out discussion of the merits of the latter.

In particular I find salutary his stress on the importance of what fills the space between individual and state in the modern world. He is surely right to stress the importance and value of what stands or might come to stand '[b]etween the intimate realm of family and friendship on the one hand and impersonal charities on the other' (p.10). And it is not only proponents of the welfare state who have ignored it. A great deal of modern liberal political theory has talked as though there was nothing of importance there. Certainly many of the quasi-organic links that bound traditional and smaller-scale societies have been much eroded over the past 200 years. But too rarely have writers, such as Montesquieu and de Tocqueville, emphasised that intermediate groupings were precious zones of attachment and protection, under threat from the modern twins, individualism and the centralised state. Indeed it is their existence, robustness, voluntariness and autonomy from state control which is one of the most important protections of, and indices of, civil liberty. So I support Dr James's call for more attention to be paid to such groupings. Indeed I would support their encouragement whether or not his optimism about their welfare-supplying capacities were borne out.

And, while I am prepared to defend the sort of 'coercion' involved in progressive taxation, voluntary provision — particularly of the sort that encourages mutual cooperation and participation — might well, if adequate, be preferable. I resort to this awkwardly qualified way of speaking, for relationships between benefactors and those in need of benefits are frequently morally problematic. They are easier for the former to manipulate or escape than for the latter. Moreover not every relationship outside the state is equally 'voluntary' for every party to it. On this surely the sociology of domination has got something right. There is enormous scope for morally relevant differences between kinds of non-state relationships. Weaker parties can be locked into relationships that are exploitative or demeaning — and if one usually the other.

Nevertheless, if it were to turn out true that '[a]ny "morality of cooperation" that prompts individuals spontaneously to provide welfare in areas that the state currently ignores would spread into areas from which the state withdrew' (p.20) then that is a powerful argument for considering withdrawal. So long as alternatives to the state do not involve demeaning exploitation, stigmatisation or arbitrariness, it seems to me that nothing in support of the idea of a right to welfare requires that the state alone provide it. To the extent that initiatives of the sort Dr James supports are cheaper, more effective or simply **preferred** to provision by the state, I see no reason to opt for the latter and certainly no reason to grant the state monopoly over it.

However I should re-emphasize that I regard certain forms of welfare as claims of right, not charity. I would thus not be satisfied to rely on David Band's assurance that: 'there may exist a wide range of motives for the relatively better-off to assist the relatively worse-off. These might include: plain unselfish generosity, egoism (making oneself feel better about oneself for giving), desire for esteem in the eyes of others, and so on'(p.35).

Of course there may be such motives, and where they can be promoted they should be. But, if there is one thing a lawyer can say about these complex matters, it is that where **rights** are concerned one should not be left to rely on benevolent motives.

Conclusion

So I end all over the place. I support the welfare state, am sceptical about the means chiefly used to implement it and favour serious thought about alternatives to it. May I conclude by saying a word in favour of this sort of wishywashiness, against the perhaps more satisfying clarity and consistency of both those who **know** that the welfare state is evil, misguided, hopeless and in every way worse than the free market **and** of those committed to defend the welfare state against any alternatives. Please let me recall the manifesto of that 'mighty International that will never exist', the Conservative-Liberal Socialists. Their credo was originally recorded by their founder and only member of whom I know, the Polish philosopher Leszek Kolakowski. I have edited it considerably for my present purpose:

> **A Conservative Believes:**
> ... That in human life there never have been and never will be improvements which are not paid for with deteriorations and evils; thus, in considering each project of reform and amelioration, its price has to be assessed. Put another way, innumerable evils are compatible (i.e., we can suffer them comprehensively and simultaneously); but many goods limit or cancel each other, and therefore we will never enjoy them fully at the same time. A society in which there is no equality and no liberty of any kind is perfectly possible, yet a social order combining total equality and freedom is not. The same applies to the compatibility of planning and the principle of autonomy, to security and technical progress. Put yet another way: there is no happy ending in human history...

A Liberal Believes:

... That the ancient idea that the purpose of the State is security still remains valid. It remains valid even if the notion of 'security' is expanded to include not only the protection of persons and property by means of the law, but also various provisions of insurance: that man should not starve if he is jobless; that the poor should not be condemned to die through lack of medical help; that children should have free access to education — all these are also part of security. Yet security should never be confused with liberty...In fact security can be expanded only at the expense of liberty. In any event, to make people happy is not the function of the State...

A Socialist Believes:

... That it is absurd and hypocritical to conclude that, simply because a perfect, conflictless society is impossible, every existing form of inequality is inevitable and all ways of profit-making justified. The kind of conservative anthropological pessimism which led to the astonishing belief that a progressive income tax was an inhuman abomination is just as suspect as the kind of historical optimism on which the Gulag Archipelago was based ...

So far as I can see, this set of regulative ideas is not self-contradictory. And therefore it is possible to be a conservative-liberal-socialist...

As for the great and powerful International which I mentioned at the outset — it will never exist, because it cannot promise people that they will be happy. (Kolakowski, 1978)

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Comments on Michael James & David Band

Hugh High

In order to properly criticise and evaluate these papers I first wish to discuss each paper in turn, necessarily recapitulating some of the main threads of their arguments and then, secondly, turn to the broader themes discussed by each.

David Band's paper begins, quite appropriately, by defining the welfare state, as that which delivers state-funded 'generosity' to the recipients. His definition is not the more narrow one, by which "income security" is delivered to the alleged beneficiaries thereof. It begins by asking why we have recently seen such unprecedented debate over the welfare state'. He suggests there are two dominant reasons: its growing cost and the creation of underclass of permanently dependent citizens.

As to the first source of concern about the welfare state — its growing cost — while Dr Band does not expressly say so, he would doubtless agree and does implicitly suggest, that the real reasons for the growing cost are (a) demographic trends (which, of course, have been mightily altered by the incentive structure created by the welfare state itself) and (b) the relatively greater inefficiency (as defined in terms of output per input, i.e defined rather more narrowly and in the conventional terms of the principles of economics) of the government that distributes these welfare benefits.

After acknowledging that one of the sources of rising welfare cost is demographic trends, Dr Band then quickly moves on to the rather more

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important source of rising cost to the welfare state, which he quite properly points out, is not an express monetary cost, but is a cost best measured in moral and/or ethical terms — the creation of a permanent **underclass** of our fellow citizens, and the dependency of them on the state. This raises, of course, important moral issues. Dr Band argues that the real issue isn't cost qua cost but rather is coercion. He points out that the rising and growing cost of the welfare state serves, quite simply, to directly and absolutely harm the poor. Examples are abundant. The important moral cost imposed by this growing dependency is the immense coercion of the underclass by those who act in the name of the state. These costs of the welfare state are 'ethical costs', including, but not limited to, the coercion attendant upon seizure of property by the state; and the creation of, arguably, immoral incentives amongst those dependent upon state largesse. And, most important — certainly most important to Dr Band — is the erosion of feelings of mutuality and obligation among the citizenry. Or, to put it in the New Zealand context, the fact that the growing welfare state serves to destroy, rather than create, a 'just and caring society'.

Along with our predecessor, Adam Smith, Dr Band reminds us that the state has only one source of income — citizenry. At most, it can but take from one set of citizens and give to another. This leads, of course, to the question (which he then very aptly poses) of why we should think that a society of relative equals is somehow morally preferable to a society where people are left to enjoy the fruits of their labour. Having made this insightful observation, he rightly suggests that the welfare state is constructed on very shaky ethical grounds indeed.

While Dr Band doesn't expressly say so, it is arguable that the 'moral' foundation of the welfare state is absolutely immoral. He begins by noting (and for this I applaud him) that it is seldom asked why, in the first place, it is ethical at all for the state to seize property and redistribute it. Such coercive activity, by its very nature, carries with it immense moral cost and damage; and it is this moral cost and damage which is of the greatest interest to Dr Band. He says, quite correctly, that the moral damage done by the 'rising welfare state' has served to importantly 'crowd out' altruism. Thus, ultimately, the defenders of the welfare state are suggesting that man is inherently imperfectible; and, that in order to induce one man to support another, he must be coerced to do so. This, of course, degenerates (as Band properly notes) into a set of arguments as to whose value judgements shall count: those of the defenders of the welfare state who wish to coerce me to support my fellow man; or those of us who, with Dr Band, are perhaps more romantic and think that were there no (or at least only a minimal) welfare state then considerably greater altruism, caring, and compassion would be forthcoming.

Dr Band then moves to his second source of attack on welfare state: that the welfare state provides no assurance that the outcomes provided by it are those which people, in fact want. Indeed, as he suggests, there is immense evidence, especially econometric evidence, to suggest that, in the presence of lower levels of state expropriation, the voluntary redistribution of material goods from those of us who enjoy greater incomes and wealth to those of us with lesser incomes and wealth would be greater than in the presence of this state coercion. And, therefore, presumably the 'mix' of goods provided would also be different. Dr Band notes that (as we have been taught more recently by econometricians and those in the field of public finance) to the extent that we are taxed, we reduce our predisposition to give to our fellow man, so that our fellow man is on balance worse off in the presence of taxation than he would have been in the absence of such coercion and expropriation.

Moreover, I would suggest (with Dr Band), this has important long run consequences, among which are:

- enhanced levels of tax evasion — which we have observed;
- increased levels of welfare 'cheating' — which we also have observed;
- and (based on a widespread and pervasive amount of anecdotal evidence) disenchantment with the state by the poor.

Dr Band, then, turns to what I think is the central issue regarding the welfare state. The central issue is not that the welfare state is inefficient; not that it destroys a 'just and caring' society; not that it destroys altruism and goodwill between men. Rather it is — as Dr Band well puts it — that the state is intrinsically anarchic, and enjoying a monopoly of coercion, it needs to follow no rules of consistency whatsoever. The central problem is not that the welfare state is less efficient and that to try to make it more efficient is mere 'tinkering'; the problem is not the promotion of altruism. The problem is that of giving to the state coercive monopoly powers, and then foolishly expecting it to be able to control its monopoly of coercive power.

Dr Band discusses potential solutions for the problem of the welfare state. In doing so, he is considerably more sanguine than am I. He thinks that, the very governors of the welfare state may well come to realise some of their errors of the past; he thinks that the rising efficiency in the delivery of welfare benefits will help lead to an increasingly competitive and voluntary environment. He has immense faith in the education of our fellow citizens. He suggests that the key to attacking the welfare state problem is, as a first measure, the reduction of taxes so that more wealth will be created thereby and all made better off. While, in this regard, he is certainly in good company, e.g Milton Friedman, I suggest this is but part of the problem. The issue is, with respect to taxation, as he seems to note, that taxation is ultimate coercion. Merely reducing the amount of coercion simply reduces the amount of pain; it does not make for a moral case for the coercion. Thus I can agree fully with David Band that, 'there is an absolutely central and quite frightening problem with the Welfare state'(p.47).

Dr James's paper, like Band's, starts by noting that the people are disillusioned with the welfare state and Dr James asks 'What went wrong?' His major answer is that the welfare state has been concerned almost exclusively with ends and not means, so that the very erection of the state has not made people more caring, or altruistic, etc., but rather has merely served to make them adapt their behaviour, and to respond to the incentives put in front of them by the state.

Now, my response as an economist to this observation by Dr James, (and indeed the similar statement by Dr Band) is that only the very naive would have thought otherwise! Of course that is what architects of the welfare state were — and are: rationalists who continue to believe in and hope for the perfectibility of man.

Dr James notes that the people in the welfare state (a) adapt their circumstances, so as to qualify for the benefits of the state (not surprisingly!); and (b) try to manipulate government so as to redistribute government benefits to themselves. Both these activities, I submit, are highly predictable; and it does us no good to condemn the beneficiaries for responding to the incentives placed in front of them. The goal, rather, is to alter the incentives.

Dr James then goes through what he calls the 'citizenship theory of the welfare state' literature. This is superb literature review. The literature, taken as a whole, says that 'full members' of the state have certain reasonable expectations of the state which the state should meet so as to ensure that the citizen can fulfil his role within the state: that, for example, the state cannot tap the citizens' altruism, his 'higher' values, unless everyone is well fed, well housed, and so on. That is, the 'citizenship theory' says that the state must 'free' man from coercion, so that he can fulfil his duties as a 'citizen'. The problem with the argument is that it assumes that other members of the state have a **duty** to feed, to house, etc. their fellow citizens. This is a heroic assumption — that I have a duty to feed you, or vice-versa — and one which, intrinsically, smacks of coercion. A second difficulty underlying the citizenship theory is that it presumes that only the state can free man from coercion. This is, frankly, a silly assumption, for the state 'frees' man via the 'collectivity' and does so in an inherently coercive manner. It is curious to me that those who would free me from coercion want to use coercion to do so.

Dr James then goes to what he considers to be the ideological heart of the welfare state; to wit, its assumptions. In doing so, he very importantly points up something that socialists have long ignored (and economists have inadequately articulated): that one cannot separate, after all, production from distribution. Socialists have focused on the distribution of the fruits of the economic order; but, necessarily, this has important implications for the productive process and therefore for the amount of fruits which can then be distributed. Those of us in the economics profession, it must be confessed, have woefully failed in our duty to make socialists face up to this problem.

Dr James next argues, as does Dr Band, that the welfare state has done vast damage to the very notion of altruism and caring — to the idea of voluntary welfare. And he cites, among other things diminishing charitable gifts attendant to rising government taxes.

Dr James suggests, rather naively, I think, that, somehow, we can gradually phase out the welfare state; that the governors of the welfare state will somehow devolve the welfare decision-making process on to voluntary action. I would suggest, that state welfare encourages persons to act in a coercive manner towards their fellow-citizen and that it is most unlikely that the governors thereof will give up their rights of coercion. Perhaps, however, this reflects my own view of mankind and his imperfectibility.

In summary, there are two central themes running through the papers. The first is that, at long last, it appears that citizens have realised that the welfare state is inefficient. Both authors are fairly optimistic that this may well lead to a lessened reliance upon the welfare state. I would rather suggest that, in the fullness of time, it might lead to more, and yet further coercive tinkering by the architects of the welfare state, who after all have vested interest therein. I see very few bureaucrats jumping into the private sector.

The second theme running through both papers is that to the extent we have a larger welfare state, we have 'crowding out' of private altruism; and both authors seem to suggest implicitly that this leads to a less desirable society than most of us would want. The authors conclude, or are at least hopeful that, the welfare state will be made increasingly small. Similarly, both authors recognise that, after all, the problem of the welfare state is not one of efficiency; and it is not one of diminishing altruism. It is, rather, the inherently coercive might of the state.

The American Experience with the Welfare State

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The American Experience with the Welfare State

Charles Murray

I. THE GREAT SOCIETY

I shall begin with a description of what has been happening to social welfare policy in the United States, then turn to my own thoughts about what it all means for the future.

First, it must be remembered that the US underwent a sort of revolution roughly twenty years ago. When President John Kennedy came to office in 1961, he was presiding over what was undoubtedly the sorriest excuse for a welfare state in the Western world. As recently as then, the only welfare measures that the American national government underwrote were modest payments to the unemployed and to single women with small children to raise, and a social security system for the elderly that provided a small monthly stipend cheque to most (but not all) people over the age of 65. Only 25 years ago, there was no national medical assistance program. There was only a minuscule public housing program, no food programs worth mentioning, no social service programs, no job training programs, no federal role in education. Furthermore, there was no strong political pressure to make major changes in that system. When Kennedy was assassinated toward the end of 1963, the prospect for major legislative changes in social policy was still generally thought to be near zero.

Then Lyndon Johnson came to office, a master legislator who hungered for political immortality and who was promptly given a huge popular mandate in the national election along with huge majorities in both Houses of Congress. Combine that with a reform-minded Supreme Court that, from the early 1960s onward, issued a sequence of decisions with sweeping impact on everything from criminal justice to education to sexual mores to electoral systems, and the result was very much like a revolution.

It was partially a revolution in money. All of the programs I just said the

US did not have in 1961 were in place by 1967, and growing rapidly: medical insurance for the needy and elderly, large educational subsidies, expanded public housing and housing subsidies, large training and jobs programs. To put it graphically, consider welfare expenditures on working-aged people and their families, as shown in Figure 1.

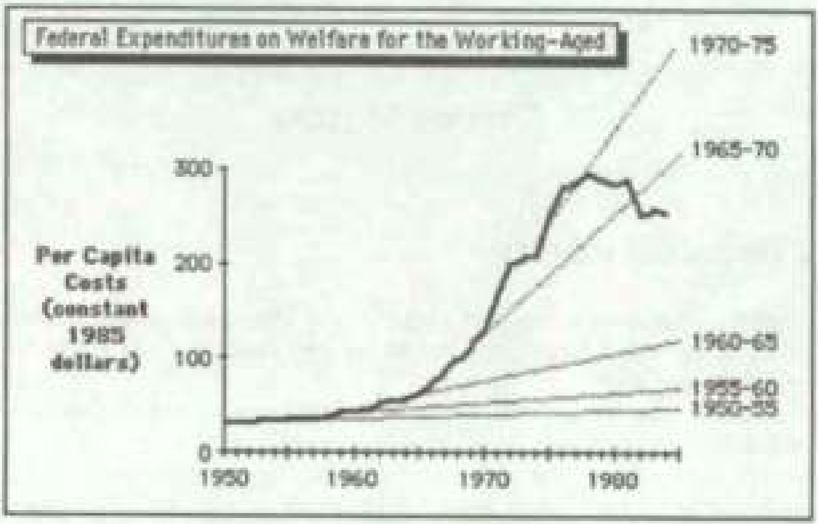

Figure 1

As you can see, the slope shifts sharply upward in the last half of the 1960s and then continued to steepen through the mid 1970s, until inflation ate into the purchasing power of budgets (which in nominal terms continued to increase until the Reagan Administration took office).

But the money was the least of the changes that made up the revolution. What really happened during a concentrated period of time, roughly 1963–67, was that the elite wisdom about poverty underwent a transformation. It was not just that by the end of that period certain types of legislation had more support than formerly, but that the premises — the 'everybody-knows-that' premises — shifted in the minds of the people who were instrumental in making policy.

Race relations. Before 1963, the consensus elite wisdom held that justice for American blacks lay in moving toward a colour-blind society, to assure equal opportunity. By the end of 1967, the consensus elite wisdom held that justice for American blacks lay in preferential treatment for blacks, to assure equal outcomes.

Poverty. Before 1963, it was taken for granted that the American economic system was a success; that anyone who was willing to work could make a decent living. Poverty was seen as something confined to a few isolated pockets of American society such as migrant workers and Appalachian farmers. By the end of 1967, it was taken for granted that the US was a nation with a huge number of people trapped in poverty.

The role of a job. Before 1963, it was taken for granted that if you had a job, you didn't get welfare benefits of any sort. If the job didn't pay enough, it was up to you to get yourself a better one. If you had so many children that your pay cheque wouldn't stretch as far as you wished, that was your problem, not society's: no one had forced you to have so many children. By the end of 1967, it was taken for granted that of course people with jobs — the newly discovered 'working poor' — should get benefits if their family income fell below an acceptable level.

But these are all specifics. The overarching change was this: Before 1963, American social welfare policy was grounded in the assumption that the American economic and social systems were benign and self-correcting. By the end of 1967, policy was suffused by the assumption that these systems were deeply flawed and tended to perpetuate evils. The new assumption was that the system is to blame. Along with that new assumption necessarily went another assumption: Individual people are *not* to blame. If a youngster skips school and doesn't study, it is because of an inept or insensitive school system. If poor people commit crimes, it is because of their deprived environment. If a young woman has a baby without benefit of a husband, it is because of the prevailing social and sexual mores. If people are poor, it is because of an unjust economic system that fails to distribute wealth fairly.

And so, armed not just with money but more importantly with a new set of premises about how people work and how the world works, the US undertook its War on Poverty and set out to build the Great Society. But over a period of years, as the programs continued to expand during the 1970s, the realisation gradually spread that things were getting worse, not better, for blacks and poor people. It was seldom put in just that way. But few could avoid recognising that the inner cities were more violent and ravaged than ever before. Drug use was endemic. Unemployment in poor communities stood at preposterously high levels — 40 and 50 per cent for black teenagers, for example. High schools in poor communities were giving diplomas to students who were still functionally illiterate. In fact, analysed closely, it became apparent that something had gone very badly wrong.

A few examples will illustrate the general point. I begin with the trend for the central target of the War on Poverty, poverty itself. In the early 1960s, a task force within the American Department of Health, Education, and Welfare created a 'poverty index', supposedly representing the amount of money (adjusted for family size) needed to live a modest but decent existence. The precise dollar amount represented by a poverty index is, of course, arbitrary, but it provides us with a useful measure for analysing trends over time. The proportion of Americans below the poverty line from 1950 to 1985 is shown in Figure 2.

Figure 2

The startling reality is that improvement was stopping, not starting, as the reforms were implemented. Poverty did fall during the five Johnson years, from 18 per cent of the population in 1964 to 13 per cent in 1968. But the rest of the graph reveals the fallacy of linking the reforms with the improvement. In the first place, as suggested by the earlier figure, the reforms had limited budgets during the Johnson administration. They were orders of magnitude larger during the 1970s. Secondly, the declines in poverty prior to 1964 were substantial — from 30 per cent of the population in 1950 to the 18 per cent of Johnson's first year. Essentially, the Johnson administration, operating with the advantage of a boom economy, accounted for its 'fair share', but little more, of the progress against poverty during 1950–68. Then reductions in poverty slowed and halted, reaching bottom in 1973.

The most obvious candidate explanation is that the economy turned sour in the 1970s. But, to summarise extensive analyses that have been conducted on this point, that explanation is unsatisfactory. The very relationship of the poverty numbers to economic growth changed. For example, from 1950 through 1968, an increase in a percentage point of GNP was associated with a drop of 0.34 percentage points in the poverty rate; from 1969 through 1985, the same increase in GNP was associated with a reduction only half as large (0.17 percentage points) in the poverty rate. In other words, what was happening to the poverty rate had become largely disconnected with economic growth.

II. WHAT WENT WRONG?

When one explores why this turn of events has occurrd, a variety of explanations is available. Looming above the others are two phenomena: A large-scale increase in the tendency of young women to have children without a husband and an equally large-scale increase in what might be called 'voluntary unemployment' among young males. Both of these effectively ensured that the poverty statistics would get worse — even though more money was being poured into transfers, it failed to keep pace with the increasing number of adults who depended on such income to sustain them.

In interpreting the statistics on these indicators, my thesis is that the US has not been witnessing a change in the behaviour of the general population but instead a profound change in the behaviour of people growing up in low-income families. In my own work I have used statistics

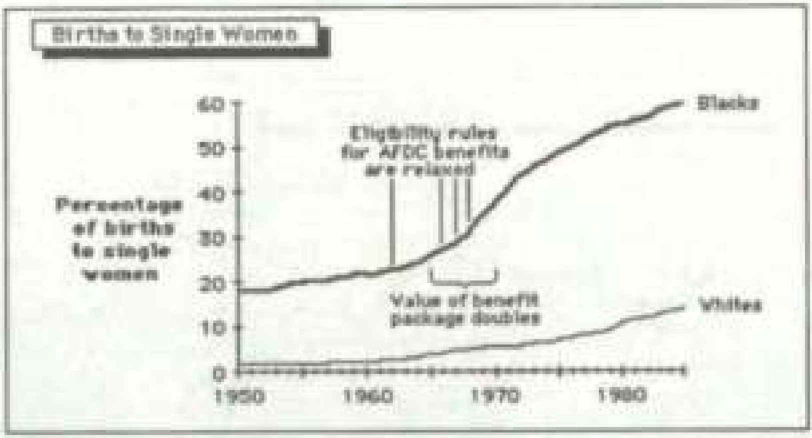

Figure 3

comparing blacks with whites to make this case, using 'black' as a stand-in for 'low-income' and white as a stand-in for the middle-income and affluent classes. I should note that to the extent my thesis is right this rough comparison softens the evidence, because the black 'lower-class' trendline is contaminated by many middle-class blacks and the white trendline is contaminated by many lower-class whites. Nonetheless, the contrasts remain striking. I will give just two examples among many.

In the case of children born to single women, the trends are shown in Figure 3. From 1950 to 1965, the changes in the proportion of children who are born to single mothers were comparatively minor — from 2 to 4 per cent for whites, from 18 to 26 per cent for blacks. In the next 20 years, the proportion of black children born to single mothers ballooned from 26 per cent to 60 per cent, while the white rate increased from 4 to 14 per cent. When such figures are broken out for poor communities, the picture is still worse: in Harlem, for example, more than 80 per cent of all black children are now born to single women. In poor white communities, the figure is up to a quarter of all births, roughly the level of blacks as of the mid-1960s. Meanwhile, in middle-class communities, the proportion of children born to single women remains small, usually under 10 per cent and often still lower. From supplementary work I have done, it appears that if the lines in Figure 3 could be divided into 'middle-class' and 'lower-class', the middle-class trendline would be nearly flat.

Next, consider labour force participation among young males. Labour force participation as I am using the term means that a person is either employed or unemployed but looking for work. See Figure 4.

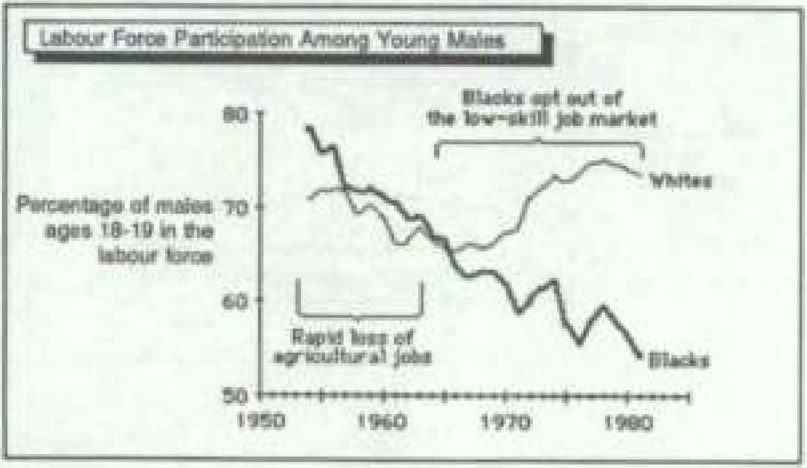

Figure 4

The shift is striking. In the 1950s, as agricultural jobs in the South disappeared, the labour force participation of young black males nonetheless remained substantially **higher** than for young white males. Then in the 1960s, the proportion of young white males in the labour market stabilised, while the black rate continued to drop. In the 1970s, the white rate increased substantially, while the black rate continued to drop. By the early 1980s barely more than half of young black males were in the labour force, compared with three-quarters of whites.

I have discussed elsewhere a variety of explanations for this phenomenon: that white baby-boomers drove young blacks out of the labour force, that blacks became discouraged from looking for jobs, that the blacks who dropped out had begun going to university instead, and so forth. None of them work. For whatever reasons, large numbers of young blacks simply dropped out of the labour force. More specifically, blacks opted out of the low-skill job market. From 1965 to 1980, the number of blacks holding low-skill jobs **dropped** by 117 000, during a period when American economy created a net of 4.8 million new low-skill jobs and black unemployment was steadily rising.

I could cite other examples in employment, education, and crime rates, and even health, but the thesis should be clear: The revolution in social welfare policy in the United States was accompanied by a variety of social trends that had profoundly unhappy consequences for the very people that the policies were intended to help. In my view, the relationship was causal. In effect, as I argued the case in a book called *Losing Ground*, the new policies changed the rules of the game for poor people and especially for poor young people. The effect of the new rules was to make it profitable for the poor to behave in the short term in ways that were destructive in the long term. We made it economically possible to have a baby without a father, possible to get a high school diploma without studying, possible to get along without a job, possible to commit crimes and suffer no immediate consequences. In the long term, all of these behaviours still had disastrous consequences: that didn't change. But we masked those long-term consequences by softening the short-term consequences, and thereby subsidised irretrievable mistakes.

III. THE CHANGING DEBATE

This interpretation has been subject to a fierce debate in the US, but over the last half-dozen years that debate has changed significantly. I no longer have to defend a variety of things I used to have to defend. Let me give you an example. In the late 1970s, the Carter administration tried to organise a White House conference on 'the family.' It failed — the conference actually had to be cancelled — because the Democratic Party, the leading political party in the US, was unwilling to offend powerful constituencies by saying out loud that the husband–wife family is a more functional social institution than a single-parent family. If, ten years ago, I had presented the labour force participation trends to a college audience, I can guarantee the response: I would have been hissed, for obviously I would have been an evil man for suggesting that blacks ought to take 'demeaning', 'dead-end' jobs.

Mind you, I can still get hissed by any number of college audiences. But more and more commonly in the US, it is recognised that it is important to a community that the two-parent family predominate, for reasons having nothing to do with abstract morality. It is simply a fact that when a teacher confronts a classroom in which perhaps four out of five children have grown up without fathers, that teacher is going to have a hard time teaching. In such a community, young males will behave in destructive ways, for their role models are not men earning a living and supporting their families but the most successful local pimp or hustler. In that community, young women will still aspire to have babies, as young women do everywhere, but they will not expect to do so within marriage — hardly anyone in their ken does, after all. Unlike a few years ago, such observations about communities with predominantly single-parent families are now intellectually respectable.

Similarly, it is now fairly easy in the US to say that it is a good thing for people to work at jobs, even if those jobs are 'demeaning' or 'dead-end.' There is a growing agreement that for a young adult to be idle, hanging out on street corners, is not just bad for the GNP but bad as well for that young adult. That way does not lie a fulfilling life.

Furthermore, there is now broad agreement, unlike a few years ago, that there is such a thing as an 'underclass' in American society, numbering several million people; an 'underclass' of people who are behaving in ways that ensure they will never participate in mainstream American society no matter how much welfare they are given or even if they are given a job.

IV. THE FALSE PROMISE OF WORKFARE

All these changes in the American debate are for the good. But, speaking as a person who has tried to promote such changes, I am a little dismayed by the way the newly revised elite wisdom is being translated into policy. In the American Congress, for example, we are now hearing enthusiasm for a new wave of solutions. What Americans call 'workfare' is suddenly fashionable — 'workfare' meaning programs that require welfare recipients to take a public service job to qualify for their benefits. We are told that we ought to have new laws to force men to support the children they father, giving (for example) government the right to deduct child support payments directly from pay cheques.

I am not sure this represents progress. For most of my career, I made my living evaluating the results of social programs. Putting on that hat for a moment, I am willing to predict what will happen. A few early successes will be publicised on the television news programs. Then the more careful evaluations will start coming in, and it will turn out that the early successes were anecdotal and illusory. The next step in the cycle will be to examine the reasons for lack of success. The evaluators will round up the usual suspects: inadequate funding, untrained staff, problems with supervision, design flaws. But as attempts are made to solve these problems, it will become increasingly clear that the problems are not idiosyncratic, but built-in. There is no such thing as the error-free implementation that will finally vindicate the program concept.

Worse yet, we will find once again that what we want and what we get from social programs will turn out to be mirror images. 'What we want' with workfare and the rest of the new solutions is to bring people back into the mainstream of American society. We want them to become productive, independent citizens. 'What we get' will be a new game that we have set up for poor people. With workfare, the prize is a benefit. The state says, 'To get this prize, you have to do some work unless you are exempt because of conditions A, B, or C.' If he (or she) fails, and ends up having to do that work, he is double stigmatised. The middle-class folks drive by as he rakes leaves for the city and are pleased that at last some of those welfare loafers have to do a little work. His friends from his neighbourhood drive by and laugh at him for having so little savvy that he can't evade the work requirement, so little self-respect that he lets himself be forced to comply. Or consider the ambitions for strict child support laws. The child support laws being contemplated do not demand that the man support his child no matter what or face criminal penalties. Rather, the man will have to support his child unless he is unable to do so — which constitutes a looming incentive for the man to be visibly unemployed at strategic moments and to keep his visible earnings below the minimum set by the program.

I am suggesting that we are about to prove Santayana's dictum that those who forget history are condemned to repeat it. As in past programs, the government will set up a game that anyone with a little imagination and pride can beat. We will not socialise people into the world of work. We will socialise them into the world of the scam and the con.

More generally, the current proposals for reform miss the point. They suffer from the same hubris of the reformers of the 1960s, vastly overestimating the power of governments to micro-manage human responses. One must constantly wonder at the naiveté of the planner's mentality, whether the planner is an American trying to use government to change the incentives of welfare mothers or a Soviet trying to manipulate the behaviour of Ukrainian farmers. Welfare mothers and Ukrainian farmers alike have a tendency to respond to reality, not to the scenario envisioned in the planning document, and the two are virtually never the same. The overriding fact is that working 40 hours a week at low-wage menial job is not something that a young person will choose to do unless there is a good reason for it. A young woman who wants a baby will not refrain from having a baby unless there is a good reason for refraining. And the 'good reason' ultimately must be grounded in the real consequences of such behaviours. I would argue that the US got into its present mess because in the 1960s it really did massively alter the consequences, and thereby removed the natural sanctions that historically have ensured that young people are prepared to work and that children are born within the framework of marriage. Behaviour changed accordingly. The present reforms leave the reality established in the 1960s essentially unchanged, and I predict that, accordingly, behaviour will change very little.

Furthermore, the current wave of reforms ignores what I believe to be another lesson that has been thoroughly documented by the hundreds of social experiments and demonstration programs conducted over the last two decades: For many of the problems we lament, we do not have it within our technology to do certain kinds of good. When a child comes to kindergarten never having heard the alphabet recited nor having seen a book, sometimes not even knowing the names of colours, we do not know how to compensate for the deficits in stimulation that the five-year-old already suffers from. We literally do not know how to change the values and behaviour of large numbers of people who have grown to adolescence with sociopathic values or no values at all.

None of this is visibly dimming the enthusiasm of the reformers, whether they be conservative or liberal — I have a sense of *déjà vu* about the optimism I observe, so reminiscent of the early days of Johnson's War on Poverty. 'This time', I hear people saying, 'we have figured out how to do it right.' What will happen when the optimism is dashed? Who will be blamed? Will the program designers finally decide they are up against some basic constraints on state interventions? Or will they persevere with another wave of ideas?

My best guess is that the US will continue to tolerate a continuing underclass of roughly the size that exists now. If I may be cynical — and there is some reason for cynicism — the important thing about social welfare policy is not that it helps the poor, but that it makes the people who support the system feel good. In particular, the politicians and policy analysts who talk about social welfare policy seem able to tolerate any increase in actual suffering as long as the system in place is supposed to be dealing with it. So people will keep saying that we must do better, and keep coming up with minor reforms that don't accomplish much. For 20th-century Americans, the underclass and government social workers play much the same role that the heathens and the missionaries played for 19th-century Americans: actors in a morality play to be watched as distant spectators.

V. SOME REFLECTIONS

Let me close with a few thoughts about how I would direct the future debate about social welfare policy, if I could. (And I'm trying.)

It seems to me that the American experience of the last half-century and more specifically of the last two decades must arouse in any thoughtful observer this question: What constitutes 'success' in social welfare policy?

For many years — certainly during my own training during the 1960s and early 1970s — social science faculties in our universities assumed a substratum of truths about why certain policies were good or bad things, and policy analysts did not have to think very hard about why the outcomes we analysed were good or bad. We knew. Fighting poverty had to be good. Fighting racism had to be good. Fighting inequality had to be good. What other way of looking at good and bad might there be? And what other way of measuring progress might there be except to measure poverty, crime rates, school enrolment, unemployment?

The trends I described earlier in this talk demonstrate how troubling this assumption has become. Fighting poverty is good, yes. But if the amount of money being given to poor people increases while the proportion of children born to single women also increases, how are those two vectors to be combined so that we know whether, in the aggregate, we are headed forward or backward? Fighting racial discrimination is good, yes. But if the laws against discrimination in housing are made ever more stringent and actual segregation in housing increases, what are we to make of it? How are we to decide what course so navigate in the future?

Underlying these questions are others that ask not just how we are to add up conflicting indicators but rather the more ancient question, What's the point? What is the point of food stamps, anyway? What are they for? Suppose that we passed out food so freely that no young man ever had to worry about whether a child that he causes to be conceived will be fed. Would that really be a better world for children to be born into? Or let us take food writ large: Suppose that we made all material goods so freely available that parents could not ever again take satisfaction from the accomplishment of feeding, sheltering, and clothing their children. Would that really be a better world in which to be a parent?

I am edging toward a large and intimidating question, what are the sources of human happiness? How is it that we may arrive at our old age, look back, and be satisfied with the human beings we have been? Let me ask you, reader, to consider this proposition: As soon as we begin to think about social policy from this point of view, the answers begin to look somewhat different and so do the policy options and priorities. As a way of leaving you with, if not answers, at least a different question, let me ask you to join with me in a thought experiment.

Imagine that you are the parent of a small child, and in some way you are able to know that tomorrow you and your spouse will die and your child will be made an orphan. You do not have the option of sending the child to live with a friend or relative. You must choose among other and far-from-perfect choices. Your first choice is to place your child with an extremely poor couple by the official definition of 'poor': which is to say, poverty that is measured exclusively in money. This couple has so little money that your child will be badly clothed and will sometimes go hungry. But you also know that the parents work hard, will make sure your child goes to school and studies, and will teach your child that integrity and responsibility are primary values. Your alternative choice is to place your child with parents who have never worked, who will be incapable of overseeing your child's education, who think that integrity and responsibility are meaningless words — but who have plenty of food and good clothes, provided by others. Which couple do you choose?

The answer is obvious to me. But if you too are among those who choose the first couple, stop and consider what the answer means. This is your own child you are talking about, whom you would never let go hungry even if feeding him meant going hungry yourself. And yet you are going to choose for that same child years of privation. Why? What is the good one is trying to achieve? What is the criterion of success?

One may attach a variety of descriptors to the answer. Perhaps you want the child to become a reflective, responsible adult. To value honesty and integrity. To be able to identify sources of lasting satisfaction. Whatever words you choose, in one way or another you will be affirming that, most of all, you aspire that your child become a self-determining, autonomous adult, reaching his decisions on the basis of sound values, realising whatever his latent capacities may be.

You will be glad to learn that, by all the evidence that contemporary psychology has accumulated on such questions, this ancient aspiration of parents for their children is empirically sound. It seems that human beings indeed need to be self-determining, accountable, and absorbed in pushing themselves to the edge of their capacities in order to achieve satisfying lives, every bit as much as they need food and shelter. But you didn't really need to be told that, did you? We know it to be true for ourselves and our children.

The crucial question that must decisively affect policy is whether it is possible to make people feel as if they are self determining, accountable, and realising their capacities when they are not. Recent social welfare policy in the US has been designed as if it were enough to get people to 'feel as if', designed seemingly on the assumption that there can be challenge without risk, accountability without judgment, self-determination without the assumption that people possess both the freedom and the responsibility to make choices. I suggest that this is an error, that smoke and mirrors don't work, that these fundamental wellsprings of human satisfaction must rest on reality.

It is extremely unlikely that any of us will ever have to make a choice for our own children anything like the one in the thought experiment. But it bears thinking about: If the choice about where one would put one's own child is as clear to you as it is to me, on what grounds does one justify support of a system that, indirectly but without doubt, makes the other choice for other children? The answer that 'What we would really like is a world where that choice is not forced upon us' is no answer. We in the US tried to have it that way. We failed. Everything we know about why we failed tells us that more of the same will not make the dilemma go away.

So I am saying to my own countrymen: Let us by all means have a society that is compassionate and tries to do good. But let us also think much harder about what 'compassion' and 'doing good' mean. And if we cannot expect to revolutionise policy, let us at least be intellectually honest and stop the double standard, stop applauding ourselves for doing unto others in the name of compassion what we would not do to ourselves or to those we love.

Bibliographic Note

The material in this paper is drawn from Charles Murray, ***Losing Ground: American Social Policy 1950-1980*** *(Basic Books, New York, 1984) and three subsequent articles by Charles Murray discussing the debate over* ***Losing Ground:*** *'Are the Poor Really "Losing Ground"?'* ***Political Science Quarterly*** *(Fall, 1985); 'Losing Ground Two Years Later',* ***Cato Journal*** *(Summer, 1986), and 'No, Welfare Isn't Really the Problem,'* ***The Public Interest*** *(Summer, 1986). Full citations for the quantitative material in this paper are given in those sources. All data in the graphs are taken from official figures published by the United States Government in the annual Statistical Abstract of the US and supplementary volumes.*

The Perils and Pitfalls of Reforming Social Security: The British Experience

David Willetts is a consultant and writer on economic and social policy. In 1984-86 he was a member of Mrs Thatcher's Downing Street Policy Unit, and in 1987 he became Director of Studies at the Centre for Policy Studies, a think tank founded by Mrs Thatcher and Sir Keith Joseph. He has worked in energy policy, public expenditure policy and monetary policy, and has contributed to books, journals and newspapers on economic and social policy.

The Perils and Pitfalls of Reforming Social Security: The British Experience

David Willetts

Reform of Social Security 1984-88

After Mrs Thatcher's landslide election victory of May 1983 — a victory even larger than her landslide of June 1987 — Ministers decided that a top priority for their second term was the reform of social security. They knew that it could not be a secret project so three public review teams were set up — looking at benefits for children and young people, housing benefits, and supplementary benefit. In addition, an earlier enquiry into provision for retirement was brought within the review process.

My task, as the member of the Prime Minister's Policy Unit inside No. 10 Downing Street specialising in social policy, was to assist Norman Fowler (the Social Services Secretary from 1981 until June 1987), keep the Prime Minister in touch with developments, and brief her for all the main ministerial meetings on the social security reform which I attended.

The review proposals were published in a Green Paper in the summer of 1985; final decisions were announced in a White Paper in January 1986. Legislation passed through both Houses and was enacted in the autumn of 1986. The main changes in the system of social security were implemented in April 1988.

Our social security system in Britain cost (in 1987) in total about £45 billion. Benefits fall into three main categories:

1. £24 billion of contributory benefits paid out of the National Insurance Fund. These are paid to everyone in a particular category with the necessary contributions record. The main contributory benefit is the retirement pension which goes to approximately 11 million people at a cost of about £18 billion per year. Unemployment

benefit goes to about one million of our three million unemployed at a cost of about £2 billion.

2. About £12 billion of means-tested non-contributory benefits. Supplementary Benefits, the ultimate safety net, goes to about 6 million people at a cost of about £7.5 billion. Housing Benefit, which pays rents and local authority rates, goes to 7 million people at a cost of around £5 billion.

3. A universal non-contributory benefit — Child Benefit. This is the main result of the consensus for tax credits in both Britain and America during the 1970s. It is a combination of the former Child Tax Allowance and the modest Family Allowance benefit. It gives £7.25 per week for 12 million children — a total cost of about £4.5 billion.

The remaining expenditure goes largely on benefits for the disabled and on administration.

The review contains important lessons for any thinker, policy adviser, or politician (not mutually exclusive categories), confronting the complex post-war welfare system.

Cost

It was a brave attempt to reform and restructure the system and at the same time save money. Normally, redistributive reform of social security ends up costing money because it is easier to implement proposals to give more benefit than take it away. But the Fowler review will save something between half and one billion pounds in the medium term. Indeed, for some the main objective of the whole exercise was to save money. Many Conservative Ministers instinctively think of cost as the main problem with social security. It all goes back to our days of endemic economic crisis. After its election in 1979, members of our Conservative government sounded, above all, like bank managers telling a tiresome borrower that he had been living beyond his means for too long.

Cost is admittedly not a bad argument. Public expenditure is too high. We do spend too much on social security. But cost is not good enough on its own. For a start, we no longer have the sense of chronic economic crisis in Britain from which we suffered during the 1970s. The British economy has now been growing at about 3 per cent a year since 1981. People don't even feel particularly heavily taxed any longer. We could afford to carry on with existing transfer payments. They are, of course, only transfer payments — they do not directly consume goods and services, though they may indirectly cost us goods and services because of, for example, damage that they do to the labour market.

But there is a more fundamental objection to the cost argument: it makes social security sound like champagne — a nice thing if only we could afford it. But how nice is it? Which bits of it are nice? Is it really a nice thing at all? We must not forget that insight which Charles Murray has powerfully brought back before us: 'We used to suffer from social evils; now we suffer from the remedies for them.'

Reforms in the Fowler Review

The review was nothing if not ambitious — Norman Fowler referred to it as the biggest review of social security since Beveridge. It does not quite score 7.5 on the Richter scale of social policy earthquakes, but nevertheless some big changes were pushed through, notably:

- A big reduction in the State Earnings-Related Pension scheme (SERPS), the contributory second top-up state pension set up in 1978 and maturing after 1998.

- The alignment in one means test of Supplementary Benefit, Housing Benefit and Family Income supplement.

- The restructuring of Supplementary Benefit (renamed 'income support') so as to get rid of additional and single payments, replacing them instead with fixed, regular premia going to particular categories of beneficiaries — the disabled, families, old people, etc.

- Taking around 1 million households out of Housing Benefit by establishing the principle that no longer should anybody get 100 per cent relief of the cost of their local authority rates met directly through housing benefit; this important principle is part of the government's attempt to revive local democracy.

- Reconstruction and expansion of family income supplement to form a new family credit to help people in low-paid work. The original idea had been to pay the credit

> through the tax system — along the lines of the American Earned Income Tax Credit — but this proposal was rejected in the House of Lords.

That is quite a reasonable package of changes. It is not the purpose of this paper to go into them in great detail. But they provide the basis for some wider reflections on the reform of social security. I will begin by setting out the problems we encountered from our Socialist and from our Conservative critics.

Criticism on the Left: Poverty Entrepreneurs

There are lots of right-wing tax experts, or economists, or foreign policy advisers; but social security policy has largely been captured by the left. Hayek describes the phenomenon beautifully in *The Constitution of Liberty* (Routledge, London 1960, pp.290-1):

> It is not only the lay members of the general public, however, to whom the intricacies of social security are largely a mystery. The ordinary economist or sociologist or lawyer is today nearly as ignorant of the details of that complex and ever changing system. As a result, the expert has come to dominate in this field as in others.
>
> The new kind of expert, whom we also find in such fields as labour, agriculture, housing, and education, is an expert in a particular institutional setup. The organizations we have created in these fields have grown so complex that it takes more or less the whole of a person's time to master them. The institutional expert is not necessarily a person who knows all that is needed to enable him to judge the value of the institution, but frequently he is the only one who understands its organization fully and who therefore is indispensable. The reasons why he has become interested in and approves of the particular institution have often little to do with any expert qualifications. But, almost invariably, this new kind of expert has one distinguishing characteristic: he is unhesitatingly in favour of the institutions on which he is expert. This is not so merely because only one who approves of the aims of the institution will have the interest and the patience to master the details, but even more because such an effort would hardly be worth the while of anybody else: the views of anybody who is not prepared to accept the principles of the existing institutions are not likely

> to be taken seriously and will carry no weight in the discussions determining current policy...
>
> This is indeed one of the factors which tend to make so many contemporary developments self-accelerating... Once the apparatus is established, its future development will be shaped by what those who have chosen to serve it regard as its needs...

These social security experts can also be regarded, of course, as social security entrepreneurs. If in an advanced capitalist society it is possible to sell stones as pets and aerosols of London air, how much easier to market the idea that we should do more for one-parent families. Social policy experts have a true entrepreneur's capacity to identify — indeed, create — hitherto unmet needs. Hence one of their proudest achievements in the West in the early 1960s was the rediscovery (some might say the reinvention) of poverty. The restlessness of the contemporary social conscience can only be sustained by experts who identify new ways in which it can find expression. For them, any review of social security should be simply a matter of extending social security to meet new needs which had not been properly recognised before. So we are told that while the position of old people might be improving, more needs to be done for the one-parent family, or the long-term unemployed. And, or course, their demands are non-commensurable — as Hayek argues on social justice. If you attend a meeting of pressure groups and social policy experts, each will argue the cause of a particular client population with no attempt to set priorities or calculate the overall burden on the taxpayer. So when Ministers embarked on their review of social security they knew that they were unlikely to have many allies among the experts and the pressure groups.

Criticisms on the Right: NIT or Nothing

But equally, we encountered a lot of opposition from people on the right — because the only welfare reform that they could imagine was a tax credit or negative income tax scheme. This has, after all, authority in the canonical texts — Milton Friedman's *Free to Choose*, for example. It rests on a simple principle: that the only purpose of transfers is to help the poor — a superficially obvious principle which I have come increasingly to doubt. It offers the apparent prospect of technocratic efficiency: a straightforward means test operated through the income tax system instead of the mish-mash of contributory and means-tested benefits which most Western countries possess. This in turn is supposed to offer much better labour market incentives, which will reduce unemployment.

Many advocates of a negative income tax speak with the same passion and commitment to modernity and efficiency as a post-war social planner tearing down all those crooked Victorian alleys to replace them with gleaming new skyscrapers. For them, any reform that did not deliver a negative income tax was no reform at all; merely a feeble compromise favouring the status quo. So some of our potential allies have not had much to say for the recent reviews. As they did not bring a negative income tax or integrate tax and social security, they must be paltry.

But there are fundamental flaws in the negative income tax proposal. One of the criticisms levelled by advocates of the negative income tax is that some people are caught in a poverty trap, whereby for every pound extra they earn gross they lose a pound through taxation and through benefit withdrawal. So lots of schemes are peddled whereby benefits are withdrawn more gently as one goes up the income scale. Not all these proposals are necessarily wrong; indeed the new Family Credit is a model example. But if you hold the starting point of benefits constant and replace the sharp 100 per cent rate of withdrawal with a gentler gradient, then many more people are brought into the benefit system and even if their net income rises, their marginal rates of tax and benefit withdrawal increases as well. This can have very serious labour supply effects in precisely that part of the earnings spectrum where people are concentrated. The famous Seattle and Denver Income Maintenance Experiments — so powerfully attacked by Charles Murray in his book *Losing Ground* — give clear empirical confirmation of these theoretical effects. Of course, the position is better if the starting-point on the vertical axis is brought down and the starting-rate of benefit is lower but you don't need a negative income tax to do that — you just need political will.

Also, negative income tax schemes rest on the view that the cure for poverty is to top up people's income. There is no interest in all the tricky problems — which Charles Murray addresses — of the values by which the poor people live and the perverse incentives which large-scale income transfers create.

Moreover, it is essentially technocratic device. It reflects a deeper failure by most neo-classical economists and right-wing thinkers who look beyond the means of delivering social security, and instead consider the ends. After all, social security is ultimately about redistribution — between income groups, between generations, between different stages of our own life cycle.

But much more effort seems to go into designing new social security policy instruments — like negative income tax — than identifying "better" distributional outcomes. Do we want to see the incomes of pensioners rise relative to those of one-parent families? That is a real question, but not one we are well equipped to answer. Privatising an industry affects the workers in it, but most people gain by improved service or getting shares at a good price. But even quite modest changes in social security can leave millions of people worse off. And whilst savings can then be ploughed back in tax cuts, the people who lose the social security will not necessarily be those who gain from the tax cuts. It is like the story of the economist come to advise the government of a Third World country. The President asked him what policies they should implement. The economist paused, and then said he could not answer that question until the President formulated his social welfare function. People on the right are wary of such distributional questions because we do not like the thought of governments getting involved in them. Your income should be determined by your own effort, and the accidents of chance, not by governmental intervention. But as a result, we either leave the field or end up with half-truths like 'target help on the poor'.

Trade-offs

As soon as one tries to reform the social security system in accordance with Conservative principles, one finds that the distribution of social security does not rest upon any one principle: it is a set of elaborate trade-offs.

First, we are supposed to target help on the poor but at the same time to alleviate the effect of the poverty trap. The poverty trap is the result of successful targetting. Anything which eases the trap will create a penumbra of beneficiaries around the core target group. One of the arguments for Britain's only main universal non-contributory benefit — child benefit — is precisely that it helps families without a poverty trap problem.

Then, do we want a simple system or do we want to help the 'deserving' poor? The 19th-century English squire and clergyman were able at their own discretion to help the deserving poor whilst giving short shrift to the undeserving poor. It is very difficult for a social security system which is supposed to operate along pure Weberian bureaucratic and legal principles to capture subtle distinctions between the deserving and the undeserving poor. We try to catch it with more and more elaborate regulations but it always eludes us. We all can think of the wrong people who are helped, and the deserving who are not. It is a source of the permanent dissatisfaction driving the poverty entrepreneurs I described earlier. Let me give you an example of the sort of pressures that Ministers face. Some British citizens are members of the Territorial Army — a voluntary reserve force to back up the professional army in times of crisis. Some of their members are unemployed, or not earning money for other reasons. Should their benefits not be cut by the expenses which they are paid when they are on manoeuvres with the Territorials? The Ministry of Defence says no. The DHSS says yes. A special disregard of income for Territorials is precisely the sort of individual concession which, multiplied by a thousand times, creates a bureaucratic nightmare. Yet simplicity means rough justice.

Then there is a trade-off between social security as social insurance or as organised giving. Is it Bismarckian social cement whereby we come together to insure against the inevitable rainy day — unemployment, sickness, old age? Or is it organised charity to help those who suffer in a way that we do not — those trapped in the ghetto, and the long-term unemployed? Nowadays we are often told in Britain that the purpose of social security is to help the poor. This belief is particularly held by people on the right and was part of the rhetoric surrounding the government's recent welfare reforms. Politicians find themselves impaled on a dilemma as the presumption is often that a leaner, fitter social security program will target help on the poorest members of society. Yet it is those programs which have less of a political constituency. The politically most popular programs — the ones most difficult to cut — are the universal contributory benefits, notably the pension.

The National Insurance pension is by far the most popular whereas supplementary benefit is much less accepted. It is very much like the division in America between social insurance for old age and AFDC. Much of this is simple self-interest, of course: we all hope to benefit from National Insurance pensions but few of us imagine that we will be dependent upon supplementary benefit. But it is not just that the sense of mutual support through nationwide insurance is of great social significance.

Practical Proposals

But we can sit around analysing social security until the cows come home. What, actually, do we think the government should do? I offer you now four practical proposals, each directed to a major group of benefit recipients.

First, old people. In an advanced capitalist society old people should, on average, be pretty rich — having acquired assets and built up savings during their working lives. The traditional Bismarckian insurance pension was well suited for the days when the working man earned so little that he had not acquired sufficient savings to keep him for his retirement. But that has changed. In the UK now, each person over 65 has assets of £24 000 on average. Since many pensioners do not have mortgages and loans to repay, they are among the wealthiest members of the community with net assets that are, on average, 50 per cent higher than those of non-pensioners. Moreover, the average income from an occupational scheme nearly doubles the basic State pension for the average recipient.

The case for a state contributory pension is weaker than it was a century ago. This was Alfred Marshall's original objection to a universal scheme for pensions. He said, in 1893, that 'I am afraid that, if started, they would tend to become perpetual. I regard all this problem of poverty as a mere passing evil in the progress of man upwards; and I should not like any institution started which did not contain in itself the causes which would make it shrivel up as the causes of poverty itself shrivelled up'. Instead, the old-age pension has become increasingly generous in Britain and elsewhere in advanced Western countries.

A first step towards reversing this trend would be the abolition of the State Earnings-Related Scheme, the top-up pension originally introduced in 1978. The government has already implemented proposals to prune it back but it would be much better if it were completely abolished. I recognise the political impossibility of doing anything to change the value of the basic State retirement pension — not least because the contributory principle has embedded it in popular consciousness as an entitlement.

Second, I turn to the unemployed. Here, the British system is a mixture of two competing principles — contributory unemployment insurance and means-tested Supplementary Benefit for the unemployed.

Contributory unemployment insurance goes back to work by Sir William Beveridge at the turn of the century. He thought of unemployment as essentially a cyclical phenomenon and was concerned to offer some protection to employees in specific industries that suffered particularly from the trade cycle. He was also concerned to help finance rational job-searching by unemployed skilled workers.

But such schemes have always run side by side with non-contributory benefits for the poor unemployed — Supplementary Benefit. In Britain this latter benefit has tended to swamp contributory benefits. This has happened partly because non-contributory benefits for the unemployed are now as generous as contributory benefits. Moreover, we suffer from long-term unemployment so people are driven on to supplementary benefit as their entitlement to unemployment expires.

I suggest here that we should reinstate the distinction between contributory means-tested benefits. It is right and rational for people made unemployed to spend some time hunting for the next job. Insurance benefits can tide them over a period of loss of income. But the maximum period of entitlement to such benefit should be six months. In return for shortening the period of eligibility for contributory unemployment benefit, its value could be increased somewhat so as to separate it from supplementary benefit. Supplementary Benefit for the unemployed should be restricted. Indeed, unconditional supplementary benefit for the employed should go. Instead, people should only be entitled to benefit if they display willingness to work; and that willingness to work may need to be tested by the offer of a guaranteed public sector job. There are practical problems in the operation of workfare schemes but the intellectual case seems to me to be compelling. In particular it signals to the unemployed that they are full members of society, sharing a pattern of mutual obligations with the rest of us. You only get payments if you are unemployed in return for a previous record of contributions, or in return for a job that you are prepared to do now. Moreover, such a system is the only sure way of testing whether those who wish to claim benefit are genuinely available for work. These considerations seem to me to be powerful, even if work-fare schemes do not have a significant impact on welfare dependency.

Third, Conservative governments want to help the family. But they are frustrated in Britain because the conventional financial device for doing so — a universal child benefit — is essentially socialist. It is a transfer payment delivered at the local Post Office to every mother in the country. But that is not matched by the classic Conservative device for helping families — easing the tax burden on them. It used to be a traditional part of British tax theory — going back to Pitt the Younger at least — that people with children had a lower taxable capacity than those without children. But the child benefit has replaced the old child tax allowance.

We should reintroduce a family tax allowance for people with dependent children. This has the advantage of keeping families out of what in England we call the 'giro-cheque culture'. Moreover, it is only of value to people who already have an income and thus are clearly helping themselves. Such a device would also be a surprisingly effective means of dealing with a significant type of poverty in the UK — low income working families. When the Chancellor increases the existing basic tax allowance for everyone, he may take large numbers of people out of tax but for every half million that leave the tax rolls, only 20 000 or so may be poor working families. Many of the others taken out of tax will be people with casual earnings, pensioners, or young single men. A family tax allowance would be much better targetted on helping a particularly deserving group.

Finally, there is the thorny problem of one-parent families. We in Britain are beginning to focus on this group as a result of the American preoccupation with dependency on AFDC.

In Britain the labour market participation rate of married women is rising steadily whereas a smaller and smaller proportion of single mothers are in work. The explanation is that single mothers receive a generous top-up of child benefit, as well as their own rate of supplementary benefit, without any expectation that they should even be trying to get work. Moreover, there are other important rewards for being single parents in the British system — notably priority in the allocation of public housing.

There are two practical policy initiatives that could be implemented.

The single mother should no longer get priority in housing allocation. The legal obligation on local authorities to house them as a priority group acts, perversely, as a reward if one gets pregnant and declares that one's parents have made one homeless. Second, there should be a work requirement for mothers with children aged over six years.

Social security is deeply embedded in British attitudes. It is not easy to reform it. Nor have we on the Right set out particularly convincing reform proposals because we do not recognise that social security is inevitably and rightly a trade-off between several different principles. We have not matched the original Fabians' ability to work away on the minutiae of the system. Nevertheless I draw some hope from our recent experience in the UK. It has been possible to improve the system and to save money. I ended by recommending further changes in the regime for pensioners, the unemployed, low income working families, and one-parent families. Together they constitute a feasible and practical program of benefit reform.

COMMENTS ON CHARLES MURRAY AND DAVID WILLETTS

Comments on Charles Murray and David Willetts

Claudia Scott

It has sometimes been said that New Zealand has yet to come of age when it comes to policy development. It is a country that seems to thrive on visits from overseas experts and at times seems too quick to consider their recommendations. A few such experts arrive with a big-country arrogance which is annoying and drop 'pearls' before the isolated and unwashed people of New Zealand. The overseas remedies may resemble proposals which have been put up (and rejected) by the locals.

New Zealand is slowly coming of age. It certainly now seems prepared to chart a new course and to lead the world in developments in the spheres of both economic and social policies. It is getting more discerning in assessing the pertinence of overseas advice to local conditions. So a first question I wish to pose is: why have we been visited by Charles Murray and David Willetts today? Are they here to blind us with the wisdom of following the US and the UK down a particular path of social reform?

Are they here to demonstrate for us the superiority of market liberalism as an underpinning to both economic and social policy?

I am pleased that neither Charles nor David have come to cast pearls. Both authors have stayed within their areas of expertise and confined themselves to comments about the country from which they come. They have presented us with their personal views of social policy reform — personal statements which have their own validity. Neither paper provides the detailed argumentation of the positions or analysis which can be challenged and so I am drawn to commenting on how my views differ or agree with theirs and on the relevance and significance of their observations to the New Zealand situation.

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Taking Charles Murray's paper first: I think a good case could be made that the US does not fully qualify as a welfare state. It certainly is a fairly late arrival on the scene. The government's role in income support and social services has been a residual one — a backstop to occupational welfare, the voluntary and charitable sectors and other non-state methods of assisting individuals who have insufficient income and limited access to social services. This is demonstrated by the fact that Americans have never accepted a role for the state in providing a universal benefit for dependent children. Their social security fund which pays for pensions is portrayed as insurance so as to divert attention from the very significant redistribution which occurs. There is growing restlessness from those women who have discovered that their contributions to social security may bring them a level of benefit that is no greater than that given to the non-working spouse of a worker.

Let me move quickly and summarise Murray's main conclusions. They are that the Great Society programmes got it wrong and that they created incentives for families to remain dependent on state support. Moreover, benefits were not targeted effectively and the middle class inventors, advisers and administrators managed to capture much of the benefits. The paper builds on his book *Losing Ground* which I have perused as well as his article "Are the Poor Really 'Losing Ground'?' published in *Political Science Quarterly* (1985) 100(3),427-45, which classifies the various arguments that have been made to refute his views on social policy. As Murray himself states on the first page of this latter publication: 'The book covers too much ground and makes too many speculative interpretations to lend itself to airtight proof'.

Charles Murray's message about the importance of analysing the incentives inherent in social policies bears repeating. If Murray's message is 'let's do things better', I fully agree, though his views provide a set of reasons why involvement by the state is both unwise and counterproductive.

While Murray is the first to point out that it is very difficult to judge expenditure on its own, his analysis is ever-conscious of the level of public spending. One gets the distinct impression that reductions in state expenditure at times become ends in themselves. This line of argument has certain dangers. One is that the amount of government expenditure becomes the goal (as indeed it often appears given current concerns about the deficit) and we lose sight of the more fundamental question of the relative efficiency and equity of occupational and state welfare systems as mechanisms for insuring risks.

It is wrong to consider social programs only in terms of their costs to government. The relevant costs are total costs to people and measures of global efficiency are required. I think the social policy debate would be furthered if supporters of market liberalism portrayed social policy choices not in terms of a struggle between individualism and collectivism but as a balance between state and occupational welfare systems.

For example, an a comparison between the costs and benefits of the American and the Canadian health insurance systems which considers both access and efficiency does not convince me that the US system (resting as it does on a mixture of occupational welfare and 'residual' state welfare) is superior to the Canadian system where the state is a dominant funder/insurer.

The second issue I would like to highlight in the Murray paper involves the concepts of morality, blame and fault and their implications for social policy. Murray's book raises some interesting questions which remain unresolved as to whether the welfare state is there so that the middle classes can feel good and to uphold the American belief in individualism and the ability of markets to deliver.

David Willetts' paper identifies four proposals for reform:

- abolish the state earnings-related scheme of pensions;
- greater emphasis on workfare over welfare;
- abolish the family benefit and introduce a family tax allowance; and
- introduce a work requirements for mothers of children over six years and remove other incentives to be a solo parent.

Support for the first proposal is based on the notion that in advanced capitalist societies old people should, on average, be pretty rich and therefore not need such a source of income support. This suggestion raises the important question of the distributional outcomes associated with state vs occupational welfare systems. While little empirical work has been done in this area there is evidence that those societies which place greater reliance on state systems of insurance over occupational welfare will tend to have a more compressed income distribution. It is my view that top-up pensions have been introduced in countries as a way of bridging the divide between those who support universal benefits and those who favour a more selective approach. The top-up has a simple function: it tries to gain further support for the system of redistribution from those who have the least need for state support. It arises not because of a lack of understanding as to the level of need for this group but rather as a device to maintain public support for the scheme — particularly amongst those whose contributions will be used in part to redistribute income to others.

Willetts raises a fundamental question for the welfare state. Is it there to help the poor? Certainly recent work on the analysis of the distributional benefits of public expenditure suggests that a strong case can be made that the welfare state is more successful in redistributing income across generations than from high to low income groups.

While Willett's personal preference is to confine the activities of the state to redistribution in cases of need, he nevertheless acknowledges the enormous support in Britain for universal benefits — something which is also true in New Zealand with regard to both superannuation and the family benefit. It was supposedly the recognition by Mrs Thatcher of such sentiments which prompted her to say: 'the NHS is safe with us'.

The case for targeting public expenditures into areas of need is sometimes made on the ground that it will allow additional resources to be channeled to those who can most use them. However, it is also possible that without the strong political support for redistribution which is maintained through a universal scheme, the adequacy of redistribution to the less privileged will be far less than under a universal scheme. If the motive for redistribution is partly self-interest, then one is not talking about ways of dividing a cake of constant size but rather saying that the size of the cake and the amount received by the least fortunate may be larger if all citizens are part of the distribution process.

Let me now turn from comments about the specific papers to their relevance for New Zealand.

It is hard to draw close parallels between the welfare state in New Zealand and those in the UK and US. Such a view is expressed strongly in a recently published book by Francis Castles (*The Working Class and Welfare*, Allen & Unwin, Sydney, 1985) which reflects on the welfare states in Australia and New Zealand. Castles's thesis is that both Australia's and New Zealand's welfare states have developed in very different ways from the rest of the world. Unlike most Western countries these countries have had high mobilisation of the working classes. However, Labour governments have only intermittently gained office. Castles suggests that the working class movements in Australia and New Zealand led to the early introduction of workfare (rather than welfare). These societies have focused on wage security rather than social security and real welfare outcomes have not necessarily been solely a function of the extent of income maintenance expenditures.

Crudely speaking, if there is full employment and wages are adequate, state intervention to alleviate poverty is largely unnecessary. Similarly, to the degree that primary wage differentials are compressed, egalitarian socialist objectives will require less state action to redistribute post-primary incomes through either social security or fiscal benefits. New Zealand migrants were from the respectable poor and they rejected the principle of government support for the indigent. The British Poor Law System was replaced by community support through charitable aid boards. In New

Zealand the state assisted the able-bodied through job creation up until the 1930s when an unemployment benefit was established.

In both Australia and New Zealand, the Labour and trade union impetus to social policy reform led to a continuing emphasis on means-tested benefits, on the assumption that a social edifice built on scarcity of labour, consequent full employment and minimum wages, guaranteed by compulsory conciliation and arbitration, required only a welfare safety net for those outside the labour market. Castles argues that outside the Australasian context universalism has been seen as an expression of collectivism and served as the guiding notion of democratic socialist thought, and selectivity has been the individualist doctrine guiding liberal-conservative philosophy in the welfare field.

New Zealand's policy of wage security (rather than social security) was based on full employment, minimum guaranteed wage levels (based on the quantity of income needed to support a wife and dependent children) and some compression of skill differentials. Having adopted an extensive and ambitious programme of economic liberalisation, the question arises as to the likely future shape of the welfare state in New Zealand. While one possibility might be for New Zealand to develop a stance on social policy which is a mirror image of its stance on economic policy, it seems to me to be equally likely that New Zealanders could choose to put renewed emphasis on social policy as a means of coping with the side-effects of the restructuring of the economy. Some major challenges lie ahead as attempts are made to link economic and social policies — and in particular to work out new relationships in the area of employment and wages policy and welfare reform.

Today's social welfare issues are part of a new environment in which government has assumed a much more circumscribed role in economic management. In the open economy the problems of inflation and employment as seen as long-term structural issues and the solutions lie as much with the actions of individuals and firms as they do with a government and the conduct of its economic and social policies.

In New Zealand the social security benefit system has been developed around the idea that there are certain crises which are worthy of state interventionism and support. But these — not unlike the concept of dependency — require redefinition. Along with Charles Murray and David Willetts, I have concerns about the potential of a welfare state to create dependency. There must surely be concern, therefore, when it becomes necessary to increase the number of individuals who require income supplementation by the state because their earnings are inadequate to provide themselves and dependent family members with an adequate level of economic support. Yet this is what has happened in New Zealand in the area of family support.

I must part company with the speakers in that I am somewhat sceptical about the merits of a family policy — which to me inevitably runs the risk of giving legitimacy to one family form over others. Moreover, I should like to have the power of ensuring that the phrase 'unmarried mother' should, wherever possible be replaced by the concept of 'disappearing fathers'. Concerns about excessive dependency on the state need not be solved by a call for all potential mothers to be married (and by implication supported by their husbands). Rather a more appropriate stance would be to underscore the responsibilities of parenthood, to provide good economic and social incentives to encourage work rather than early parenting and to design policies which support the principle of both male and female adult independence and child dependence. The challenge ahead is not to develop a family policy but to promote adult independence and a policy which defines the circumstances/crises in which the state will recognise dependency and provide assistance.

The New Zealand social welfare system is in urgent need of redefinition in a very new climate in which dependency is no longer the responsibility of the wage system but of the income maintenance and tax systems. Major progress has been made on the integration of the tax and benefit systems but problems remain in trying to link a wage-tax system based on individuals to a social security system based on the concept of a family unit. In this fiscal climate a major question is: how will the poor get themselves out of poverty if there are few jobs available for those with limited training, in a period when the economy is sluggish and the state is under pressure to cut government expenditure?

Comments on Charles Murray & David Willetts

James Cox

The papers by Charles Murray and David Willetts raise important issues that need to be considered most carefully by those who are concerned about the future of social policy in Australia. The papers are essentially complementary. Charles Murray's paper is concerned with the diagnosis of the problems of the welfare state while David Willett's paper suggests some directions that the reform of social security might take. I would like first to summarise very briefly the arguments of the Murray paper and then make some points about its relevance for Australia. Then I would like to do the same for the Willetts paper.

Human beings often divide history into three periods and Charles Murray is no exception. The age of innocence in post-World War II US social policy lasted up to the middle of the 1960s. Social programs were modest but the official poverty rate marched steadily downwards. The period from the 1960s to the end of the 1970s was the age of expansion. Social spending increased enormously during this period but the results were curiously mixed. Because of the increase in unemployment among young men and in sole parenthood among young women the poverty rate stabilised in the 1970s. The third period is the Reagan period of the 1980s. Not much is said about this but I note that the upward march of births to single women has continued (see Murray's Figure 3, p.75).

Why did births to single women and unemployment increase? Murray's answer is that the incentive structure facing many people who have little to offer by way of labour market skills has made it rational for them to act in this way. If, as Murray and I would tend to agree, work and the two-parent family are good for you, it may not be in people's long-term interests to become (or

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remain) unemployed or sole parents. But many of us are not very good at perceiving our long-term interests.

There are two important lessons to be learned from Murray's paper. The first is that the adverse incentive effects of welfare programs for work, family stability and so on have turned out to be greater than expected by sensible people in the early 1970s. The second is that the ability of governments to do good through active social intervention is less than was thought previously. Whether one supports or opposes redistribution through the welfare state, intellectual honesty should force us to accept that these are the facts of the matter.

The most interesting question is whether the Murray story holds true also of Australia. There are obvious parallels. The age of innocence in Austalian social policy lasted up to the early 1970s. Benefits were low and relatively few persons of working age received them. Poverty was so little considered to be an issue that no attempt was made to measure it on a nationwide basis until the Commission of Inquiry into Poverty began its work in the early 1970s. The age of expansion in Australian social policy can be dated to the McMahon and Whitlam governments. New benefits (such as the supporting mother's benefit) were introduced, existing benefits became more generous, and eligibility conditions for receiving benefits were eased. The generosity of the Australian social security system reached its peak around 1976. Since then, benefits have tended to fall in terms of average earnings and eligibility conditions have tightened. In particular, the Labor government first elected in 1983 has made the benefit system more closely targeted by making means tests more stringent, by emphasising payments directed at areas of special need rather than general pensions increases, and by paying greater attention to the review of beneficiaries to ensure their continuing eligibility for benefit.

It remains the case, however, that social spending is much greater now than it was in the early 1970s. And it has become increasingly apparent that, at the very least, increased social spending is not an easy answer to the problems of poverty. One result of the increased attention given to social problems from the early 1970s is much better income statistics. We now know that poverty among persons of working age has increased since the early 1970s despite much greater levels of social spending. As in America, this increase is largely due to higher numbers of unemployed people and sole parents.

Why have unemployment and sole parenthood increased? The increase in unemployment reflects both general economic developments and changes in the relationship between wages and productivity. The weight of the evidence suggests, however, that more generous unemployment benefits have also played a part, and are especially important for young people. To say this is not to suggest that Australians are lazy or dishonest. If people are persuaded by unemployment benefits to take slightly longer in searching for jobs than would otherwise be the case, the result can be a significant increase in overall unemployment.

Growth in sole parenthood is a similarly complex matter. While ex-nuptial births have increased in Australia, much of the growth of sole parenthood has been due to increased rates of separation and marriage breakdown. No doubt sole parenthood would have increased even if pension provisions had remained unchanged. And no doubt the extension of pensions eligibility was as much a response to as a cause of changing social conditions and reflected, in part, a deteriorating labour market situation. However, it seems very likely that the rise in sole parenthood has been assisted by the extension of pension eligibility in the 1970s. Thus, in Australia as in the US, it is necessary to frame social policies in the knowledge that such policies are likely to have serious disincentive effects. Social policy is inevitably a compromise between the objective of providing an adequate level of assistance to those in need of it and the avoidance of disincentive effects.

Well, what can be done? Policies for the unemployed and sole parents are a most difficult area and I have little encouragement to give either to the left or the right. I think the evidence does suggest that unemployed people (particularly married persons with children) and sole parents live in poverty, at least if poverty is interpreted as living at a standard of living markedly below that enjoyed by most Australians. And, as argued earlier, I think that the disincentive effects of these benefits have to be taken seriously. I agree with Charles Murray that workfare schemes — schemes that make the payment of benefit dependent on undertaking work — are in practice likely to do more harm than good.

I am not sure whether Charles Murray would wish to abolish the payment for sole parents in the US but such proposals cause me some concern. Alternative methods of meeting the income needs of sole parents would no doubt develop, perhaps at the State or local community level, in the absence of pensions; but such arrangements could tend to be patchy and could take time to develop, and, in the meantime there would be hardship. Charles Murray rightly points to the unintended and undesirable consequences of the expansion of social programs. It could well be that the contractions of such programs would also have undesirable consequences. I suspect that the best course of action may be to continue the moves that have been made in recent years to make the targeting of welfare benefits more stringent both by tighening income tests and by removing the eligibility of some groups for benefit. These policies, while providing assistance to the poorest, at least limit the numbers who are affected by the adverse incentives that such programs provide.

In his paper David Willetts reviews the reforms that the British Conservative government has made to its social security system. He rightly stresses that social security policy is a series of trade-offs — between targeting assistance on the poor and avoiding poverty traps, between directing assistance to particular groups and simplicity, and between programs that assist the poor and those that are more likely to benefit marginal voters. I would like, however, to consider his proposals for the practical reform of social security and to discuss their relevance for Australia. As I understand it, the proposals are as follows:

- abolish the state earnings-related pensions and, for those in a position to save for their retirement, replace state pensions by self-provision;
- reinstate the distinction between contributory unemployment benefits and social assistance by increasing the former (and limiting the maximum lenght of receipt to six months);
- reintroduce a tax allowance for those with dependent children;
- reduce the generosity of treatment of sole parents by no longer giving these families priority in housing allocation and imposing a work requirement for mothers with children aged over six years.

It is arguable that Willetts's first proposal has to a considerable extent already been implemented in Australia. By contrast with many European and North American countries Australia does not have an earnings-related state pensions but pays flat-rate, means-tested age pensions. At least in principle, those with significant private resources would not draw the pension. Of course, in practice things are more complicated since persons may have the freedom to arrange their financial affairs so as to qualify for the pension. In particular, persons with tax-supported occupational superannuation may be able to retire early, run down their assets (or convert them into exempt forms such as housing) and qualify for the pension once age-pension age is reached.

It is apparent that better integration is required between the age pension and private saving. This could in principle be achieved either by paying pensions free of means test or by making changes to the taxation and means test arrangements concerning private saving (and particularly superannuation) to ensure that it is more effective than at present in replacing pensions expenditure. The first of these approaches would require increases in tax rates and this may well be considered undesirable on economic and general social grounds. (Why should working families have to pay more in tax to pay pensions to the more prosperous aged?) Policy in recent years has been following the second approach. Many issues require further attention, however, including the form in which superannuation benefits are taken (whether as pension or lump sums) and the terms on which superannuation benefits can be taken before age- pension age is reached.

David Willetts's second proposal is that greater emphasis should be placed on contributory unemployment benefits at the expense of social assistance benefits financed from general revenue. At present the Australian unemployment benefits scheme is of this second type. But one could, in principle, envisage a move to a system where flat rate unemployment benefits were financed by premiums relating to the risk of unemployment. A residual social insurance scheme would remain for those with insufficient or exhausted insurance benefits. Although many difficult issues would have to be addressed in the design of such a scheme it would offer a number of advantages and hence deserves serious consideration:

- Unemployment benefits would be extended to groups now excluded from them. (At present the benefits incomes test prevents members of most two-income families from receiving benefits. While this is appropriate for a social assistance scheme based on redistribution, there is no need to exclude certain classes of persons from schemes in which they are financing their own benefits on an actuarially fair basis.)
- The cross-subsidies within the existing unemployment benefit scheme would be reduced. Persons and industries with an intermittent record of unemployment would no longer be subsidised by the rest of the community. There might be a significant improvement in the allocation of resources.
- There might be a favourable effect on work incentives and hence on unemployment since persons would have to consider the effects of becoming or remaining unemployed on future premiums.
- There might also be scope for private sector involvement in the provision of unemployment benefits.

The third proposal is for the reintroduction of tax advantages for families with dependant children. This amounts to a reversal of the 1976 family allowance change when tax allowances for children were replaced by direct expenditures. Such a change could be used to provide additional assistance for families with children, were this desired (as could higher levels of family allowance). It is not an unmixed blessing, however, since tax allowances for children (or higher rates of family allowance) would need to be financed through increases in marginal tax rates on the general population. The efficiency losses arising from higher taxation would need to be set against any increases in equity that might result from higher levels of assistance to families with dependant children.

David Willetts's final proposal, to make sole parenthood less attractive by no longer giving these families priority in housing allocation, also raises some difficulties. It is true that many tenants of the Australian state housing authorities are sole parents and the expectation that inexpensive housing will subsequently become available may sometimes contribute to the break-up of marriages. But, in practice, the administrators of such programs are unlikely to deny housing to families with children that are in crisis. The idea that benefits should be paid free of work-testing only to sole parents with young children is a promising one which is consistent with the recent direction of Australian social policy. Such benefits would increasingly be seen as a short-term measure to cope with a period of crisis, and concerns that such benefits may create long-term welfare dependency would be diminished.

In conclusion, then, the future development of social policy, both in Australia and elsewhere, is likely to be a most difficult enterprise. Progress will be made only if we face the difficulties that exist in an honest and open-minded manner. The Murray and Willetts papers are most useful in this respect in reminding us of the problems we have to face and some of the choices before us.

Private Versus Public Provision of Social Welfare Services in New Zealand

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Private versus Public Provision of Social Welfare Services in New Zealand

Alan Woodfield

I. INTRODUCTION

Before reporting in April 1988, the Royal Commission on Social Policy encouraged submissions from a very broad cross-section of New Zealand society, including children, as to what is perceived as a 'fair and just' society.

Of particular interest was whether or not the provisions of the current welfare state satisfied 'the general humanitarian conviction that people had a right to be financially protected from misfortune beyond their control such as ill health, unemployment, widowhood, orphanhood, and old age'. This is a fairly standard justification for the emergence of the welfare state as encapsulated in the 1938 Social Security Act, and which represents principles held to be confirmed by the 1972 Royal Commission's investigations.

Few would argue that 'general humanitarian convictions' are not an integral part of a civilized society. What is less obvious, however, is why the state is required to play a dominating and growing role in giving effect to these sentiments. My purpose is to investigate aspects of the interface between the public and private sectors with regard to the financing and production of welfare services in New Zealand.

II. THE PRESENT SITUATION

This section provides some data on the changing extent of public and private sector involvement in the delivery of social welfare.

As for the public sector, in 1940 there were 135 279 social welfare benefits in force, 69 per cent of which were age/superannuation benefits. Ten years later, total benefits had increased to 473 328, of which 54 per cent represented the universal family benefit. By 1960, benefits had reached

581 969, the growth in benefits being dominated by the cumulative impact of the post-war baby boom on family benefits.

The developments since 1960 are given in Table 1. Benefits reached a maximum of 1 220 541 in 1985, and declined to 1 104 269 in 1987. This decline, however, is more illusory than real, since it results from removing family care payments (164 776 in 1985) and compensating low income families through the family support scheme administered by the Department of Inland Revenue.

Benefits per head of adult population remained nearly stationary until the mid-1970s. Increases in superannuation benefits and their extension to a younger age group, the introduction of Domestic Purposes Benefits, and the payment of unemployment benefits at historically high levels far offset the tendency for benefits to decline in response to falling numbers of family benefits. Between 1976 and 1985 (when family care was introduced), there was a 32 per cent increase in benefits per adult. In 1976, 40 per cent of the adult population received at least one social welfare benefit. A decade later, 48.2 per cent were on welfare.

The growth in benefits per capita is also reflected in growth in benefit payments per capita, which are also determined by the generosity of the welfare system. In constant price terms, per capita benefits declined slowly during the period 1960-72 (reflecting gradual erosion by inflation), jumped in 1973, and then grew fairly steadily until the mid 1980s. During 1960-72, real benefit payments per adult fell by 14 per cent, but doubled during the next 15 years. Social welfare payments' share of GDP shows a similar trend, falling by 25 per cent during 1960-72, and rising by 116 per cent during 1972-86.

The changing composition of benefits can be seen by examining three time slices, for 1960, 1975, and 1987, as shown in Table 2. First, note that the age distribution of the population changed significantly during 1960-87, the per centage of adults in the population rising from 67 per cent to 76 per cent. It would be expected that with lower birth rates, the share of family benefit payments would decline. The fall in the share of family benefits, however, was by a factor of more than seven. The growing proportion of elderly people in the population would also have raised the share of superannuation benefits. The increase in this share, however, was a huge 38 per cent.

Shares for invalidity, sickness, and maternity benefits remained roughly constant, while widows, medical, hospital, and supplementary medical benefits fell somewhat. Increased shares are evident for pharmaceutical, unemployment, and domestic purposes benefits. The increase in unemployment benefits has been especially dramatic in percentage terms, but this is mainly due to the extremely low base in the period to 1975. The payment

Table One: Social Welfare Benefits and Expenditures in New Zealand, 1960-87

Year	Benefits per capita[1]	Expenditure Share in GDP[2]	Expenditure per capita Nominal[3]	Real[4]	Year	Benefits per capita	Expenditure Share in GDP	Expenditure per capita Nominal	Real
1960	36.8	7.5	136	1214	**1974**	37.3	6.8	302	1360
1961	36.3	7.5	137	1202	**1975**	37.7	7.1	340	1349
1962	36.2	7.5	138	1179	**1976**	37.3	7.6	417	1414
1963	36.1	7.0	136	1143	**1977**	40.5	7.6	498	1487
1964	36.0	6.8	139	1139	**1978**	41.4	10.0	673	1753
1965	35.8	6.3	139	1086	**1979**	41.9	10.7	817	1927
1966	35.3	6.2	142	1084	**1980**	42.1	11.0	949	1890
1967	38.6	6.2	144	1051	**1981**	42.8	10.7	1121	1939
1968	37.4	6.4	153	1063	**1982**	42.7	10.9	1313	1960
1969	36.6	6.3	158	1039	**1983**	43.6	11.3	1593	2110
1970	36.5	6.1	169	1063	**1984**	43.3	11.8	1692	2061
1971	36.8	5.9	185	1057	**1985**	49.2	11.3	1826	2061
1972	37.3	5.6	198	1042	**1986**	47.7	12.1	2011	2011
1973	37.1	6.5	254	1264	**1987**	43.9		2482	2098

Notes

1. Total social welfare benefits in force at 31 March.
2. Vote Social Welfare as a percentage of Gross Domestic Product.
3. Payments made under the Social Security Act in current dollars (including health benefits) per head of adult population.
4. Payments made under the Social Security Act in constant 1986 New Zealand dollars, using CPI as deflator, per head of adult population.

Sources

Department of Social Welfare ; Annual Reports
New Zealand Official Yearbook; various issues
Monthly Abstract of Statistics; various issues

Table 2: Monetary and Health Benefits Paid Under the Social Security Act

	Percentages of Total Value of Benefits Paid		
	1960	1975	1987
CASH BENEFITS			
Age/Superannuation	42.3	49.8	58.5
Widows	3.9	3.8	1.5
Domestic Purposes	—	4.1	11.4
Family Benefit	31.4	20.8	4.4
Invalids	2.1	1.9	2.6
Unemployment	0.2	0.7	7.4
Sickness	1.7	2.2	2.0
Other	5.2	1.6	2.2
TOTAL CASH BENEFITS	86.8	84.9	90.0
HEALTH BENEFITS			
Maternity	0.5[1]	0.7	0.5
Medical	3.2	3.2	1.5[2]
Hospital	1.2[1]	1.4	1.0
Pharmaceutical	5.9	7.7	7.1
Supplementary	2.4	2.1	0.9
TOTAL MEDICAL BENEFITS	13.2	15.1	11.0

Notes
1. Adjusted to compensate for reallocation of funds after 1964.
2. Estimated

Sources
Department of Social Welfare; Annual Reports.
Department of Health; Annual Reports.

share of domestic purposes benefits has also increased dramatically, by 178 per cent since beginning operations. Finally, the shares of cash and medical benefits have fluctuated considerably, that of medical benefits increasing by 14 per cent between 1960-75, and falling by 34 per cent in the later period.

In the year ended 31 March 1987, the state removed more than $NZ6.2 billions from New Zealanders, representing $2482 per adult, and transferred it to welfare beneficiaries as either cash benefits or subsidized medical care. These figures do not include the completely subsidized public hospital system.

The picture so far is clear. During the 1960s and early 1970s, the welfare state had appeared to be in a long-run equilibrium, slowly evolving in response to long-run changes in the age distribution of the population. The subsequent period is clearly one of rapid growth of dependence and expenditures, many of which are in non-traditional areas. The external economic circumstances facing a small open economy since the early 1970s have not always been easy, and the economy's growth record has been erratic and unimpressive. Recent administrations emphasizing a deregulatory environment in certain sectors of the economy have led to considerable structural changes in the composition of output and employment, and the welfare system has had to respond to short-term difficulties created by this environment. But two questions immediately arise. First, does the welfare state deliver benefits in a manner that exacerbates New Zealand's economic difficulties in a significant way? Secondly, has the growth in dependence on the state really been in response to those 'general humanitarian convictions' with which we so readily endow ourselves?

No comprehensive answer to these questions is attempted here. Rather, some light on the issues is provided.

III. THE RECENT HIGH-GROWTH AREAS OF SOCIAL WELFARE

The growth in social welfare expenditures over the past decade can be attributed (in an accounting sense) to four factors, namely, growth in (i) the number of benefit applications, (ii) the proportion of successful applicants, (iii) the average length of the payment period, and (iv) the value of the benefit per period. In what follows, I consider growth in National Superannuation, the Domestic Purposes Benefit, and the Unemployment Benefit.

National Superannuation

Until 1975, New Zealand had a pay-as-you-go pension scheme, harking back as far as 1898. There were two types of pension: a means- and income-tested age pension payable from age 60, and universal superannuation payable at age 65. In 1974, these pensions were paid at the rate of a little more than half of the gross ordinary time average wage.

The third Labour government intended to replace this with a fully funded scheme financed by levies on employers and employees, and which would construct a fund to pay pensions with income from the fund fully supporting these pensions. The National Party proposed national superannuation as an alternative. Pensions would be payable to all persons aged 60 and over at the rate of 80 per cent of the average weekly wage, financed from general revenue. According to Angus and Manning (1986: 1), it was 'widely held that their pension proposal was a dominant factor in the (1975 election) win, enabling them to capture a large share of the votes of the elderly'.

Subsequently, two major changes have occurred in the scheme. First, in August 1979, the pension was reduced by being linked to the net weekly wage. Secondly, the fourth Labour Government quickly introduced a tax surcharge on income greater than a certain exempt level. At 31 March 1987, the tax surcharge was at the rate of 18 per cent, while the income exemption was $7 202 annually for single superannuitants, and $6 006 for married couples. National superannuation is taxable, but is not subject to an income test except where some is paid in respect of a non-qualified spouse. At present, many people appear to accept that national superannuation cannot continue in its present form for much longer, and many above-average income earners have substantially risk-discounted the potential future income that the scheme offers.

The following data illustrate the nature of the growth in national superannuation (NS) over the past decade.[1]

National Superannuation Data

NS benefits in force 31 March 1987	473 401
NS benefits per adult (per cent change)	18.8
Percentage of total benefits	42.9
Total NS payments during 1987	$3650 millions
NS payments per adult < 65	$1 802
Percentage of total cash welfare payments	65.7

Percentage of adult population receiving age-related benefit

1976			1986		
M	F	Sum	M	F	Sum
10.3	16.3	13.34	16.0	20.7	18.4

Percentage of applications for NS declined

1977	1987
1.17	2.41

[1] Sources for this data include Census of Population and Dwellings, 1976, 1986, and Annual Reports of the Department of Social Welfare.

Number of NS benefits in force for at least:[a]

		10 years	15 years
	1977	163 894	89 471
	1987	229 817	133 817
Percentage change 1977-87		40.2	49.6
Percentage change in adult population 1977-87		12.8	
Percentage of total NS benefits			
	1977	45.6	23.0
	1987	48.5	28.2

[a] In 1976 'as if' NS had been in force for 10 years.

The data show clearly the dominating role of NS in the social welfare picture. It accounts for nearly two thirds of cash welfare payments, and 43 per cent of all benefits. Between 1976 and 1986, there was a 55 per cent increase in the proportion of superannuated males. If NS had been in operation since 1962, then, *ceteris paribus*, the number of NS benefits of at least 10 years duration would have increased by more than three times that of the adult population, while the number of benefits of at least 15 years duration would have increased by nearly four times that of the adult population. Further, the proportion of NS benefits received by those who would have been on NS for at least 15 years accounted for 28 per cent of all NS payments in 1986, an increase of 23 per cent over the decade.

Unemployment Benefits

The growth in unemployment benefits (UB) over the past decade has been spectacular. Only 3651 benefits were in force at 31 March, 1977, while 63 922 were in force a decade later. Payments increased from $NZ13.4 millions to $459.7 millions over the period, and represented $183 per adult, 5.8 per cent of total benefits in force, and 8.3 per cent of total cash welfare payments in 1987.

Unemployment benefits are payable, in the description of the Department of Social Welfare, to persons over 16 years of age who are able and willing to undertake suitable work, who have engaged in reasonable job search activity, or are in an approved training program. A necessary condition for receipt of UB is registration as unemployed with the Department of Labour. At 31 March 1987, 78 166 persons were registered as

Table 3: Unemployment in New Zealand, 1977-87

Year	UB Average Duration in weeks[1]	Percentage UB ≥ 6 months[1]	Percentage Registered Unemployed ≥6 months[2]	Registered Unemployed % of Labour Force[3]
1977	8.6	4.3		0.33
1978	8.3	4.8	6.0	1.74
1979	14.0	15.1	10.0	1.92
1980	14.7	15.0	9.5	2.23
1981	13.7	12.8	13.0	3.71
1982	16.6	18.6	16.0	3.51
1983	15.5	15.4	17.5	5.61
1984	17.6	20.0	18.5	5.69
1985	18.1	19.4	14.0	4.49
1986	18.7	20.0	14.0	3.72
1987	21.2	27.5		5.05

Notes
1. Years 1977-80 are previous calendar years, March years thereafter.
2. September years.
3. April years before 1979, February years thereafter. Estimated after 1985

Sources
Department of Social Welfare; Annual Reports.
Labour and Employment Gazette; various issues.
Monthly Abstract of Statistics; various issues.

unemployed, and 88 per cent of these persons were in receipt of UB. Registered unemployment has increased significantly in recent months, and is in excess of 91 000 at the time of writing.

Table 3 illustrates the changing pattern of unemployment over the past decade. There was fairly steady growth in the unemployment rate from a very low level in 1977 to 1983, at which point the unemployment rate stabilized significantly.

The per centage of the labour force registered as unemployed for at least six months grew fairly steadily until 1984, then declined quite sharply during 1985-86. The average duration of UB payments followed a fairly steady upward trend over the entire period, showing no tendency to stabilize or fall in the early-mid 1980s. Similarly, although more volatile, the per centage of UB recipients who had received the benefit for at least six months behaved in a similar manner.

The 1986 Census of Population and Dwellings reveals the following information concerning the composition of the unemployed. The Census uses a wider-ranging definition of 'unemployed and seeking work' than used above, but under this definition the following pattern emerges. Unemployment is concentrated among the young, and falls continuously with age except that the unemployment rate rises somewhat for males nearing retiring age. In addition, there are significantly different unemployment rates at every age by ethnic origin.

For example, among 15-17 year olds, the male and female reported unemployment rates among the population exclusive of Maoris and Polynesians is 23 and 26 per cent respectively. These percentages are, respectively, 35 and 38 per cent for Maoris, and 37 and 40 per cent for Polynesians. The overall unemployment rate among Maoris is 15 per cent, among Polynesians is 31 per cent, and among the remainder of the population is 5.6 per cent.

Unemployment is also concentrated in the group currently non-married. Among males, those not married are 6.6 times more likely to be unemployed than married males, while those separated are 4.3 times as likely to unemployed. Among females, those unmarried are 2.6 times more likely to be unemployed than married females, while separated females are 2.8 times more likely to be unemployed.

Further, for every age group, between 50 and 70 per cent of unemployed males have no formal school qualifications, while between 45 and 63 per cent of unemployed females are similarly unqualified. Overall, 58 per cent of the unemployed have no formal school qualifications. Approximately one third of the adult population excluding Maoris and Polynesians have annual incomes under $10 000, while the respective population proportions for Maoris and Polynesians are 74 and 70 per cent.

Domestic Purposes Benefit

The Domestic Purposes Benefit (DPB) is payable to three categories of beneficiary. The first includes unsupported solo parents over 16 years of age. The second category consists of women, without dependent children, who are deemed unable to support themselves and who have no other means of support. The third includes persons over 16 who are required to give full-time care and attention to a person who would otherwise be hospitalized.

Prior to the inception of the DPB, persons in the above categories received state support, if at all, under the provisions of the general category of Emergency Benefits. The benefits were awarded at the discretion of the Social Security Commission. The 1972 Royal Commission, however, recommended that a new category of benefit involving statutory entitlement

Table Four: Domestic Purposes Benefit in New Zealand, 1975-87

March Year	Applications	Granted	Percent Granted	Number in Force	Ceased during Year	Average Duration[1]	Increase
1975	14 176	11 342	80	17 231	6 711		4 631[2]
1976	18 130	14 492	80	23 047	8 676		5 816
1977	19 014	15 862	83	28 401	10 508		5 354
1978	20 462	16 683	82	31 465	13 619		3 064
1979	21 015	18 008	86	35 385	14 718		3 290
1980	19 823	16 584	84	37 040	18 168	32	1 655
1981	20 601	17 540	85	39 412	15 168	34	2 372
1982	22 744	19 001	84	43 447	14 966	35	4 035
1983	24 530	19 745	80	48 121	15 071	37	4 674
1984	25 880	21 218	82	53 114	16 195	38	5 023
1985	27 035	22 005	81	56 548	18 601	40	3 404
1986	28 450	22 009	77	62 570	15 987	40	6 022
1987	31 153	25 949	83	69 146	19 373	41	6 576

Notes
1 Months.
2. Net of Estimated 12,600 beneficiaries transferred during 1974.
Source
Department of Social Welfare; Annual Reports.

be created. In the five years prior to the DPB coming into force, emergency benefits for 'domestic purposes' were as follows.

1970: 3092 1971: 4432 1972: 6186 1973: 9234 1974: 12600

The 1973 Annual Report of the Department of Social Welfare contains the following laconic remark. 'It seems likely that there will be a steady increase in the number of benefits within this classification'(p.22). The evidence has certainly validated this prediction.

Table 4 records the history of the DPB since its inception. Apart from 1980, applications have increased in every year, and the proportion of successful applications has been in the range 80-90 per cent apart from 1986. Since 1975, numbers in force have grown by a factor of four. The rate of increase of numbers of benefits in force slowed markedly five years after the scheme was introduced, but accelerated during the 1980s. Between 1980 and 1987, the average duration of DPBs in force increased from 32 to 41 months, an increase of 28 per cent.

In the decade to 1987, the number of DPB's in force increased by a staggering 143 per cent in comparison to a 13 per cent increase in the adult population. During that period, 198 742 new benefits were granted, while 161 866 ceased.

IV. RATIONALISING THE WELFARE STATE

Given that cash welfare payouts exceed $NZ5.5 billions, representing over 25 per cent of government spending (about one third of government spending net of debt interest) and about 10 per cent of GDP, the 'official' view of the development of the welfare state makes for interesting reading. Thus, in the 1986-87 New Zealand Official Yearbook, the description of the social welfare system includes the following excerpts:

> Social services and the whole concept of state-supported or state-subsidised social welfare are continually evolving in response to the changing needs of society and the greater recognition of the responsibilities of that society towards all its members, but more particularly those who have personal, family or financial difficulties.

> The present system cannot be characterised according to any single principle, theory or formula. For example, it looks like a form of community insurance, but is not financed, funded or administered on an insurance basis. It is funded from general taxation; but a person's benefit bears no relation to his or her tax contribution. While basically income-

> tested and selective as to need within classes of benefit, it is also universally applied without regard to other income or means in 3 main cases (national superannuation, family, and medical benefits)..... It transfers income from the more to the less affluent, mainly on the basis of greatest help for those in greatest need. It reflects the traditional humanitarian, egalitarian and pragmatic approach of New Zealanders and, most importantly, reflects an acceptance of community responsibility for social welfare.(p.197)

A description of the main features of the system includes the following. Eligibility for almost all benefits is independent of tax paid and essentially involves meeting a residence requirement. For non-means-tested benefits, 'it is assumed that for everybody over 60 years of age, and for all families with dependent children, a community-financed income supplement is necessary and desirable, irrespective of actual financial need or resources'. Flat-rate benefits financed under a progressive personal income tax regime 'distinguishes the New Zealand system from many of those in other countries'. Persons receiving benefits 'are given incentives to help themselves and to work. From the start, amounts payable from standard benefits have been set below the award wages of low-earner groups ...', while 'national superannuation for people over 60 years, and the benefits for widows and domestic purposes beneficiaries with dependent children, or over a prescribed age, recognise these people's right to stop working if they want to.' Taxpayers' right to contract out of their financing responsibilities on the grounds that they may not require assistance is 'denied in the community interest, as it is with other State Services such as education, defence and police'. Finally, standard rates with supplements 'relate benefits to need rather than cause of need'.

In terms of a well-defined and consistent set of principles for defending the involvement of the state in the delivery of social welfare, the official view is exceedingly disappointing. In particular, the official view does not seek to explain why the general principles of humanity and equality are required to be satisfied via a regime of compulsory taxation and income redistribution, while the 'principle' of pragmatism could be used to justify almost anything.

The issues of the insurance and incentive aspects of the system will be discussed in the following section. There are, however, certain other properties which deserve attention. First, implicit in the official view is the notion that there exists a 'society' responsible for the welfare of all its members. A society, however, is a group of individuals and does not, in my view, exist independently of those individuals. The concept of responsibility then involves a relationship between individual members of society. Many moral responsibilities, such as the care of children, have also become legal responsibilities. But many effectively legal responsibilities arising through the government's power to tax and redistribute have no counterpart in moral responsibility.

The reason for this is one of distance among individuals. People will be more willing to accept moral responsibilities when there is a personal liaison between giver and receiver. The vast amount of income redistribution that occurs within families is consistent with this view. People will also be willing to accept moral responsibilities when they can monitor the activities of recipients in order that recipients can be encouraged to become independent of income transfers, to the extent that this is possible. People will often be willing to accept short-term responsibilities for groups of people unknown to them but who require emergency relief, or even long-term relief. But these manifestations of humanity and equality cannot easily be extended to a general willingness to support substantial numbers of the population who, if the government did not provide them with access to other people's income, could be reasonably expected to support themselves during their lifetimes.

In particular, it is misleading to claim that social welfare benefits are 'basically means-tested and selective' when 74 per cent of payments made under the Social Security Act are universal benefits. Much of this expenditure is unrelated to need in any useful sense of the word. At age 20, each male and female has a life expectancy of a further 52 years and 57 years respectively, and markets exist whereby retirement funds related to contributions can be accumulated, and where insurance against failure to attain a minimum income in old age, conditional upon survival, can be purchased. As Angus and Manning (1986: 12) conclude, 'there is no reason why people cannot try to provide for their own retirement, although this may need to be buttressed by government provision of pensions to those who fail to otherwise ensure an adequate income in old age'. As it stands, NS is a prime New Zealand example of middle class encroachment of the welfare state.

Similar remarks hold for the provision of medical benefits. Medical insurance has grown dramatically in New Zealand over the past 25 years, with over one third of the population currently insured with private funds. Much of this growth can be attributed to the unwillingness of the welfare state to deliver non-acute hospital care at a zero price, to provide for choice of surgeon, or to maintain the share of fees for primary care paid by patients. Moreover, the erosion of medical funding and the growth of health insurance has been closely associated with growth in NS expenditures, suggesting a crowding-out of medical benefits by superannuation benefits as governments have made some attempt to contain the growth of total public spending.

Family Benefit is also non-targeted, and its welfare status has suffered a major decline from that of top dog in 1950 to bit part in 1987. At present, the benefit is $NZ6.00 per child per week, which, at the time of writing, buys about 1517 grams of baked beans. Inflation has seriously eroded this benefit, reducing its real value by over 60 per cent since its last adjustment in October 1979. It does very little to support really needy families with children. If it were a really serious component of a welfare system, it would be indexed against inflation at the very least, as is NS. The failure to index universal benefits other than NS (and, implicitly, pharmaceutical benefits) is extremely curious given the stated objectives of the social welfare system; perhaps this is an example of 'pragmatism'. The most likely explanation is that indexation of the big spender among universal benefits, NS, has resulted in the crowding out of less voteworthy competitors.

The major classes of benefits for which income-testing is applicable include those for invalids, sickness, widows, unemployed, and DPBs. At 31 March 1987, those beneficiaries with dependents could earn up to the equivalent of $NZ60 weekly without abatement of the benefit, $60-$80 with an abatement rate of 30 per cent, and if income exceeded $80, the abatement rate was 70 per cent. In addition, widows and DPB beneficiaries could have $20 weekly disregarded in assessing income. During the early 1980s, however, no more than $25 weekly could be earned without abatement. For income between $25 and 40, the abatement rate was 40 per cent, and above that income range, the abatement rate increased to 80 per cent. In 1987, however, benefits became taxable.

Income-tested benefits are adjusted each six months to account for CPI movements. National superannuation is adjusted on the basis of changes in weekly wage rates, except when it is decided to do otherwise. For example, during the wage freeze/price drip of 1982-84, NS was indexed on the basis of price changes rather than wage changes. During this period, indexed benefits increased relative to earnings.

V. MORAL HAZARD AND INDUCEMENT EFFECTS OF WELFARE

The official view argues that the social welfare system resembles a form of community insurance (but without the financing and administrative trappings of insurance), and that incentives to work are provided. In insurance markets, the commodities traded involve contingent claims. For payment of a premium, a payout is made if certain prescribed adverse events occur, otherwise, no payment is made. Premiums are closely related to expected payouts, and total premiums paid by individuals are closely related to the value of the relevant insurable interests. Those who are uninsured receive no compensation if adverse events occur.

The social welfare system resembles insurance only in that payouts are made in response to adverse states of the world; for example, widowhood, invalidity, sickness, or desertion of the breadwinner. Compensation, however, is independent of contributions and is unrelated to insurable interest. The system basically involves minimum payouts, with dependent-related supplements, financed by compulsory participation by taxpayers. It is clearly more of an income-transfer mechanism than a representation of the insurance contracts which would be written voluntarily in the absence of the welfare state.

When adverse events occur entirely as a result of random events, competitive insurance markets are efficient. Where **moral hazard** occurs, the probability of an adverse event is affected by actions of insured individuals. The problem is essentially one of incentives. If a person is compensated when a specific event occurs, there is an incentive to generate the event, or at least make the event more likely to occur. If these actions could be observed, say, by an insurance assessor, no payout would be made to the extent that the adverse event is induced by the behaviour of the insured. The real problem of moral hazard is that the contributions of the random event and the behaviour of the insured cannot be determined by observation where the actions of the insured are hidden from the insurer.

There are interesting properties of competitive insurance contracts when moral hazard is present, and which may be compared to the design of social insurance in New Zealand. Assuming exclusive contracts, competitive insurance contracts will not only specify the price of insurance (the ratio of premium to payout), but, in general, the quantity of insurance will also be rationed. That is, there will generally be a positive rate of coinsurance offering implicit incentives to economize on moral hazard and encourage adverse-event prevention effort. The rate of coinsurance will generally be linked to the severity of the inducement effects of insurance, and if inducement effects are very pronounced, people may be unwilling to buy insurance at all because the price is too high for the amount of cover provided. Such individuals will engage in more prevention effort and self-insure by saving against adversity. Nevertheless, due to circumstances beyond their control, some individuals will experience adversity and hardship, and most people would agree that some form of relief from these circumstances is necessary. In designing relief mechanisms, it is clearly important not to create substantial inducement effects.

Some aspects of inducement effects created by the social welfare system in New Zealand will now be illustrated with respect to National Superannuation, Domestic Purposes Benefit, and other benefits.

National Superannuation

At 31 March 1976, there were a little over 300 000 people on age/superannuation benefits, representing 9.6 per cent of the total population. One year later there were over 371 000 on NS, or 11.8 per cent of the population. Approximately 70 000 New Zealanders were induced into becoming old-age beneficiaries by NS, representing nearly one-quarter of existing beneficiaries.

Two aspects of behavioural changes induced by NS will now be examined. The first concerns the impact of NS on saving. It is widely argued that the presence of NS leads to a reduction in the economy's aggregate saving rate. The reasons for this can be seen in a life-cycle context for saving decisions. After NS came into operation, those already retired experienced a windfall gain and would consume at a higher rate than expected. Those in the workforce had their lifetime resource constraint tightened by having to pay additional current taxes, but relaxed due to the increase in the present value of future superannuation benefits. Among older workers there would be a net relaxation; among younger workers, a net tightening. Older members would tend to increase both their current and future consumption, while younger members would tend to reduce both their current and future consumption compared to that planned in the absence of NS. For the young, the reduction in consumption essentially arises because of their increased tax liabilities, so that their saving also declines.

No attempt is made here to directly test this argument. A test of its implications, however, is as follows. If NS crowds out savings, and if the economy can be usefully represented as being on a balanced growth path with a steady growth of output per worker, a fall in saving should shift the economy on to a different growth path, involving a lower rate of growth of output per worker in the short run, an unchanged rate of growth in the long run, and a lower level of output per worker at every point on the new path relative to that which would have occurred in the absence of NS.

Figure 1 provides evidence in general support of the argument. Real GDP per employee grew at a rate of 1.7 per cent per year during 1962-76. NS was first paid in February 1977, and there is little deviation of output per worker from trend in the year ended March 1977. Thereafter, output per worker was persistently below its previous long run trend value, on average, by $1370 in 1977-78 prices.

The second piece of evidence concerns the impacts of NS on labour force participation and working hours. At the time of the 1976 Census of Population and Dwellings, the labour force characteristics of the older section of the population were as follows. For males aged 55-59, there was a 90 per cent probability of being in a job, while for the 60-64 age group, the

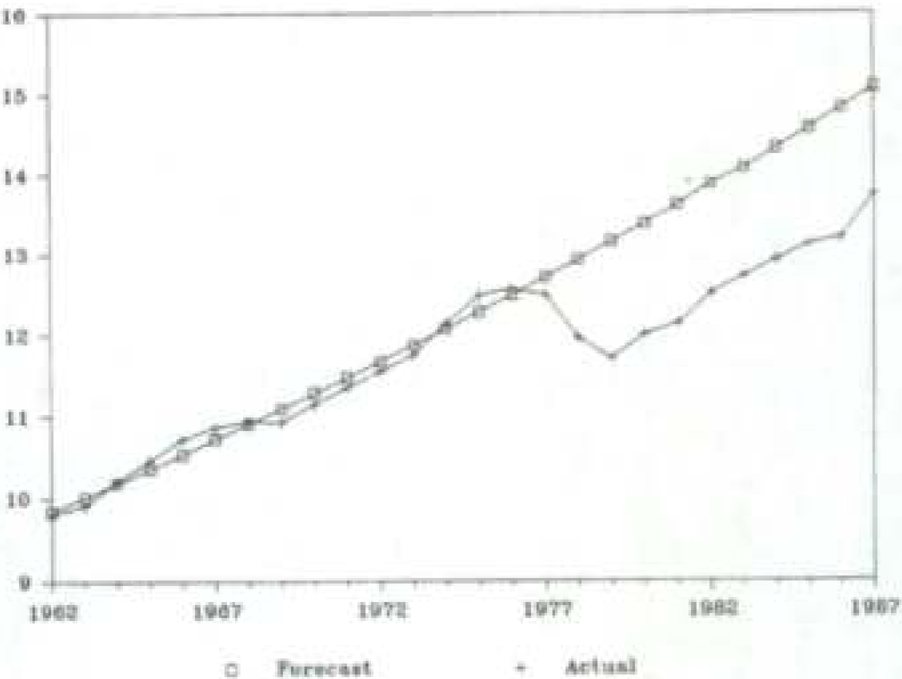

Figure 1: Real Gross Domestic Product Per Employee

Source: Monthly Abstract of Statistics (spliced series) employment rate was only 60 per cent, and only 19 per cent for the group over 65. For females, the comparable employment rates were 35, 18, and 4 per cent, respectively. The official view is that NS recognises 'people's right to stop working if they want to'. Since NS is not a funded scheme, however, this 'right' was not earned by the first generation of beneficiaries.

Further, there are good reasons to suppose that the young generation would not be willing to join a scheme involving high contribution rates and generous payouts because of the low internal real rate of return of the scheme relative to the high rate of time preference of the young. (Angus and Manning [1986] estimate an internal real rate of return of 2.31 per cent for a 15 year old with average expected lifetime earnings.) The 'right' to retire early is only beneficial to the older section of the working population, given that a third party is paying the bill. However, as Angus and Manning point out, middle-aged and old people have an interest in the perpetuation of the scheme so that a person who would not purchase superannuation on NS terms when young has no incentive to reject the scheme as he/she ages. If the middle-aged and elderly dominate the voting population, the permanence of an inefficient scheme is nearly guaranteed.

By 1981, the pattern of employment amongst the elderly had changed substantially, as is evident from inspection of Table 5. The employment rate among males aged 60-64 fell by 18 per cent, and that among females fell by 15 per cent. Although these reductions are quite pronounced, nevertheless, in 1976, 40 per cent of males and 82 per cent of females aged 60-64 were not in employment anyway, so that superannuation had no impact on their employment status and just raised their incomes unexpectedly.

For the oldest age group, the proportion of employed males fell by 28 per cent, while the proportion of employed females fell by 21 per cent. NS might here be thought of as making a significant contribution to releasing the old from the burdens of work. But 96 per cent of females and 81 per cent of males were not working anyway; again, to them, NS was a pure income transfer. As a means of inducing non-employment among the old (and, presumably, poor), NS represents a sledge-hammer approach of great cost.

These trends clearly extend to 1986. In part, this is surprising, and can be partly accounted for by increased unemployment among the working elderly. For example, the 60-64 male unemployment rate increased from 0.3 per cent in 1981 to more than 3 per cent in 1986. But the proportion of males employed in this age group fell from 49.51 per cent in 1981 to 40.99 per cent in 1986, a reduction of 17 per cent. Growing unemployment could account for only one third of this change. There is a modest 7 per cent reduction in the proportion of females employed, of which unemployment growth can account for nearly half of the change. But during the period, a surtax on income above an exempt level was imposed. Especially for beneficiaries

Table Five: Labour Force Commitment by Age: 1976,1981,1986.

Percent of each age group with status of	1976[1]				1981				1986			
	60-64		≥65		60-64		≥65		60-64		≥65	
	M	F	M	F	M	F	M	F	M	F	M	F
Part-time (≤ 29 hours weekly)	4.85	6.91	5.44	1.47	6.41	7.29	4.91	1.82	6.60	6.69	3.83	1.47
Full-time (≥ 30 hours weekly)	55.50	11.34	13.79	2.56	43.10	9.18	9.02	1.37	34.38	8.65	6.96	1.25
Not working or unemployed	39.65	81.75	80.77	95.97	50.49	83.54	86.07	96.80	59.01	84.66	89.22	97.28
Employment Rate	60.35	18.25	19.23	4.03	49.51	16.46	13.93	3.20	40.99	15.34	10.78	2.72

Note
1. Workers not specifying whether part-time or full-time in 1976 are allocated using respective shares for 1981.
Sources
Census of Population and Dwellings, 1976 (Table N226, unpublished), 1981, 1986.

who earned income from capital, the surtax was a strong marginal disincentive to earn income from working. Although the surtax claws back part of the cost of superannuation, it appears that it may be doing so at the expense of considerable employment reductions.

Very similar effects show up in average weekly hours of work. For example, at each census, the modal range of working hours for 60-64 year old males was 40-44 hours per week. In 1976, 27.94 per cent of such males worked these hours. Five years later, only 22.39 per cent were working 40-44 hours, and, by 1986, the figure had fallen to 14.96 per cent.

Doubtless, changes in employment patterns are more complex than just a simple attribution to the presence of NS. But if workforce participation rates in 1986 had been equal to those of 1976 for people who became national superannuitants at that time, there would have been 89 436 members of the workforce aged 60 and over, which is 213 per cent higher than the actual workforce in 1986. The additional labour force numbers of 47 532 represent 3.19 per cent of the economy's total 1986 workforce. And as Angus and Manning (1986) note, in the absence of NS since 1978, government spending could have been 14 per cent lower, and either legislated taxes could have been lower by this amount, or, alternatively, there would have been no fiscal deficit over the eight years since the scheme was introduced.

Domestic Purposes Benefits

As Table 2 makes evident, the DPB is a very rapid growth component of social welfare spending in New Zealand. Here, I examine this benefit more closely. First, note that the benefit is heavily female-oriented, 94 per cent of beneficiaries in 1987 being females. In 1976, 1.8 per cent of adult females were on the DPB, and this increased to 4.2 per cent within one decade. New benefits granted increased at an annual rate of 5.2 per cent between 1975-87, while numbers in force grew at 10.1 per cent per year during the same period.

Figure 2 illustrates the rates of growth of DPB cash payouts in nominal and real terms over the period. Nominal payouts increased by a factor of 23.5 while real payouts increased by a factor of over five. Between 1975-86, the share of DPB payments in GDP increased from 0.3 per cent to 1.35 per cent.

The composition of current beneficiaries. A snapshot of the composition of current beneficiaries is provided in Table 6. Seventy per cent of DPBs are paid to solo parents living apart from their legal or de facto spouses. Twenty per cent of DPBs are paid to unmarried solo parents. These proportions have been very stable over time.

The great majority on the DPB are, therefore, women deserted by their legal or de facto spouses, along with unmarried mothers. The benefit, therefore, mainly supports these women and their children, and constitutes

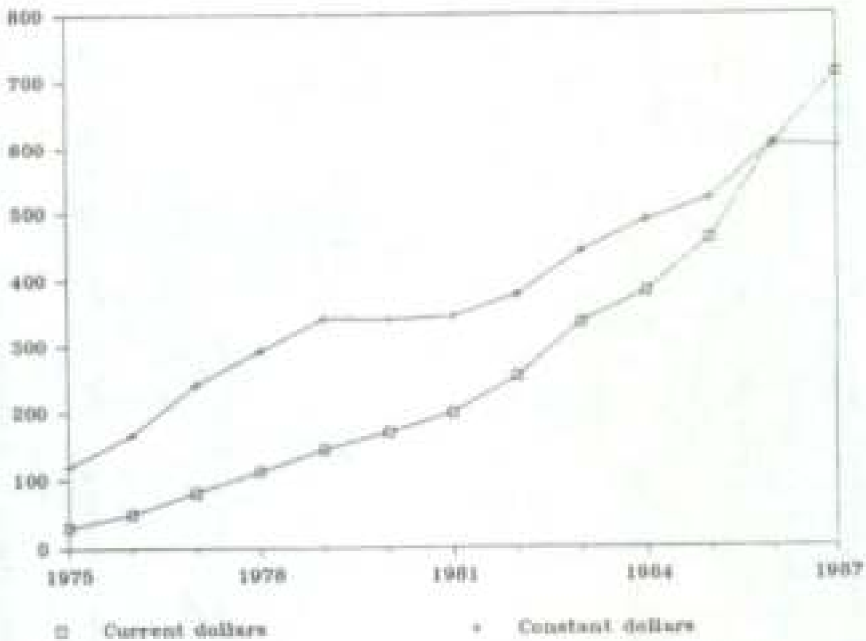

Figure 2: Nominal and Real DPB Expenditure 1975-87

Sources: Department of Social Welfare, Annual Reports
Monthly Abstract of Statistics (for CPI deflator)

a very large proportion of total income for the typical beneficiary: in 1987, only 6.7 per cent of DPBs were reduced on account of earned income in excess of $3120 annually. Clearly, this group is highly dependent on welfare. Further, solo parents with children are over-represented in the lower income ranges. The 1986 Household Expenditure and Income Survey reveals that 9.25 per cent of such persons had annual incomes of less than $8000, 32.6 per cent had incomes in the range $8000-$12 399, and 19.38 per cent had incomes in the range $12 400-15 999. These bottom three deciles

Table 6: Domestic Purposes Benefits in force at 31 March 1987 by Benefit Category

	Number in Force	Percent of Total DPB's
Solo Parents		
Living Apart from Spouse	33 963	49.1
Living Apart from de facto	14 944	21.6
Divorced	1 835	2.7
Unmarried	14 076	20.4
Other Solo Parents	1 227	1.8
All Solo Parents	66 045	95.6
Care of Sick	441	0.6
Women Alone	2 660	3.8
Total DPBs	69 146	100.0

Source
Department of Social Welfare, Annual Report, 1987.

accounted for 30 per cent of all households, but 61 per cent of solo parent households. It is, however, necessary to be wary of these figures, since solo parent households had, on average, only 2.7 members compared to 4.1 members for households of couples with children. Household income per family member is therefore much more equal than is household income when comparing solo parent households with other households.

In addition to the 69 146 recipients of the DPB, there were 109 963 children of recipients living off this benefit, representing 13.8 per cent of

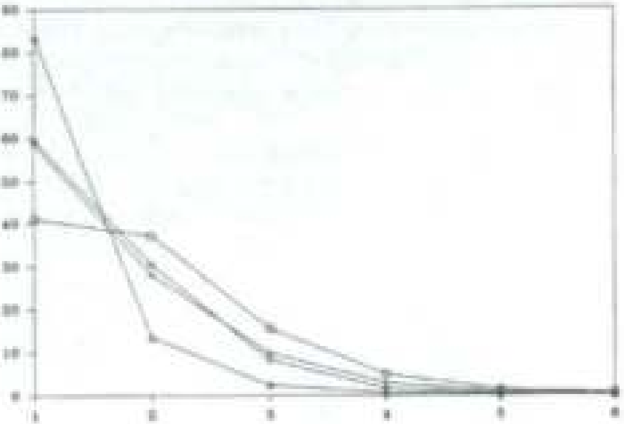

Figure 3: Domestic Purposes Beneficiaries by Number of Children, 1987

Source: Department of Social Welfare, Annual Report 1987

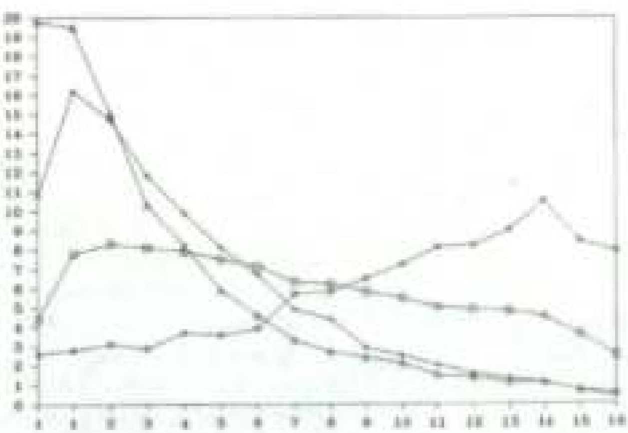

Figure 4: Domestic Purposes Beneficiaries by Age of Youngest Child, 1987

Source: Department of Social Welfare, Annual Report, 1987 persons less than 15 years of age. There are significant differences in the distribution of children by type of solo parent, as Figure 3 makes clear. Over 80 per cent of unmarrieds have one child, while 13.5 per cent have two children. Only 41 per cent of those living apart from their spouse have one child; 37 per cent have two children, and 16 per cent have three children. The remaining categories of solo parents occupy a middle ground between these two categories.

Long-term dependence. Since those who live apart from their spouse have, on average, more children, it is expected that these beneficiaries will receive welfare for a longer period than other groups. Their period of specialized rearing of young children will be greater. But once their youngest child reaches school age, there are opportunities to enter the workforce and get off welfare. Figure 4, however, demonstrates that solo parents do not necessarily get off welfare in these circumstances. For example, the percentage of those living apart from their spouse and receiving the DPB declines very slowly as the age of the youngest child increases from one to 16. Of these 33 963 beneficiaries, 64 per cent have a child aged five or more as their youngest child. For divorced beneficiaries, the per centage of beneficiaries increases in the age of the youngest child until aged 14, and then falls slightly. For this group 85 per cent have their youngest child aged five or more. For those living apart from their de facto, 37 per cent have a school-aged child as their youngest. For the 14 076 unmarrieds, the percentage of beneficiaries falls rapidly as the age of youngest child increases. Nevertheless, 27 per cent of unmarrieds have families the youngest of whom is at least 5 years old. And there were 2534 in the 'women alone' category, most of whose children were adults, and for whom public welfare was still supporting.

The issue of long-term dependence can be considered further by examining data showing the relationship between benefits granted during a given period and the number of subsequent periods for which the benefit is paid. Consider Table 7. Here, I have taken the cohort of beneficiaries who were granted the DPB in 1982 and continued to receive the benefit for more than six months, and estimated the probabilities of receiving the benefit for year N+1 conditional on the benefit being received for year N. Examining the aggregate DPB category, it is evident that a number of benefits expires quite rapidly, grants made and ceased during 1982 accounting for 25 per cent of all grants made. The likelihood of a beneficiary who is on welfare continuing to be on welfare in subsequent years increases rapidly after the first year, and there is still an 80 per cent chance that a typical beneficiary who has received welfare for four years will receive it for a fifth. In addition, over one quarter of all grantees in 1982 were still on the DPB five years later.

Similar patterns emerge for each of the individual DPB female catego-

Table Seven: Long-Term Dependence of the 1982 Domestic Purposes Beneficiaries Cohort

	ALL	FEMALES				
Conditional Probability of being on DPB for additional years	Beneficiaries	Living apart from spouse	Living apart from de facto	Divorced	Unmarried	Women Alone
1	069	0.66	0.72	0.76	0.89	0.86
2	0.74	0.73	0.72	0.67	0.79	0.92
3	0.77	0.75	0.79	0.76	0.79	0.88
4	0.82	0.80	0.83	0.78	0.84	0.92
5	0.80	0.79	0.81	0.67	0.83	0.88

Source
Monitoring and Evaluation Section, Department of Social Welfare.

ries considered, although there are some interesting differences as well. Those living apart from their spouse were somewhat less likely to be long-term dependent than those living apart from their de facto, while divorcees tend to get off welfare rather more quickly than either. Unmarrieds have an even higher likelihood of longer-term dependency, although less so for women alone, 56 per cent of whom are still on the DPB after five years.

Although divorcees on average tend to be less dependent than other groups, 4.65 per cent are still on welfare after at least twelve years have elapsed. A surprisingly high 2.2 per cent of unmarried mothers have been on welfare for twelve years or more, while nearly 17 per cent of women alone (whose children are of sufficient age to be in the labour force) are still on welfare after twelve years or more.

Labour force behaviour of solo parents. In a recent paper, Rochford, Dominick and Robb (1986) examined the labour force status of solo parents (including parents on the DPB and Widows Benefit). The authors point to two distinguishing characteristics of employed and non-employed solo mothers in different countries, namely, their educational qualifications and work experience. In general, longer schooling, higher qualifications, and prior work experience are all positively associated with higher employment rates among solos. These results are also found in the New Zealand experience.

Wylie (1980) found that, of those solo parents who had never received the DPB, most were working at the time of separation or pregnancy, while 40 per cent of those receiving the DPB had spent at least three years out of the workforce prior to becoming a beneficiary. Few of these had any specialized qualifications. Shipley (1982) interviewed a small sample of recipients of the DPB who wanted part-time or full-time work. It was found that abatement rates of the DPB significantly affected the decision to seek employment, especially since childcare imposed a limitation on work opportunities. Most women interviewed were unskilled, and could not earn sufficient to compensate for the loss of the benefit and the additional child-care costs that full-time work would impose.

Rochford et al examined a 10 per cent sample of the 1981 Census Family File, dividing solo parents into full-time employed (at least 30 hours weekly) and not full-time employed. For solo mothers, educational background was strongly associated with the probability of being employed. For example, 62 per cent had no secondary qualifications, and only 17 per cent of these were employed. The remaining 38 per cent had an employment rate of 42 per cent, some 2.5 times as great as the unqualified. Both the age of the youngest child and the number of dependent children influenced employment rates, although the former had more striking effects. Although the employment rate for solos with the youngest child aged three or less was only 6 per cent, this increased to 40 per cent when the youngest child was aged 13 or more. Thus, there is little evidence that being a solo mother in the short run is a permanent handicap in obtaining employment in the long run. However, only 16 per cent of solo mothers whose youngest child had recently reached school age were in full-time employment.

At the time of the 1981 Census, the DPB plus family benefit for a solo mother plus one child was $NZ5730 expressed as an annual rate. In addition, 46 per cent of beneficiaries received an accommodation benefit, worth, on average, $500. A solo mother receiving these benefits would get $119.81 weekly, and would generally forgo these benefits if employed. What would she have earned? If she was one of the majority of solo mothers with no secondary qualifications, and could have obtained employment at zero search cost in the trade, restaurant, and hotels sector (or similar), she would have earned $152.88 after tax (and family rebate). The net gain by becoming employed would have been a mere 27 per cent, equal to $33.07 weekly, or less than $1 per hour. And from this income, the mother would have to cover travel and other employment-related expenses, child-care costs, and lose 40 hours a week of leisure in favour of a rather tedious job. Evidently, the opportunity cost of joining the workforce would have been extremely high, and higher still if the mother had additional dependent children. Even if she could have earned the average female wage, she would have only been 30 per cent better off, or 42 per cent better off if she had not received assistance with accommodation. The labour market signals implicit in the DPB payment levels and abatement procedures are clear. If you are a solo mother and are prepared to work full-time to support yourself, do not expect any financial support from the state unless your wage rate is extremely low. Thus, in 1981, only 8 per cent of solo mothers in full-time employment received financial support through the DPB.

During 1976-81, the employment rate for solo mothers fell. Yet mothers in two parent families experienced increased employment rates. By 1984, 71 per cent of solo parents were on the DPB, compared to 66 per cent in 1981, and 58 per cent in 1976. Rochford et al estimate that if the solo parent population grows at the same rate as the beneficiary solo parent population, there would be 151 000 solo parent families by 1991, comprising 33 per cent of all families. They argue that further education, training, or low-cost childcare will be necessary to avoid the conclusion that 'the alternative is to accept that in the future the great majority of solo mothers will always be outside the labour force'. They do not, however, discuss the case for relating the benefit to the earnings capabilities of beneficiaries, thus reinstating some incentives to work or to avoid being a solo parent.

Statistical analysis. A preliminary statistical analysis of the relationship between beneficiary numbers and the ratio of the payment rate of the

DPB to wages did not reveal any simple positive associations. Partly, this is a problem of choosing an appropriate measure for the independent variable. One series used defined the benefit rate as the rate for a solo parent with one child plus the sum of the family benefit and the maximum accommodation benefit (and additional benefit where applicable), while the wage variable was the rate of gross of tax average ordinary time weekly earnings for females in the trade, restaurants, and hotels sector of the economy. Defining the ratio of benefit payments to wages as a replacement ratio, there was no significant association between either applications, grants, or numbers in force and this ratio.

There was, however, a moderately significant association between the change in benefits in force and the replacement ratio, and which implied a elasticity of change in benefits with respect to the replacement ratio of 2.83. An implication of this result is that if the 1986 replacement ratio had been 0.70 instead of 0.77, the increase in numbers on the benefit would have been smaller by about 1700 beneficiaries.

It is, however, extremely difficult to correctly identify the alternative income available to a 'typical' beneficiary. For example, a woman with young children may have little opportunity or incentive to join the labour force especially if she wants to be closely involved in raising her children. Her alternative income may be what she is allocated by her spouse. If there is positive assortive mating, low-income husbands and wives will be associated with each other, and some women may not have a level of financial support even equivalent to that offered by the benefit.

A further contributing factor to inducement during the post 1981 period, when benefit numbers again began to grow rapidly, is the dilution of the income test due to inflation. As noted in Section IV, during 1980-86, the income test was unchanged. Beneficiaries could earn up to the equivalent of $25 weekly without loss of benefit, after which the abatement rate on taxable earnings up to $40 was 40 per cent, and abated at 80 per cent once more than $40 weekly was earned. Between 1980 and 1986, however, the CPI nearly doubled, causing a 50 per cent reduction in the real value of the income exemption.

In the Annual Report of the Department of Social Welfare for 1984, it was argued that 'there is no doubt that the tighter employment situation has been a major contributing factor resulting in solo parents finding continuing difficulty in securing employment'(p.23). As Figure 5 illustrates, however, there is very little association between the average duration of the benefit and the unemployment rate as was claimed therein. The relationship appears clear until 1984, but thereafter, the unemployment rate has fluctuated considerably (as has the vacancy rate, which tends to mirror the unemployment rate) while the benefit duration continued its seemingly inexorable

Figure 5: The Relationship Between the rate of Unemployment and the Average Duration of the Domestic Purposes Benefit 1980-87

Sources: Department of Social Welfare, Annual Reports

Figure 6: Ex-Nuptial Births and Adoptions, 1974-86

Sources: Department of Social Welfare, Annual Reports climb.

Crowding-out adoptions. The DPB has enabled many children to maintain their attachment to one (but not both) of their natural parents. As a consequence, many couples who wish to have children and who are willing to support them without cost to taxpayers, have their perfectly reasonable desires thwarted. In recent times, it has not even been possible for some hopeful couples to even get on a waiting list for a child. Traditionally, ex-nuptial births have been a major source of such children. As Figure 6 illustrates, the ratio of ex-nuptial to total births increased dramatically during 1974-86, by some 71 per cent. The ratio of ex-nuptial adoptions to ex-nuptial births, however, fell dramatically during 1974-82, by a factor of more than three. While 40 per cent of ex-nuptial births were placed for adoption in 1968, only 21 per cent were so placed a decade later. By 1984, only 8 per cent of ex-nuptial births resulted in adoptions. Adoption orders also fell from a peak of 3967 in 1971 to a mere 1230 in 1986.

The response of the state. In 1981, the state responded to the growth in DPB numbers in two potentially significant ways. On 23 August of that year, a Review Committee was established to investigate the 'continued rapid growth' reflecting 'disturbing social trends'. The recommendations accepted by government included the following. There would be no change in statutory entitlement, and current rates of payment would continue. Counselling in preference to the use of legal adversary procedures was to be used to assist couples to reach agreement, and to make unmarried mothers fully aware of whether they wanted to keep a child or to adopt. While some suggestion was made that the benefit should be less financially attractive in the 'initial stages', nevertheless, it was argued that hardship should not be imposed.

Prior to a DPB pilot counselling scheme, the National Marriage Guidance Council reported that they were able to offer 'positive help' in 30 per cent of cases, but this increased to 60 per cent during the pilot scheme.

As shown above, the rate of growth of benefit takeup did slow down at this time. Subsequent events, make it obvious that these effects have been transient.

In addition, the Department of Social Welfare introduced the Liable Parent Contribution Scheme, intending it to eventually supersede the older maintenance payments lodged on account of beneficiaries. The Department assesses an amount that the liable parent is expected to contribute towards the cost of the DPB, according to a quite complex ability to pay formula. However, the LPC scheme is designed to ensure that liable parents are not impoverished by their liabilities.

How has this scheme performed in financing the DPB? First, the collection rate of the LPC scheme was only 36 per cent at outset, but it has fluctuated between 40 and 48 per cent in subsequent years. However, the combined maintenance and LPC recovery expressed as a fraction of benefit payouts has fallen on a more or less continuous basis from 13.8 per cent in 1975 to a mere 5.3 per cent in 1987.

Ethnic aspects of the DPB. In Charles Murray's *Losing Ground* (1984), the US welfare system is seen as substantially to blame for causing mass dissolution of urban black families. It is an intriguing question as to whether or not the New Zealand welfare system has aided or hindered Maori and Polynesian families on balance. But as recent Census data make evident, there is a substantial over-representation of these groups in the composition of recipients of the DPB. Given the differences in the age compositions of different ethnic female populations, it might be expected that Maori and Polynesian females would be larger recipients of the DPB than females of European origin. But age distribution is unlikely to account for the fact that 13.5 per cent of New Zealand Maori, 13 per cent of Maori/Polynesian, 8.8 per cent of European/Maori, and 6.9 per cent of Polynesian adult females receive either the DPB or the DPB plus Family Benefit, while 2.4 per cent of European-origin females are recipients of similar welfare support.

VI. THE GOODMAN-STROUP PROPOSALS

In a recent National Center for Policy Analysis Report, Goodman and Stroup analysed the poverty-welfare debate in the US and concluded with some quite radical proposals. First, they acknowledge that public welfare does help some people who would otherwise be in difficult financial circumstances, but also argue that 'there is overwhelming evidence that the welfare state is creating dependency, the breakup of families and the emergence of the single-parent household' (1986:1). Given this conclusion, they argue that an ideal welfare system is one which helps people in genuine need, without at the same time encouraging anti-social behaviour. The point, however, is that in their view this ideal cannot be attained by reform of existing public institutions; instead, 'the solution to the U.S. welfare-poverty crisis is to privatize the welfare state'.

In what follows, I deal with certain aspects of both the conclusions and the proposals in a New Zealand context.

Properties of a Good Welfare System

Goodman and Stroup (GS) pose the question of what most people want in terms of an effective, responsible welfare system, and argue that the following guidelines would command widespread support.

1. Most people can and should take responsibility for supporting themselves and their families.

2. Aid should be directed toward the most needy.

3. Aid should be given in a manner that encourages independence and self-reliance.

4. The welfare system should not encourage family dissolution.

5. Short-term help should be available to the many and long-term help should be reserved for a few.

6. The goals of the welfare system should be achieved at minimum cost.

Some people, especially long-term welfare beneficiaries, may find these principles uncongenial; but let it be supposed that they are taken as given. GS then proceed by arguing a case for public sector failure and private sector success in the area of welfare delivery according to these principles. First, they note that private charity plays an extremely important role, although little is written about it. Next, they argue that there is a basic philosophical difference between public and private sector entitlement to welfare. The public sector structures programs in such a way that benefits are assigned to people displaying certain characteristics. Applicants may not have to explain the circumstances under which these characteristics arise, and may not be required to change their behaviour so that the characteristics disappear. As we have seen, DPB applicants basically need to demonstrate the presence of dependent children, low income, and the absence of a breadwinner. Moreover, once on a programme, the beneficiary is usually entitled by statute to stay on the program as long as the characteristics persist.

Private welfare, argue GS, is fundamentally different. They argue that the best private charities do not view assistance as a right. Instead, assistance can be used so as to provide relief, and to change behaviour. The level of assistance is typically discretionary, and private agencies reserve the right to reduce or remove assistance if recipients do not make some attempt at self-help. A major reason for this difference is clear. Unlike the state, private agencies do not have the power to tax, and must fund-raise in order to provide their services, so that supporting long-term dependents is a luxury they neither desire nor can afford.

In addition, GS pose the question as to whose preferences are to count in the design of a welfare system. Public welfare is beneficiary-geared, with the funding of the scheme a by-product. The preferences of beneficiaries implicitly determine the behaviour of those who pay the taxes. The relationship between the individual taxpayer and the ultimate recipient of his/her tax dollars is extremely tenuous. In contrast to the purchase of goods, or the intra-family distribution of income, the individual taxpayer has no way of monitoring the behaviour of the recipients of his/her earnings. Private welfare agencies, argue GS, instead view the preferences of those who pay the bills as the standard, so that recipients must adjust their behaviour to the preferences of contributors.

GS conclude that it is only through a 'hands-on' management approach, rather than entitlement programs, that will allow the ideal of welfare relief to the really needy to be satisfied without encouragement of dependence. Private sector welfare generally involves support, counselling, and follow-up help which contrasts with public welfare that exists mainly to transfer cash. Further, they argue that the state makes a generally poor job of getting support to those who need it most, so that the private sector provides the real social safety net while the state continues to offer financial support without much concern whether the recipients could do well or badly without it. In addition, it is argued that it is generally difficult to get on public welfare, but easy to stay on, while the converse is true for private welfare.

As for the cost of giving, GS argue that the private sector makes far more efficient use of resources than do public programs, by requiring evidence of need before long-term help or cash is provided, by checking alternative sources of support, by avoiding unnecessary spending arising from error or welfare abuse, by using goods-in-kind, and by using volunteer labour. They note, however, that the choice of beneficiary may be threatened by growth in government funding of private agencies; currently, over 50 per cent of revenues of US private agencies come from government.

Competitive Markets for Welfare

GS accept that government has a taxation role with respect to welfare, but not necessarily a provider role. The taxation role is justified on the basis of the free-riding associated with public-good externalities. It is argued that, if left to themselves, people will contribute too little to welfare causes because they ignore the benefit to third parties that their gifts to the needy would provide. They do not, however, examine the properties of an efficient tax scheme in these circumstances.

But even if governments are justified in taxing to support the needy, GS argue that it does not follow that 'government should nationalize the charity industry ... As it happens, however, government has assumed the role of a public monopoly in the welfare industry. It has put itself in the position of being exclusive recipient of charitable contributions taken by coercion (through the tax system) and of having sole discretion over how these dollars are spent'(p.33). Further, they clearly do not accept that many of these transfers constitute a Pareto-preferred outcome; thus 'whoever heard of anyone voluntarily giving money to the AFDC or food stamps programs?'(p.34). Instead, many transfers are seen as the result of powerful political lobbying by the beneficiaries of the spending of those assisted. The appropriate response, argue GS, is to denationalize public welfare.

The process by which this could be achieved is to continue to require that people give their 'fair share' to welfare, but to permit individuals a degree of choice on how their tax dollars are allocated. Taxpayers could allocate some of their tax dollars currently used for government welfare projects to either government projects or private projects, depending on their preferences. In this way, the principle of 'general humanitarian convictions' could be given some operational meaning at the margin. GS discuss various degrees of denationalisation, from 10 per cent of total personal income taxes up to the one third of such taxes that would have financed the entire US public welfare programme.

There would be free competitive entry into the market for private charity. Individuals could contribute directly, and claim equivalent tax rebates, or else instruct the Treasury via their income tax returns to pay all or part of their permitted tax allocation limits to their chosen private welfare agencies. If they did not want to use any or all of their allocation, the tax dollars would be assigned to the public sector as at present. The effect would be that, up to a limit, private charity would crowd out public charity on a dollar- for- dollar basis.

A New Zealand Reaction: A Survey of Christchurch Private Welfare Agencies

Do New Zealand private welfare agencies fit the GS mould? What is their reaction to proposals to increase the participation of the private sector in the provision of welfare services? Are there eager welfare entrepreneurs ready, willing, and able to engage in the scramble for welfare dollars?

To try and throw some light on these questions, I invited the private welfare agencies listed in the yellow pages of the Christchurch telephone directory to answer a questionnaire. The response rate (26) was approximately 50 per cent, and included almost all of the major agencies. The general results are as follows.

First, it is evident that private agencies in Christchurch produce a remarkably wide range of welfare services, assisting the elderly, homeless, solo parents, street kids, the sexually and physically abused, the physically and mentally disabled, families who seek counselling, pregnant women, people with long-term disabling medical problems, people requiring financial assistance, emergency relief, gays, alcoholics, the poor, those lacking sex education, new mothers, and many more. Some 85 per cent of these agencies receive government funding, ranging up to 90 per cent of total funds, with a median funding rate of 30 per cent. These agencies hire over 500 full-time workers, over 1100 part-time workers, and have well over 3000 volunteers — some of the larger agencies were unclear as to how many volunteers they used.

Second, it is evident that these agencies strongly encourage the promotion of independence among their clients. Eighty five per cent seek to modify the behaviour of their clients in this direction. The procedures used include counselling, education to develop problem-solving, vocational and social skills, rehabilitation, early intervention in medical diagnosis and treatment, self-management training, and the removal of children from violent households as a deterrent to future similar behaviour by the children concerned.

Third, some 42 per cent of agencies pay cash benefits to their clients, but of these, the majority make payments rarely or in emergency situations only. Some of those who make no payments appear vehemently opposed to the principle of offering cash to their clients. If offered more resources, only one agency would give any away as cash benefits.

Fourth, the Department of Social Welfare refers clients to 73 per cent of these agencies, although the rate of referral is generally small, mainly between 2 and 10 per cent. The largest referral rate is 33 per cent, but 30 per cent of the agencies note that such referrals have been increasing. The reasons for the increased referrals include the following: the movement of the aged and psychiatric cases from hospitals to the community, increased numbers and dependency of the aged, the emergence of street kids, referrals from the police and family courts, declining government residential care, medical cases, cases where the government has no mechanism of assistance, and those with benefit-related problems. A number of agencies noted that a number of these cases were those for which the welfare state might be expected to assist, but does not. On the other hand, in response to the question 'Would the people assisted by your organization be able to obtain similar assistance from a government welfare agency?', 65 per cent answered in the negative, and 31 per cent argued that government could only deliver a few of the services offered under present arrangements. In particular, it was noted that government dealt with those things which it was obliged to by statute, suggesting an inflexibility of approach not shared by private agencies.

Fifth, in response to a question asking whether additional resources would be preferred from the public or private sector, 50 per cent were indifferent, 23 per cent preferred government support, and 19 per cent preferred private sector support (the remainder did not want more resources!). The reasons given were interesting. Those that preferred government support were generally receiving a substantial amount of government support anyway. Reasons favouring government support included arguments that private sector grants are 'too thin', that government grants 'have no strings attached', and 'it's their responsibility'. Those preferring private support, emphasized that they wanted 'no strings attached', or wanted a diverse resource base, or regarded public involvement as 'essential'. One agency claimed that government funding would 'prejudice independence', while another claimed that there was no private sector resource sufficiently large, or able to offer long-term funding. The majority, however, would accept funding from anyone, although many were concerned that it not be tied to specific projects. One agency, for example, noted that it currently had access to private funds, but no program in which the funds could be used.

Sixth, in response to the question 'Should a government agency be producing the services you provide?', 54 per cent answered in the negative, 27 per cent noted that the government might provide some of their services, but no agency accepted that the government had a role in welfare delivery equivalent to its own. However, almost every agency argued that the government should be providing them with more funds, although often this was to expand particular areas of support for which the government was felt to fail to provide the support it should. These included assistance to the aged, hospitalization, prevention, education, legal assistance, relief team equipment, and social worker service. One agency argued that it should get the government funds going to its competitors, on the grounds that it provided a more cost-effective service.

Seventh, the majority of agencies appear to require some formal assessment of need, usually by a trained caseworker, before assistance of any form is offered. But many agencies take their clients at face value, this being sufficient evidence in many cases. An overwhelming impression is that assistance is offered to people whose alternative opportunities are extremely limited, although this may be only a short-term state of affairs. For continued assistance, 34 per cent of agencies require a formal demonstration of continuing need, assessed on a case-by-case basis. Ninety-two per cent of agencies provide help to a relatively large number of people for a relatively short time period, with few if any being denied assistance, while only 8 per cent specialize in long-term assistance. However, 46 per cent provide some form of both types of assistance, and try not to refuse people they perceive as needing help. For those agencies not providing long-run assistance, two argued that such assistance 'creates dependency'.

The final two questions relate to the issue of funding. The scarcity of funds, and the constant devotion of energy to fund raising (neither of which are problems faced by the public sector) are clearly sore points to private sector agencies. Like the rest of us, they feel that they could do some really useful things if only they had the money. Each of the last two questions asks the reactions to two mechanisms that could provide substantially more funds for private agencies, but not necessarily at a zero cost to them. The first is as follows.

> A recent suggestion is that in order to obtain best value for government funds, private sector welfare agencies should be required to contract their services on the basis of competitive tendering. Is your organization in favour of this suggestion? Why or why not? Would your answer be different if public welfare agencies also had to compete for funds in this manner, so that a much larger volume of funds was potentially available to your organization?

Thirty-one per cent of the agencies provided no answer, or no useful answer to this question. In some cases, the concepts seemed too alien for comprehension. Thirty-eight per cent were not in favour of competitive tendering, 19 per cent were in favour, and the remaining 12 per cent noted (rather smugly) that they had a monopoly and would be bound to get the contract. For the latter, presumably, there is little conception of the possibility of market entry when new opportunities arise.

The reactions to competitive tendering deserve some attention. The following are some examples from those hostile to the suggestion.

A needless attempt to bring competition into social services.

Bizarre. I don't believe it will happen.

May not be workable or in the best interests of the client.

Not in favour as we would be competing with associated groups. Market forces don't apply in welfare.

Don't want to have to use resources to present a good case.

Ongoing needs may be sacrificed to fashion.

Makes people into marketable commodities. There are risks of private (extreme?) groups getting the tender.

> State is trying to get things 'on the cheap' already.
>
> How do you tender for care of disability? ...:The idea is too new to really give a considered answer. At the moment, most voluntary organizations lack information and are frightened of the idea.

While not favouring tendering, two agencies supported the ability to contract to provide specific services. And for those favouring tendering, there was a general desire for a formal specification of the contract, its evaluation and accountability for results. One agency already engaged in contracting claims the government is not honouring the contract! Another noted that only accountable and efficient agencies would survive, while one agency supported tendering if the full operating cost was funded so as to relieve the necessity of fund-raising.

Given the generally negative reaction to this question, consider the responses to the following, which posed the GS suggestion.

> Suppose taxpayers were required to allocate to public or private sector welfare agencies of their own choice, some of the money they currently pay as taxes. Would your organization support such a proposition? Why or why not?

In this case, 23 per cent of respondents produced no useful answer, 23 per cent were in favour, and 54 per cent against. For the six agencies in favour, one 'would consider it' while another believed it to be 'better than tendering', not a wildly enthusiastic response. The remaining four agencies were strongly supportive. They argued themselves to be high-profile and efficient producers of welfare services, and would expect good support. One noted that agencies with good reputations would get more income, and another expected to attract funds because of its 'squeaky-clean' image. One agency which had 'no policy' on the issue, did note that donors would be in a 'more immediate, relevant and involved position, and they would feel a greater sense of control and hence satisfaction over the way their money was being spent'. One agency was not in favour because 'compulsory' funding was contrary to their philosophy, although they were receiving 20 per cent of their funds from government, and would be happy to receive more government support.

The over-riding concern of those who disfavour the GS proposition, and one which even supporters of the scheme readily acknowledged, is that smaller, less well- known agencies could be expected to suffer under such a scheme, and the possibility that anybody could be worse-off is clearly anathema to most welfare agencies, large or small. One agency claimed there would be 'discrimination for fickle reasons', another believed it would be 'unfairly discriminated against because of the stigma attached to solo parents', another claimed the scheme to be 'unworkable, open to gross abuse, and inequitable', while another claimed that national-based organizations would be favoured, presumably because of economies of scale in information provision. There was a clear and serious concern, not that taxpayers would fail to assign dollars to the private sector, but that in so doing they might fail to support, either consciously or otherwise, what one agency described as the 'unworthy' among the current recipients of private welfare. Finally, one agency, while expecting the scheme to be to their own advantage, 'did not agree with the consequent breakdown of a universally available public system of social services'.

While this 'Three Musketeers' philosophy is not unworthy, a number of points about the alleged Achilles heel of the GS scheme should be noted. First, there are good arguments that can be advanced as to why a reduction in government welfare spending should take place and why an increase in private sector spending should occur. These are based on the relative needs of the marginal groups assisted by the two sectors. Secondly, the gains to the high-profile private agencies should not come at the expense of the low-profile groups in an absolute sense. The low-profile groups may not attract many additional tax dollars under the scheme, but it is not clear why they should lose funding unless there is a massive switch in favour of the high-profile groups caused by additional advertising. This could only occur if taxpayers switch some of their current funding of low-profile groups to high-profile groups when the scheme begins. If this occurs, the high-profile groups could allocate some of their additional funds to the low-profile groups, or government could tax them in order that no agency is made worse off. Again, there is the prospect of mergers of agencies to deal with the issue. Nevertheless, there must be concern for people who are unable to support themselves, and who are unknown or unloved. It may be that this is the appropriate role for the public sector in its funding of private agencies.

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Unemployment Benefits and their Consequences in New Zealand

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Unemployment Benefits and their Consequences in New Zealand

James Cox

I. INTRODUCTION

During the first 30 years following the end of World War II, unemployment benefits were a relatively unimportant part of the New Zealand welfare system. As recently as 1977 fewer than 4000 New Zealanders were receiving unemployment benefits. During this period it was natural that policy should focus on providing an adequate benefit to those few unfortunate enough to be unemployed.

The number of unemployment beneficiaries has increased since 1977 to reach its present level of around 120 000 people. As unemployment has increased so has the average duration of spells of unemployment. Moreover, unemployment has increasingly become concentrated among disadvantaged groups such as Maoris and the young.

The performance of the labour market in New Zealand and many other countries has deteriorated in recent years. Over the medium term, the rate of unemployment depends largely on the efficiency with which the labour market works. If the labour market is functioning well, pay is closely related to differences in individuals' productivity and hours of work. Given labour market flexibility, and stability in macroeconomic policy, it should be possible for most of those who want work to find it in normal circumstances. In these circumstances most unemployment should be of relatively short duration and frictional in nature. In the New Zealand case, however, the correction of past imbalances in the economy and a rapid rate of structural change has, combined with wage rigidity, led to the emergence of persistent structural unemployment. This, in turn, has focused attention on unemployment benefit as a major policy concern.

It is important to note here that labour market and income support reforms are linked. If minimum award wages are set at levels that prevent many adults from finding work, and if the structure of wages does not respond adequately to changes in labour market conditions, there is little alternative but to provide unemployed workers with income support on a long-term basis. By contrast with North America and Japan, European and Australasian societies with their inflexible labour markets tend also to have generous unemployment compensation schemes.

II. THE OBJECTIVES OF UNEMPLOYMENT BENEFIT

There are two ways of considering unemployment benefit. In the first place, unemployment insurance is a service that at least some people would, in the absence of government action, wish to buy or sell. On the other hand, unemployment benefit may also be regarded as a mechanism for governmental income redistribution.

Insurance

For those who are interested in investigating alternatives to government action, an interesting question is the extent to which a private market in unemployment insurance would emerge in the absence of government action. On the face of it, the prospects are not especially promising. Because of the ability of both employers and employees to affect risks, the problems of adverse selection and moral hazard are likely to be particularly acute for unemployment insurance. ('Adverse selection' refers to the tendency for insurance policies to be attractive to the worst risks. Those with least risk of unemployment will, at any given price, prefer to carry their own risk rather than to purchase insurance. This, in turn, may lead to further price increases. 'Moral hazard' refers to the possibility that the decision to purchase insurance may subsequently influence individuals' behaviour. Those who have purchased unemployment insurance may choose to indulge in more frequent, or longer, spells of unemployment than would otherwise have been the case. Insurance companies have open to them a number of strategies to reduce, but not eliminate, these factors.)

It may be that unemployment insurance is so costly to provide that many individuals would not find it an attractive proposition. However, it is worth noting that, prior to the introduction of government unemployment compensation schemes, trade unions and friendly societies in Britain, Australia and New Zealand provided unemployment and sickness compensation. Mortgage insurance schemes that are operated today include elements analogous to unemployment insurance. And individuals can and do provide for the possibility of their unemployment through private saving. On balance, the scope for self-provision for unemployment is considerable, although not all individuals would be in a position to do this.

Redistribution

As a means of income distribution, unemployment benefit provides both income support (a minimum income in unemployment) and income maintenance (an income in unemployment that is commensurate with income when employed). Flat-rate unemployment benefit arrangements of the New Zealand type provide income support and also a degree of income maintenance for low income workers. Social insurance schemes following the North American or European pattern that pay earnings-related benefits are less successful than flat-rate schemes in providing income support (since they provide a small benefit for those with low earnings when in employment) but result in a higher degree of income maintenance for middle to upper income earners.

It can be argued that income maintenance is not an appropriate objective of government redistribution policy, which should be confined to ensuring the provision of a minimum income in unemployment. First, as argued previously, the scope for self-provision in unemployment appears to be considerable. Secondly, in view of the accumulating evidence of the seriousness of the disincentive effects of marginal tax rates, it is undesirable for governments to undertake tasks that individuals are perfectly capable of performing for themselves should they so wish.

Finally, the payment of substantial government benefits to individuals enjoying high incomes when in employment would not appear to be desirable on distributional grounds.

It is frequently suggested that income support arrangements should be assessed in terms of the following criteria:

- adequacy — the provision of an acceptable minimum income;
- incentives — the avoidance of adverse effects on the incentives of recipients to work, save or engage in education or training;
- cost — to minimise the cost to the taxpayer (and hence permit reductions in marginal tax rates);
- simplicity — ideally income support schemes should be easy to administer and use, and should avoid stigmatising the recipients.

An inescapable difficulty with income support policy is that simultaneous achievement of all four objectives is impossible. Suppose that society decides on a level of benefits that would be adequate and, to avoid means testing, also decides that this level should be paid to everyone in the defined category, irrespective of income. The cost to the taxpayer would be likely to give rise to concern and the result, particularly in times when incomes in general are not increasing rapidly, would be the payment over time of less generous benefits of this type.

Alternatively, the cost of paying a given level of benefits may be limited through income-testing, but this may discourage the unemployed from supplementing their benefits through part-time work. Moreover, the more generous the basic level of benefit (whether income-tested or not), the greater is the incentive to the individual to become or remain unemployed rather than take full-time work, and the greater the cost to the taxpayer is likely to be. For any level of benefits, the incentive to become or remain unemployed can be reduced by more careful attention to such features as work-testing, waiting or stand-down periods and the detection of abuse. But these increase the costs of complying with the system both for beneficiaries and the administration.

Income support policies must therefore be a compromise between desirable but competing objectives. But there are grounds for arguing that some compromises are to be preferred to others. In particular, closely targeted income support schemes are likely to provide a more precise balance between equity and efficiency objectives than more universal schemes. Targeting involves two main aspects: the use of additional payments directed towards beneficiaries with particular needs (such as the presence of dependent children) and income or assets testing. The gains from income testing, in terms of a more precise direction of assistance to the most needy and reduced marginal tax rates, are in general likely to outweigh the costs in terms of the disincentive to take part-time work for those subject to the benefits income test. (Some would argue, however, that for some groups part-time work is the more realistic option.) This is particularly the case if care is taken to ensure that the decisions of not too many people are influenced by the high effective tax rates generated by income testing. Assistance should therefore be withdrawn at a rapid rate in an area of the income distribution that is not dense. Provided that tax rates in general can be kept low, the 'short high fence' may, for a given level of benefits, minimise the obstacles for the currently unemployed in seeking full-time employment (for further discussion, see Blinder and Rosen, 1985, and Cox, 1986).

III. THE SIDE EFFECTS OF UNEMPLOYMENT BENEFIT

Work Incentives

Unemployment benefit provides an income to those who are not currently working but who are looking for work. A benefit of this type is almost bound to give rise to disincentive effects: both the incentive to become unemployed (if currently working) and that to remain unemployed are affected. To say this is not to imply that New Zealanders are lazy or that they are making fraudulent claims for social welfare payments. Persons who are genuinely looking for work may, by the existence of unemployment benefit, be induced to search longer than would otherwise be the case. While some period of job search may be desirable in terms of achieving a better match between workers and jobs, periods of job search can clearly be longer than is useful.

If workers who become unemployed have the alternative of receiving unemployment benefits, then the level of benefits sets, in effect, a floor to wages. Persons are unlikely to provide labour to the market unless they receive a margin above unemployment benefits to compensate them for the trouble and expense of working. Employers may therefore argue that they find it hard to fill vacancies in low-paying occupations because potential employees prefer to continue to receive unemployment benefit.

It is generally agreed among economists that disincentive effects exist but there is less certainty as to their magnitude. Two main propositions arise from empirical studies of unemployment benefit. The first is that, the higher benefits are in relation to earnings, the longer is the average period of duration of unemployment. According to a review of the US literature by Danziger, Haveman and Plotnick (1981), 'despite the problems, a positive relation between unemployment insurance and duration of unemployment appears robust'. A more recent British study by Atkinson and his colleagues (1984) has concluded that the evidence is not so robust. Thus, although it is probable that a more generous level of benefits would increase the average duration of unemployment, the size of this effect is still subject to debate.

The second question, which has been studied in the US, is whether the **structure** of unemployment insurance increases unemployment, particularly through incomplete experience rating that subsidises industries and workers with a pattern of intermittent employment. Feldstein (1978) and Topel (1983, 1984) argue that this effect is important. In contrast with the situation in the US, the New Zealand (and Australian) system of unemployment insurance includes no element of experience rating. Experience rating, as well as being actuarially fairer than the present New Zealand system, improves the incentive aspects of the scheme in a number of respects. Employees know that the greater the number and length of spells of unemployment that they experience, the higher will be the premiums they would pay on regaining employment. Employers would have a greater incentive to clarify separations accurately into resignations and redundancies since their experience rating would depend only on the latter. This would reinforce other aspects of the system (such as waiting periods and work tests) that are intended to discourage voluntary unemployment.

Incentives for Education and Training

In general, unemployment benefits make labour force participation more attractive than would otherwise be the case. If a person enters the labour force and is unable to find work, unemployment benefit is available. The availability of unemployment benefit both increases the expected return to entry into the labour force and reduces the risk from such entry. Unemployment benefit is therefore likely to make labour force participation higher than would otherwise be the case.

These arguments are of particular relevance for young people. At present the only support available for young people in the post-compulsory years of secondary education in New Zealand is through family support (and, where relevant, the guaranteed minimum family income) and family benefit. By contrast, unemployment benefit of around $NZ100 a week is available regardless of labour force experience to 16 and 17-year-olds should they enter the labour force and fail to obtain work. As the importance of upgrading the skills and adaptability of the New Zealand labour force to enable successful competition in world markets is increasingly realised, it is likely that greater emphasis will be placed on the need to move towards a system of income support with fewer distortionary effects on the choice between continuing education and entering the labour force. The New Zealand government has announced its intention to introduce a consistent, age related system of income support for young people in education and training, or who are unemployed.

IV. THE NEW ZEALAND UNEMPLOYMENT BENEFIT SYSTEM

New Zealand pays income-tested, flat-rate (i.e. not earnings-related) unemployment benefits, the size of which depends on family composition but not earnings. Benefits are financed by general taxation and not through specific contributions. In comparison with the earnings-related unemployment insurance schemes that exist in most European and North American countries, benefits tend to be generous to employees with low earnings but less generous to employees at higher income levels. In this section the New Zealand benefits system is assessed in terms of the objectives outlined above of adequacy, incentives, cost and simplicity.

Adequacy

One of the most difficult issues in social policy is the size of the minimum income that the state should provide. Although many people would consider adequacy to be an absolute concept — a minimum income necessary for subsistence — the historical record has been for unemployment benefits to be established at a level below the earnings of persons in low-paying employment.

In New Zealand the usual method has been to assess the adequacy of benefits by relating them to a measure of earnings or award wages. A benefit standard was established in terms of wages following the report of the 1972 Royal Commission on Social Security. But this standard has not been updated to reflect movements in wages. Real wages increased in New Zealand up to around 1975 but have since declined. The result has been a tendency for benefits to move upwards in relation to earnings, although this has to some extent been offset by the taxation of benefits and the provision of supplements to the incomes of low-to-middle-income families. This is illustrated in Table 1.

It is of considerable interest to compare the levels of benefit provided by the Australian and New Zealand systems with the levels of earnings in each country. This is done (for early 1988) in Table 2. In summary, Table 2 shows that benefits in New Zealand are generally higher in relation to average earnings than in Australia. This is particularly the case for single people and married people with children, and for single people under the age of 18 years.

The New Zealand, Australian and British system of flat-rate benefits is generous to low income employees and particularly to those with family responsibilities. Figure 1 shows that unemployment benefit replaces a higher percentage of income in Australia and the UK than it does in Canada, Germany and the US where unemployment benefits are related to earnings.

The New Zealand system also includes extensive supplements for those with special needs or high housing costs. Many beneficaries also receive subsidised housing through the Housing Corporation of New Zealand.

It can be concluded that the New Zealand system meets the adequacy criterion extremely well. The question for New Zealand policy makers is whether these gains in adequacy have been achieved at too high cost in terms of disincentives for work and education participation, and of high effective marginal tax rates.

Incentives

Two aspects of incentive effects require particular consideration:

- The replacement ratio — the ratio of income in employment to the income the person could expect in full-time work; and
- The effective tax rates that beneficiaries and low income earners face if they decide to increase their work effort.

It has been estimated that 4 per cent of New Zealand wage and salary

Table One: Benefits as a Percent of After Tax Earnings in New Zealand

Year	Single	Married	Married (Plus two children)
1971	34.04	60.08	65.611
1975	40.37	65.06	70.83
1980	42.35 (63.36)*	69.04 (60.30)*	67.94
1985	46.56 (4.26)*	77.60 (63.83)*	80.26 (73.89)**
1987	45.53 (40.28)*	75.89 (60.66)*	70.00 (78.65)***
1988	45.49 (40.24)*	75.81 (60.60)*	69.93 (80.16)***

Notes

(a) Until 1979 no benefits were taxable. From 1979 to 1986 only the unemployment benefit paid to those **without** children was taxed. From October 1986 all benefits have been taxed. The benefit rates used are those which are applicable in January each year (1987 rates are for April).

(b) Earnings are average ordinary time weekly wages — all persons, all sectors.

* Figures in brackets give net **unemployment** benefit rates which, since 1979, have been lower than other benefit rates for beneficiaries without children.

** Figure in brackets is after allowing for the family care supplement payable to low and moderate income families.

*** Figure in brackets is after allowing for family support which is payable to low and moderate income families. The figure not in brackets gives the ratio of net benefit before family support to the net average ordinary time weekly wage.

earners presently face replacement ratios of more than 70 per cent while 21 per cent face replacement ratios of over 50 per cent. Not surprisingly, young single people and families with children are the groups most likely to have high replacement ratios. On the face of it, these ratios do not appear to be unduly alarming — four-fifths of New Zealanders can expect to be more than twice as well-off in work as out of it.

As noted, an important reason why replacement rates in New Zealand are not higher is the extensive system of income support for low income persons in employment. These arrangements tend to reduce replacement rates (since they add to the incomes of low wage earners) but result in high effective tax rates as assistance is phased out over wide ranges of the income distribution. The phasing-out of the family support payment implies tax rates of at least 48 per cent over the range of $NZ288 a week in private income to $NZ577 a week (for a family with two children). These high rates are likely to contribute to a climate of lack of enterprise and initiative in New Zealand. In March 1986 some 116 000 families were receiving family care, the predecessor of family support. In contrast, the universal family benefit was paid to 524 000 persons.

Because of the concern to ensure that persons in work have incomes similar to the unemployed, the assistance schemes for low income earners have been closely linked to unemployment benefit. If it were possible to reduce unemployment benefit rates, for example, then it might be possible to reduce the guaranteed minimum family income. A more rapid abatement of unemployment benefit would make it possible to reduce the level of income at which the family support scheme itself begins to reduce.

Cost

As the number of unemployed persons has grown, expenditure on unemployment benefits has grown from almost nothing in the early 1970s to $673 million in the year ended 31 March 1988. This increasing fiscal burden emphasises the importance of improving labour market performance to reduce unemployment, and of achieving any available economies in unemployment benefit policy.

Simplicity

The government goes to considerable lengths to ensure that the unemployment benefit and family support systems are convenient for the recipients, despite their seeming complexity. Although this activity is admirable from many points of view, it should be recognised that the result is likely to be higher levels of social welfare spending (and hence tax rates) than would

Table Two: Benefits in Relation to Net Earnings in Australia and New Zealand

	Australia $A (per week)		**New Zealand** $NZ (per week net)	
	1987	**1988**	**1987**	**1988**
Single, Under 18	50.00 (0.151)	50.00 (.140)	99.86 (0.327)	108.63 (0.326)
Single, 18 to 20	91.20 (0.276)	91.20 (.255)	99.86 (0.327)	108.63 (0.326)*
Single, 21 and over	99.20(0.300)	112.10(.314)	123.20(0.403)	134.02 (0.402)*
Single plus 1 child	138.70 (0.395)	154.05 (.408)	234.08 (0.713)	250.94 (0.720)
Married Couple	77.10 (0.510)	200.10 (.538)	185.52 (0..606)	201.80 (0.606)
Married Couple (plus two children)	219.60 (0.603)	244.10 (.628)	278.08 (0.794)	296.88 (0.800)
Average ordinary time earnings (persons)	427.00	466.00	396.92	436.97
Net of tax -				
- Single Persons	331.00	357.00	305.83	333.02
- Single plus 1 child	351.00	377.00	328.31	348.36
- Married couple	347.00	372.00	305.85	333.02
Married couple (plus two children)	363.00	389.00	350.31	370.36

Note
Figures in brackets give the ratio of benefits to net earnings. Family allowance/family benefit and family support are included where relevant.
* Adult rate is paid from age 20 in New Zealand.

otherwise be the case.

Changed attitudes towards receipt of social welfare benefits have generally been a factor in the growth of social welfare spending over the past 20 years.

The administration expenses of the Department of Social Welfare for the unemployment benefit are about 2 per cent of its total expenditure. The Australian experience suggests that there are returns to more vigorous administration in terms of reduced total expenditure even though such action will tend to increase administrative expenditure. New Zealand has also begun to improve administration but much remains to be done.

V. POLICY APPROACHES

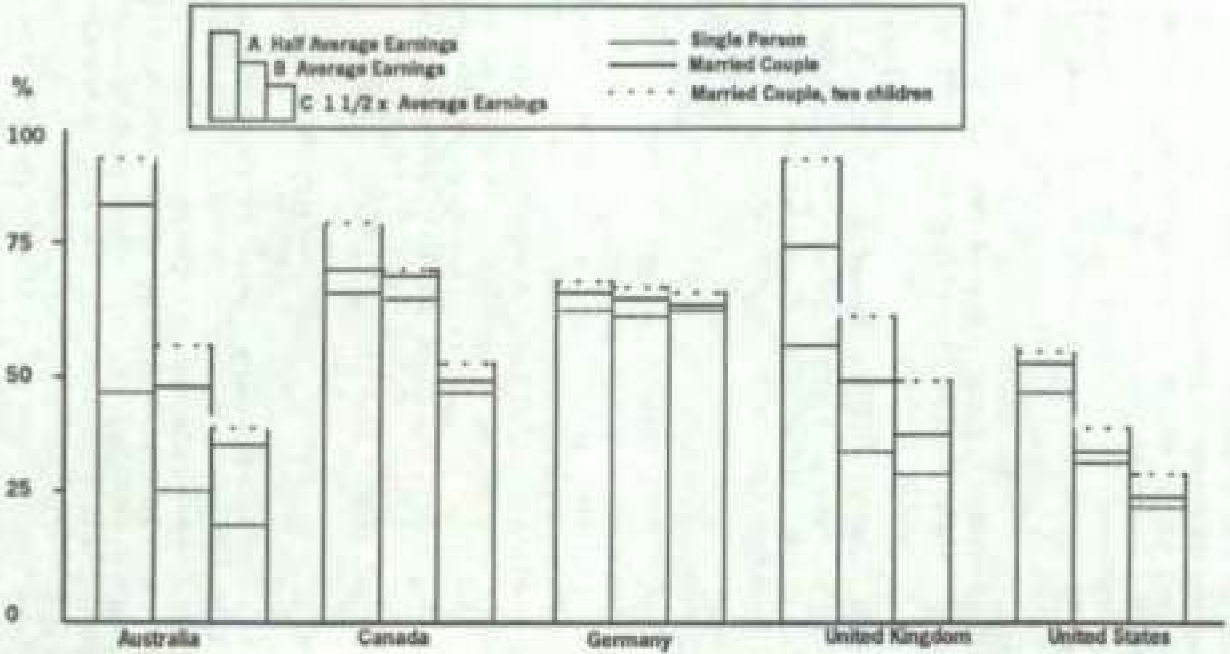
The preceding analysis suggests that the New Zealand unemployment benefit system meets the adequacy criterion well but in doing so may give rise to significant incentive problems. This section of the paper reviews possible reforms of the New Zealand benefit system to achieve a more precise balance between equity and efficiency objectives. The first stage involves the redesign of the minimum protection offered by the state to the unemployed and low-income families. In the second stage, this is combined with a shift in the financing of unemployment benefit from general revenue to premiums that involve an element of experience rating. Finally, the scope for increasing private provision for unemployment is assessed.

The State Schemes

Young people. As noted above, unemployment benefits for young people are high in relation to the incomes they can expect in employment. This high level of benefits is likely to have substantial disincentive effects on incentives to work and to engage in education and training. The following strategies should be carefully examined:

- Introduce a lower rate of benefit for persons aged 16 and 17 (or, alternatively, raise the age of eligibility to 18 years in which case family support would become payable to low-income families of unemployed children).
- Pay benefits to persons aged 16 and 17 years subject to a parental as well as a personal income test.
- Introduce longer waiting periods for those leaving secondary and tertiary education. (This would lessen any effect that the availability of unemployment benefit might have on decisions to enter the labour force rather than to continue in education or training.)

Figure 1: Income Replacement by Family Size and Previous Earnings
First Year of Unemployment



Source: OECD 1984

All unemployment beneficiaries. The following strategies are available:

- Allow benefits to fall in terms of earnings, for example, by freezing certain benefit rates. Reduction of benefits in terms of earnings is likely to lead to an increase in the number of persons experiencing financial hardship, and provision would need to be made for meeting their needs. One possibility would be to make increased use of special benefit.
- Tighten income tests by reducing the free areas, abating benefits more rapidly and by introducing an assets test.
- Review the operation of the work test.

Assistance to low -income persons in full-time employment. A major problem in New Zealand is the wide range of incomes over which assistance to low income families is withdrawn. The measures relating to unemployment benefit outlined above would reduce pressure to make the income support system for those in employment still more generous. In addition consideration should be given to freezing or reducing both the amount of assistance provided and the range of income over which it is withdrawn. If the abatement rate on family support was increased from 18 per cent to 50 per cent, the abatement range would be reduced from the present $NZ288 a week to $NZ577 a week (two children) to the much shorter $NZ288 to $NZ392. Effective tax rates would be raised to 80 per cent over the abatement range which would be shorter (and would affect fewer individuals) than at present. Such a change is likely to have favourable incentive effects particularly in the context of overall reductions in marginal tax rates.

Financing the State Scheme Through Premiums

A more ambitious step would be to replace the present system of financing benefits from general revenue by contributions levied explicitly on employers and employees. This would permit the introduction of experience rating, as presently occurs in the US.

A system of premiums combined with experience rating would offer a number of advantages. When making hiring and redundancy decisions, employers would have to consider the effect of redundancies on the premiums that they would have to pay in future, while employees would have to consider the effect of redundancy (or a longer spell of unemployment) on future premiums. To the extent that experience rating can be implemented on an actuarially fair basis, individuals (such as seasonal workers) and industries (such as construction) with a pattern of intermittent employment would no longer be subsidised. This would be fairer and would encourage a better allocation of resources. Topel (1984) argues that the United States system of experience rating is incomplete and that an important reduction in unemployment may be achieved by adjusting methods of financing unemployment benefits without changing the level of benefits available to workers.

It would no longer be appropriate to limit the payment of benefits by income or assets test if, rather than receiving tax financed benefits, individuals purchased unemployment insurance from the government. Coverage would therefore be extended to groups (such as most two-income families) who are presently excluded from benefit. Through premiums, individuals would be purchasing unemployment insurance on an actuarially fair basis, although government subsidies might — for distributional reasons — continue to be directed towards the long-term unemployed.

The premiums that would be charged under experience rating would depend on the level of benefits offered and the risks (for each group) of becoming and remaining unemployed. These premiums would not enter into effective marginal tax rates unless the benefits offered varied with income. Replacement of taxes with premiums would therefore reduce marginal tax rates overall. Experience rating would discourage the employment of workers who are likely to become unemployed but would reduce the costs of employing persons with stable employment records. But, since some groups with relatively high incomes tend also to have unstable employment patterns, introduction of experience rating need not adversely affect average rate progression in the tax and benefit systems combined, although there are likely to be some low income persons with poor employment records who would be disadvantaged by the introduction of experience rating. The distributional implications of the proposal would, therefore, require further examination prior to implementation.

Self-provision for Unemployment

It was suggested above that there is a variety of routes through which individuals can provide for unemployment and that the proper role of the state is to provide a minimum level of protection.

A major question is how private provision for unemployment relates to the minimum required by government. In general, two models are possible:

- The supplement model, in which individuals who are not satisfied with the level of benefit provided by government are able to purchase additions in the market.

- The opting-out model in which individuals with unemployment protection that meets standards set by the state are not required to pay premiums or specific social security taxes. (However, these individuals may be permitted to re-enter the government scheme if their benefits from private sources become exhausted.)

In a sense, a version of the first model is already available in New Zealand. Individuals who are concerned about the risk of unemployment can and do save against this possibility. The re-examination of the minimum protection offered by the state would increase the scope for self-provision. Beyond this, self-provision can but be encouraged through a general climate of monetary stability and low marginal tax rates.

The opting-out model offers the prospect of additional gains through competition in the supply of the minimum unemployment benefit required by the state. Because, for distributional reasons, the government is likely to provide a minimum income in unemployment, the danger of 'free riding' is a real one. In the absence of restrictions some individuals will choose to pay premiums neither to the government scheme nor to private insurers, secure in the knowledge that income support from the government would be forthcoming should they need it. To avoid these dangers the state itself would have to decide the circumstances in which people could opt out of its unemployment insurance scheme. In doing so, officials may adopt an unnecessarily cautious and restrictive attitude. More serious, perhaps, is the danger of political interference in the premiums charged by insurance companies and in the redundancy provisions offered by superannuation funds and employers. It is a matter for further consideration whether, in practice, the opting-out model would be an advance over the simpler supplements model.

The feasibility of the opting-out approach, and its strengths and weaknesses, are illustrated by the health insurance arrangements that applied in Australia during the first years of the Fraser government. (As with unemployment insurance, moral hazard and adverse selection have to be addressed in the provision of health insurance.) Under the Fraser scheme, individuals who belonged to approved health funds were not required to pay the identified Medibank levy. This scheme was, without doubt, a reasonably successful alternative to a government monopoly in health care financing. But the development of innovative approaches to health insurance was impeded by the restriction of approval to traditional health funds of the community-rated type.

Since health funds were already offering health insurance before the opting-out system was introduced in 1976, it could be argued that this example differs importantly from the example of unemployment insurance in New Zealand. Although it is likely that the industry would develop innovative approaches to unemployment insurance were opting-out permitted, this would certainly take some time. But while competition may, for a time, be relatively limited it is unlikely to cause harm. There is, therefore, no reason to prohibit opting-out on these grounds.

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Family Allowance Benefits and Possible Alternatives for Reform

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Family Allowance Benefits and Possible Alternatives for Reform

Susan St John

I. INTRODUCTION

The family unit provides its members with a measure of security in an uncertain world. It is really the idealised welfare state in miniature, where the sharing of resources, cooperation and encouragement to self-help and self-discipline, support in times of adversity, enable its members to achieve their full potential and maximum independence.

If families perform their task well there should be a reduced need for other welfare spending such as on the unemployment benefit, sickness benefit and the Domestic Purposes Benefit. Instability and family failure on the other hand, will be reflected in the wider arena as failure of the welfare state.

Unfortunately, the sheer hostility of the economic and social environment is not conducive to families doing their task well. Unemployment, high inflation, high interest rates, increasing costs of health and education, peer pressure, fast foods, AIDS, VD, drugs and alcohol, fast cars and accidents are but a few of the factors that make the rearing of children an arduous and often fruitless task.

The best parents in the world will find it difficult, let alone those under financial pressures. Unwanted pregnancies, unemployability, violent and criminal adolescents, poor education and poor health are symptoms of family failure. My view is that unless we are prepared to do far more in supporting modern stressed families of all types we will face enormous social consequences in the coming years.

I realise that I am writing in the context of a substantial attack on the role of the welfare state. There is certainly persuasiveness in the argument that welfare benefits have undermined the traditional socialisation function of the family. There may well be a case for changes to the sickness, unemployment and domestic purpose benefits so that they give more appropriate signals to young people. Family assistance too should be carefully designed. But I see no alternative to increased state support if we are to tackle the basic causes of poverty. Only some aspects of family poverty, however, may be resolvable through more generous financial assistance alone. What is needed is a clear statement of the ultimate objectives of family policy and a willingness to ensure that all policies are consistent with these ultimate objectives.

II. GOALS OF FAMILY POLICY

I don't think there would be much quarrel with the idea that the ultimate goal of all family policy should be that children are reared to be fully contributing, socially responsible, well-educated, healthy individuals that became part of the solution of society's problems rather than part of the problems themselves.

Goals of social policy in New Zealand are, however, not usually stated in this way. The objectives are often expressed in terms of the intermediate aim which is seen as the provision of adequate income. Thus the 1972 Royal Commission on Social Security emphasised the rights of all to enjoy an income that was sufficient to enable participation in and belonging to society. But the counterpart to rights is responsibility. The obligations of parents and children are left unstated and unclear.

Focusing on the intermediate goal of ensuring an adequate income may obscure the need to be committed to wide support for families of all kinds, not just the poorest. For example, the unavailability of adequate counselling and rehabilitation facilities for young drug abusers affects all income levels, as do shortcomings in the education system.

All economic and social policies should be evaluated in terms of the objectives of family policy and not just in terms of objectives relating to economic performance such as low inflation or balance of payments stability. If this were the case, recent policies such as a user-pays approach to contraception, would be carefully thought through for their implications for families before implementation rather than as an afterthought.

III. ROLE OF THE STATE

I suggest that there are three major roles for the state consistent with the ultimate goals of family policy.

A suitable economic climate. First, the state has a crucial role in creating a suitable economic climate. High inflation, unemployment and high interest rates are devastating to the security of the family unit and there must be commitment to reducing these pressures even if it is at the expense of the achievement of some efficiency in the economy.

I am aware that there are dangers in makework programs and employer subsidies that retard the economy and thus impede the creation of permanent jobs. However, I suggest that one of the major impediments to job creation is the notion that new jobs must come from the private sector rather than the state. Our future standard of living may well depend on an expansion of job opportunities in areas where it is unrealistic to expect profit-seeking entrepreneurs to have much interest.

We need more teachers of all types, more health workers, especially in light of the impending AIDS disaster and the ageing population and more attention to conservation and environmental issues. The successful government of the future may be that one which can best persuade us that it is in our own interests to contribute taxes to expand employment in these and other community areas. It will be expensive and will require a new commitment and a renewed confidence that state involvement can be successful.

Attitudes. Lester Thurow (1985) in a telling critique of modern economics, argues that economists place far too much emphasis on the costs and benefits that are involved in determining an individual's course of action and too little emphasis on the formation and moulding of preferences and attitudes. Thus the literature on the economics of crime stresses the need to raise the costs to the individual relative to the benefits to inhibit criminal behaviour. An efficient society is not, however, one that devotes huge resources to the detection, prevention and punishment of crime. The truly efficient society is one that ensures that values of socially acceptable behaviour are inculcated at an early age. A society where the the strong expectation is that children will be reared, mostly in non-teenage two-parent families, to become responsible, well-educated, self-supporting, is one in which it is far easier to operate a humane and generous social welfare system without encouraging dependency and destroying incentive.

Lest all this sound utopian, the success of Switzerland in minimising welfare problems while dealing with the relief of poverty can be attributed in good part to the strong community support for the family. There is considerable emphasis on the responsibility of the family to produce productive, stable young people who in turn are also aware of their responsibility to become useful and productive citizens. Early marriage and teenage pregnancies are unusual and one-parent families are not common. Young people are dependent on their families for longer and the whole community takes an interest in the job that the family does. For example, truancy is rare, but if it does occur it becomes a matter of wide community concern.

Other countries' solutions may be examined but the environment at home is always different. Very low unemployment and inflation in Switzerland make it much easier to wean dependent people from welfare as much as does the very strong socialisation process provided by the home and the church.

But what clear signals do we give our children that early marriage and teenage pregnancies are not socially desirable and that child-raising and marriage itself are often onerous for parents who are young? The Board of Health Standing Committee on Child Health suggests that if current trends continue 25 per cent of New Zealand girls now aged ten will become pregnant by the age of 20.

In 1977, the Domestic Purposes Committee set up by government concerned at the escalation in this benefit, reported: 'There is not much doubt in our minds that the availability and generous nature of the DPB structure not only diminishes the fear of pregnancy but can also be very attractive to a young teenager and it is clear in many instances that the amount of money that can be received from the benefit is higher than what the girl herself could earn in normal employment. No one wishes to see a child deprived by reason of too limited a benefit, but also no one wishes to see a child disadvantaged a little later in life by reason only of the mother's ability to retain it.'

The unfortunate fact, ten years on, is that the DPB may be seen as preferable not to employment itself but to life on the unemployment benefit. Perhaps we do need to look at restricting the availability of the DPB in the interests of dissuading teenage parenthood. I would rather see the provision of realistic and meaningful alternatives to the dole, professional educative programs, and a clear statement to the young of their responsibilities and obligations to society.

If attitude formation is left to interested private sector groups, then I fear like other 'public goods' such as AIDS prevention, anti-smoking campaigns and environmental protection there will be far too little done. There is also the risk that opposing factions will cancel each other out.

We need professional school programmes that teach teenagers the realities of coping with babies as opposed to the mechanics of sex and reproduction. Are we afraid to introduce meaningful educative programs that clearly state community values because we are such a divided and non-homogeneous community?

Financial assistance. Critics of welfare may seriously debate whether the state should provide financial assistance to families. While I concede that the ready availability of some benefits may encourage welfarisation problems, family assistance could be regarded in a different light. In principle it recognises that families of different size have different abilities to pay tax. It cannot be the function of the wage system in a modern competitive economy to ensure sufficient income for those with varying numbers of dependants on minimum incomes. There are no realistic alternatives to tax-funded support to ensure that all families do have sufficient resources to perform their socially valuable tasks. Such support is not a dignity-sapping handout, eroding the breadwinner's function, but a reflection of community involvement in the socially important task of rearing the next generation.

Telling criticisms of the welfare state are that its mechanisms have become institutionalised and inflexible, that its programs reinforce outmoded concepts of dependency and that the goal of poverty reduction is often not achieved. I believe that we can take some pride that in New Zealand we have been willing to adapt our family assistance programs, when they appeared to be failing, in often very far-sighted and innovative ways. The sequence of reforms since the early 1970s reflects an increasing desire to target assistance more effectively to low income families in a way that emphasises the joint role of the two parents and de-emphasises the dependency of women.

IV. EXISTING STATE SUPPORT SCHEMES

Early in the 1970s, tax exemptions for children were abandoned(those on higher tax rates had gained the most in tax relief), and replaced by universal payments of the family benefit. Those on benefits received supplements related to the number of children. Then, following the realisation that family poverty was not confined to those on benefits there was a period of intense experimentation with ways to provide assistance to earners through the tax system. A variety of tax rebates was introduced with differing aims and criteria, with the result that assistance was not particularly well focused. Eventually, in 1982, the spouse rebate, young family, and low income family rebates were amalgamated into one family rebate that was abated against total household income. This, however, was insensitive to the numbers of children on the family, and, with the realisation that larger families were inadequately catered for, family care, a benefit that did adjust for family size, was introduced. More recently, family care and the family rebate were combined to give a single, adjusting and abating family rebate called family support. In addition to family support, the family benefit, a universal payment of $NZ6 per week per child is still paid. This has been allowed to steadily erode in value since it was last adjusted in 1979 in favour of the more selective approach.

In addition to family support and the family benefit, a top-up became available for those on very low incomes in the form of guaranteed minimum family income (GMFI) payments.

The truly innovative features of family support and GMFI programs include:

1. The treatment of the family concession as a tax credit to augment gross wages when the tax liability is insufficient to enable the full credit to be offset against tax due.

2. The determination of eligibility on grounds of household income and abatement against household income while retaining individual as the unit for positive tax assessment.

3. The splitting of the tax credit equally between both parents in a two parent family and the adjustment of the family support for extra children.

4. The equivalent treatment of beneficiary families by making benefits taxable and thus ensuring the eligibility for family support payments.

Less exciting and innovative, as in other countries where the general experience is that family assistance measures are not indexed, our new support package was introduced with no provision for formal automatic adjustments for inflation.

Family assistance includes the family benefit and the value of any tax rebates. Although different family groups have been affected differently by the various changes that have occurred, the real value of assistance for many has fallen.

The true casualty of the tax benefit reform package of 1 October 1986 was the small family. Here there was little or no gain from the extension of the rebate to allow for additional children and actual total family assistance in real purchasing power terms continued to decline from the position of the early 1980s, as the accompanying table shows.

Innovative as we have been, then, in other areas of family assistance this problem of inadequate protection in times of high inflation remains. Adjustments at the whim of government are too infrequent and usually inadequate, reflecting a lack of commitment to the principle of family support.

The maximum level of support for families may appear quite generous, but families need to be on very low incomes to fully qualify. By the time family income is at the level of average weekly earnings, currently $23 000 per annum, total family assistance for the one-child family is only approximately $14 per week. This is scarcely a generous level of support.

The slow erosion of the family benefit as a universal measure could be hastened by its incorporation into a more generous, family support tax credit — maybe one that recognises the extraordinary costs of teenagers, especially if they prolong their education.

Table One: Change in Real Family Assistance in New Zealand Over Time
One Child Family on 75% of Average Weekly Earnings (excludes GMI payments)

Year	AWE	CPI Family	Maximum Assist.	Family Assist. At 75% AWE	Real Family
	$NZ		$NZ	$NZ	$1980/81
1980/81	213	711	27	27	27
1981/82	256	821	27	27	23
1982/83	287	947	27	27	20
1983/84	295	995	32	27	19
1984/85	311	1081	39	33	21
1986/87	411	1428	42.5	35	17.5
1987/88	450	1616	42	34	15

AWE = Average Weekly earnings including overtime (approx. $23 000 1987/88)
CPI = Consumer Price Index
All figures are averages for the financial year and incorporate changes made part way through the year.
Family assistance is the difference between disposable income of a family and a couple alone on the same gross income. It includes family type rebates and the family benefit.

Sources
Department Statistics, Department Labour and St John (1985).

Suggestions that the family benefit be abolished are resented by those who view it as their source of independent income and raises the contentious issue of who would be the recipient of state support. Should all family assistance be paid to the carer parent, usually the mother, as is the family benefit? In many countries it is thought that the payment specifically to the parent at home is important in achieving intrafamily equity.

In New Zealand, we split the family support payment and all married rate social security benefits equally between the couple. This quite radical innovation says male and female are equal and both parents have equal responsibility for the care and upbringing of children. One partner may choose to be primarily responsible for the day to day care while the other earns family income; but the message should be that the parent who earns the money is no more important than the parent that stays at home. Other social policies such as the Matrimonial Property Act are consistent with this view. There is a fundamental hypocrisy in the idea that after divorce, family assets are equally shared, but before divorce the earner's income is his or hers alone.

Should the state be involved in the payment of benefits in lieu of fairness in sharing? A carer's benefit, as has recently been suggested, would be a retrograde step. There are severe design problems which include targeting the payment to contain the expense. More important, the creative work or parenting has a very high social value, and the idea that an augmented family benefit payment would in any sense reflect this value is absurd. In practice, the payments would not be high enough to help the low income families that really need the assistance, nor high enough to reflect the real value of the work done. The dangerous social signal may well be that earners rationalise inadequate sharing of their income because of these payments.

Why not an educative program for those at school or for those intending marriage that spells out the dual ownership of family income and assets, not just after divorce but as an accepted community practice within marriage? The success of this strategy demands that care givers value their contribution enough to believe that they have an equal right to the disposition of family income, and that there be recourse in the courts when fair sharing does not occur, such as is the practice now, through maintenance orders.

V. CONCLUSION

Those who choose to have children should be required to do a good job of educating and caring for those children. Support from the state has its counterpart in responsibility for contraception, preventive health care measures and adequate educational opportunities. It is time that these were spelt out as clearly articulated family policy. Generous financial assistance must be maintained in real terms in an environment that is conducive to family stability and supplemented by strong social signals. Then and only then, I believe, will we contain the problems of the modern welfare state.

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Relative Poverty and Welfare Distribution

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Relative Poverty and Welfare Distribution

Susie Kerr

I. INTRODUCTION

Poverty is usually defined in terms of a 'poverty line' income. This income level is determined by the consideration of the needs of individuals. In New Zealand the percentage of individuals who would fall below an absolute level of this type is probably fairly small (although still socially significant).[1] Therefore it seems sensible to define poverty as a relative concept where an individual's welfare is dependent on the level of income of others in society as well as his or her own income. This leads naturally to the measurement of relative poverty in terms of inequality indices (see Yitzhaki, 1979 and Berrebi & Silber,1985). Brian Easton (1983) measured Gini Coefficients, an inequality index, for the period 1953/54 to 1976/77. In this paper, however, we use four different inequality indices over the period 1977/78 to 1985/86.

Section II of this paper considers the properties of the four indices. Section III discusses the methodology of using 'equivalence scales' which adjust household income for the number of the people in the household. Results are presented in Section IV and are briefly discussed in Section V. Section VI offers some conclusions.

II. PROPERTIES OF THE WELFARE INDICES

The four inequality measures used are: the Gini Coefficient, the Coefficient of Variation, the Standard Deviation of Logs, and Atkinson's Indices of Inequality.

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[1] In New Zealand no study to measure absolute poverty in this way has been done. Brian Easton (1983) defined a relative poverty line and found that significant numbers of new Zealanders fell below this.

The Gini Coefficient is an intuitive measure of inequality which comes from the Lorenz Curve. The Lorenz Curve maps cumulative population ranked from poorest to richest against their cumulative income. The Gini Coefficient is twice the area between the line of complete equality (i.e. the poorest 10 per cent of the population receive 10 per cent of total income etc.) and the Lorenz Curve.

The Gini Coefficient has several important properties.

1. The sensitivity of the Gini to income transfers depends not on income levels but on the number of people between income levels. For example, in a three-person society the worst-off person is weighted five times as heavily as the best-off person while the intermediate person is given three times the weight of the best-off person.

Thus in New Zealand even though the income distribution is skewed towards the low-income groups and therefore causes the Gini to put heavy weights on those around the model income (which is below the mean), the frequencies in the very low-income groups are small. This means that transfers among the poor are given very low weights in New Zealand measures of the Gini Coefficient.

2. The Gini satisfies the Pigou-Dalton Condition which states: 'Any transfer from a poorer person to a richer person, other things remaining the same, always increases the value of the inequality measure'(Atkinson, 1970:249).

3. The Gini is symmetric. This means that if any two or more individuals have their situation interchanged, the level of the inequality measure will remain constant. Thus individuals are 'anonymous'.

4. Proportionate changes in all income levels do not change the value of the Gini Coefficient, i.e. it is independent of mean income.

The formula used to estimate the Gini Coefficient is:

$$G = 1 - 2 \sum_{t=1}^{T} [S(y_t) / N \mu \;.\; f(y_t) / N]$$

$$y_1 \leq y_2 \leq \ldots \leq \ldots y_n$$

$$\text{where } S(y_t) = \sum_{i=1}^{t} y_i \;.\; f(y_i)$$

$$\mu = \sum_{t=1}^{T} y_t / N$$

The Coefficient of Variation is also symmetric, independent of mean income, and satisfies the Pigou Dalton Condition. It weights individuals' mean income levels by the square of their distance from the mean. It has the same sensitivity to transfer of income at all levels of the income distribution (Atkinson,1970:255). Thus neither the Gini nor the Coefficient of Variation weights low income groups heavily. One other disadvantage with the Coefficient of Variation is that it only compares income levels with the mean income whereas the Gini compares all incomes with every other income.

The formula for the Coefficient of Variation is:

$$C = \sqrt{\frac{\Sigma\,(y_i - \mu)^2/N}{\mu}}$$

The Standard Deviation of Logarithms is defined as:

$$H = \sqrt{\left[\frac{\Sigma\,(\log \mu \; - \; \log y_i)^2}{N}\right]}$$

Because of the log transformation, this measure puts much greater weights on the lowest income groups and is very sensitive to transfer to (or from) these groups. It is a symmetric measure and independent of mean income. One major drawback of this measure is that when the mean income level is high it may not satisfy the Pigou Dalton Condition which is a basic requirement for an inequality measure (Sen, 1973:32).

The last measure used was Atkinson's Inequality Index. This is derived directly from a symmetric, strictly concave (i.e. it satisfies the Pigou Dalton Condition) additive social welfare function that is independent of mean income. Additivity is not necessarily a desirable property because it implies that individual utilities are independent.

Atkinson's index is defined as:

$$I\ (\varepsilon \neq 1) = 1 - \left[\sum_{i=1}^{n} \left(\frac{yi}{\mu}\right)^{1-e} f\,(yi)/N\right]^{\frac{1}{1-e}}$$

$$I\ (\varepsilon = 1) = 1 - \frac{\exp\left[\sum_{i=1}^{n} \log_e\ (y_i)\ \cdot\ f(y_i)/N\right]}{\mu}$$

ε is a measure of society's aversion to inequality. If ε is large, society is very averse to inequality and heavy weights are put on the lowest income groups. If ε is small, the opposite is true.

Thus different measures of inequality change the emphasis on the income levels of different groups in society. Further, each measure has different properties and these must be considered when interpreting the results.

III. DATA AND METHODOLOGY

The data comes from the Household Expenditure and Income Survey 1977-78 to 1985-86.[2] The Household Income data were adjusted to give a per capita income distribution. It would be possible to convert household income to per capita income simply by dividing each household's income by the family size. However this process does not allow for economies of scale in running a household. (For example, it does not cost three times as much as a one person household to provide a three person household with an equivalent standard of living.) Instead, equivalence classes are constructed to show the income necessary to give a larger household (i.e. 2,3, ... n persons) the same standard of living as a one person household.[3] In this paper we use a scale constructed by Easton (1973), which is given in Table 1. We then divide each household's income by the appropriate value. This gives a per capita income distribution from which the four measures are estimated.

Table 1: Easton's Equivalence Scale

1	2	3	4	5	5.5*	6	6.5*
1.0	1.371	1.70	2.03	2.23	2.355	2.48	2.689

* These values are constructed by interpolation.

[2] However, as the data was not available in published form after 1982/83 it was supplied by the Department of Statistics.

[3] Muellbauer (1974) discusses the use of equivalence scales and their implications.

IV. RESULTS

The estimated measures of the four inequality indices are given in Table 2. The numbers in brackets are approximate standard errors multiplied by three.

All the measures (except the Coefficient of Variation) rose considerably over the period 1977/78 to 1981/82. The first three measures fell significantly between 1981/82 and 1983/84 and then began to rise slowly. Atkinson's indices fell in 1982/83 and then began to rise slowly.

These results can be seen graphically in Figures 1 to 4.[4]

In Figure 2 the Coefficient of Variation and the Gini Coefficient are closely related in terms of proportional changes. However, although the Standard Deviation of Logs follows the same trend as the others, its proportional changes tend to be larger (smaller) in absolute value when inequality is rising (falling). This suggests that the lowest income groups are becoming relatively worse-off causing inequality generally to rise, while middle-income groups are relatively doing better. Together these cause the Gini coefficient to rise by less than the Standard Deviation of Logs due to their different properties.

Figure 3 graphs the Atkinson's Indices. These show a similar pattern to the others, although with smaller changes, except in 1983/84 where they rise slightly, while the other measures are still falling.

In general the results from the different measures corroborate one another to show a pattern of rising inequality between 1977/78 and 1981/82, a fall between 1981/82 and 1983/84 and then a further rise up to 1985/86.

[4] The absolute values of the Coefficient of Variation shown are C.V. minus three.

Table 2: Results

Year	Gini Coefficient	Coefficient of Variation	Standard Deviation of logs	e = 0.5	e = 1.0	e = 1.5	e = 2.0
1977-78	0.2847 (0.0075)	0.5413 (0.012)	0.2333	0.0642	0.1251	0.1828	0.2380
1978-79	0.2929 (0.0077)	0.5431 (0.014)	0.2536	0.0686	0.1371	0.2076	0.2886
1979-80	0.2936 (0.0069)	0.5343 (0.014)	0.2632	0.0698	0.1419	0.2188	0.3066
1980-81	0.3066 (0.0061)	0.5634 (0.014)	0.2734	0.0765	0.1541	0.2319	0.3086
1981-82	0.3126 (0.0081)	0.5693 (0.015)	0.2927	0.0815	0.1672	0.2563	0.3461
1982-83	0.2987 (0.0065)	0.5378 (0.014)	0.2696	0.0455	0.1235	0.2068	0.2945
1983-84	0.2814 (0.0062)	0.5045 (0.011)	0.2602	0.0657	0.1361	0.2116	0.2920
1984-85	0.2849 (0.0063)	0.5138 (0.011)	0.2590	0.0682	0.1422	0.2230	0.3104
1985-86	0.2902 (0.0065)	0.5228 (0.012)	0.2740	0.0706	0.1469	0.2298	0.3187

Figure 1

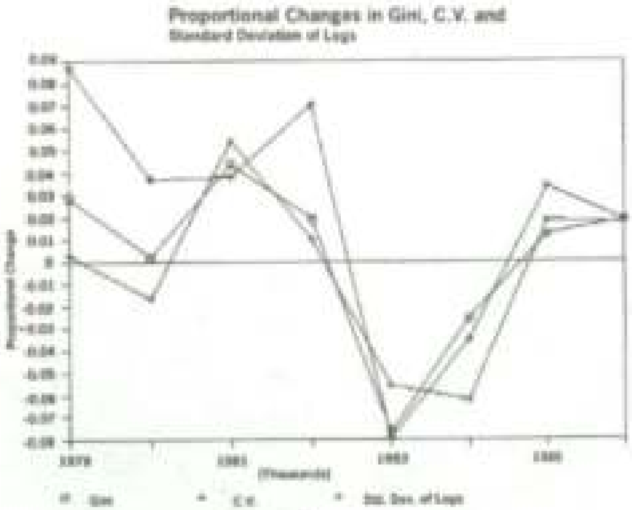

Figure 2

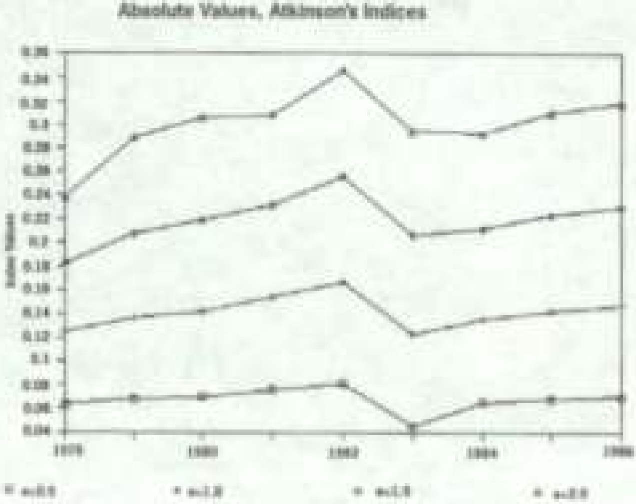

Figure 3

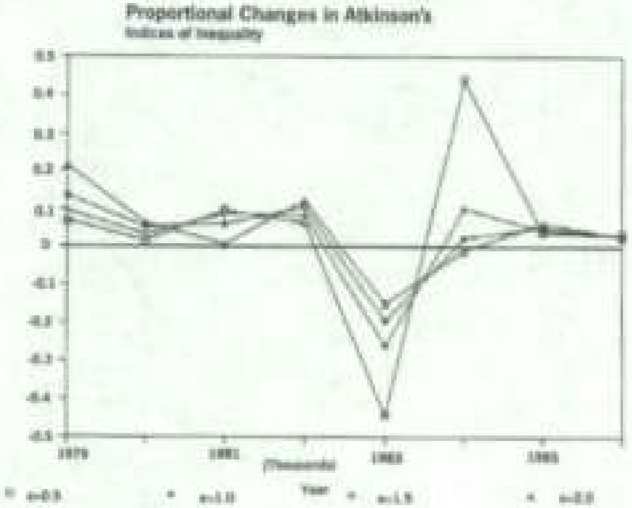

Figure 4

Unemployment 1977-78 to 1985-86

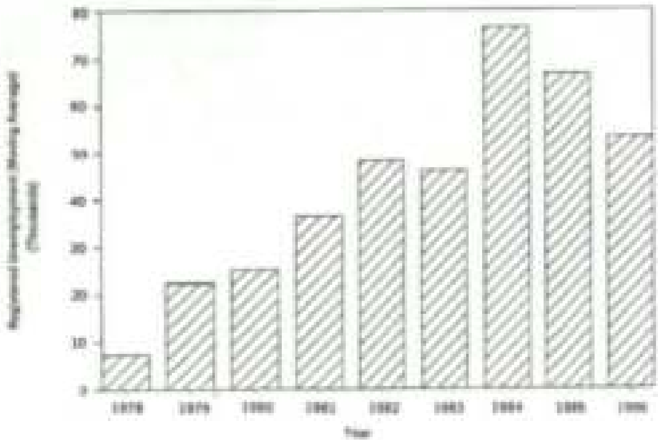

Figure 5

Inflation 1977-78 to 1982-83

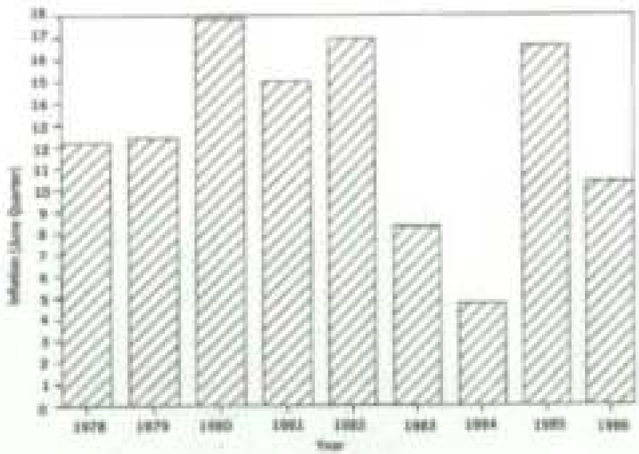

Figure 6

V. INTERPRETATION OF RESULTS

Three possible explanations for the changes in inequality will be considered within this section, although many other factors will clearly be involved.

First, **unemployment** could be expected to directly effect inequality. From Figure 5 we see that unemployment increases from 1977/78 to 1980/81, and then falls until 1982/83.[5] This feature relates well to inequality measures. However, for the later periods, changes in unemployment do not correspond to changes in inequality and this is shown in particular, by the changes being negatively correlated.

Second, **inflation** may have some relationship with inequality. This is because inflation disadvantages those on relatively fixed incomes who also tend to be in low-income groups (e.g. pensioners, beneficiaries, workers with weak [or no] unions). Figure 6 graphs inflation over the period being considered.[6] Inflation is very high in the first part of the period when inequality was rising. From 1982/83 to 1983/84 inflation is much lower, while inequality was fa'ling. This was the period of the wage and price freeze. After 1984 inflation rose considerably and then fell. This suggests at least a tentative relationship between inflation and inequality.

Finally, one further possible interpretation relates to the **rise in the income share of the middle income groups.** This is shown by the smaller rises (larger falls) of the Gini Coefficient compared to the Standard Deviation of Logs. Welfare 'encroachment' by the middle classes could possibly be a factor involved in this. If the middle classes are receiving an increasing share of welfare benefits this would directly raise their income and by reducing available state resources lower the share of state assistance received by low-income groups.

VI. CONCLUSIONS

In this paper we extend the work of Easton (1983) in measuring inequality in New Zealand. We estimate four different inequality indices with varying properties and apply a different methodology, namely the use of 'equivalence scales'.

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[5] Data come from the Monthly Abstract of Statistics and consists of unemployed females combined with unemployed males (registered unemployed). Average over four quarters at December.

[6] Data comes from the Monthly Abstract of Statistics. It consists of the Consumer's Price Index, all groups (1983(4) = 1000) Inflation in year to June.

In terms of 'direction of change', the different indices tend to support one another, showing an increase in inequality up to 1981/82, followed by a decrease until 1983/84 and then a further rise. However, the indices differ in the size of proportionate changes. In particular, the difference between the Gini Coefficient and the Standard Deviation of Logs suggests that most of the increases in inequality are caused by the poorest groups becoming relatively worse-off while middle income groups may be doing better through the period. This latter result suggests that the government needs to take into account increasing 'income inequality' in its policy making and in particular social welfare reform.

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Possibilities for Lifecycle Health Insurance

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Possibilities for Lifecycle Health Insurance

John Logan*

1. GOVERNMENT INVOLVEMENT IN HEALTH CARE FUNDING

Health services in Australia have, for many years, been funded from a mixture of public and private sources. Until recently, the proportion funded from public (i.e. tax-funded) sources remained roughly constant at about two-thirds of total health expenditure. This proportion has since expanded with the introduction of our 'universal' health scheme, Medicare, and now stands at about 74 per cent of a total expenditure of $A19 billion (7.2 per cent of GDP)(ABS, 1987).

Under Medicare, most of the costs of medical services are shouldered by the taxpayer, with the patient paying fees that range from nothing, up to 1 per cent of MBS[1] fees for services rendered outside hospital (2 per cent for in-hospital services). Patients pay more if the doctor chooses to charge fees that are above the MBS level, but competition amongst doctors can be predicted to drive fees down towards the scheduled fee for 'expensive' services, and down to the 8 per cent discounted level at which doctors bulk-bill, for 'cheaper' services (i.e. with MBS fee set below $133[2]). The evidence suggests that the incidence of bulk-billing has grown over the Medicare period.

If a person is able to find a bed in a public hospital and joins the other 8 per cent of public hospital patients who elect to remain 'Medicare' patients, then he or she pays nothing in return for forgoing the right to choose one's

* I would like to thank Paul Collins of the CIS, for assistance with the statistics and calculations for this paper, and John Walsh, actuary, for valuable comments and suggestions.

[1] This is the Medical benefits Schedule, or 'official' price list which is used to determine the Medicare rebate.

[2] The economics of market-clearing fees under Medicare is outlined in Logan, 1986: 45-78.

doctor for in-hospital services. Even a 'private' patient in a public hospital indirectly receives a subsidy of $50 per day from the taxpayer.

People who prefer private accommodation in hospitals (public or private) must pay out of their own pockets either directly to the hospital of their doctor's choice, or indirectly via private insurance. Currently, government legislation sustains a cartel of private health funds each of which offers a limited variety of health policies. No health insurer offers policies that contain any provision for a person to contract for long-term (or life) cover in return for premiums that are lower than those applying to policies that are currently offered.

Applying mixed socialism to health-care financing has three consequences relevant to the theme of this paper. The first consequence is that demand for health services expands because Medicare subsidies enable patients to ignore the full costs of the services they consume. This inevitably means that either taxpayers are 'asked' to contribute more to the the funding of health care for their fellow Australians, or patients' non-money costs rise (e.g., having to wait excessively for services), or both. The upshot is that other people give up more in value than is delivered to patients in the form of additional, or marginal services and so resources become inefficiently allocated.

The second consequence is that Medicare, together with the regulations imposed upon the restricted set of official, registered health insurers, has resulted in an available portfolio of health policies that do not meet the preferences, and incomes, of disparate individuals to the same extent as would be expected in a free (or less restricted) insurance market. Prior to Medicare, several for-profit insurers offered policies at a far cheaper premium, but with incentives for economising behaviour by patients built in through front-end deductibles, non-smokers' discounts, and so on. Naturally, this dual system of for-profit insurers (shockingly unregulated) trading alongside the registered funds, who are required to practice community rating, meant that the registered funds became insurers of last resort for many high-risk, costly, people. This adverse selection further inflated the premiums from the registered funds. The non-registered insurers had to go, and in September 1985 they were precluded by law from writing any new business. The higher premiums and lack of alternative policy options would, predictably, have contributed to people taking out less private insurance than otherwise. In addition, people predictably opted out of costly private insurance, anticipating access to the cheap alternative — Medicare[9] — at prices of almost zero.

[9] Changes in the insured population are presented, for example, in: Voluntary Health Insurance Association of Australia, *Statistical Bulletin*, various.

The third consequence is that there is a massive redistribution of income (and hence wealth) to those who consume more health services, or services that are relatively more expensive, than the average family consumes. Although a proportion of the favoured recipients are 'poorer', at least in income, than are those who fund the transfer, there are no doubt many who are not so disadvantaged. The richer person who chooses Medicare status at a public hospital, and has managed to be early in the queue, crowds out the poorer person waiting (patiently) for a bed. Medicare is a universal club of which everybody, rich and poor alike, are compulsory members, and so everybody, including the ultra-rich, receives the subsidy for medical services consumed[4]. Finally, the elderly, who consume a far greater proportion of health services, are not necessarily poor in terms of wealth; poverty of cash flow can be easily bundled with an abundance of physical, or non-income-earning assets.

This is certainly not to argue here that equality in the distribution of income and wealth is, or is not, a 'good thing'. It is to argue instead that the goals of redistributive policies are not achieved through subsidising health in the way that this is done in Australia. Even if the goals were met they would be met inefficiently, as is the case with all redistributions in kind. The best way to redistribute income is simply to redistribute (cash) income.

II. LIFECYCLE HEALTH COSTS

The average costs of health care vary according to age and to sex. The accompanying Figures 1 & 2 exhibit estimates of annual average lifecycle costs for people within a number of age cohorts that each range from 0-4 years up to 85 plus. The estimates were derived from a number of sources and computed by making some assumptions about hospital costs and other components of demand.[5] The dollar amounts are therefore 'what if?' estimates only, and so the usual caveat applies.

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[4] Note that the Medicare levy (often erroneously regarded as some kind of 'membership fee') does not 'pay' for health services; it is a tax-surcharge entirely unrelated to the consumption of health care, and could just as well be called simply a 'tax surcharge'.

[5] Hospital and Nursing Home bed-day utilisation by age and sex are for NSW (other data was not readily available), and medical costs are from Medicare data adjusted upwards for the Medicare discount of the MBS fee for rebate purposes, plus an estimate of the costs of medical services rendered to 'Medicare' patients in public hospitals (NSW institutional data for 1984 kindly supplied by the NSW Department of Health, medical services data from the Health Insurance Commission *Annual Report*, 1985/86). Hospital non-medical costs were, for the purposes of the exercise, taken to be $250 per OBD (occupied bed-day), and a $90 per OBD allowance for a public hospital patient's medical costs was assumed. Other assumptions can easily be incorporated into the model.

HEALTH COSTS per YEAR

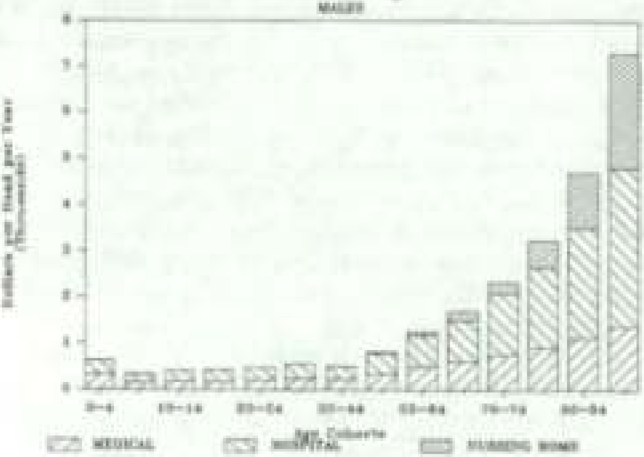

Figure 1

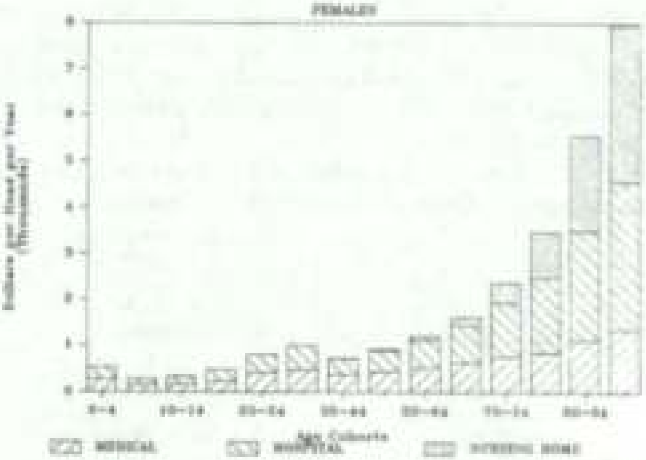

Figure 2

Within each cohort, costs are further broken down into medical, hospital, and nursing home, costs. There are, of course, other components of health expenditure that are not included here, such as expenditure on pharmaceuticals, social workers, and community care; but these might not be expenses against which one would normally insure if given the choice. We may also note at this point that predictable expenses of moderate amounts — such as the costs of regular visits to one's GP — would not normally constitute insurable risks, in the same way that people do not insure against regular services for motor vehicles (Lees & Rice, 1965: 140-54). On the other hand, the estimates for expenses within the model are probably greater than those that would emerge under free market conditions. This is not only because of upward adjustments to the estimated figures but, more importantly, because a free market in health care and insurance would result in economies in the otherwise lavish expenditures on marginal, but perhaps expensive, procedures, that are now funded by the taxpayer.

From Figures 1 & 2, it is readily observed that costs rise exponentially towards old age, and that these additional costs are intensive in (expensive) institutional care. It should be emphasised that these are averages taken over the entire population within each cohort, and so do not capture the variety of costs for any single age group. For example, whereas the average cost per head of all females aged 85 or more is estimated at just under $8000, an institutionalised aged person might generate upwards of $30 000 per year in health costs. Since expenditures of this order of magnitude would be difficult to finance from family resources, were the taxpayer given respite from this particular burden, the question that then arises is: are there other alternatives?

III. REDISTRIBUTING OUTLAYS OVER TIME

The model to which Figures 1 & 2 refer shows average health costs remaining at reasonably manageable levels for many years over one's working life, and then rising from about age 55 onwards. The intertemporal cost profile for the average female shows a small and temporary rise in the 25-34 age group This appears to be largely the consequence of reproduction, which is nowadays a relatively controllable, and therefore predictable, event. In fact, the graphs understate (pictorially) the length of time before which average health costs begin to rise significantly, since the mid-life age cohorts are of 10 years duration as compared to 5 years both for the young and for the elderly.

The question then is: if one's expected future life-stream of health expenditures were converted to an annuity beginning at some point early enough in one's working life, would the outlays be modest enough to remain affordable? If so, then an unregulated insurance market might be expected to generate policies that offered to take on the risk that one may perhaps not follow the path of the average family, but that one's future health demands became unexpectedly large.

To investigate this, we chose two crude methods of estimating the 'fair' premium. Our computations ignore the loadings for the cost of producing insurance such as administration costs and loadings required to reduce the probability of insurers' bankruptcy to a minimal acceptable level.[6] To this extent we understate the final cost to the consumer. The reader could, however add about 15 per cent (roughly) to our figures; the intertemporal time paths that we now develop are each raised uniformly by this percentage, and so our basic conclusions are only marginally affected.

IV. THE FAMILY

The first method was to compute the expected present value of average future health costs for individuals and for families in alternative circumstances, weighted by survival probabilities derived from ABS mortality tables, and truncated at age 99 (beyond which the survival probabilities as at, say age 20, become extremely small).[7] The present values were then converted to constant-premium annuities from entry age (the age at which the person takes out a lifecycle policy), up to exit age; this is the period over which the person, or family, must pay premiums. After exit age, the insured adults are covered for the rest of their lives without further payment of premiums. The annuities were calculated by choosing a real (inflation-free) rate of discount of 5 per cent for this exercise.

Some of the results for families are shown in Figure 3, the dollar amounts for which are presented in Table 1. For families, it was assumed that the male and female ages were 24 and 22 respectively at marriage (or equivalent), that the first child was born three years later, and the second child two years after that. Naturally, other assumptions can easily be used in the model, but this appears consistent with data on what constitutes the 'average' Australian family.[8] Children were assumed to be supported by their parents, at least in so far as health expenditure is concerned, until the end of their 19th year, after which they are on their own. The calculations are biassed upwards in assuming only male children, as they are more costly on average than are

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[6] Reinsurance and insurers' 'ruin' has received an extensive treatment in the literature. See, for example, H. Seal (1969).

[7] Some upward adjustment in the calculations that follow would be necessary if it is anticipated that survival probabilities will *rise* over the long run.

[8] See for example, demographic data presented in ABS, *Social Indicators*, No. 4, 1984, ch. 2.

Table One: Premiums for Families

Exit Ages	Single Male	Single Female	Couple	Couple With:- 1 Child	2 Children
50	955	1383	2293	2647	2969
55	875	1268	2114	2440	2736
60	822	1191	1992	2300	2579
65	785	1136	1906	2200	2467

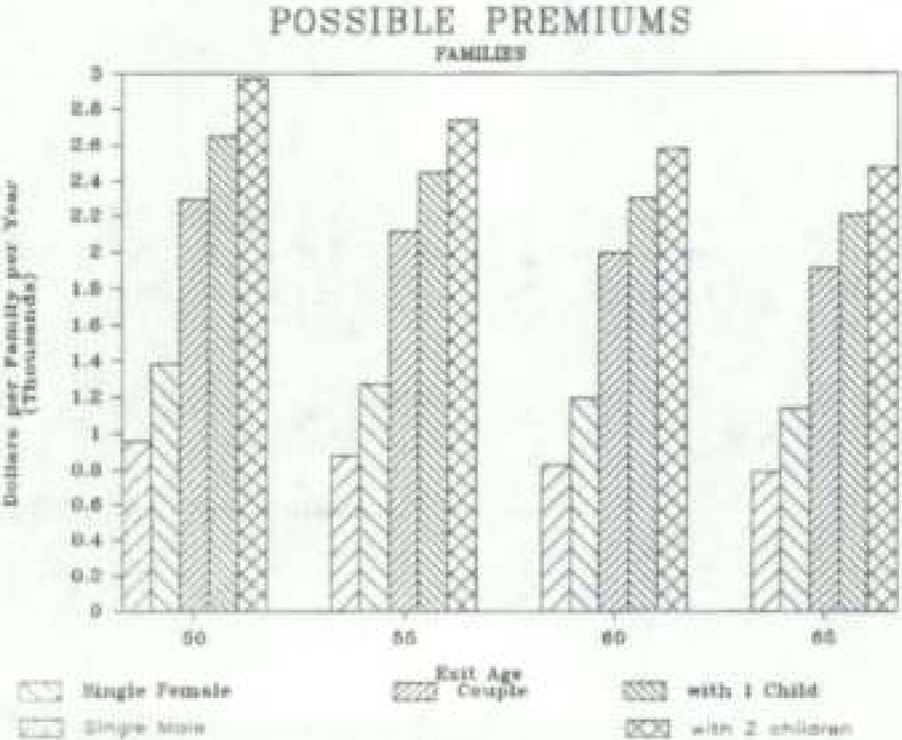
POSSIBLE PREMIUMS
FAMILIES
Dollars per Family per Year (Thousands)
0
0.2
0.4
0.6
0.8
1
1.2
1.4
1.6
1.8
2
2.2
2.4
2.6
2.8
3
50
55
60
65
Exit Age
Single Female
Single Male
Couple
with 1 Child
with 2 children

Figure 3

females, in terms of present value, in the age range 0 to 19 ($5900 compared with $5100 as at age 0, calculated at 5 per cent rate of discount).

Figure 3 and Table 1 show the annual outlays assuming that, if single, then the individuals in the examples take out their policies at the same age at which they would have if married (i.e. 24 and 22 for him and her respectively). The alternatives for the periods over which the payments might extend are given as the exit ages. At this point we are assuming that insurers discriminate on the basis of sex in order to set rates. For example, a single male would pay $785 a year ($15.10 per week) if he contracts to continue payments up to age 65, whereas a single female would pay $1136 a year ($21.85 per week) from age 22 to age 65. If each took their policies out at age 20 and planned to pay premiums until age 65, the respective outlays would be $716 per year ($13.77 per week) and $1078 per year ($20.73 per week) respectively, as may be seen from inspecting the appropriate cells in Table 2. The difference between the (two) sexes reflects the averaging effects of pregnancies plus longer life expectancies, and hence higher downstream costs, for females.

Quite probably, and certainly under the hostile atmosphere that today surrounds inter-sex differentials in almost everything, insurers may be expected to charge the same premium independently of sex; in this case the actual rates charged would lie somewhere between those specified above. More seriously, since part of the inter-sex cost differentials arise from pregnancies, there is the question of proportioning the burden of this cost; it takes two to tango. A market solution might perhaps include incentives in the form of downstream discounts for childless females. In any case, the problem is solved, at least in respect of child-bearing, when parents are united as a family, in which case the premiums coalesce indissolubly, 'till death do them part'.

The figures for families with children are calculated by assuming that the parents take out a policy at marriage (or its modern equivalent) to cover the costs of health for the children that they will eventually have. Again, other assumptions about the costs of family outlays may be incorporated, and the numbers here are primarily for purpose of illustration. A two-child family (males only) would entail a family outlay of $2467 per year (47.44 per week) to age 65, or, alternatively, $1906 per year ($36.65 per week) for just the couple, with the parents covering the childrens' health care costs as they occur. On average, this would amount to annual payouts of between $390 and $470 per annum for each child over the course of his dependency, but parents would then be bearing the risks of self-insuring the children, as embedded in the frequency distributions of health costs for each of the younger-aged cohorts.

No doubt many two-child families would regard with dismay any proposal that, in the current environment of cross-subsidised caring, asks them to incur these higher outlays in order to avoid the risk of unexpectedly high family health costs. In Australia, the traditional form of health insurance in the private market has been to offer premiums for families that were simply double the rates for singles (rates being set independently of sex), regardless of family size. The numerical illustration here is indicative of the large cross-subsidisation that favours families with children. This is analogous to motor vehicle insurers offering one-car and multi-car family policies with the rates for the latter set at twice the rate for the former, independently of how many extra vehicles are owned by the multi-car family. It is instructive to contemplate the rates for motor vehicle insurance that would have to be set for single-car families.

V. OUTLAYS FOR INDIVIDUALS: THE EFFECTS OF POSTPONING ENTRY

Premiums were computed for individuals using the above methodology, with the additional assumption that people might opt for alternative ages at which they plan to enter a lifecycle health insurance scheme. For purposes of this exercise, alternative entry ages were chosen at five-year intervals from age 15 up to age 60 for policies equivalent to those that were assumed to be available in the family examples given above. The premiums are shown as the first 4 rows of each of Parts A and B of Table 2, and are depicted as graphs in Figure 4 as the four uppermost lines. In addition we computed premiums for a lifecycle contract under which premiums would continue to be paid past retirement age and, we assumed, would be paid up to the expected life of the individual. Premiums for this last set of cases, allowing people to enter the scheme up to age 65, are listed in the bottom rows of each Part of Table 2, below which are listed the life expectancies at each of the alternative entry ages. The relevant graph for males is the lowest line in Figure 4. The profile for females is similar, as can be seen from reading across the rows of Table 2.

As a particular example, consider a young male who chooses a lifecycle policy at age 20, assuming for purposes of illustration that the sexes are distinguished for rate-setting. He would pay \$828 per annum (\$15.92 per week) if he contracted to pay premiums only up to age 50, and, as for the previous section, \$716 per annum (\$13.77 per week) if he elected to pay until age 65 (read down the second column of Part A of Table 2). If he elected to pay premiums until his expected age of almost 74 years, then he would pay \$688 per annum, or \$13.23 per week, which is a minor saving of 54 cents a week over the cost of a contract under which premiums are paid only up to age 65. That is, the option of not having to pay for health insurance in one's

Table Two: Premiums for Alternative Entry Ages

A: MALES — **Entry Ages**

Exit Ages	15	20	25	30	35	40	45	50	55	60	65
50	718	828	970	1158	1484	2203	4426	0	0	0	0
55	686	777	890	1024	1236	1639	2481	4708	0	0	0
60	662	741	835	939	1093	1365	1846	2640	5151	0	0
65	644	716	797	882	1002	1207	1538	1964	2888	5319	0
T*	625	688	753	817	905	1039	1246	1446	1739	2042	2526
*Expected Life,T:	73.5	73.8	74.2	74.5	74.8	75.0	75.4	75.9	76.7	77.8	79.3

B: FEMALES — **Entry Ages**

Exit Ages	15	20	25	30	35	40	45	50	55	60	65
50	1043	1246	1424	1614	1943	2825	5540	0	0	0	0
55	996	1170	1306	1427	1618	2101	3106	5979	0	0	0
60	961	1117	1226	1308	1431	1750	2311	3352	6595	0	0
65	936	1078	1170	1228	1312	1548	1925	2494	3698	7109	0
T*	894	1015	1081	1102	1135	1271	1465	1660	1986	2338	2933
*Expected Life,T:	79.7	79.9	80.0	80.1	80.3	80.4	80.7	81.1	81.6	82.3	83.2

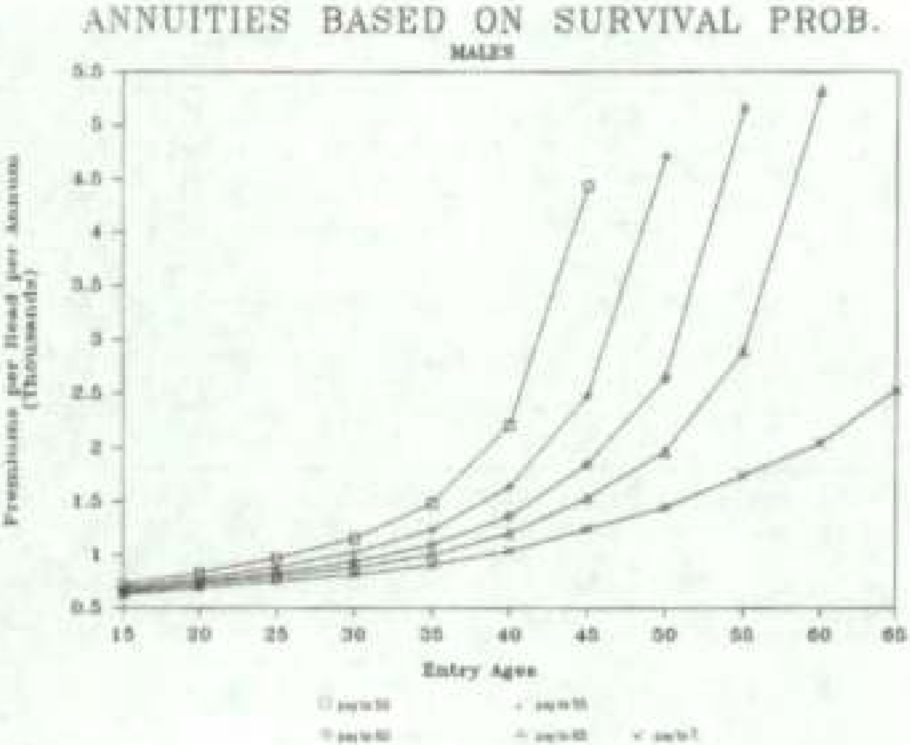
ANNUITIES BASED ON SURVIVAL PROB.
MALES
Premiums per Head per Annum (Thousands)
0.5
1
1.5
2
2.5
3
3.5
4
4.5
5
5.5
15
20
25
30
35
40
45
50
55
60
65
Entry Ages

Figure 4

post-retirement years can be purchased at the modest cost of 54 cents per week up until retirement, provided that one enters the scheme at age 20. For a female entering the scheme at age 20, the equivalent amounts are: $1246 per annum ($23.96 per week) payable up to age 50, $1078 per annum ($20.73 per week) payable up to age 65, and $1015 per annum ($19.52) payable up to an expected life of just under 80 years of age (from the second column of Part B of Table 2). That is, she can buy the option of not paying health insurance premiums past age 50 for an outlay of $4.44 per week ($23.96 minus $19.52), or the option of not paying past age 65 for a cost of $1.21 per week ($20.73 minus $19.52). In reality, the relative costs under non-discriminatory pricing would lie somewhere between those computed for males and those computed for females.

As we noted earlier, the relatively greater loading for a female at age 20 reflects her likelihood of greater resource utilisation both because of pregnancies and because of her longer expected survival as an elderly person. It is interesting to note at this juncture that the premiums for exit ages of 65 are 51 per cent greater for females than they are for males entering at age 20, and are just below 30 per cent greater when comparing premiums for males and females entering in the 'post-pregnancy' years of 35 or older. A second interesting observation is that these relativities expose the cross-subsidisation implicit in the present system of private health insurance under which the same premiums are charged regardless of the sex or age of the insured person, and regardless of family size.

In general, the effects on premiums of postponing the age of entry are discerned by scanning across the various rows of figures in Table 2. The 20-year-old male of our previous example, who now postpones entering until age 35, would pay a premium of $1002 per annum ($19.52 per week), in order to exit at age 65 with 'free' cover thereafter, and this would rise to $2 888 per annum ($55.54 per week) if he entered at the late age of 55. However, this outlay would last only up until age 65 in this example. On the other hand, if he enters at age 55, and elects to pay premiums until his expected life of almost 77 years of age, then the premium would be $1,739 per annum, or $33.44 per week, which is within the financial capacity of a (male) person with a reasonably satisfactory superannuation arrangement. Similar calculations can be made for families.

For males, the postponement effects are show in the graphs in Figure 4 by following any one of the lines from the earliest entry age of 15 years onwards. The striking feature of these graphs is that the premium payouts remain remarkably steady at around the $1000-$2000 (per annum) level for entry ages up to 35, and are closely grouped for exit ages from 65 down to as low as 55. In particular, the rise in the premiums that are payable until one's expected life is not nearly as steep towards retirement as it is for the policies with earlier exit ages. Even for entrants at age 65, the premiums remain at $2526 per annum ($48.58 per week) for males and $2933 ($56.40 per week) for females assuming separation of premiums by sex). Whilst these amounts are not within the ranges of the modest payments for insurees who are, temporarily, blessed with youth, they are not completely beyond the means of all retired persons. One alternative, for example, would be for a person to spend part of his or her lump-sum superannuation encashment as a lump-sum purchase of a health policy for its present value. Under the assumptions of our present model, this would amount to $25 005 for a male and $34 280 for a female, or somewhere in between under common premiums.

VI. IMPLICATIONS FOR IMPLEMENTATION

One implication of the shape of the time-profiles of premiums over varying entry ages is that it usefully informs us about implementation strategies. Deregulation obviously harms those who are presently in receipt of net subsidies from the current tax-funded system, but benefits others who are currently paying out amounts greater than they receive as health benefits.

A sudden rash of deregulation and privatisation would especially harm the elderly and infirm whose financial decisions had been taken within an environment in which health policy had created expectations of the availability of continuing subsidies. A similar consideration obviously applies to a lesser extent to people who are now approaching their retirement ages. With an almost certain prospect of large subsidies for health, it makes sense not to arrange one's economic circumstances so as to adequately provide for one's future, but instead to rely on the promise of tax-funding. When governments renege on promises of the kind that profoundly affects peoples' entire lifetime activity, windfall losses are imposed upon those unfortunates for whom it is too late to alter course. The gainers are those who, in the post-regulation environment, pay less for health services now more efficiently delivered, and in addition receive a lighter tax burden.

Given the relative stability of the lifecycle premiums up to entry age of 35, a possible implementation strategy might be to announce a package that has a long-term goal of complete privatisation combined with short term tax-funded support for older persons. For example, the policy might set a threshold age for implementation of somewhere between 30 and 35 (with varying tapers, the design of which can present a useful challenge to the creative genius of bureaucrats). People who, at the date of implementation, were older than the threshold age would have the right to receive exactly the same subsidies as before, whereas these rights would be denied to those who were younger than (or of age equal to) the threshold age.

These younger persons with a longer productive life ahead would find it necessary to decide whether they wished to devote a part of the fruits of their productive activities to save and to hedge against health risks. Naturally, these people should be the ones to first receive the benefits of tax-savings from the gradual implementation of a privatised system. A further variation might be to enable older persons to opt out of all future subsidies in return for tax-savings, but this would remain a voluntary choice. The subsidised cohorts who had been above the threshold at the date of implementation would shrink over time, as its members inevitably depart for alternative policy-environments elsewhere. Full implementation would be almost complete in about 50 years, which is consistent with time horizons that politicians appear to adopt when they wax enthusiastic about tree-preservation programs or tunnels under harbours.

Finally, a feasible strategy that may enhance the marketing of lifecycle policies, would be to incorporate the premiums with superannuation contributions, perhaps as an optional extra. One advantage of this would be to reduce the effect of anti-selection bias — that young, temporarily low-risk, persons do not choose to take up health insurance.[8] Given that superannuation contributions are tax-deductible (up to a fixed limit), tax-deductibility could be extended to loadings for lifecycle health cover, perhaps even on top of the limits for normal superannuation deductions. As an extension of a policy of providing incentives through the tax system, a tax-deduction or tax rebate for insurance premiums could be made available to all taxpayers who opted for a lifecycle policy, but who had not chosen to join a superannuation plan.

VII. VARYING THE DISCOUNT RATES: THE IMPORTANCE OF TAX POLICY

Because the streams of expenditures and payments extend over long periods, the results are sensitive to the discount rates that insurers might choose, or are driven to adopt by the economic forces at work in the insurance marketplace.

As an example, we computed alternative premiums calculated for different rates of discount ranging from 1 per cent to 7 per cent in real terms for a female who enters into a lifecycle contract at age 20. The same set of alternative exit ages were chosen as in the previous examples. The results are listed in Table 3, with the effects of variations in the rate of discount discerned from reading across the row for any particular exit age. The present values of expected health costs, again weighted by survival probabilities are also shown, in the top row of the Table. The results are displayed graphically in

[8] I am indebted to John Walsh for this point.

Table Three: Premiums for Various Discount Rates
Female: Entry Age of 20

Real Rates	1.00%	2.00%	3.00%	4.00%	5.00%	6.00%	7.00%
Present Values	66239	45117	32354	24360	19159	15639	13161
Exit Ages							
50	2567	2014	1651	1409	1246	1136	1061
55	2252	1805	1506	1305	1170	1079	1016
60	2017	1649	1400	1231	1117	1039	987
65	1835	1530	1320	1176	1078	1012	967
T*	1492	1309	1176	1081	1015	969	939

* 79.9 years

Figure 5, from which it is readily seen that the effects of higher discount rates are more pronounced for contracts with lower exit ages. For example, a fall in the rate of discount from 5 per cent (our rate chosen for the previous computations) to 1 per cent would result in an increase in the premium of 47 per cent (from $1015 to $1492) for an exit age equal to an expected life of 80 years of age, and an increase of 106 per cent (from $1246 to $2567) were this person to choose to pay premiums only up to 50 years of age.

Similar profiles result from applying the same methodology to individuals in other age-sex cohorts, with the general result that premiums are sensitive to discount rates, and are relatively more sensitive the shorter is the period over which payments are made.

In turn, real rates of discount are sensitive to marginal rates of taxation on income-earning assets, especially because the tax is generally applied to nominal interest earnings rather than to real earnings (capital gains tax excepted). For example, if the nominal rate were 15 per cent and the rate of inflation were anticipated to be 8.5 per cent, a tax rate of 20 per cent would yield a real net return at $3.2 per cent, and a tax rate of 50 per cent would yield a real return at -0.92 per cent, in which case saving $100 results in a loss of 92 cents. Thus negative, or at least very small, net real rates can apply for quite realistic combinations of interest rates, inflation rates, and tax rates. At an anticipated inflation rate of 8.5 per cent and a market interest rate of 12.5 per cent, anybody on marginal tax rates of more than 32 per cent earns a negative rate of return on their savings, and people who pay a marginal tax rate of 29 per cent earn the enormously attractive rate of 0.35 per cent; less if they also pay the Medicare levy. These three groups together account for all income earners with a taxable income of more than $12600 under current tax scales, and so it is not just 'the rich' whose return to savings are significantly affected under our iniquitous system of taxing nominal earnings.

Clearly, lower marginal tax rates that could feasibly be introduced upon freeing Australia's tax-producers from the burden of funding the many areas of welfare, health, and education (to begin with) as is the case at present, would enhance the feasibility of lifecycle health funding at reasonable cost to the individual, provided that the policies were taken out prior to the (late) age of around 35 to 40. As is so often the case, tax policy is not independent of policy implementation in other areas.

VIII. AGEING POPULATIONS: THE EFFECTS OF INCREASED LIFE EXPECTANCIES

The life expectancies for men and women have both increased remarkably over the last 15 years. Over this same period, the general trend appears to

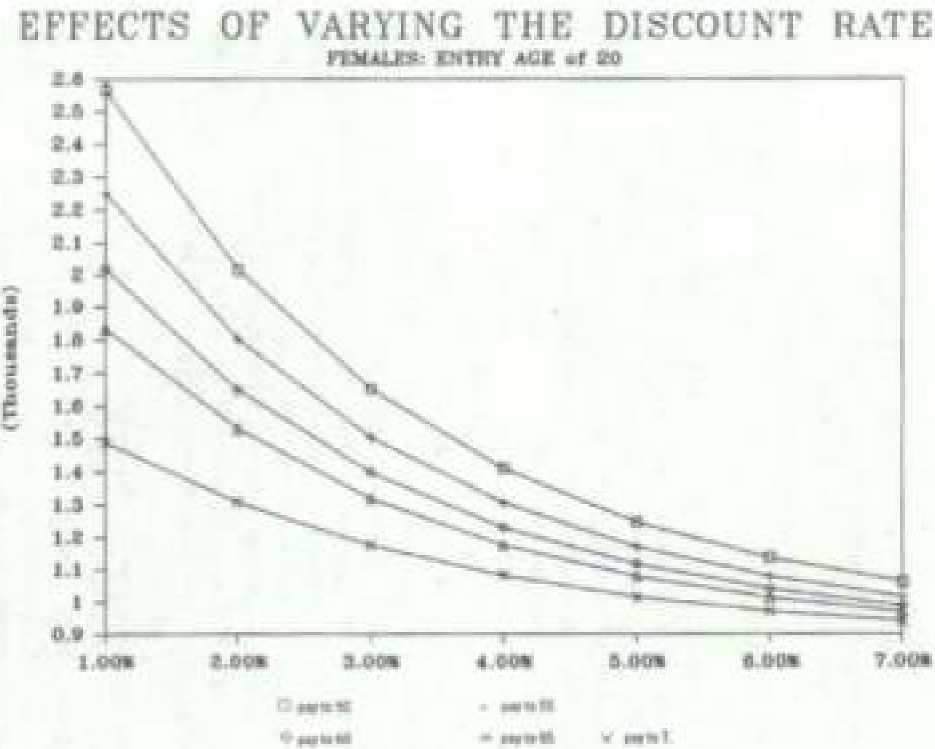
EFFECTS OF VARYING THE DISCOUNT RATE
FEMALES: ENTRY AGE of 20
(Thousands)
2.6
2.5
2.4
2.3
2.2
2.1
2
1.9
1.8
1.7
1.6
1.5
1.4
1.3
1.2
1.1
1
0.9
1.00%
2.00%
3.00%
4.00%
5.00%
6.00%
7.00%

Figure 5

have been towards earlier retirement, particularly amongst males. That is, there are increasing numbers of people in those age categories that, on average, generate significantly higher health costs particularly in regard to institutional care (see Figures 1 and 2). Demands for health resources have arisen from this cause whilst smaller proportions of the population are devoted to producing the wealth necessary to make available those extra resources. Taking these factors together leads to the immediate conclusion that demographic factors are creating increasing demands upon health resources which, under our present system, can only be met from placing even heavier burdens upon the shoulders of the income- and tax-producing classes. Unless there is significant improvement in the morbidity characteristics of the elderly, a continuation of the current trends will mean, other things equal, either increasing budget costs for health care or shortages that place their own particular non-monetary burdens upon the shoulders of the elderly and infirm (such as queuing for a hospital or nursing home bed), or a combination of the two.

This raises the question of the probable effects that the ageing phenomenon might have upon premiums for lifecycle policies. To address this question, rather than shift survival distributions, we took the simpler approach of recomputing lifecycle premiums by finding the present (unweighted) values of health costs from entry ages, taken up to a set of alternative life expectancies ranging from those presently observed up to 99 years of age. As before, these were converted to annuities (at 5 per cent in this example) to run from the entry age up to the usual set of exit ages, including for comparison the option of continuing to pay premiums after retirement, say up to one's life expectancy. As it turns out, the premiums for the current life expectancies under this methodology are not significantly different from the premiums calculated for the previous examples when survival probabilities were used.

As a sample, the results for males and females entering at age 20 are displayed in Figures 6 and 7. For example, an increase in the life expectancy of 5 years for both sexes would raise premiums by about 7.7 per cent for males and 7 per cent for females under policies for which each pay premiums up to age 65. These ageing effects are proportionately less for premiums paid up to one's expected life, but proportionately about the same for premiums paid only to the earlier retirement ages, as is evident from inspection of Figures 6 and 7.

These increases naturally reflect, in terms of annuity-equivalents, the effects that increased life expectancies have upon health costs, under the simplifying assumption that more people move into the age categories with the same larger utilisation of health services as we assumed for the previous examples. These costs might be reduced if morbidity amongst the aged were reduced, or innovations in health care for the aged were successful in reducing the costs of medical and institutional care. We note that here the latter is more likely to occur in a free and competitive market environment.

IX. GAINS FROM ENHANCED COMPETITION

Deregulating the health insurance market can be expected to have the beneficial effect of reducing the cost of lifecycle, and other, health insurance to the individual. If recent events in the US are any guide, insurers can be expected to innovate in the variety of policies on offer, and in methods for monitoring medical and hospital costs.[18] For example, the 'moral hazard' that is maximised under the current system of tax-funded health expenditure is avoidable by making the correct choice of built-in incentives, such as indemnity insurance, as an alternative to insurance that is based solely upon the cost of care. Secondly, a premium structure that would emerge in a free market would probably discourage people from insuring against regular, relatively small, outlays such as a standard consultation with a GP, just as one does not insure for regular motor vehicle servicing (Lees & Rice, 1965). Finally, many people would quite probably not choose to insure against a number of the 'elective' expenditures, such as facial-elevation or tummy-tucks (the costs of which are included in our estimates since these relate to the present system).

The large gains that are possible, however, would come from privatisation in the health sector itself. With insurers and patients monitoring costs directly, and doctors and hospitals competing for business, the actual lifecycle premiums that might ultimately emerge would in all probability be below those computed above, even after allowing for loadings for the costs of production in the insurance industry.

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[18] See D.G. Green, 1986. Some of the recent literature on possible insurance outcomes open markets is outlined in J. Logan & C. Trengove, 1987.

PREMIUMS FOR AGEING POPULATIONS

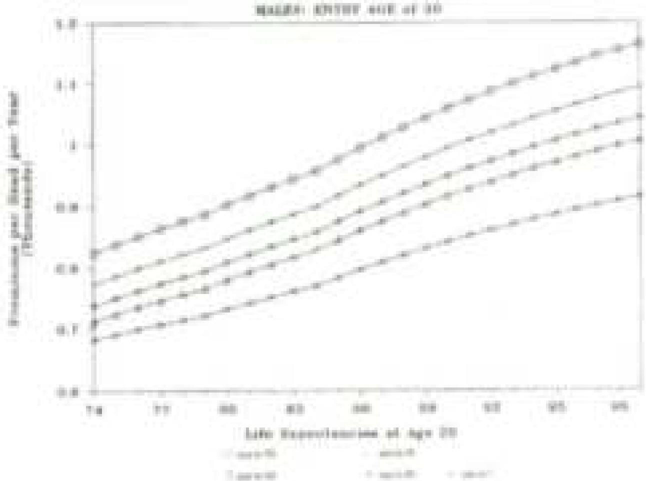

Figure 6

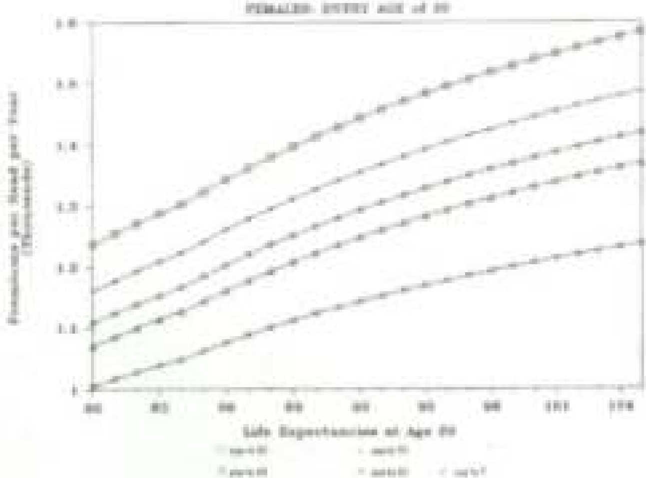

Figure 7

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Support for Single Parents

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Support for Single Parents

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I. INTRODUCTION

We are all familiar with examples of regulatory actions that have unintended consequence.1 One example which might be amusing (if our lives were not threatened by it) concerned US air traffic controllers in the early 1970s who were rewarded with generous pensions and early retirement if they could provide evidence that they were suffering the effects of stress. Systems errors in which planes came too close to each other due to controller 'mistakes' provided such evidence. As Staten and Umbeck (1983) point out, there was a considerable increase in the number of such violations when young controllers were offered the prospect of a generous disability scheme.

Sometimes these unintended consequences are of such monumental importance and produce such catastrophic results that it is very difficult for society to come to grips with the issue, and perhaps to recognise that society's response to a perceived problem may be part of the problem itself. If the consequences of major public policy programs are counterproductive and ultimately hurt those very people whom they are designed to benefit, it may nonetheless be difficult to convince policy makers that their own actions may be largely to blame. Academics, public servants and politicians who have framed such programs do not wish to be told that the way their programs have been set up and managed has inevitably led to initially serious problems being compounded many times over.

Charles Murray in his best-selling book, *Losing Ground: American Social Policy 1950-1980* (1984), has taken on the monumental task of explaining the failure of American social policy in these terms as essentially one of self-destruction. He begins by pointing out (p.8) how a four-fold increase in social welfare expenditure between 1968 and 1980 produced no change in the proportion of poor Americans. In subsequent chapters, he depicts in graphic terms the dimensions in which the position of ghetto blacks, the poor, the underprivileged, and single-parent families have deteriorated.

Thus, he is not describing minor failures of regulation, but wholesale failures of massive Great Society programs which go into the very fabric of the American people and especially American families. The well-intentioned solution to American social ills — larger welfare payments and more financial and social transfers — has not only added to the problem, but become the problem, according to Murray. The magnitude of the disaster suggests that good intentions on the part of policy makers should never be allowed as an excuse to justify the promulgation of programs that ultimately deny a future to the very groups that society has deemed to be most in need.

What is required instead is a much more hard-nosed approach to social programs in which anti-social behaviour is not rewarded in the way it is today as an unintended consequence of attempts to bring about greater equality of outcomes. The adverse consequences of many social policies is by now obvious, yet very little is done to correct the situation. Murray's proposed solution, which is to remove income-maintenance for the working-aged (Chapter 17), is sufficiently radical and drastic to frighten most of today's policy-makers. Yet the unthinkable at least deserves a hearing, and Murray provides the basis for a reconsideration of welfare policies.

If Murray's great vision of the self-destructive nature of social policies is the theme of his book, then his *dramatis personae* in the form of Harold and Phyllis, who make choices so as to maximise their short-term advantages, are a good expository device, but little more. The fact that a 'street smart' couple with no moral qualms or other restraints would make the choices that they do does not establish of itself that couples actually behaved in the way described in Chapter 12. What is required is a broader economic framework in which the regulatory framework facing Harold and Phyllis can be seen more clearly. There are a number of anomalies and inconsistencies with the simple story that a more sophisticated analysis can correct.

II. A BROADER ECONOMIC FRAMEWORK

A broader framework has been developed by Bernstam and Swan (1986*a*, 1986*b*) and Swan and Bernstam (1987, 1988). The innovative feature of the approach is to integrate the social welfare opportunities of couples such as Harold and Phyllis with their labour market opportunities or the lack of them. A sequential decision-making approach could be applied to see whether becoming a single parent could be a sensible career choice. Even at this early stage, references to career choices will offend all those who believe that ex-nuptial births and marriage break-ups leading to single parenthood are either accidental in some sense or are emotionally based and thus separated from rational choices. In our framework we do not have to believe that single parenthood is consciously planned; only that individuals act as if single parenthood is a rational career choice.

Let us put ourselves in the position of an immature teenage girl, lacking education and work-skills, who may have become pregnant by accident. We will admit some accidental or random events. A number of choices are possible. In the 1950s or even 1960s, there would almost certainly have been a shot-gun wedding to the father who, although poorly paid, at least had a job. Since that time, an increasing proportion of young men have become 'unmarriageable' in the sense that their prospective income is too low to support a traditional family. The unemployment rate for young males is exceedingly high in Australia, and for black ghetto youth in the US the prospects are far worse again. Even if a job can be obtained, the wages will not generally be much above the mandated minimum, and the probability of lay-off will remain high. In the Australian case at least, it is not so much the unemployment rate per se that matters. High unemployment but of short duration, as in an unexpected temporary slump of when school leavers are engaged in job search before choosing a career, is not really the problem. A virtual permanent inability to find a job, as with the increasing **duration** of unemployment that has occurred in Australia in recent times, may be a better indicator of the long-term unemployment prospects.

What have been the principal factors contributing to the decline in employment, and particularly youth employment, in both the US and Australia? Bernstam and Swan (1986*b*) find that in the US the employment of black teenagers particularly is highly sensitive to both the coverage and the level of minimum wages. Although Murray makes no reference to mandated minimum wages, this makes his point about the perverse effects of social welfare policy nicely. The ostensible reason for rising minimum wages and increased coverage has been to prevent 'exploitation' of under-privileged workers, particularly unskilled black ghetto workers. The presumably unintended result has been to deny these groups access to job markets and thus destroy their marriageability.[1]

In Australia, the story is depressingly similar, despite the fact that we have numerous minimum wages rather than a single rate. A recent study of the Australian youth labour market by Miller and Volker (1987:215) con-

[1] Kaus (1986:22) describes a 'community': 'where 90 percent of the children are born into fatherless families, where over 60 percent of the population is on welfare, where the work ethic has evaporated and the entrepreneurial drive is channelled into gangs and drug-pushing. In the District of Columbia ghetto, 'getting paid' is slang for mugging somebody'.

cludes that 'the picture of the labour market which emerges from this analysis is one in which the institutionally determined wage structure has been set too high'. Evidence on the reservation wage of unemployed youth obtained by the Bureau of Labour Market Research indicates that they would be prepared to accept a 25 per cent lower rate of pay for the skill class in order to obtain employment.

The setting of excessive award rates for youth workers protects the incomes of older and more experienced workers, at the same time reducing the amount of on-the-job training that employers are willing to provide.

We, as the teenage girl, have been thwarted in our desire to marry and have children, especially in US black ghettos. The next most desirable option of the number of poor alternatives facing us is to terminate the pregnancy and enter the job market. The prospects are bleak here for the same reason that a conventional marriage is difficult. The next step in Australia would be to become unemployed and thus receive benefits. In the US there would be no eligibility for benefits, even temporary benefits, without a work history. Short of living off street activities such as prostitution, the black US teenager may have little option but to allow the pregnancy to go its full course and qualify for Aid to Families with Dependent Children (AFDC). Marriage is now out of the question, as benefits would be threatened by Harold's occasional bouts of work. Nonetheless, Harold, the boyfriend, and Phyllis, if that is the teenager's name, continue to live together. The lifestyle is far more comfortable than if the pregnancy had been terminated. The whole cycle is set to repeat itself as only a minimal investment is made in the child's education or wellbeing. Grandmothers at the age of 24 are by no means unknown.

In Australia, the girl's decision whether or not to terminate the pregnancy is more difficult. Unemployment benefits are readily available, although there may be hassles from time to time over the so-called 'work-test' (*Sydney Morning Herald*, 26 October 1987). For the very young teenage girl, the May Statement of 1987 (Keating, 1987) will have reduced benefit levels to a minimum level ($A25 a week) in an effort to encourage her to stay at school. Perversely, she may be tempted to have the child and gain the full benefits which go with the Supporting Parent Benefit (SPB). If she is over 18 years of age, she will still expect to be able to improve her overall disposable income before rent from $106 to $159 per week or a higher proportionate amount if the child enables access to subsidized housing (see Swan and Bernstam, 1988).

When the SPB (at the time Supporting Mothers Benefit) was first introduced in 1973-74 under the Whitlam Government, there were some 'minor' drawbacks to entering the scheme. You might be literally raided by field officers of the Department of Social Security, and the slightest evidence of the presence of a man could produce disqualification. In these more enlightened times, for those other than taxpayers, disqualification is very difficult since the determining officer of the Department of Social Security has to assess your 'attitude' to the relationship and whether or not the breakdown is permanent (Sawyer, 1986:65). Naturally, the beneficiary is given the benefit of the doubt. Cohabiting is no bar to benefits so long as it represents 'attempting a reconciliation'. There is no limit to the number of children you can conceive, or adopt for that matter, while on SPB. Each child represents added benefits. Nor is there any bar to entering the workforce, other than the 50 cent reduction in benefits for each dollar of earnings that you report.

We return now to the predicament of the US teenager who has little option but to go full term with her pregnancy. In the 1950s and 1960s, the social stigma attached to welfare recipients may have had a discouraging effect. Access to benefits was also far more tightly controlled than it is today. Peer-group pressure now goes the other way. Since most of the community is on welfare and it is highly respectable, there is no problem in joining the millions of other teenagers having babies on welfare. It is presumably also in the interests of welfare workers to look after their clients and promote a demand for their own services. Welfare workers and the system are vigorous in promoting the idea that benefits are a right, with no stigma attached.

The state she is living in may, however, be a problem. Some of the poorer Southern states may provide only one-quarter of the AFDC benefits of New York or the richer Northern states. Since ex-nuptial births are a higher proportion of the teenage population, and a higher proportion of all births, in these low-benefit states, her decision to have the child may seem questionable. Bernstam and Swan (1986*b*), however, point out that while benefit levels are poor, labour market opportunities are even worse, given the inadequacy of her skills and those of her potential marriage partners relative to the minimum wage. High benefit levels indicate high rates of ex-nuptial births once the confounding effects of skill levels and the job market are taken into account. Her relatives in New York have already contacted her, offering to get her and her boyfriend established there on far higher benefit levels once the baby has arrived. In fact, she notices that in her home town with low AFDC benefits, all the welfare mothers at the local mothers' club are the friends she grew up with. In New York the story is quite different. Most of the welfare mothers have come from low ADFC-benefit states as indeed she has. While our story has been told here in terms of the representative couple, Harold and Phyllis, we have found strong statistical support for our hypothesis.

We return across the Pacific to Australia where an older version of Phyllis married and had two children in the 1960s and early 1970s before the two wages explosions of 1974 and 1982 destroyed labour market prospects and put more than half a million on unemployment benefits. Her marriage to Harold is now on the rocks because of financial difficulties, despite the fact that he is earning reasonable money, given his limited skills, although less than average earnings. Heavy taxes, and especially high marginal tax rates, have taken their toll. Only those in work and not on welfare can fund the rise in welfare expenditure in constant 1987-88 dollars from $A6.9 billion in 1970-71 to $22.7 billion in 1988-89.

She may be advised by her local welfare office that the best way she can assist her struggling family is to announce a permanent breakdown in the relationship with her husband, although she can continue to see him. As Swan and Bernstam (1988) show, if her husband continues to be employed, the combined family disposable income can effectively rise by about $102 per week from $350, once she is in receipt of benefits. The gain could be greater if access is obtained to subsidized accommodation. Her husband will officially give her little, if any, maintenance payments so as not to jeopardise her benefits. Privately, she may share in some of the overall gain to the family unit (Cabinet Sub-Committee on Maintenance, 1986:13).

If her husband becomes unemployed, each may officially look after one child so that both parents can obtain SPB. Once again the overall benefits to the family unit are quite sizeable.

If Phyllis worked before the 'marriage breakdown', she is far less inclined to now that she is a single mother. Before SPB or SMB was introduced there was no difference between the workforce participation rates of married and single mothers. However, by 1986 had single mothers the same participation rate as married mothers, there would be the equivalent of an additional 27 000 women in the workforce (computed from Social Security Review 1986:65). Now her household responsibilities have increased, she is effectively paid if she does not work and she is 'taxed' twice if she does work and does report her earnings. Not only does she pay regular tax, but her pension is reduced as her market earnings increase. As yet another perverse consequence of the SPB scheme, her work-related skills will gradually disappear leaving her more vulnerable once she is no longer eligible for the benefit, or there is a change in policy and the benefit level is reduced or abolished.

III. THE CONSEQUENCES OF SUPPORT FOR SINGLE PARENTS

The consequences of social welfare policies in the US, including the minimum wage along with the AFDC program, have been quite startling. An incredible 56 per cent of black females will become single mothers by the age of twenty-five. In 1979-80 nearly 37 per cent of black children lived on

AFDC (Bernstam and Swan, 1986*b*). Marriage breakdown as a result of AFDC has not been as severe a problem as the explosion in ex-nuptial births.

In Australia the success rate, if one can call it a success rate, has been even greater. The number of SPB beneficiaries has grown from 33 000 in 1974, following the introduction of the benefit, to 176 000 at 30th June 1986 and 182 007 at 30th June 1987. Expenditure on the SPB Program for 1987-88 is $1.525 billion with an additional $1.001 billion on Widow's Pensions. While the number of female recipients due to ex-nuptial births has increased 160 per cent over the period 30th June 1975 to 30th June 1986, there has been a 450 per cent increase due to separation and marriage breakdown. If we include all single parent families including those on Widows Pension benefits or not in receipt of benefits at all, the number of such families rose by 73 per cent from 183 000 in 1974 to 316 000 in 1985. In the mid 1970s, sole parents made up 9 per cent of all families. In 1985 they made up 14 per cent (Cabinet Sub-Committee on Maintenance, 1986:7).

While the severe downturn in the employment market as indicated by the duration of unemployment and the abolition of the six-month wait for benefits in 1980 have been major factors influencing the increased number of beneficiaries, it may also be possible to account for the greater preponderance of separations as the cause of single parenthood in the Australian case. In the US the combination of a single minimum wage, which largely affected teenagers and blacks, and the unavailability of unemployment benefits for young people put the maximum pressure on teenagers, particularly black teenagers, to create or retain babies. On the other hand, Australia's far more rigid labour market with award wages for thousands of occupations created severe pressures over a wider range of age groups. The ready availability of unemployment benefits for teenagers relieved some of this pressure, so that particularly established families were more squeezed by economic pressure than the US.

For established families, the children are already there so that it is relatively easier to become a beneficiary. It is easier (and quicker) to announce a marriage breakdown than to give birth. Since the onerous controls on cohabitation regulating this process quickly broke down, along with the stigma, the rapid increase in separations is not that surprising. In effect, two-parent families are being heavily subsidised to become single-parent families.

IV. CAN ANYTHING BE DONE WITHOUT EXACERBATING THE PROBLEM?

One major consequence of the rapid rise in the number of welfare beneficiaries has been a reduction in the work ethic. It has been subject to twin simultaneous pressures. First, the easy availability of welfare benefits to virtually anyone who is prepared to claim them, and, second, the rapidly rising level of taxation necessary to fund these welfare benefits paid for by those millions of workers who would currently be better-off if they, too, became welfare recipients rather than low-paid workers in boring jobs. These twin pressures could easily create further major falls in labour force participation, once again lowering our living standards. Given Australia's already precarious position with the dramatic falls in the stockmarket, massive overseas debt and balance of payments deficits, further considerable rises in welfare beneficiaries to be funded by the taxpayer and declines in the numbers of employed workers would hardly be welcome. The task of undertaking decisive action has become far more urgent.

It cannot be said that the Hawke Labor Government has taken no action at all. In the May 1987 Statement, the Treasurer (Keating, 1987:36) announced that single parent beneficiaries would no longer be able to go on receiving benefits for children over the age of 15 and under the age of 24 who are still attending school. Naturally, this announcement was greeted with a great outcry from the affected single parents with many threatening to withdraw their children from school should the measure be implemented. Phasing-in measures were announced in the 1987-88 Budget (Commonwealth of Australia, 1987:157-161). Those advocating the preservation of the existing system seemed to show little concern for the children of equally poor but intact families whose children may also be required to leave school prior to year twelve because of financial pressure.

The government also announced the phasing out of so-called Class B Widow Pensions which are provided to women 45 years of age or older. At 30 June 1988 there were 86 692 beneficiaries. The change has been made very cleverly so that no woman who is in receipt of benefits will ever lose them, and future eligibility is maintained for some. These benefits are paid to women without dependent children to support when a male provider has been lost. This loss could also arise from death, divorce or desertion. In 1986 there were 81 341 beneficiaries, of which 57 per cent are widows, 24 per cent are divorcees, 17 per cent are deserted and 1 per cent are de facto. Given the name of the benefit, a fairly broad definition of widowhood has been adopted. Clearly, the justification for these benefits stemmed from a time in which it was considered that married women should be protected from ever having to enter or re-enter the workforce. Given high labour force participation rates for married women, such an attitude seems archaic, not to say sexist, today. Both men and women who have never married are discriminated against.

These measures are significant, not because there are enormous savings in social security payments, but because for the first time an effort is being made to rein in a system which has generally grown virtually out of control.

Nonetheless, they are by no means adequate considering the nature of the disaster which has befallen the whole social security area.

For some time now, the government has been attempting to increase the level of financial support from non-custodial parents to custodial parents and their children, that is, generally from the former husband to the now separated or divorced wife and children. These maintenance payments are generally either low or non-existent, leading to poverty for the custodial parent, greater disparity between the parent's income and additional welfare payments (Cabinet Sub-Committee on Maintenance, 1986). At 30 June 1987, there were more than one quarter of a million sole parent families containing 440 000 children who relied almost exclusively on social security payments for support.

The key to proposed reforms in this area are:

- a legislative formula for the determination of maintenance to replace Family Court determinations. Such determinations often represent the Court's collusion in maximising the availability of welfare payments; and
- the use of tax mechanisms to automatically withhold the income of non-custodial parents to ensure that maintenance payments are actually made.

The government has run into strong opposition to these reforms. Employer lobby groups oppose the plan to garnishee wages since these collection costs will largely fall on employers. The social welfare lobby, the Australian Council of Social Service (ACOSS), essentially wants higher guaranteed income levels for custodial parents via higher than proposed welfare payments, where the non-custodial parent cannot be traced or is unemployed (*Sydney Morning Herald*, 6 November 1987).

Although there are many arbitrary elements to it, we must support the efforts which are being made to increase maintenance payments and to discourage default, on the principle that parents are responsible for their offspring. As of 1 June 1988 custodial parents in receipt of pensions are supposed to receive support from the non-custodial parent via the Child Support Agency established in the Taxation office. Even if the scheme obtains some limited success, it will not have a major effect on the problem of abuse and excessive benefits resulting in marriage break-up and ex-nuptial children.

In the Hawke Government's work leading up to the proposals for the reform of child maintenance, attention is drawn to some of the reasons for the increased reliance of sole parents on social security (Cabinet Sub-Committee on Maintenance, 1986:8):

> The increased rate of marital breakdown is one obvious contributing factor. Another has been changes in social security policy, including abolition of the six month waiting period [in 1980], extending benefits to supporting mothers in 1973 and to fathers in 1978.

It is surprising to us that the government seems to see little, if any, connection between marital breakdown and the very policies that the government has brought in to subsidise single parenthood.

Our statistical results (Swan and Bernstam, 1988) confirm that the abolition of the six-month wait for benefits has been a major contributing factor to increased welfare dependency along with the increased duration of unemployment. Naturally, the availability of substantial benefits with the qualifying factor being little more than statements about relationship breakdown has encouraged welfare dependency. No doubt there are strains, particularly financial strains, in all relationships, and some of these relationships would have ended (and other relationships re-emerged) without strong financial inducements from the taxpayer/donors funding social security. It would seem almost inconceivable that relationship breakdown could have occurred on the same scale without the very governmental policies which were supposed to deal with the problem, not exacerbate it.

If governmental policies must take at least some of the blame, then reform of those policies may help to correct some of the worse excesses and perverse outcomes of the present system. For example, the six-month qualifying period could be re-introduced. The real level of benefits could be reduced in recognition that it is the innocent victims of relationship break-ups — the children — who need to be assisted, whereas custodial parents can nowadays be expected to be able to enter the workforce, at least on a part-time basis.

The government recognises (Cabinet Sub-Committee, 1986:8) that the most severe sacrifices are borne by female sole parents with young children, since this group has the most limited labour market opportunities, especially for full-time participation. Temporary benefits could be reserved for supporting mothers of young children only, or benefits could be limited to six months or a year for parents of older children to ease the shock of adjustment to a new and difficult situation. The private sector could be encouraged to provide child-care facilities for working parents. At present, more and more regulations are coming into force which raise the cost of both private and publicly provided child care.

Another possible avenue for reform which is receiving extensive discussion in the US but not in Australia is 'workfare', that is the provision of jobs for single parents rather than welfare of some kind of community work in return for welfare. Kaus (1986) points out that the existing so-called workfare programs in the US are little more than voluntary job-training programs which currently fail to address the real issues. There may be little option other than to begin to address the ways in which current policies promote the very conditions of poverty that the programs are supposed to prevent.

Finally, our work on single-parenting emphasises that reforms are needed in job markets at the same time that changes are made to social security programs. The number one priority is a more flexible labour market without award and minimum wage provisions. These are simply devices used to deny poorly-skilled workers access to jobs. A low-paid job that encourages learning and productivity improvements is better than a notional high-paid job that is out of reach of those most in need who lack job skills. Greater use of bonus and profit-sharing schemes, as exemplified by the Japanese system, may also promote the additional flexibility that is crucial to assisting families and single parents in need.

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Panel Discussions
Wellington and Sydney

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Panel Discussion: Wellington

Ian Calder: After this morning's session I felt overwhelmingly grateful I live in New Zealand, not in the United States or Britain. It's very important to take account of the culture of the society in which we live. American and British culture are different from, and almost alien to, that of New Zealand. This is most obviously so in the contrast between individual and collective responsibility. New Zealanders believe that collective responsibility is important, whereas Americans are wedded to individual responsibility. This means that welfare policies in America are quite different from those of New Zealand.

Take for instance the concept of property. If we were on a marae, we would not be talking about my property: we would surely be talking about our property, our resources, our responsibilities to others in our communities.

In my view, we in New Zealand are getting things right and beginning to lead the way in the delivery of welfare services. Despite our mistakes, we are consulting the people as a whole, indeed to the point of consultation fatigue.

I was intrigued by the concept of coercion that was mentioned this morning. The concept was applied in the case of taxation. But it wasn't applied in the case of the single woman with small children, who is expected to go to work. If this conference had all women speakers, certain topics — such as individual responsibility — wouldn't have been brought up. In New Zealand we do have a sense of collective responsibility, and we have the right to choose how we want to exercise that responsibility.

The state versus market issue is a false one. It establishes terms of debate on which it's impossible to win. In New Zealand we have a mixture of state and voluntary provision. All methods of delivery have problems: it isn't the case that state provision is all bad, and private provision all good. We should be looking (as some of the later speakers were beginning to recognise) at how we can improve welfare delivery methods, private and state.

As for the issue of selective benefits. I would suggest that where selectivity fails, the fault does not lie in the fact that such benefits are state-provided, but is intrinsic to the selective approach, which can generate poverty traps. I would like to propose that services should be provided for all, so that those who are disadvantaged automatically get access to them. My own area of work — the provision of child care and family day care services — is a good example. Many people who are held back by the poverty trap but who want to improve their situation can be greatly assisted by such services, which should therefore be universally available. In recent years a great deal of child care has been made available to the Maori as a result of the Te Kohanga Reo movement. Kindergartens and play centres have perhaps provided services for the privileged in New Zealand, since they come free or at only a nominal charge. As for child care, you pay the full cost. These are the sorts of issues we need to examine.

Allan Levett: An issue of great concern in New Zealand is dependence and independence. Particularly when we were a British farm, we didn't have the economic resources to enable us to be truly independent. Most of us have been concerned that it's at the high ability end of the scale that we are especially in need of independence and entrepreneurship. We spend as much on the standard tertiary education bursary as on the Domestic Purposes Benefit. We actually pay smart kids to qualify for the best paid jobs in the community, whereas kids who leave school at age 15 have to go out and learn to live on their own. That's an example of dependency that we still encourage in New Zealand; and it's more of a moral than a distributive issue.

I'm less concerned about dependency at the poorer end of the income distribution scale. In New Zealand we've been lucky enough in the past to have full employment; and when there is full employment, people will work. However, we now have an economy that doesn't provide enough jobs; and our problem now is not so much dependency as how to live with less than full employment. Hence the great importance of the education we give to the people who create jobs.

I think Alan Woodfield's paper exaggerated the extent of dependency at the lower end of the scale. In my experience, divorced or separated people don't stay for long on welfare benefits — no more than about three years. Problems arise not so much from dependency as from general incompetence and psychological disturbance. Insofar as dependency is a problem, it is much more serious at the higher end of the scale than at the lower.

J.B. Munro: Speaking from the standpoint of a provider of services, it seems to me that the job of the state is not necessarily to provide welfare services itself, but to ensure that welfare services get provided. I personally favour contracts between the government and service providers. These should be for fixed periods and should be very clear about such matters as accountability, evaluation and monitoring. For too long we've tended to assume that welfare problems could be solved just by throwing money at them. But it's equally important to assess the needs of individual recipients in the effort to shift them from dependence to independence. Many of the submissions made to the Royal Commission's task forces clearly indicate that the recipients would like a greater say in what should be available to them.

In the IHC, we've found that the more independent people become, the less costly they are. But we still take a national board figure for everybody irrespective of their degree of dependency. As a result some of the more able are subsidising the less able. So the more we can target monies from the taxpayers towards the specific needs of the individual, we will get a better and more appropriate distribution of funds.

I'd like to touch on the view taken in some of the papers that welfare reform should be conceived as a cost-cutting measure. Perhaps we should ask the community to donate voluntarily so that less is taken from the taxpayer. But we shouldn't for a single minute entertain the idea that welfare should be reformed with a view to cutting costs. In IHC I have to find in 1987 $NZ8 million by public fund-raising. It's almost impossible but it has to be done. I believe that public funds should finance direct, day-to-day services. The additional money raised from voluntary donations should be used for research, for pioneering, and other things that don't fall within everyday maintenance. We can't expect citizens to make voluntary donations towards the cost of essential services. It's hard enough as it is to capture the volunteer and to keep up with inflation.

It's important that services should be available to people locally. But this means more than just geographical devolution of service provision. Just now the Maori community is pressing for funds to be given directly to the Ewi, the tribes. I'm not sure whether that would mean that the individual member of the tribe receives money (by way of a benefit or a tax rebate) and then decides to pay the Ewi, or whether the money goes to the Ewi and they decide who gets the money. This is one of the welfare debates taking place at the moment.

Charles Murray: I'd like to make a few comments about the idea of dignity that has been mentioned in general discussion today. Dignity is not only important; it's essential to the pursuit of happiness. But in the welfare debate we tend to lock ourselves into stereotypes, such that, if I am a critic of the welfare state I must think in terms of a social Darwinist competition between individuals, whereas if I am for the welfare state I am caring and compassionate.

Michael Walzer draws a distinction between self-esteem and self-respect. (You can say that someone has too much esteem for himself, but hardly that he has too much **respect** for himself.) Walzer says that self-esteem is something that comes from outside; people can tell us that we're good at something, and that translates into esteem. But self-respect is internal: it comes from measuring up to being a citizen. Using self-respect as a stand-in for dignity. I can easily understand how a person unemployed through not fault of his own can continue to feel self-respect, even if he receives an unemployment benefit. He does so by being internally committed to getting a new job as soon as possible and becoming self-sufficient again.

I find it difficult to see how one can 'give' dignity to someone who, though able-bodied, voluntarily remains on the dole. What difference can it make to such a person if a social stigma is attached to the dole? Self-respect is acquired only in a community in which one gives as well as takes. A solo mother who can't be expected to work can feel self-respect by raising her children as well as possible; but that means imparting values to them by behaving in certain ways, and that in turn means giving something back to the community.

I would like to see a society in which the meeting of human needs, an important part of the stuff of life, is left in the community. That gives a solo mother something valuable to do. To the extent that meeting human needs is removed to a distant capital and involves a divorce between taxpayers and recipients, individuals are deprived of opportunities to acquire self-respect.

Ian Calder: But New Zealand is a very small community, and if we decide to attend to welfare needs in a collective manner, that's our choice. Nor does that choice result in a serious dependency problem. For every case of voluntary dependency on welfare, there are several cases of single mothers working hard to avoid being dependent on the state.

Charles Murray: New Zealand as a small homogeneous community is perhaps free from many of the problems we have in the United States, where many people are living miserable lives for reasons that have little to do with the level of state welfare spending.

I'd like to take up another idea that came up in discussion, that of coercion. There's a tendency to assume that the only people who complain that the welfare state is coercive are the well-to-do who just want to pay less tax. But poor people are subjected to serious coercion. In the US the public school system in the large cities is execrable. People with money either move to affluent suburbs whose public schools they can control, or they stay in the city and send their children to private schools. The difference between the private and the public schools is not determined by the amount of resources they have at their disposal. State schools often have better facilities, and pay their teachers more, than private ones. Yet the private schools generally are better at teaching.

Poorer people, meanwhile, are trapped in rotten state school systems which they are coerced into maintaining through taxation. Why not give them the discretionary use of their money to buy the kind of education they want their children to receive? Some people are deeply unhappy about the way their taxes are used, but have no choice but to continue paying those taxes. Why not let them spend their money in the ways they see fit? That wouldn't stop those who want to do things collectively, through the tax system, from continuing to do so.

David Willetts: The British experience is relevant to this problem. The Thatcher government has a reform agenda in public education and housing that takes us in the direction Charles Murray advocates. We've had cases of poor, often black, communities in inner London trying to set up private schools to give their children the opportunities they weren't getting from the state system. The policy is to enable schools to opt out of local government control and become independent while still receiving state funds. There are similar plans to enable tenants in state-owned housing estates to opt out of local government landlordism and take over estate management themselves.

Another issue I'd like to comment on is the division that some speakers have introduced between state collectivism and rampant individualism. But this distinction overlooks mediating structures. In the 19th century the emerging welfare state supplanted, not individualism, but the various mediating structures whereby people were already voluntarily coming together to provide for themselves. By the end of the 19th century 8 million British working men were members of friendly societies. The state then colluded with the large insurance companies and medical doctors who didn't like being employed directly by working class men, and displaced these private and voluntary efforts. The idea that the state is the poor man's friend because he has no other resource in times of difficulty is historically inaccurate.

Finally, on the issue of dignity, a financial contract can dignify both parties to it. In my experience, people who consult a state-financed medical doctor behave humbly and apologetically, whereas those who pay for their own medical care don't, regardless of their social status. Similarly, people queuing to collect supplementary welfare benefits feel no dignity, unlike recipients of contributory benefits (like the old-age pension), who are conscious of collecting money they have already paid in during their working lives. The contributory principle is thus a source of financial reciprocity that preserves the dignity of those who benefit from it.

Ian Calder: Making welfare benefits universally available helps to sustain the dignity of recipients, since such benefits are in effect contributory.
I would like to stress once again that the debate over state versus private provision misses the point, since both the public and the private sectors do some things well and other things badly. We should therefore concentrate on trying to agree on the kinds of welfare policy we want to pursue.

Alec Pemberton teaches sociology and social policy studies at the University of Sydney. His interests include studies of fraud of the welfare system, research on the place of professions in modern society, and he is presently writing a book on the role of Good Samaritanism in the welfare state today.

Peter Saunders is an economist who has taught in universities in the UK and Australia. He has worked with the OECD in Paris on public expenditure analysis and as a consultant to the office of EPAC. His interests include public expenditure, social security, taxation, inequality and redistribution. He is currently Director of the Social Welfare Research Centre at the University of New South Wales.

Bettina Cass is Associate Professor of Social Policy at the University of Sydney. She has been Consultant Director of the Social Security Review, 1986-88.

Panel Discussion: Sydney

Alec Pemberton: I think Michael James set the appropriate context when he spoke about the contrast between market failure and government success, and how that contrast has been taken for granted in so much of the welfare state debate over the last 15 years or so. What we've heard today has challenged that notion: it has put the possibility of government failure on the agenda. The issue is how deep that failure goes.

I want to take up some remarks by David Band and Charles Murray. David Band argued that the welfare state rested on immoral foundations. He used terms such as 'imposition' and 'expropriation', and he also said that the effect of the welfare state had been to erode the bonds of fraternity and community. Charles Murray said there had been a revolution in social policy that has **caused** some social trends that have had unhappy results.

I suggest that perhaps we've had a rather narrow and restricted diet of examples; we've concentrated mostly on unemployment benefit and single parents' benefit. A different diet may have resulted in some different conclusions. There is a great deal of community support for welfare programs such as the widows' pension; it would be quite misleading to use the term 'expropriation' in this case, since I believe that taxpayers are willing to finance such programs. My own reading of the welfare state is not that it only creates dependency — which, it must be recognised, it does — but that it often also **empowers** people; and there is evidence that it has actually benefited them. I haven't heard very much recognition of that latter fact today. The welfare state has often helped to inculcate attitudes favouring private property, authority, stability, and the family. A more balanced picture of the welfare state should include the ways in which it has increased people's life chances.

If it is the case that the welfare state has eroded our sense of community, then I'd like to hear it said also that some people have deliberately tried to discredit the welfare state by stigmatising welfare recipients: to create social divisiveness and then to use this as evidence against the welfare state. I think this is a pity

The sheer size and scope of the welfare state suggests to me that there will always have to be a role, and a central role, for governments in the delivery of welfare services. State-guaranteed welfare allows families to undertake the rational, long-term planning of their lives that wouldn't be possible if they had to rely on capricious, non-government sources of welfare such as charity.

Charles Murray is probably right to a large extent to claim that state welfare creates chronic dependency as manifested in an 'underclass' of beneficiaries. Yet when my Marxist colleagues tell me that the welfare state is there to mop up the problems caused by capitalism, I have to remind them that poverty existed long before capitalism. Equally, dependency and the underclass existed long before the welfare state, and that fact needs to be addressed in our debates. That is, to what extent is dependency caused by the welfare system itself, over and above that dependency which one might anyway expect to find in the lower stratum of any sociopolitical system?

Whereas Charles Murray and Peter Swan explain dependency by reference to the incentive structure of the welfare state, my own experience of the underclass, at least in Australia and the UK, suggests that it consists of people who know **least** about the welfare system: their problem is precisely that they **underuse** the system. The American underclass may be different, of course, and we would be wise to listen to Professor Murray on this score; some comparative sociology would help here.

Finally, it's worth noting that markets and governments behave differently in the presence of one another than they might behave on their own. I'm a fan of both markets and governments. There's value in having public **and** private schools and public and private health care. We should recognise that it's not only governments that produce distortions and harmful unintended consequences. In the long pull I think we do best to have a balance, a mixture, of both public and private activity.

Peter Saunders: I want to make a number of general points arising from the discussion today. My first point relates to the concept of the welfare state, which no one has really attempted to define. In my conception of it, the welfare state consists first of all of a variety of **programs** — income support, education, and so on; secondly, of a variety of **forms** of intervention — tax concessions, regulations, and the like; and thirdly, a variety of **objectives**. These objectives are concerned with aspects of equality: equality of outcome, of opportunity, of access, and of treatment. The discussion at this conference has been very much narrower than that, concentrating mostly on unemployment and single parents' benefits for young people.

The second point I want to make concerns the idea of the 'middle class capture' of the welfare state. 'Capture' means taking possession of something which is not yours by right. But if the welfare state is meant to promote equality of treatment, then the idea of 'capture' doesn't apply, since the benefits are supposed to go to everyone as of right.

Third, the issue of whether state welfare crowds out voluntary giving. Let's assume that the welfare state does crowd out an equivalent amount of voluntary charity. Then, if we abolished the welfare state, the vacuum would be filled by voluntary action. But that means that all the problems that people currently associate with the welfare state — the various perverse incentive effects and so on — would still be there to exactly the same degree. Furthermore, on this crowding-out assumption, it can't be maintained that taxation is coercive, since taxation simply replaces what we would choose to give anyway.

My fourth point relates to evidence, and counterfactuals in particular. If we are trying to assess the consequences of the welfare state, we must be comparing observable outcomes with the outcomes that would exist if the world were different, i.e. with counterfactuals. Suppose I were to argue that the fact that employment is higher now than 30 years ago proved that the welfare state has had no effect on the incentive to work. Everyone would reject such an argument, quite rightly. And yet it seems to me that some of Charles Murray's comparisons are not too dissimilar to that. Evidence about the incidence of poverty doesn't provide a useful basis for estimating the effectiveness of the welfare state. The relevant counterfactual is the incidence of poverty that would have emerged in the absence of increases in welfare spending as compared to the actual incidence that we can observe.

Finally, the impact on the performance of the economy. We haven't really succeeded in unravelling the contribution that economic performance has made as compared to the contribution that increased welfare spending itself has made in influencing final GDP indicators.

Bettina Cass: First of all, I want to draw attention to the results of research undertaken by the Economic Planning Advisory Council and the Australian Bureau of Statistics. This shows that the Australian tax-transfer system provides for a life-cycle redistribution and also does redistribute income to the lowest-income households.

Second, I want to explode one of the myths propagated about the relationship between economic growth and social expenditure. Evidence from the OECD shows that there is little or no inverse relationship between high levels of social expenditure (as a percentage of total government spending and of GDP) and economic growth. Some of the countries with high levels of social spending have had good records of economic growth in recent years.

Third, we need to be aware of what's been happening in Australia. The recessions of 1974-75, 1978-9, and 1982-83 saw rises in the unemployment rate, in the duration of unemployment, in the numbers of sole parent families, and in the proportion of the population of workforce age and capacity becoming dependent on social security. This happened also in the other countries we've been looking at today, the UK and the US. Since 1983 there have been signs of recovery in Australia: higher rates of employment growth, decreasing rates of unemployment, a stabilising of the numbers of sole parents receiving the sole parents' benefit. The major problem is that long-term unemployment has been concentrated, not among the groups identified today as giving rise to moral outrage, but among prime-age and older people suffering from a serious mismatch of skills in demand by the employers and the skills which they have acquired. I would like to see a conference devoted to those problems.

Fourth, some facts need to be stated about sole-parent families in Australia. Only 4 per cent of sole parents receiving social security are teenagers who are parents as a result of ex-nuptial births. The vast majority — 85 per cent — result from the end of a relationship (predominantly a marriage relationship). The duration of receipt of the sole parents' pension is very short. The median duration is between two and three years. The younger the parent, the shorter the duration. Older women find it most difficult to get off welfare, which indicates their lack of opportunities to participate in the labour market and to form new relationships. As for the claim that the sole parents' benefit reduces the incentive to work, the fact is that the part-time labour force participation rate among sole parents is currently the same as the part-time rate for married mothers; and their participation rates overall are increasing. The pension thus typically looks after women and their children for a relatively short period during which they are coping with economic and emotional crises in their lives and preparing re-entry into the workforce, or entry into a new family relationship.

Fifth, some facts about unemployment. Since 1983, unemployment rates have fallen, and fallen mostly among the young. The problem, as I mentioned before, is with prime-age and older worker workers, many of whom are looking after families. Jim Cox has identified the nub of the problem: the tragic choice between the adequacy of benefits, and the possible disincentive effects of such benefits. The replacement rate of unemployment benefit for single people in Australia is actually very low: they are far worse-off on unemployment benefits than even in relatively low-paid work. As for married people with children, the new Family Allowance Supplement means that a breadwinner with two children, even in the lowest-paid work, will be 30 per cent better-off than on the unemployment benefit. So we do need to look at the facts when we start talking about the disincentive effects of social security benefits.

David Willetts: One problem with the welfare state is that it has become involved in areas where it's not clear that it any longer has a major role to play.

Bettina Cass defended the welfare state in terms of its provision of life-cycle redistribution; and I'm happy with that idea of what transfer payments should be doing. But some qualifications are in order. First, it's been a conventional mistake to assume that there's little the private sector can do to smooth out the traditional life-cycle of rises and falls in income. In fact there's a great deal the capital markets can do. But much of this is crowded out by extensive state welfare provision. Second, in modern Western societies old people tend to be quite well-off. In Britain, old people have assets of 30 000 pounds sterling on average. Yet half of all transfer payments in Britain go to old people.

On labour market participation rates, the British experience seems to have differed from the Australian. In recent years more and more married women in Britain have been participating, but fewer and fewer single-parent families.

Charles Murray: Many of the issues involved in the Australian debate on the welfare state are going to be resolved empirically. Bettina Cass and I have been saying different things about the term of duration of welfare; but we're working with the same data base, and over time the truth will come out. In the US there has been a great deal of convergence on such matters by people starting from different viewpoints.

However, some issues are not so easily resolved. This morning Martin Krygier referred to the role of the welfare state as enabling all people to interact as 'moral equals'. I want to say as emphatically as possible that our central problem in the US is that we have a very large number of people whom we have decided not to treat as moral equals. It's not that the recipients of welfare are likely to starve in the streets, or that they pose a great material problem for the comfortable middle classes, or that they are likely to riot out of fear that their benefits will be cut. It comes down to looking at the nature of the people affected, and asking ourselves whether they have in effect become Red Indians on a reservation: people whom we will take care of as wards of the state, leaving them to enjoy themselves as best they may in that condition, while the rest of us go about our business. My own view is that that state of affairs will become unacceptable, and so it should.

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The Social Welfare Research Program
Current Publications

The Centre for Independent Studies' Social Welfare Program has commissioned studies by qualified economists and other social researchers and thinkers into the various aspects of the welfare issue and the policy options available to governments dedicated to serious welfare reform. A series of books will be published under the Social Welfare Research Program — three have already appeared, including *The Welfare State: Foundations and Alternatives*. The other two books are:

Social Welfare: The Changing Debate by David G. Green.

This book summarises the research findings and arguments of several recent studies of welfare dependency.

Green makes two especially important points. The first is that the terms of the new debate on welfare are not really so new, but go back several centuries. Reformers have always agonised over what to do about 'the undeserving' poor, those who seem determined to scrape through life by depending on others. Green's second point is that the Victorian era coped remarkably well with dependency; not so much because of the rigours of the workhouse, but because the friendly societies, those voluntary, mutual aid organisations, did such a fine job in sustaining the independence and self-respect of the working man and his family. A reduced state welfare system would encourage localised, voluntary self-help organisations based, like the friendly societies (and the family), on an ethic of reciprocity. Any hope for curing the malaise of dependency lies here, rather than in the welfare state.

David G. Green is currently the Director of the Health Unit at the Institute of Economic Affairs, London. He is the author of several articles on politics and social policy, and his latest book, *Everyone A Private Patient*, was published by the IEA in 1988.

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Max Hartwell is a Visiting Professor at the Australian Graduate School of Management and a Senior Fellow of the Centre for Independent Studies. He is also Professor of Economics at the University of Virginia in the US. He has been a Fellow of Nuffield College in the University of Oxford since 1956.

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