



BASIC INCOME OR A SINGLE TAPERING RULE?

Incentives and inclusiveness for the case of Finland



Jon Pareliussen 21 March 2018, Rome.



Outline

- Introduction: why reform?
- Benefit reform scenarios to understand current weaknesses and form a vision for the future.
- Findings from the scenarios.
- Survey recommendations.

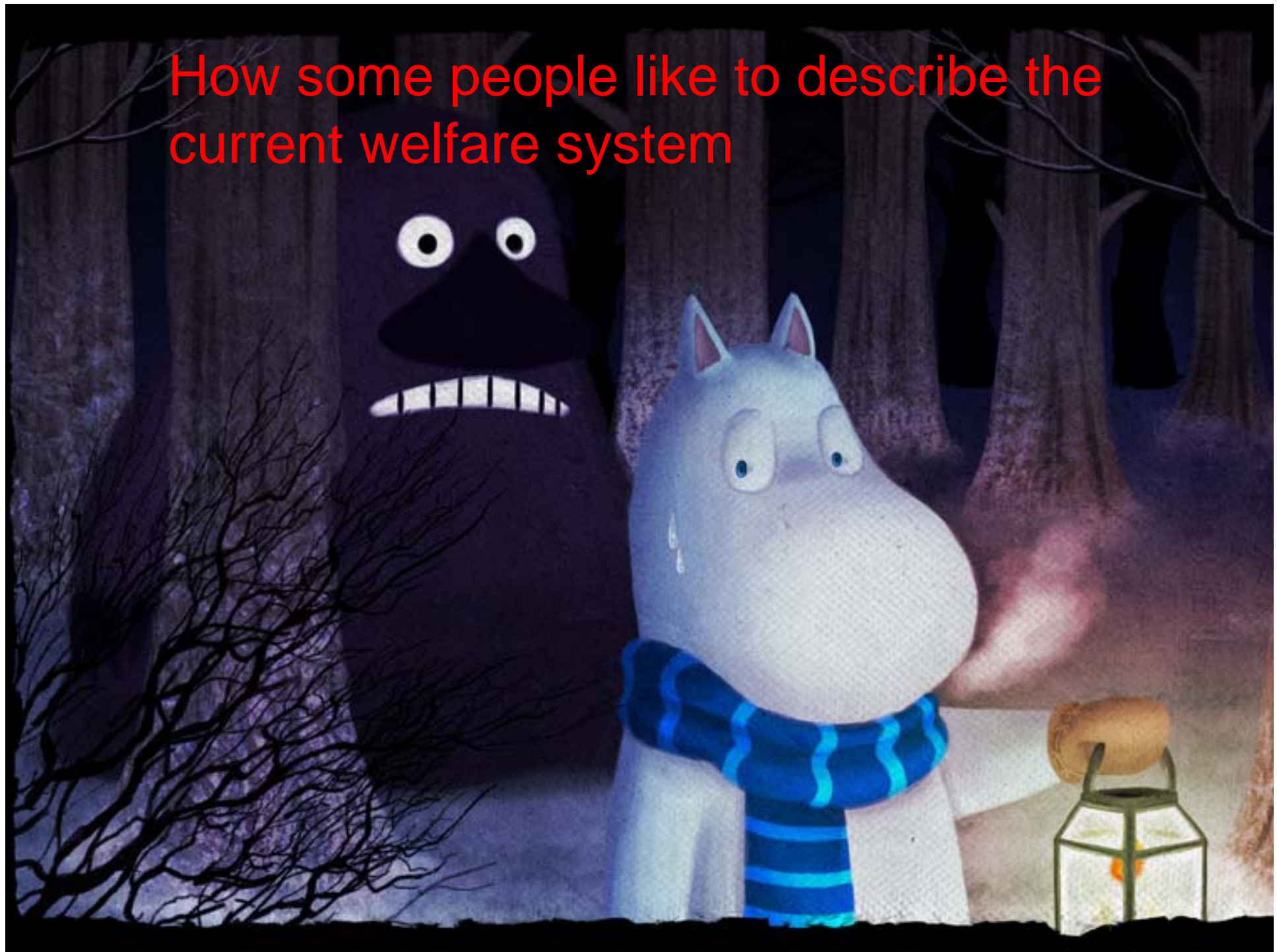


“If you don't know where you are going, you might wind up someplace else.”

- Yogi Berra



How some people like to describe the current welfare system





Benefit reform scenarios

a uniform benefit

vs

a uniform tapering rule



ARE YOU
UC
READY?



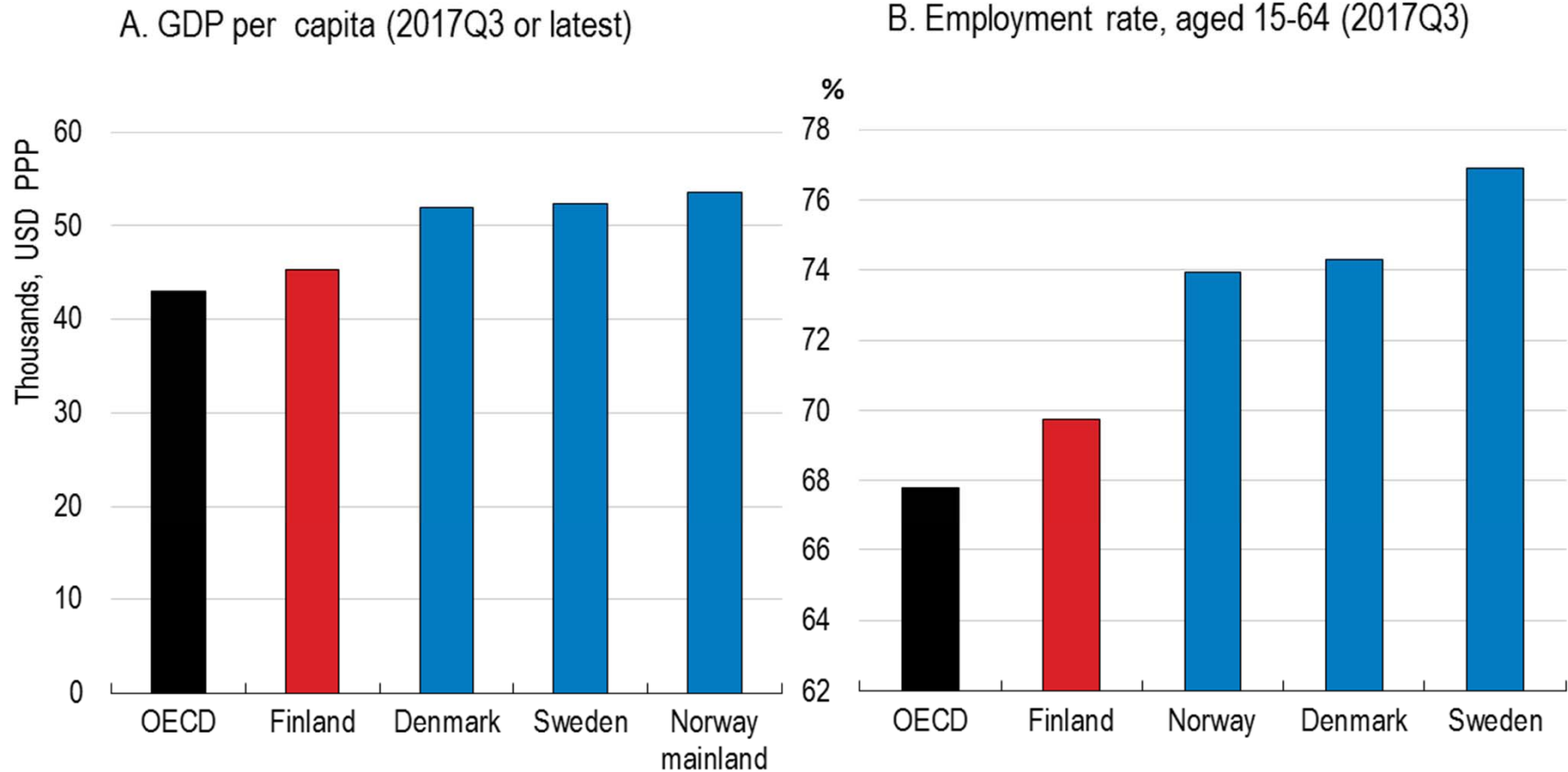


INTRODUCTION: WHY REFORM?





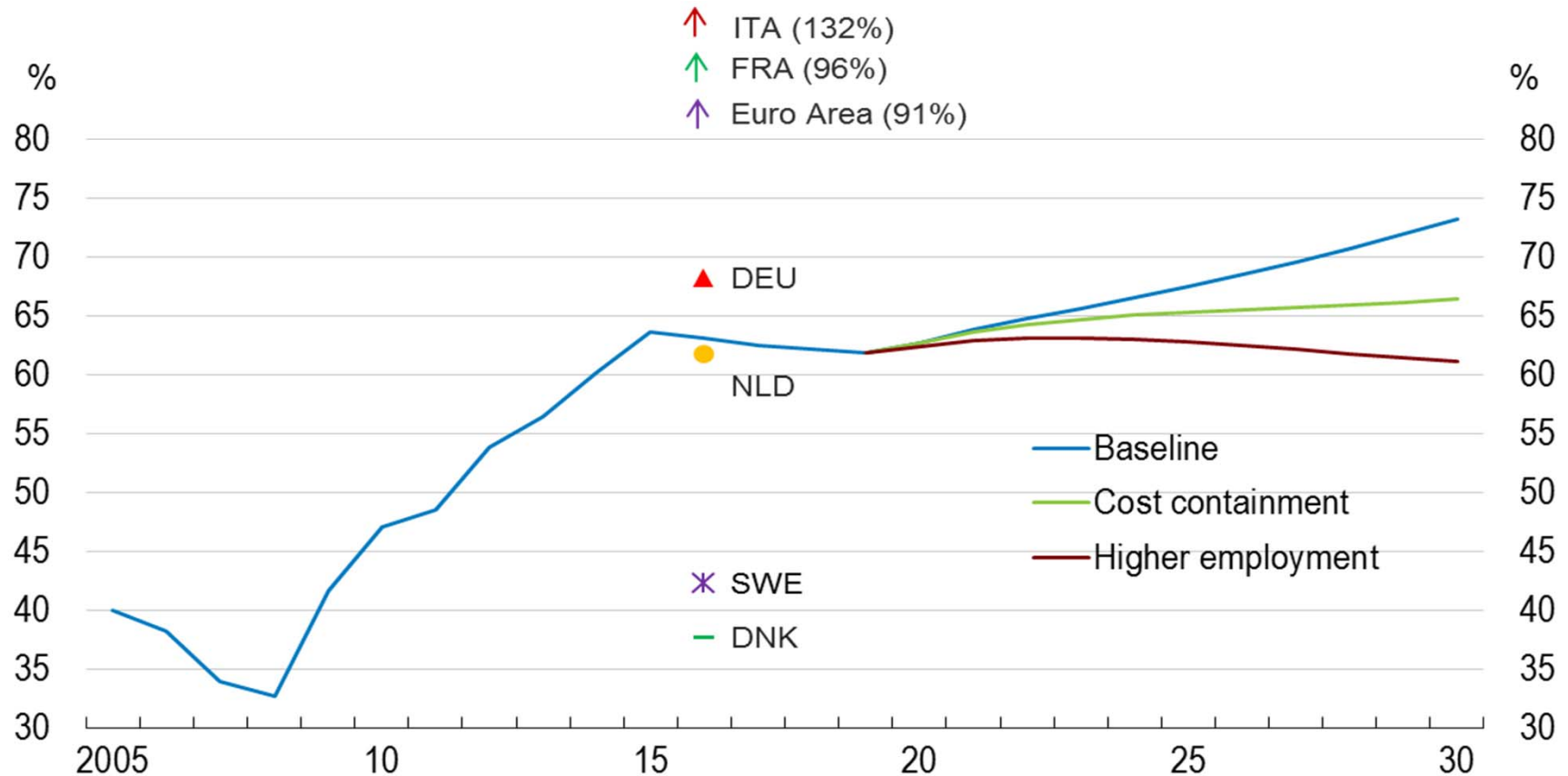
High employment cornerstone in Nordic model, but Finland lags behind other Nordics



Source: OECD Economic Outlook database; and OECD Labour Force Statistics database.



Higher employment important to meet demographic challenge



Note: The cost containment scenario assumes that reforms to the provision of health care and social services reduce growth in related spending by half. The higher employment scenario assumes cost containment in age-related spending and a higher employment rate of the population aged 15-64, which rises to 74% in 2030.

Source: OECD Economic Outlook database and OECD calculations.



The government and social partners have done a lot lately

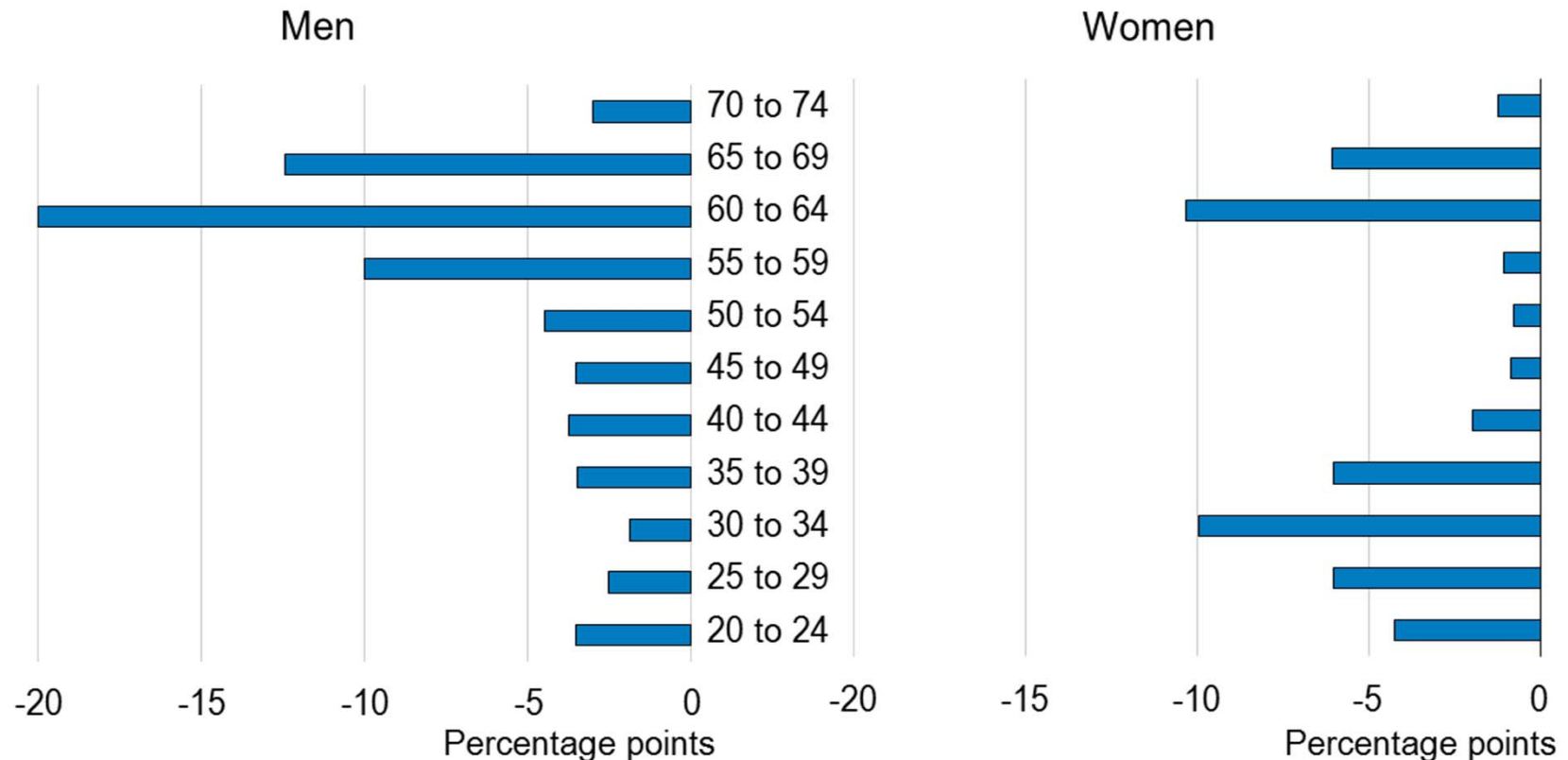
- New wage bargaining model.
- Reducing unemployment insurance duration.
- Job search requirement and new activation model
- Extended trial period for new hires.
- Education reform.





But incentives, complexity and the future of work calls for further benefit reform

Employment gap to Nordics (2016)¹



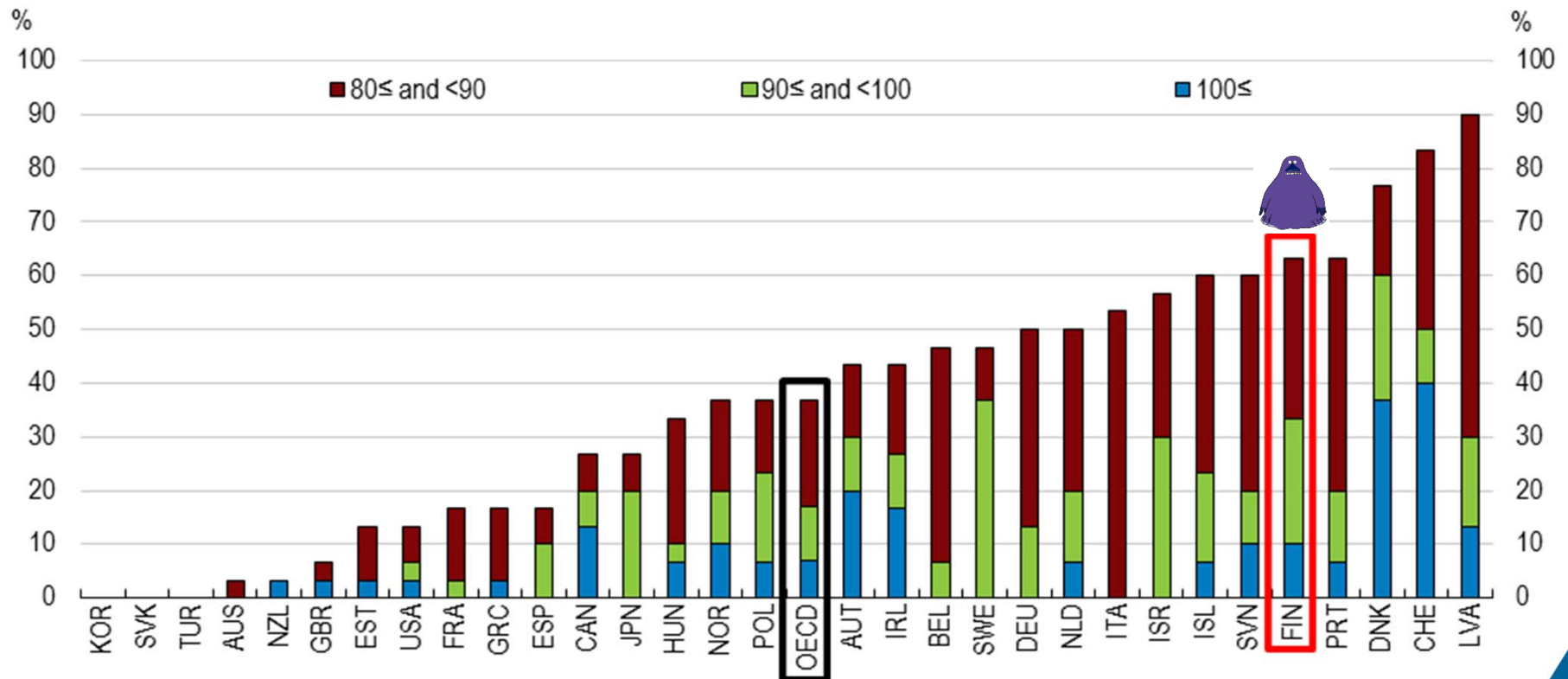
1. Difference in employment rates between Finland and the Nordic average (Denmark, Norway, and Sweden), within each age-gender sub-group.

Source: OECD Labour Force Statistics Database.



Incentives can be weak in the current system


% of modelled households facing high average effective tax rates when transitioning from unemployment to full-time work (synthetic indicator).



Note: Average effective tax rates are modelled in the OECD TaxBen model for six stylized household types and for five income levels: 33%, 50%, 67%, 100% and 150% of national average wage. Households with children are assumed to have two children aged four and six.



A complex welfare system reflects complex individual situations

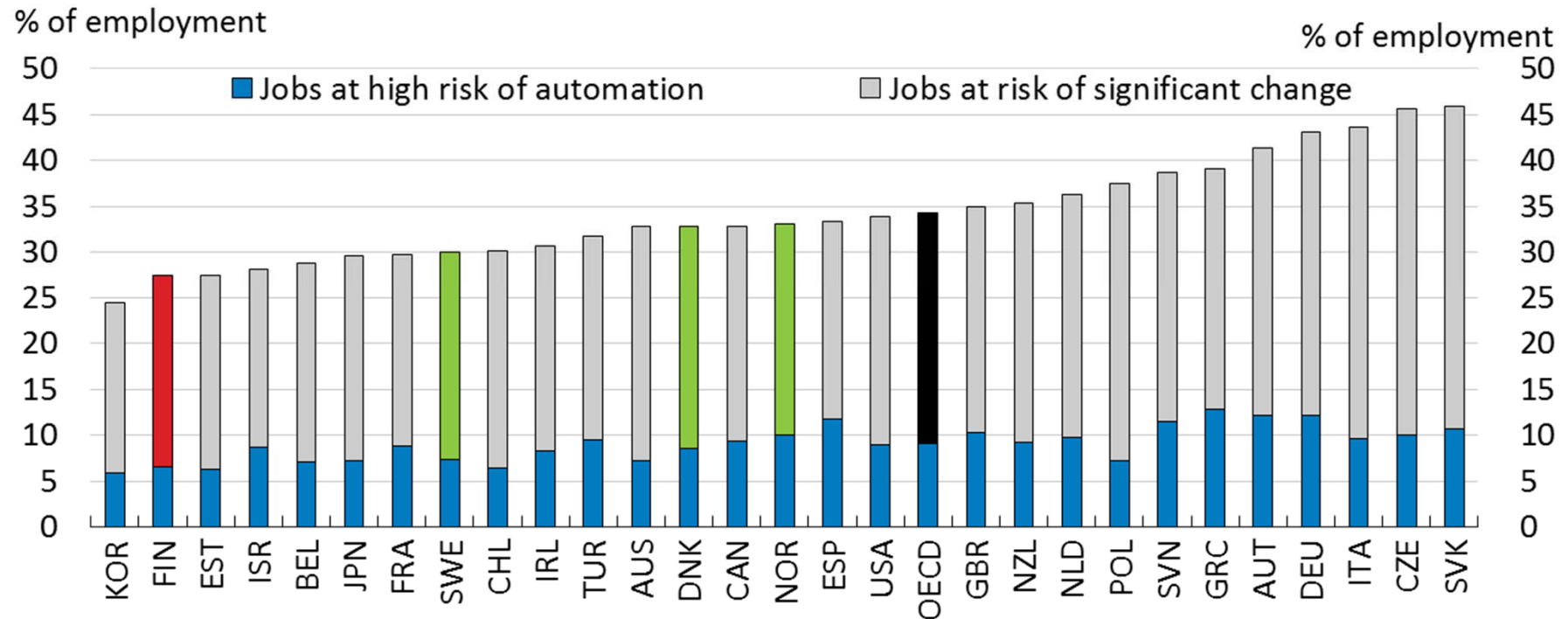
Current system		
<i>Benefit / fee</i>	<i>Programme description</i>	
Family benefit	Child and lone parent (lump-sum)	Lone parent child maintenance allowance
		Lone-parent supplement to child benefit
		Child benefit
	Childcare benefit	Homecare allowance
		Homecare supplement
		Municipal homecare supplement
Unemployment benefit		Labour market subsidy
		Basic unemployment insurance
		Income-related unemployment insurance
Social assistance		Basic and household related amount
		Housing supplement
Housing benefit		Housing allowance
Childcare fee		Income related
		Floor and ceiling

- Each benefit has a tapering rule reducing the incentive to work.
- These rules interact in complex ways, compounding disincentives.
- May also cause “bureaucratic traps”.



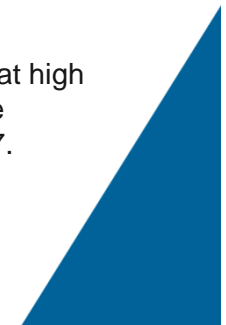
A changing world of work calls for more streamlined and flexible solutions

The risk of automation in OECD countries



Note: Based on the analysis of the task content of individual jobs using the OECD Adult Skills Survey (PIAAC). Jobs are at high risk of automation if the likelihood of being automated is at least 70%. Jobs at risk of significant change are those with the likelihood of being automated estimated at between 50 and 70%. For more details, see OECD Employment Outlook 2017.

Source: OECD Labour Force Statistics database; and OECD Employment Outlook 2017, OECD Publishing, Paris.





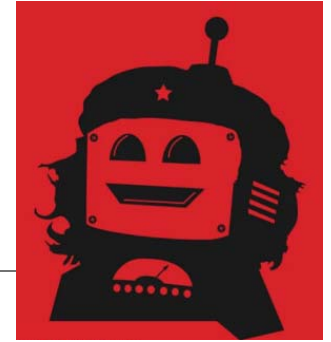
BENEFIT REFORM SCENARIOS: UNDERSTAND THE PRESENT TO PLAN FOR THE FUTURE





Basic income

– a universal benefit for all






- Basic income high on the agenda, a limited trial is ongoing in Finland.
- Already OECD work on the subject.
- Consistency problems unmasked with microsimulations:
 - Social welfare trilemma between incentives, inclusiveness and fiscal cost.
 - Can a basic income both fix incentives and be inclusive when taking cost into account?





Summary of the scenarios

Current system		Basic income scenario	Universal credit scenario	
Benefit / fee	Programme description			
Family benefit 	Child and lone parent (lump-sum)	Family benefit (lump-sum)	Family benefit (lump-sum)	
		Lone-parent supplement to child benefit		
		Child benefit		
	Childcare benefit	Homecare allowance		Basic income 
		Homecare supplement		
		Municipal homecare supplement		
Unemployment benefit	Labour market subsidy	+ increased income taxation	Universal credit 	
	Basic unemployment insurance			
	Income-related unemployment insurance			
Social assistance	Basic and household related amount →	Social assistance		
	Housing supplement			
Housing benefit	Housing allowance	Housing benefit		
Childcare fee	Income related	Childcare fee	Childcare fee (lump-sum)	
	Floor and ceiling			



Universal Credit -a universal tapering rule

Make
work pay!

Welfare
that works!






- Merge benefits into one and withdraw them at one single and moderate rate.
 - Removes benefit interactions.
 - Increases transparency.
 - Improves incentives.
 - Keeps targeting (and hence income distribution) as in the current system.
 - Limited fiscal cost.
- Technically more demanding than a basic income.





Summary of the scenarios

Current system		Basic income scenario	Universal credit scenario	
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Family benefit 	Child and lone parent (lump-sum)	Lone parent child maintenance allowance	Family benefit (lump-sum)	
		Lone-parent supplement to child benefit		
		Child benefit		
	Childcare benefit	Homecare allowance	Basic income 	 Universal credit
		Homecare supplement		
		Municipal homecare supplement		
Unemployment benefit	Labour market subsidy	→	→	
	Basic unemployment insurance			
	Income-related unemployment insurance			
Social assistance	Basic and household related amount	→	→	
	Housing supplement			
Housing benefit	Housing allowance	→	→	
Childcare fee	Income related	→	→	
	Floor and ceiling			
		Childcare fee	Childcare fee (lump-sum)	

Taper rate 65% of earnings after tax

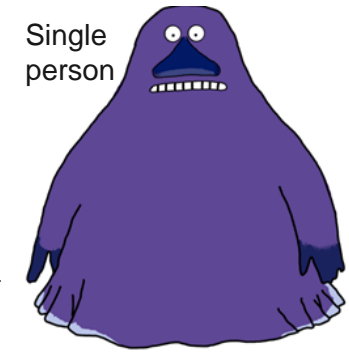


FINDINGS FROM THE SCENARIOS

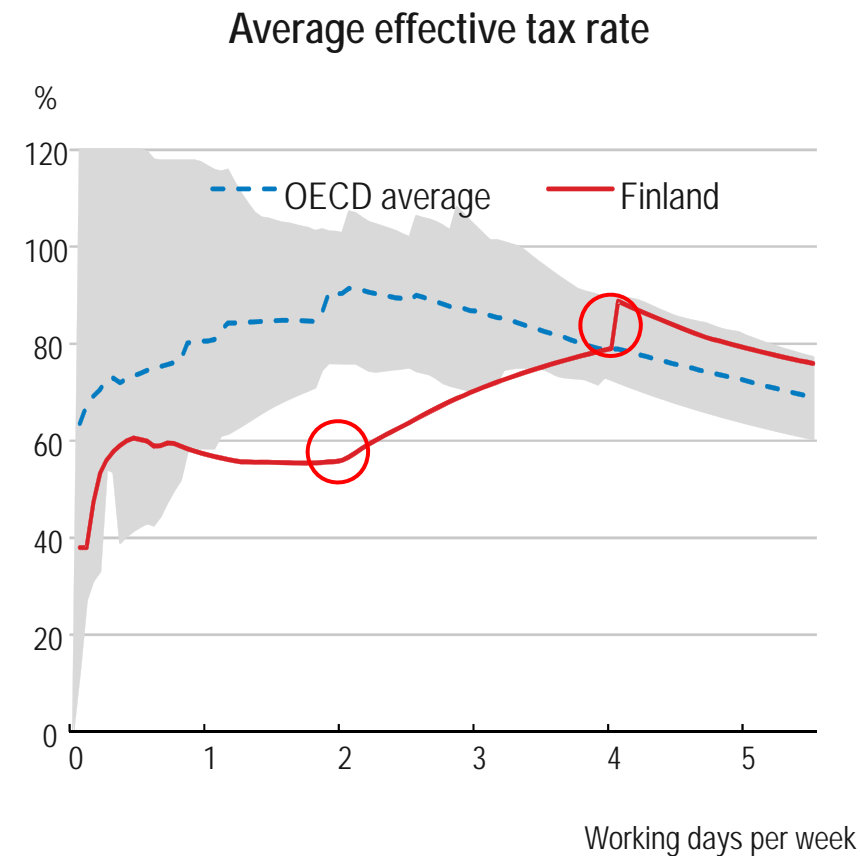
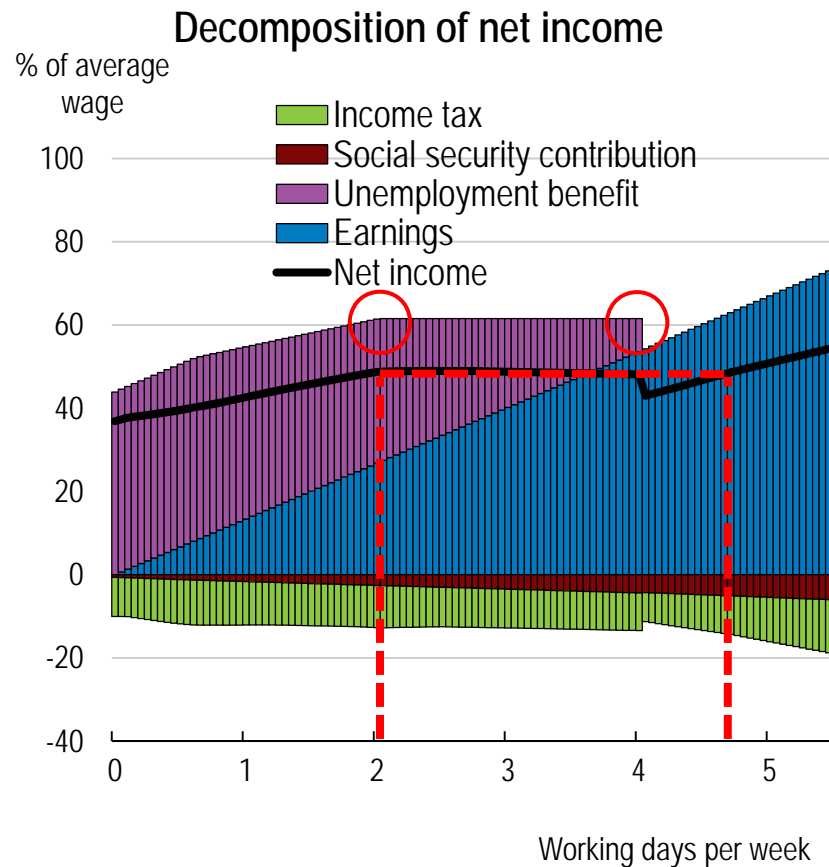




Unemployment insurance rules create disincentives



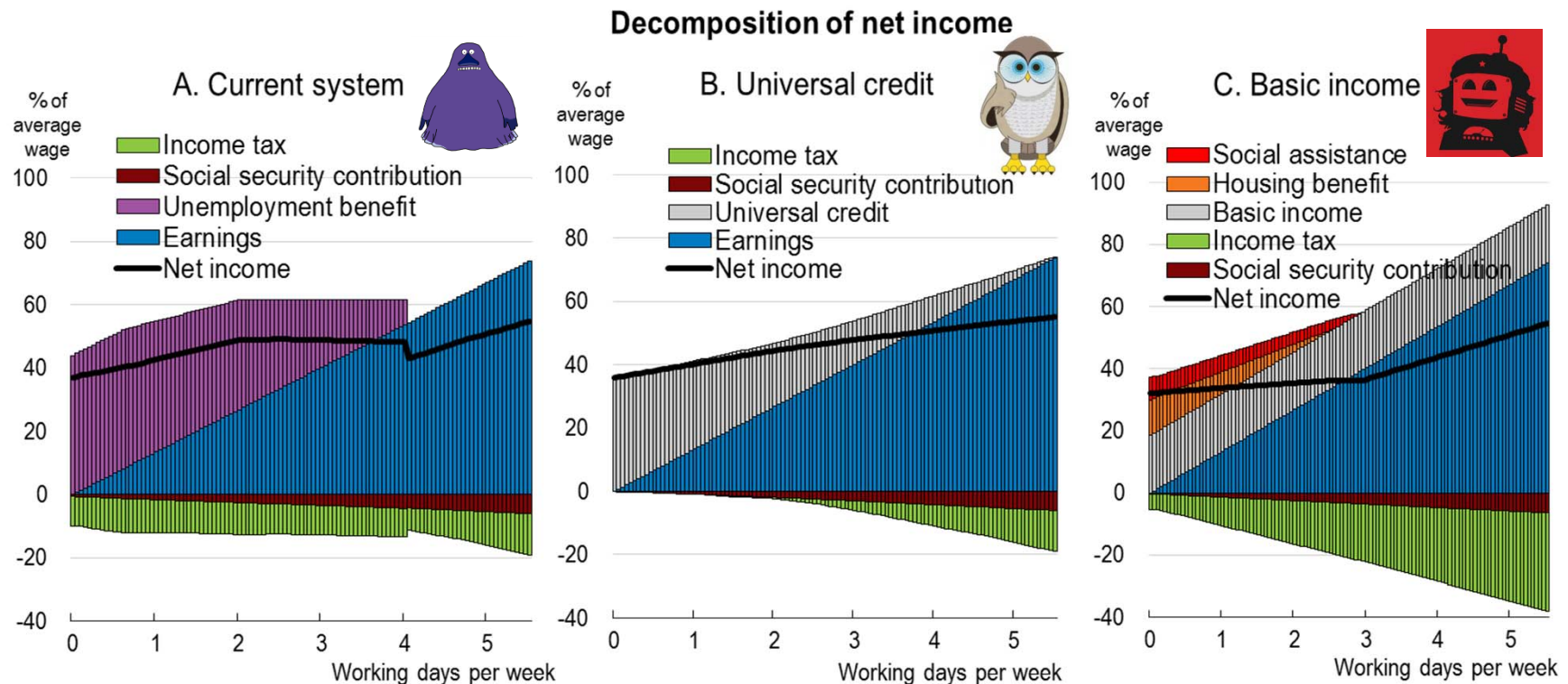
- 100% cap (unemployment insurance and earnings combined).
- Cliff-edge loss of unemployment benefits when working more than 80%.



Note: Simulations based on the OECD TaxBen model. The shaded area denotes the range between the 25th and the 75th percentile in the OECD area. A single person entitled to unemployment insurance. Extreme negative and positive rates have been capped at -20% and 120%.



Unemployment insurance rules create disincentives - solutions

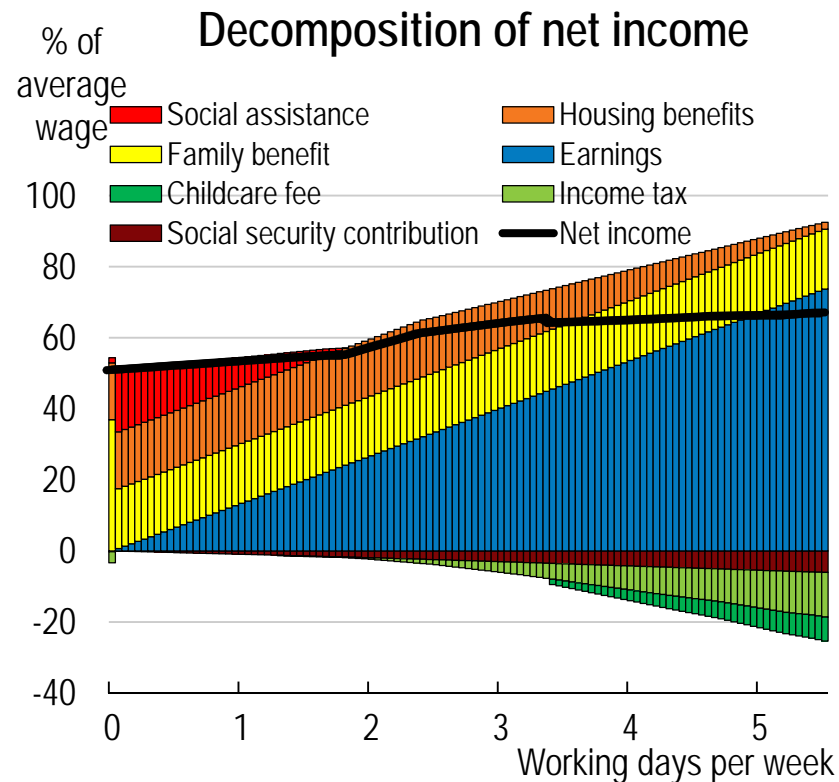
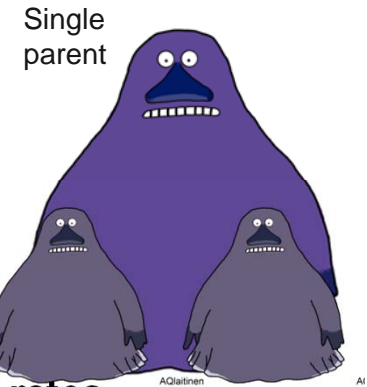


Note: Simulations based on the OECD TaxBen model. A single person entitled to unemployment insurance.

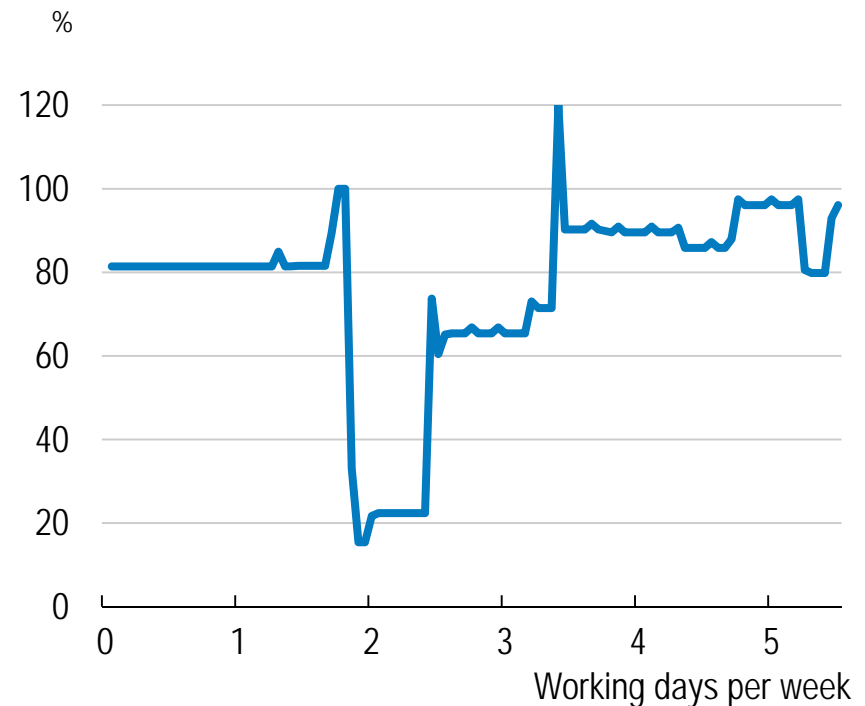




Complexity compounds disincentives



Marginal effective tax rates

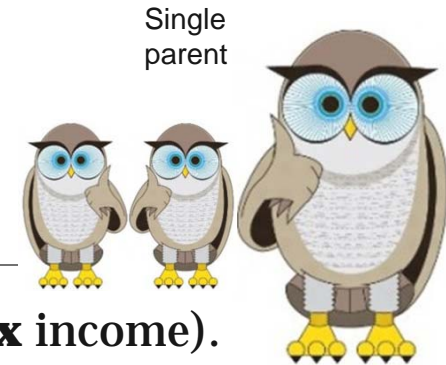


Complex interactions between different benefits and income taxation create incentive traps.

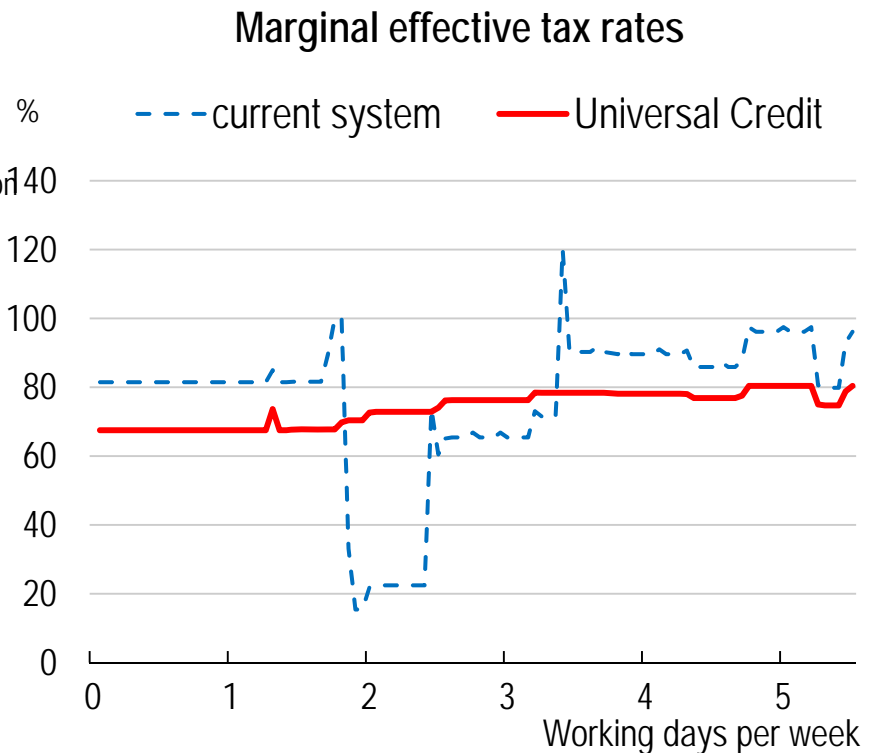
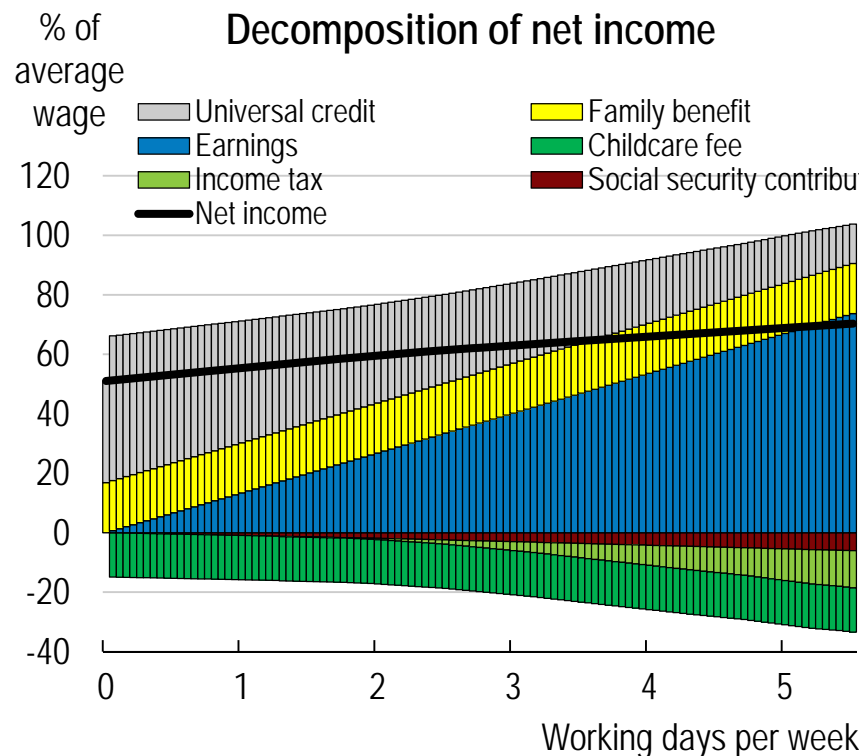
Note: Simulations based on the OECD TaxBen model. A lone parent not entitled to unemployment insurance. The different benefits apply different income definitions and different tapering rules. Social assistance is tapered at a rate of 80% of net income up to a threshold. The housing benefit has relatively complex tapering rules translating to a taper rate of approximately 34% of gross household income. The childcare fee is calculated on the basis of household income.



Complexity compounds disincentives - solution



- Only one tapering rule in the universal credit (65% of **after-tax** income).









In other words, the net gain from working will be 35 cents of each euro earned after tax. Tapering on after-tax income secures by design that the marginal effective tax rate never exceeds 100%.

Note: Simulations based on the OECD TaxBen model. A lone parent not entitled to unemployment insurance. Extreme positive rates have been capped at 120%.



Both scenarios enhance incentives, universal credit more consistently (1)

Comparative average effective tax rates – unemployment insurance







		Going back to work full time with 100% of previous earnings			Going back to work full time with 80% of previous earnings		
Household type \ Scenarios							
		Single	79.1	72.0	73.4	89.4	78.3
Single parent	97.7	86.2	73.4	99.5	91.4	72.2	
Single earner in childless couple	86.5	68.2	73.4	90.3	73.6	72.2	
Single earner in couple with children	88.3	74.4	73.4	93.8	81.3	72.2	
Second earner in childless couple	74.6	43.9	64.8	83.7	43.2	71.5	
Second earner in couple with children	102.0	66.1	73.4	118.0	71.0	72.2	

Note: Simulations based on the OECD TaxBen model. Previous earnings 67% of national average wage. Households with children are assumed to have two children aged two and five.



Both scenarios enhance incentives, universal credit more consistently (2)

Comparative average effective tax rates – no unemployment insurance

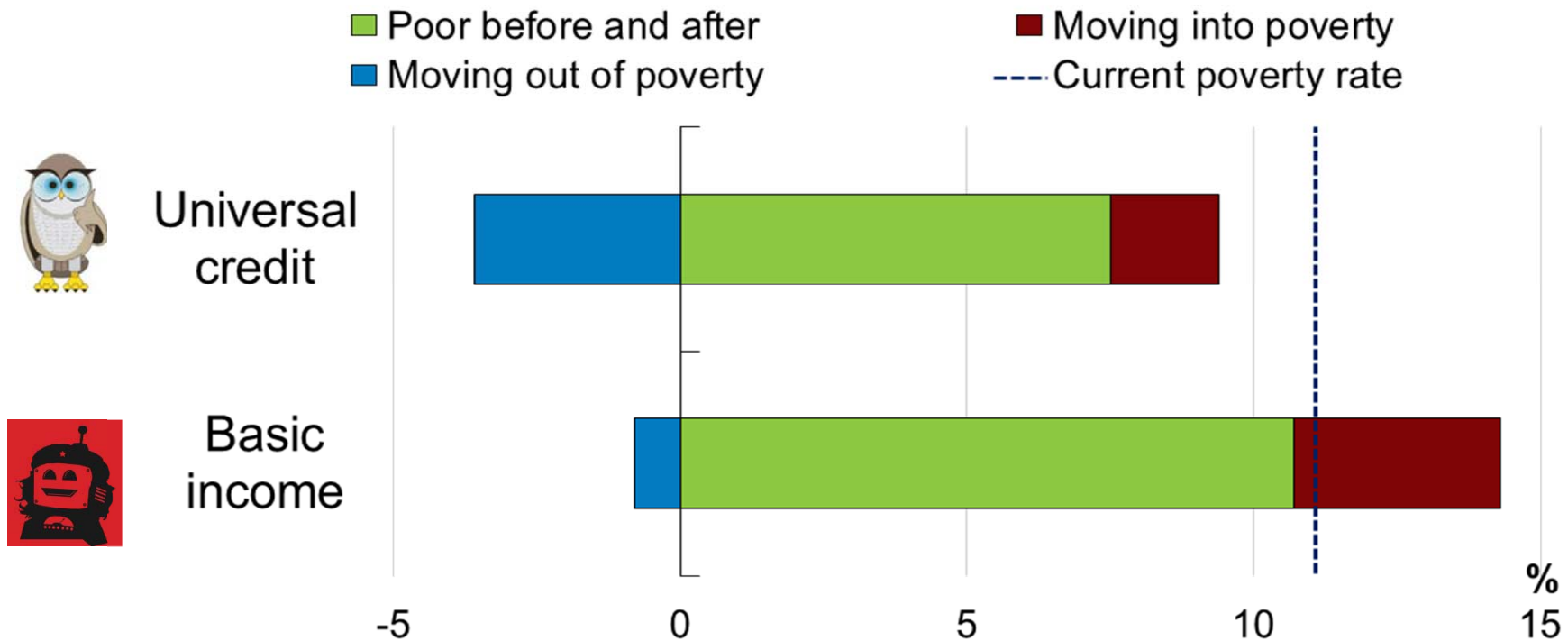
	Going into half-time work			Going into full-time work		
Scenarios						
Household type						
Single	87.6	87.9	69.1	72.0	72.0	72.0
Single parent	67.6	92.5	69.1	77.1	86.2	73.4
Single earner in childless couple	87.6	87.9	69.1	86.5	68.2	73.4
Single earner in couple with children	87.6	87.9	69.1	80.6	74.4	73.4
Second earner in childless couple	11.6	41.9	11.6	24.0	43.9	24.0
Second earner in couple with children	89.4	86.3	56.0	66.6	66.1	46.3

Note: Simulations based on the OECD TaxBen model. Potential earnings 67% of national average wage. Households with children are assumed to have two children aged two and five.



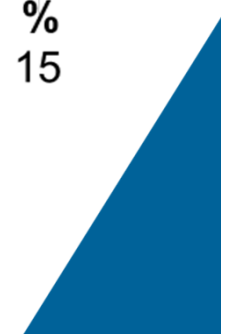
Basic income increases poverty while universal credit reduces it (1)

Inflows to and outflows from poverty



1. Percentage change compared to pre-reform disposable income within each income decile.
2. Share of individuals in working-age households.

Source: Simulations with the TUJA model.



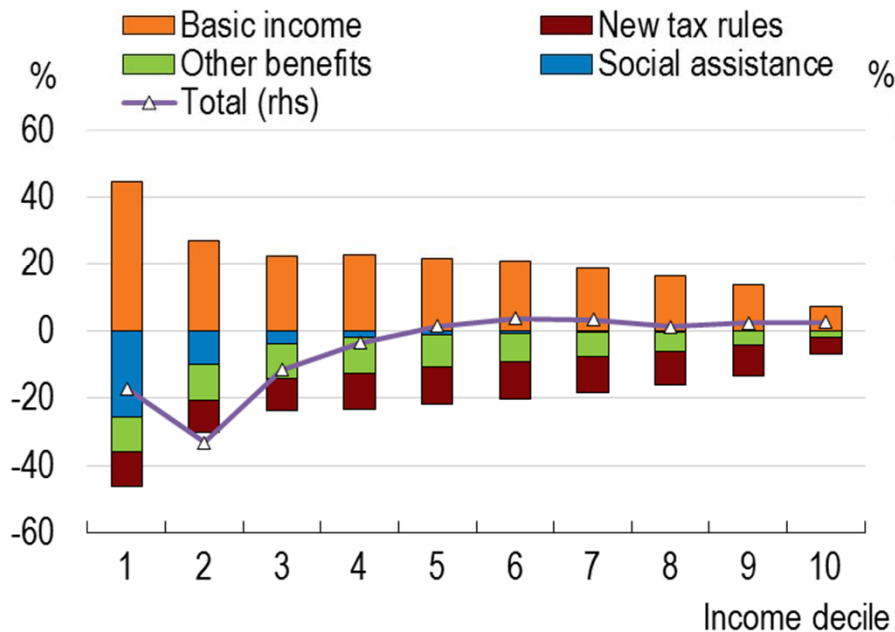


Basic income increases poverty while universal credit reduces it (2)

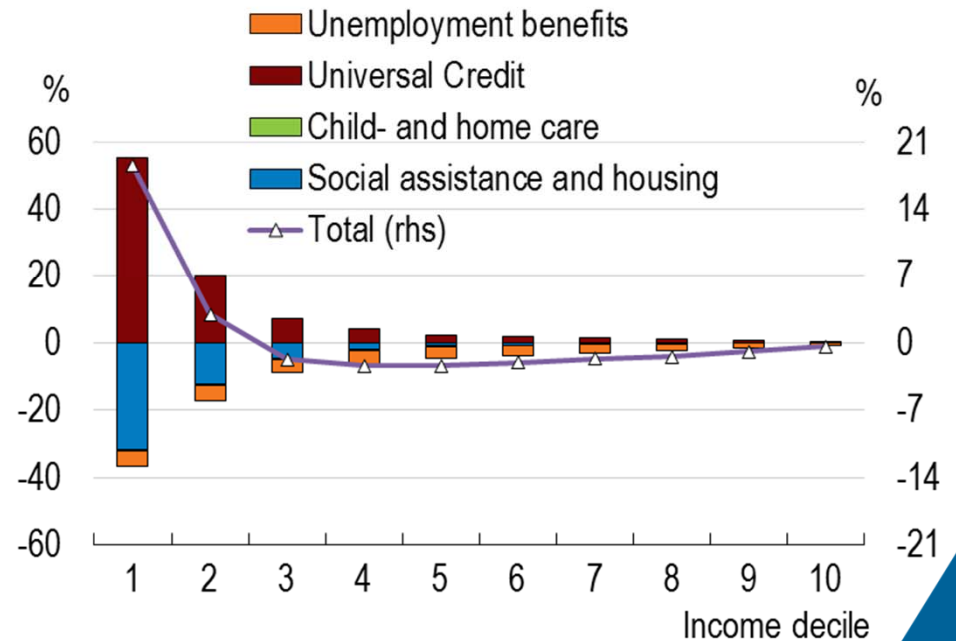
Changing disposable incomes under benefit reform scenarios¹



A. Basic income

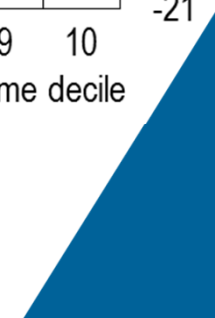


B. Universal credit



1. Percentage change compared to pre-reform disposable income within each income decile.

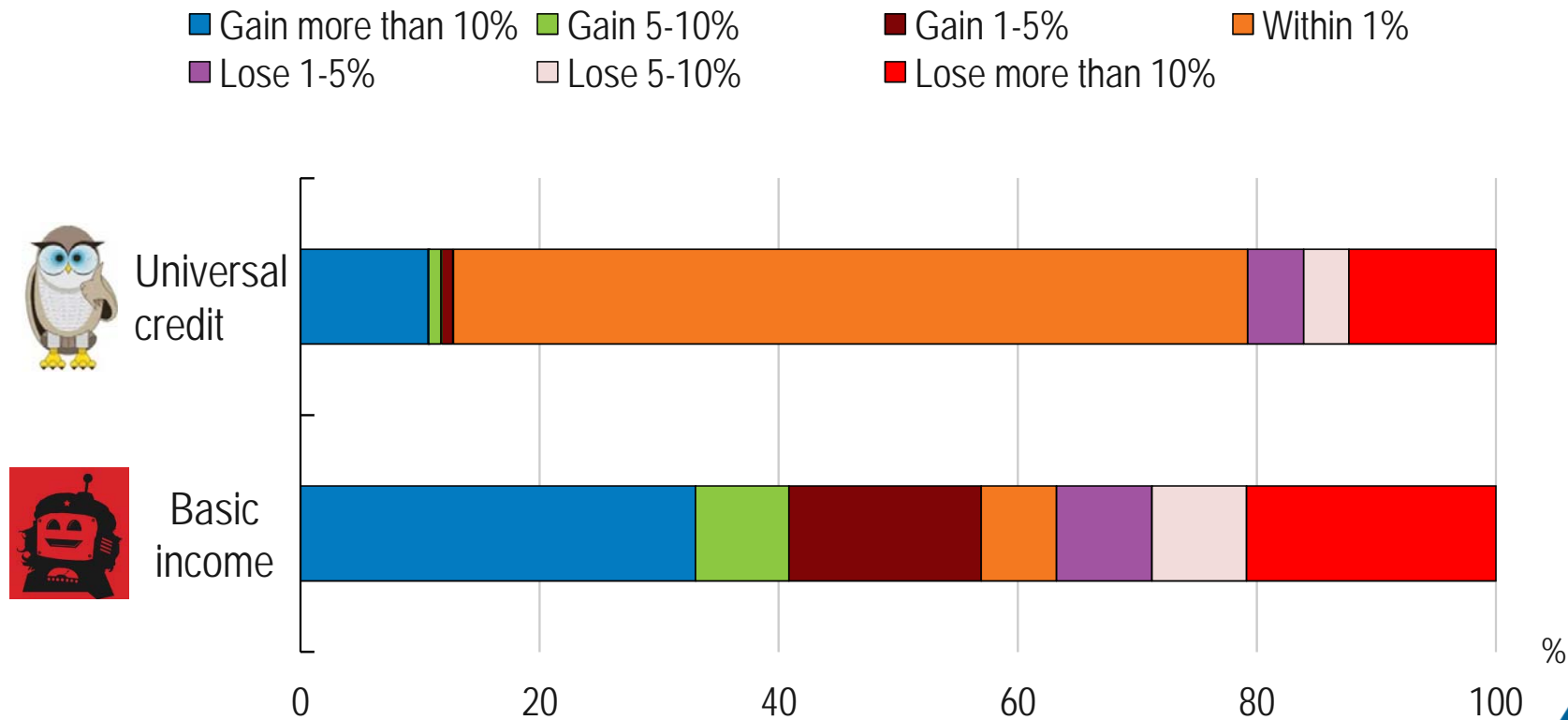
Source: Simulations with the TUJA model.



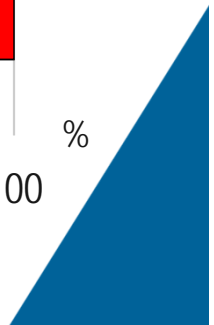


Basic income leads to profound redistribution of income

Gainers and losers
Share of individuals in working-age households



Source: Simulations with the TUJA model





CONCLUSIONS





Direction/vision for reform: Harmonise benefits and coordinate their tapering

- **Universal credit improves on the current system, and outperforms basic income along all dimensions.**
 - Assuming that current benefit targeting / distribution of income reflects social preferences.
 - Some general lessons, but not universal conclusion.





NEXT STEPS





Next steps

- Paper will be released as OECD working paper soon.
- Perhaps journal submission of edited version.
- No extensions of the analysis planned, as it puts very high demand on data, models and resources.
- But more interesting, what will happen in Finland?





FINANCIAL TIMES

Free Lunch **Universal basic income**

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Welfare lessons from Finland

Basic income and universal credit, mano a mano

Martin Sandbu FEBRUARY 28, 2018



Orpo: OECD's recommendations a sound basis for next coalition

FINLAND / CREATED: 01 MARCH 2018

NEWS FROM FINLAND

HELSINKI TIMES



Liisa Heinämäki @HeinmkiLiisa · 7h

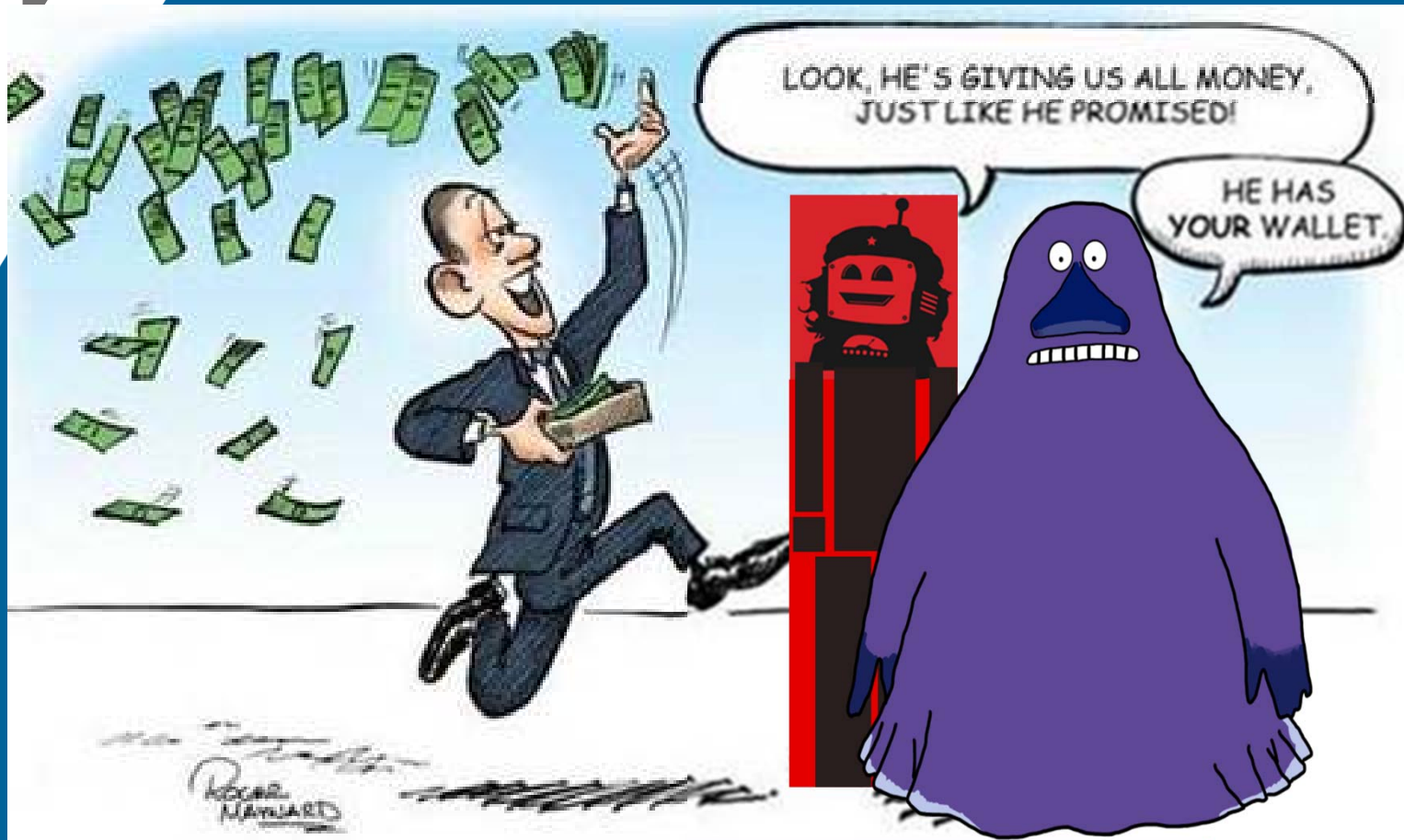
Thank you so much for great job with #OECD Economic Survey 2018, and good conversation with #Toimi2030 Jon Parelius & Christophe Andre @OECD. We have a lot to think, and base to work.. This was such a joy, that my first selfie ever got to be taken!



Petteri Orpo (NCP), the Minister of Finance, has welcomed the recommendations made for Finland by the Organisation for Economic Development and Co-operation (OECD).



THANK YOU!





More Information...

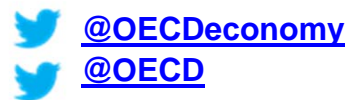
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Pareliussen, J., H. Viitamäki and H. Hwang (2018), “Basic income or a single tapering rule? Incentives, inclusiveness and affordability compared for the case of Finland”, *OECD Economics Department Working Papers*, forthcoming, OECD Publishing, Paris.

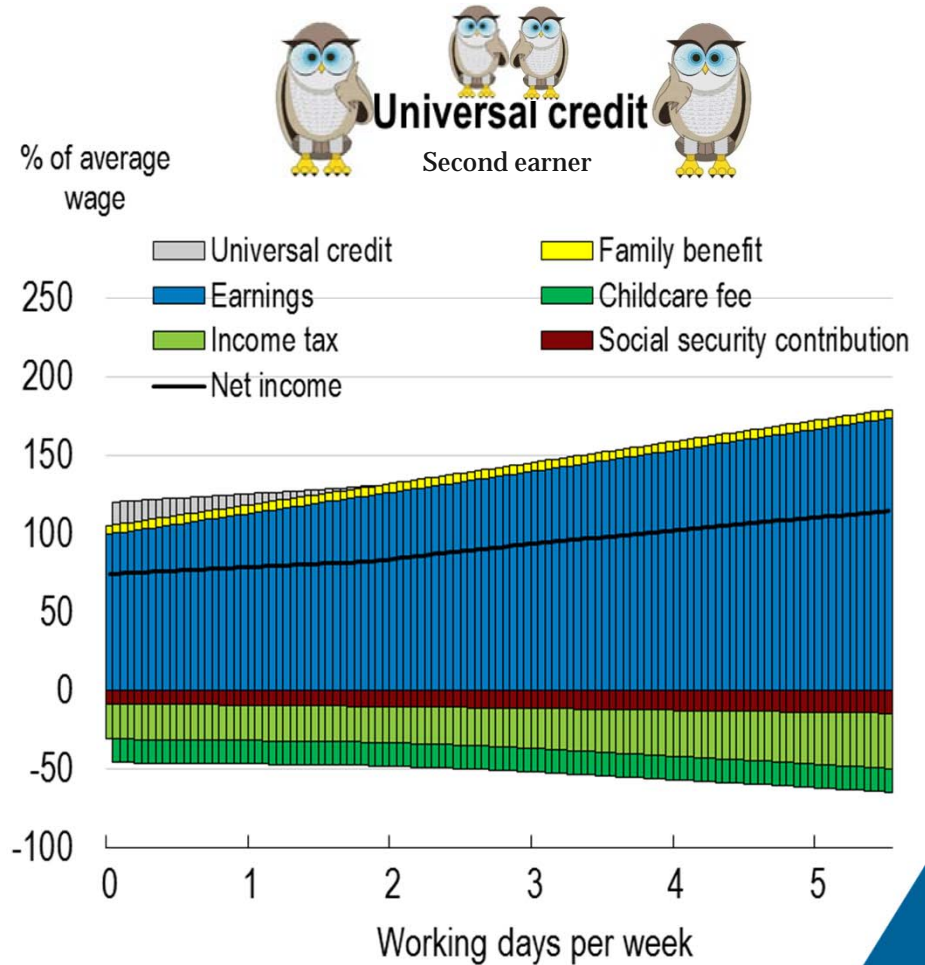
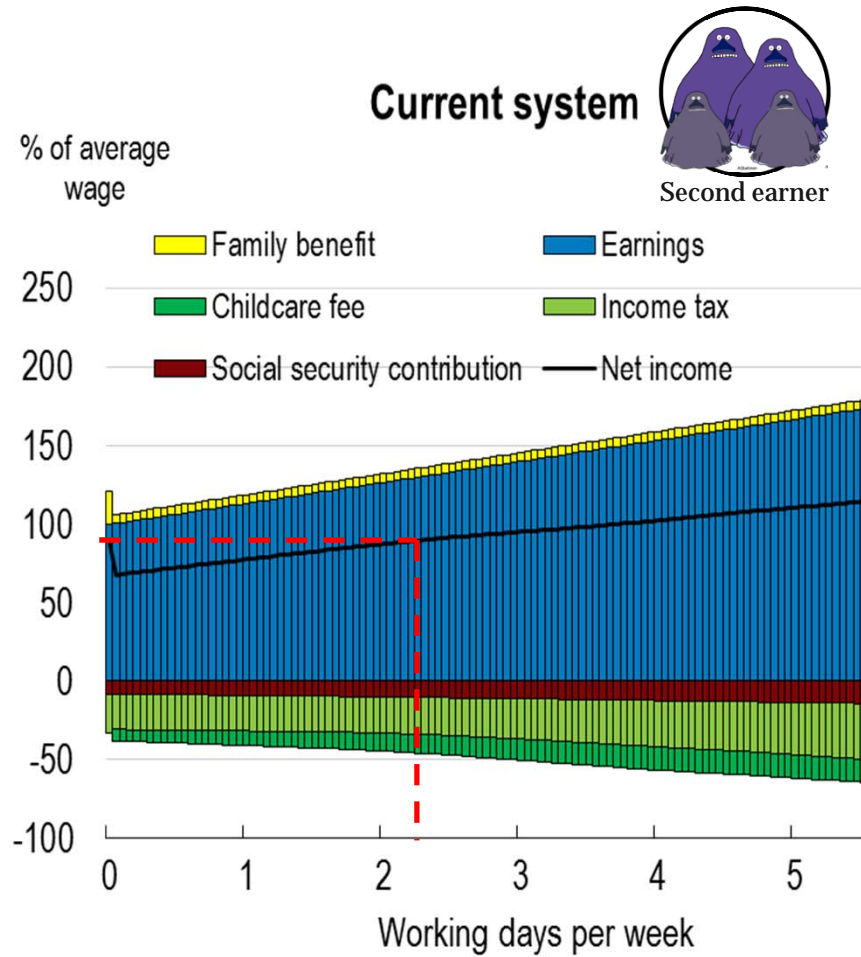




EXTRA SLIDES



Make work pay for parents (1)

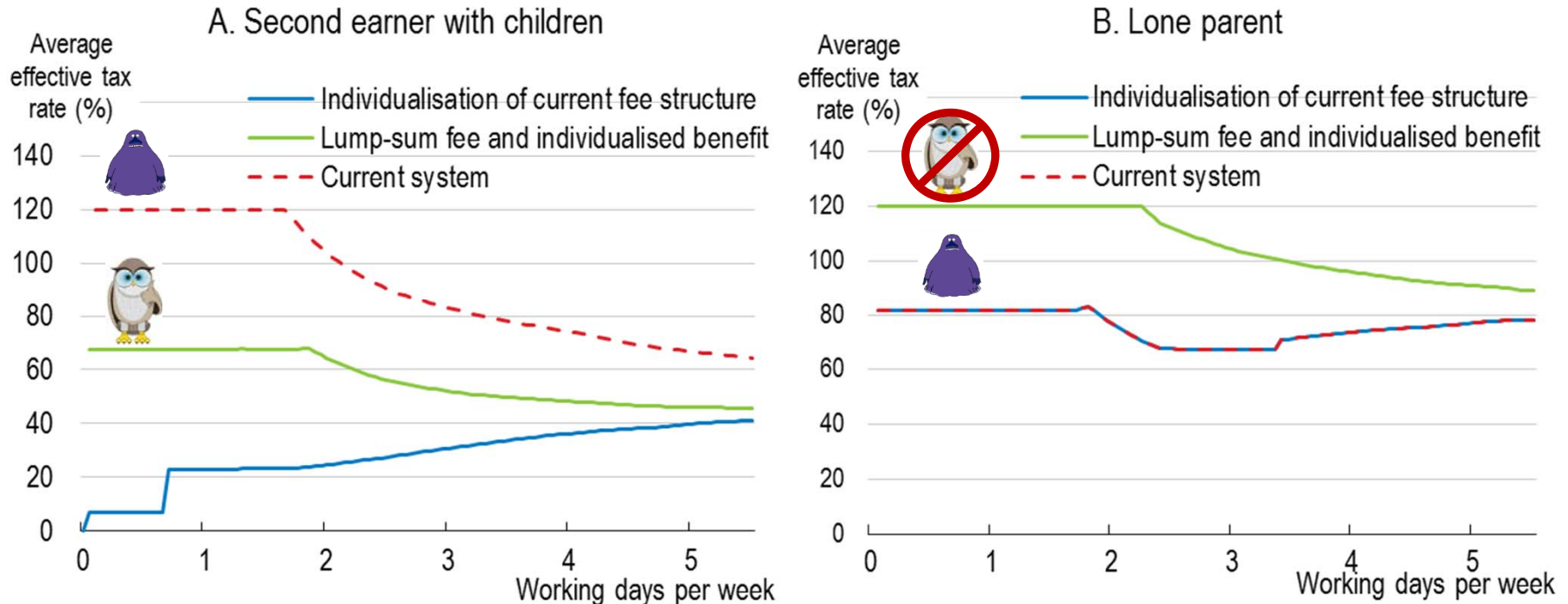


Note. For a person going into work with hourly earnings of 67% of the national average wage.
Source: Calculations based on the OECD TaxBen model.



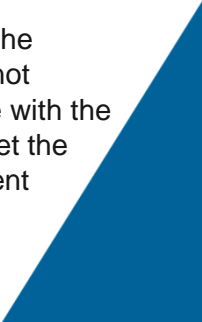


Make work pay for parents (2)



Note: The homecare allowance is abolished in both scenarios. The “lump-sum fee and individualised benefit” scenario replaces the childcare fee structure by a lump-sum fee combined with a childcare benefit tapered off by 65% of after-tax income. Tapering is not coordinated with tapering of other benefits. In couples, the benefit is individualised and tapered against the income of the spouse with the lowest earnings. The “Individualisation of current fee structure” keeps the current childcare fee structure, but the income test to set the level of the childcare fee is applied to the spouse with the lowest earnings. The modelled individual is not entitled to unemployment insurance, and he or she is going into work with hourly earnings of 67% of the national average wage.

Source: Simulations with the OECD TaxBen model, in Pareliussen et al. (2018a).





Make work pay for parents (3)

- **Restructure the homecare allowance, for example by:**
 - Removing the homecare allowance (fix incentives).
 - Increasing the basic parental leave benefit amount (compensate losers).
 - Extending the allowed period to take out parental leave to three years (preserve free choice).
- **Individualise the childcare fee (ref. individual income taxation).**
- **But: these proposals are not fiscally neutral.**





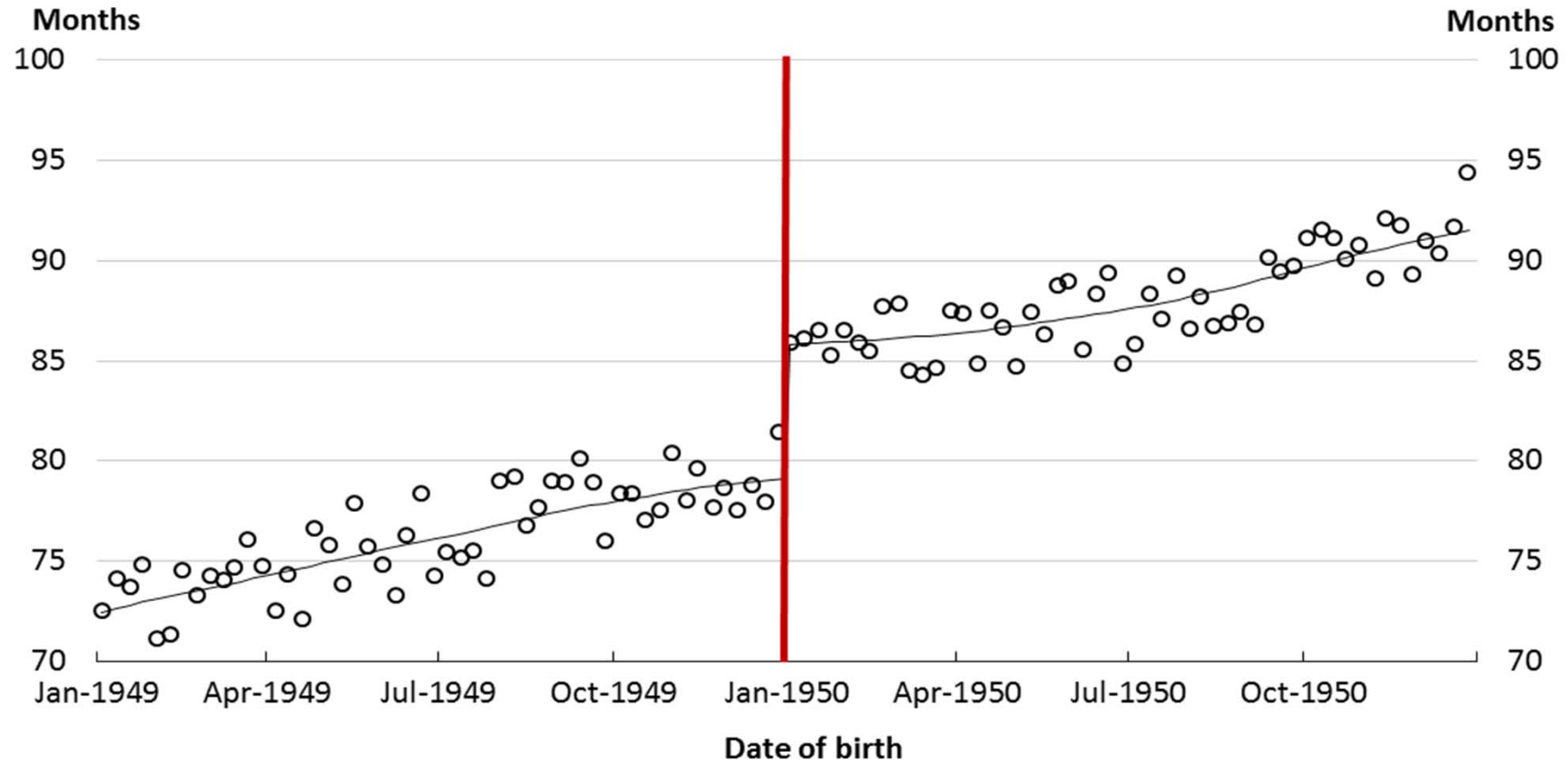
The real time income registry: Make it happen

- **Linking benefits to the registry in 2020 can be a game-changer:**
 - Allow for real-time coordination of benefits and earnings.
 - Allow for better tools (apps) to evaluate financial consequences of work decisions.
- **Technical and legal design and implementation important success factors.**





Increase the unemployment tunnel age limit in line with other pensions (at least)



1. The unemployment tunnel age threshold was increased from 55 to 57 years in 2005, only applicable to individuals born after 1949.

Source: Kyyrä and Pesola (2017).



Mattila considering extending earnings-related benefits to all unemployed

FINLAND / CREATED: 06 MARCH 2018



News 4.3.2018 11:54 | updated 4.3.2018 11:54

Blue Reform's Terho pitches new form of basic income, not a "stipend for being lazy"

The breakaway populist party, Blue Reform, proposes an alternative bundled state benefit to replace Finland's current mosaic of state aid.

