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The New Zealand Centre for Political Debate

The Future of the Welfare State in NZ

WHAT kind of welfare state should New Zealand have in 30 years? If the trends of the past 30 years were to continue, we could end up with more than a quarter of working-age adults living on benefits, a huge retired population relying on a hopelessly overstretched pension and health system, and younger workers struggling under a massive tax burden as government soaks up almost half the nation's gross domestic product to pay for it all.

This would be a deeply undesirable outcome, for widespread reliance on government would undermine the spirit of independence and destroy work incentives by driving up the tax burden. It would also politicise everyday life by giving even more power to politicians and enticing even more pressure groups to queue up with their begging bowls.

Fortunately, all this is avoidable, for NZ is getting richer as a nation. Over the last 30 years, real GDP per capita has increased by 50%, and this should be surpassed over the coming 30 years. If this happens, many Kiwis will be able to afford buy what they need without relying on politicians to provide for them. But for self-reliance to flourish, changes to the welfare state are needed now. In particular, something has to be done to reduce tax-welfare churning.

Most people think the welfare state is like Robin Hood, taking money from the rich and giving it to the poor. But only about half of the

money spent on welfare state benefits and services is redistributed in this way. The other half is churned. In other words, the same people who pay the tax receive the benefits.

Some churning takes place immediately. Many middle-class families, for example, pay large sums in tax each fortnight but then immediately get much of it back in the form of tax credits, thanks to Working for Families. Other examples of churning take place over a longer period. Tax paid one year might be received back many years later in the form of an age pension, for example. Over a lifetime, even people who experience poverty at one point can end up paying for most or all of the government benefits and services they receive, for as their fortunes fluctuate, so too does their tax-welfare balance sheet.

Cutting down churning would not mean depriving the needy of help, for they would still get the benefits and services they receive now. Rather, it would mean spending less on those who pay high taxes only to have their money recycled back to them. If churning were reduced by cutting their taxes, for example, more parents could raise their children without government family payments or childcare subsidies, and more workers could save for their retirement. Rather than relying on WINZ when they are out of work, more people could use their own savings instead. Likewise in health, more people could afford private health insurance rather

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than relying upon public hospitals.

In Australia, Prime Minister Paul Keating showed how it is possible to reduce churning and increase self-reliance when he introduced the superannuation guarantee 15 years ago. Thanks to his foresight, millions of Australians now have their own retirement savings, which will increase their independence in old age while reducing the strain on the government age pension.

New Zealanders could similarly benefit from the introduction of a personal savings scheme, and there is no reason why it should be limited to retirement savings. The idea of personal savings could equally be extended to cover things like health care, unemployment and sickness cover as well as retirement.

As a starting point, personal savings accounts could be created for every New Zealander using the money the government is currently hoarding in its Superannuation Fund. This money has been collected from New Zealand taxpayers. If it were redistributed back to the population, every adult and child in the country would get about \$3000 to start their own personal savings fund. They could then supplement this over time with regular contributions from earnings.

There would need to be restrictions on how the money can be spent. One possible use of these funds might be to reduce reliance on government unemployment and sickness benefits by giving everyone something to fall back on when their earnings are temporarily interrupted. And for people who wanted to take more responsibility for their own lives, funds could also offer the opportunity to opt out of other government services.

Personal funds could also be used to bolster self-reliance in health, for example, by encouraging people to cover more of their medical costs. They could also increase

autonomy in retirement, by enabling people to build up their own savings. People who prefer to remain in the state system could do so, but those who choose to opt out of the government's health and/or retirement schemes could be given tax reductions to compensate them. The money they save would then go into their personal fund and would be used to pay for routine doctor and pharmacy bills, to buy health insurance, or to fund a retirement annuity.

I would suggest that people should only be able to opt out of state health and retirement schemes up to the level of tax they pay into them. In other words, they should be able to cash in some of their contribution. A more 'socialist' version of the same idea might allow people to trade in their full entitlements, not just their contributions, so those who pay little tax would receive tax credits to buy the services they need. There are arguments for and against both of these proposals, but at the moment none of our political leaders is discussing either of them.

We urgently need a serious political debate about opt-outs and self-funding, based on the recognition that an increasingly affluent society such as ours no longer needs a large welfare state. Many of us could and should be looking after ourselves in the future, but it won't happen until we find politicians with the vision to introduce reforms now from which later generations will benefit.

This is a revised version of article which originally appeared in The Australian on 30 January 2007. Peter Saunders is social research director at the Centre for Independent Studies. He will be talking about these issues in Wellington next Wednesday, with commentary from Sir Roger Douglas. Wednesday 28th March 6pm – 7:15pm Turnbull House, Bowen Street, Wellington Entry is free, to register please visit www.cis.org.nz or ph (04) 499 5861.

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