Removing Poverty Traps: Taxation and Welfare Reform in Australia

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Abstract

This article uses data on the interactions of income taxation and state welfare transfers on effective marginal tax rates (EMTRs) in Australia to argue policy reforms for removing poverty traps created by high EMTRs. This highlights the need for state welfare and income taxation reforms to target those elements of income taxation and social welfare interaction that are most significant for high EMTRs and for high EMTRs extending across wide incomes ranges. Proposed welfare changes involve simultaneous reductions in base-level state welfare transfer payments, along with eligibility for supplementary transfer payments for able persons that are proportional to market labour activity. Proposed taxation changes include removal of distinctions between taxable and tax-exempt state welfare transfers and a gradually-progressive revised taxation scale.

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1. Poverty Traps

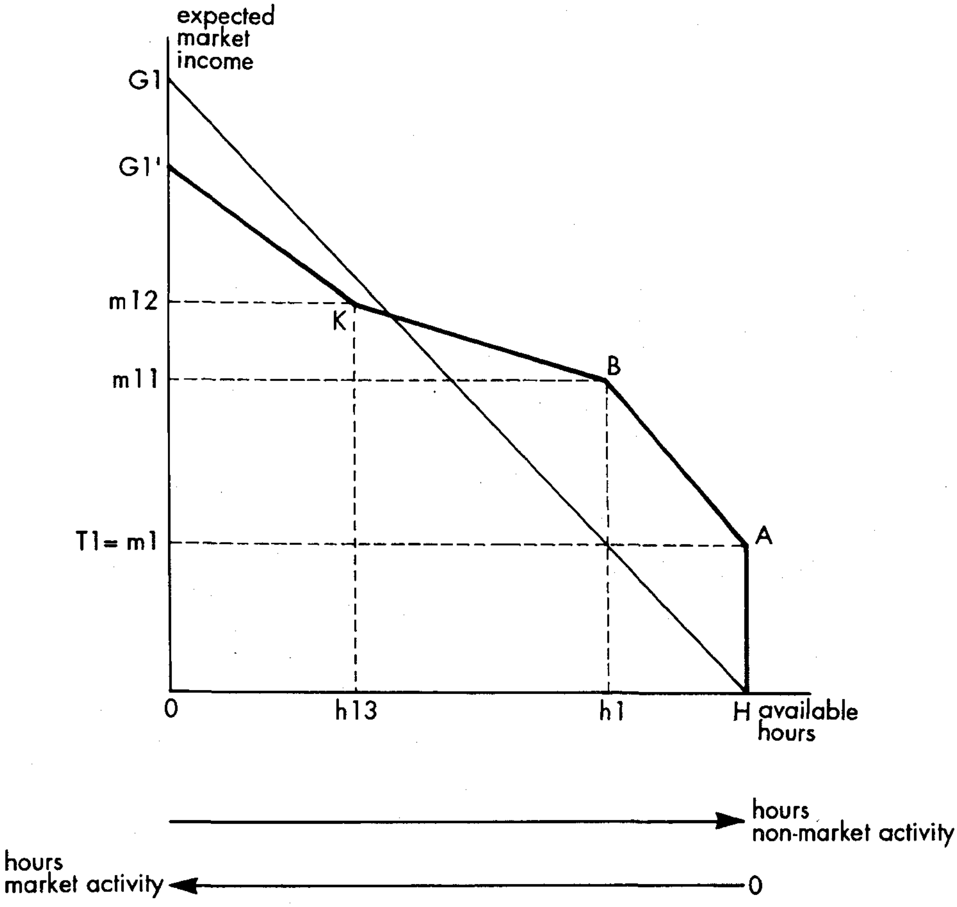
Poverty or welfare traps arise where the interaction of social security and income taxation systems result in net increases in disposable incomes that are insufficient to call-forth offers of market labour services and that lead to continuance in low-income welfare state dependency. Poverty traps are usually indicated by high "effective marginal tax rates" (EMTRs). Where increases in incomes from wages and sources other than state welfare transfers[1] lead to withdrawal of state welfare transfers, EMTRs state the percentage difference between increments in gross-incomes and incremental changes in disposable incomes.

Assessing whether the interaction of taxation and social security systems "trap" people in the poverty of state welfare dependency depends upon more than simply the *levels* of EMTRs (for example, whether EMTRs exceed the top of the PAYE tax-scale). Poverty traps are stronger the longer the *ranges* of non-transfer-incomes over which high EMTRs apply. Understanding the factors that most influence EMTRs and the ranges of non-transfer-incomes that attract high EMTRs points to key policy changes for taxation and welfare reform.

Although many studies on EMTRs are available for Australia,[2] wide understanding of the policy issues is inhibited by the complexity of EMTR calculations and their presentation (e.g., Edwards, 1985), or by a clouding of the key causal influences for high EMTR estimates (e.g., SSR, 1988). This paper uses a graphical exposition of poverty traps that highlights impact upon activity choice within and outside the labour market, and presents simple tabular data for 1990 that illustrate (a) the components of EMTRs, (b) income ranges for high EMTRs, and (c) upper non-transfer-incomes ranges for high EMTRs as a proportion of adult average weekly earnings (AWE). This highlights the need for reforms to target those elements of income taxation and social welfare interaction that are most significant for high EMTRs for persons seeking to move from state welfare dependency to wage employment.

Figure 1 shows a budget constraint between (a) expected money incomes from market labour activity, and (b) hours applied to non-market activity. This budget constraint shifts to A where state welfare transfer payments are received, and rises parallel with the original budget constraint between A and B where non-transfer-incomes are within the "free area" allowed to recipients of state welfare transfers. Notes to Figure 1 more fully explain the HABKG1' line. The BK section in Figure 1 illustrates the range over which substitution of time from non-market activity to market activity leads to the withdrawal of state welfare transfers and to smaller increases in disposable money incomes. EMTRs in excess of 100 percent give rise to

Figure 1: Activity Choice: Influence of poverty traps for market and non market activity.



Notes:

G1 = (H . w1) . (prob.); where H is available hours, w1 is the going bottom-rate hourly-wage before taxation, and prob. is the expected likelihood of obtaining a job at w1. G1' shows after-tax money income where all available hours are applied to market activity. Production of non-market goods and services is a direct function of the allocation of hours outside the market.

The HABKG1' line is formed where state welfare transfers for wage-unemployment of m1 dollars lift the HG1 budget constraint to point A. The AB section represents for the going low expected wage rate of w1 the range of hours from zero to Hh1 over which increased market labour activity involving non-transfer incomes of up to m11m1 dollars involves no reduction in state welfare transfers (the "free area"). Extension of market activity beyond Hh1 hours gives rise to both pay-as-you-earn (PAYE) tax deducations and to tapered withdrawal of state welfare transfers. The BK section thus illustrates growth in disposable incomes with increasing market labour activity over the "tapered withdrawal" range. At Hh13 hours market labour activity and a disposable income of m12 dollars, state welfare transfers for wage-unemployment are zero. The construction of the Figure as developed in McGavin (1992, p. 25) also locates a change in PAYE rate at before-tax earnings for Hh13 hours at an expected wage of w1, and the KG1' section shows after-tax increases in market incomes as further available hours are applied to market activity. The HABKG1' line thus illustrates a budget constraint between disposable money incomes and non-market activity, the shape of which is determined by welfare and taxation arrangements, with the BK section illustrating welfare and taxation interactions creating a poverty or welfare trap. G1 without the "prime" sign illustrates gross or before-tax market income; G1' illustrates net market income after taxation and net state welfare transfers for wage-unemployment. The exposition of course also applies for other state welfare transfers, such as supporting parent payments, etc.

Drawing of this figure was kindly undertaken by Corporal Cheryl Kluver of the Australian Defence Force Academy.

Source: Adapted from McGavin (1992, p. 27).

reductions in disposable incomes with increases in market labour activity, and are thus marked examples of poverty or welfare traps. It is an empirical question to judge where EMTRs are "high" and are thus associated with continuance in the poverty trap of low-income state welfare dependency. For example, using data for AWE for full-time adult male non-managerial employees for Australia at May 1990 ($576.80) and for median AWE ($533.30) as an indication of wages received gives for persons moving from unemployment welfare dependency an EMTR of 40.25 percent.[3] That is, the relevant section of the budget constraint for these persons as illustrated in Figure 1 increases at 59.75 percent of each extra dollar earned at the relevant gross hourly wage.

2. EMTRs by Recipient Category

EMTRs are determined by six influences: (1) the amount of the base-rate of state welfare transfers, (2) the rate of expected hourly pay for market labour activity, (3) the relevant incremental marginal tax rate and steps in that rate scale, (4) any tax rebate withdrawal-rate, (5) the Medicare levy rate (including shade-in rate), and (6) the impact of Department of Social Security (DSS) income tests.

Table 1 provides an illustration that takes the mean for the lowest-decile of weekly earnings for adult males at May 1990 ($317) for a level of non-transfer-incomes. Relatively low EMTRs apply for single persons and for married persons with a dependent spouse and with a dependent spouse and one dependent child. But for persons with a dependent spouse and two or more dependent children, a 121 percent EMTR is estimated. Thus, under conditions obtaining at May 1990, persons offering market labour services at an average rate for the lowest-decile of male AWE would actually have their disposable incomes *reduced* by 21 cents for each additional dollar earned.

This outcome arises because tax-exempt state welfare transfer payments are being replaced by taxable income.[4] Tax-exempt state welfare transfers rise with the number and status of dependants as claimed by recipients. For persons with non-transfer-incomes falling in the May 1990 average for the lowest-decile of wage non-transfer-incomes, the interaction of the various influences determining EMTRs is dominated by the Department of Social Security income test. In short, for these recipients of unemployment transfers, it is the replacement of taxable income by non-taxable income such as child allowances and private rental-assistance that determines EMTRs at or in excess of 100 percent at these non-transfer-income levels.

Table 1. Components of EMTRs (percent) for non-transfer-incomes set at lowest-decile adult male AWE, May 1990 ($317)

Recipient class for unemployment transfer	EMTR	Marginal tax rate	Rebate withdrawal	Medicare levy	DSS withdrawal
S1	22.25	21	0	1.25	0
S2	22.25	21	0	1.25	0
MX	21.00	21	0	0	0
MXIA	21.00	21	0	0	0
MX1B	21.00	21	0	0	0
MX2A	121.00	21	0	0	100
MX2B	121.00	21	0	0	100
MX3A	121.00	21	0	0	100
MX1A2B	121.00	21	0	0	100
MX4A	121.00	21	0	0	100
MX2A2B	121.00	21	0	0	100

Notes: Non-transfer-incomes are incomes other than state welfare transfer payments to persons in wage unemployment.

S1 = single aged under 18 years. S2 = single aged 18 years and over. M = Married. X1, X2, X3, X4 = with dependent spouse (X) and with one to four dependent children. A = dependent child/children aged under 13 years. B = dependent children aged 13 years and over. R = receiving private rental-assistance. (Thus, e.g., X3R = welfare recipient with dependent spouse and three dependent children and also in receipt of private rental-assistance).

EMTR component of Rebate Withdrawal Adjustments (of 6.25 or 12.5 percent) arises from a rebate directed to ensuring that no income tax is payable by taxpayers whose only income is a state welfare transfer payment. At the relevant AWE at May 1990, the rebate withdrawal was zero. The Medicare levy accelerated phase-in rate is 20 per cent; at the relevant AWE, the range of the accelerated rate is passed, and the rate applying to the whole of taxpayer income applies (1.25 percent).

Estimation of the lowest-decile of adult AWE was undertaken by linear interpolation of class-interval distribution of ABS 6305.0.

Average weekly earnings (AWE) data are published for the mean and for the median and may be estimated for the lowest-decile for full-time adult male non-managerial employees. Only arithmetic mean data are available for ordinary-time earnings for males (adult and junior). Award-hours earnings are ordinary-time; weekly employment of 35 hours or more is full-time.

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Source: Compiled from Cashel and McGavin (1990, Annex E), who used Australia (1989) (1990), DSS (1990) and Keating (1990), and ABS 6305.0, May 1990.

3. Non-Transfer-Income Ranges for High EMTRs

Table 1 shows only EMTRs for various categories of recipients having non-transfer-incomes at the mean for the lowest-decile of weekly earnings for adult males at May 1990. Of greater interest are the non-transfer-incomes *ranges* over which high EMTRs apply. Table 2 gives for the various categories of recipients the non-transfer-income the ranges over which there occur EMTRs in excess of the 1990 top marginal rate for personal income taxation (48.25 percent). For weekly non-transfer-incomes over $70, the EMTRs in these ranges in fact are 100 percent or more, so the table also serves to give the *ranges* of non-transfer-incomes over which EMTRs *of 100 percent or more apply* for various categories of recipients (see Table 2 notes).

These data show for all categories that increases in earnings over a wide range result in no change or *negative* increments in disposable incomes, and that the non-transfer-incomes ranges over which there occur no change or negative changes in disposable incomes *lengthen with the number and ages of dependants* -

- For single welfare recipients aged under 18 years,[5] the weekly non-transfer-income range is $70-154 (while junior male ordinary-time AWE at May 1990 were $257.30).
- For married recipients with a dependent spouse and four dependent children (two under and two over 13 years of age)[6] the weekly non-transfer-income range is $70-391.
- For the same category of married recipient who is also in receipt of a private rental-assistance,[7] the weekly non-transfer-income range is $70-416 (while adult male ordinary-time AWE at May 1990 were $497.40).

The practical seriousness of the length of the ranges over which EMTRs of 100 percent or more apply would be further emphasized by comparison with *median* adult male ordinary-time earnings or with estimates of *lowest-decile* adult male ordinary-time earnings - but these data are not available for *ordinary-time* earnings.

4. Non-Transfer-Incomes Ranges and Adult AWE

Because data on earnings distributions for ordinary-time earnings are unavailable, comparison is made with (a) the arithmetic mean, (b) the median, and (c) the lowest-decile AWE for adult males. Data from Table 2 for the *top* of the relevant non-transfer-incomes ranges for the various categoriesof of recipients of state welfare transfers to persons in wage unemployment

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Table 2. Incomes ranges (dollars) over which non-transfer-incomes attract EMTRs in excess of the top personal income tax rate (r)*, May 1990.

Recipient class for unemployment transfer	NTY + weekly dollars
S1	30-154
S2	30-175
MX	30-272
MX1A	30-296
MX1B	30-307
MX2A	30-320
MX2B	30-342
MX3A	30-344
MX1A2B	30-366
MX4A	30-368
MX2A2B	30-391
MXR	30-297
MX1AR	30-321
MX1BR	30-332
MX2AR	30-345
MX2BR	30-367
MX3AR	30-369
MX1A2BR	30-391
MX4AR	30-393
MX2A2BR	30-416

Notes: * r = the top marginal rate on the personal income tax scale at 1 January 1990 of 47 percent plus 1.25 percent Medicare levy = 48.25 percent. For S1 and S2 non-adult earnings are used in making comparisons, because not all awards specify 18 years as adult.
+ Non-transfer-incomes up to $30 per week fall within the "free-area", and between $31 and $70 per week within the 50 percent "shade-in area". Once $70 non-transfer-income is exceeded, the loss of state welfare transfers for each additional dollar of other income is a full dollar, and these income ranges give EMTRs *in excess of 100 percent.*

Source: Compiled from Cashel and McGavin (1990, Annex E).

are presented in Table 3 as percentages of mean, median, and lowest-decile adult male AWE at May 1990.

Arithmetic mean AWE. Except for recipients with a dependent spouse but without dependent children, the top of the weekly non-transfer-incomes ranges is higher than 50 percent of *mean* adult male AWE.

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Table 3. Non-transfer-income maximum* as a percentage of adult male AWE, May 1990.

Recipient class for unemployment transfer	Mean AWE	Median AWE	Lowest-decile AWE
MX	47	51	86
MX1A	51	55	84
MX1B	53	57	97
MX2A	55	60	101
MX2B	59	64	108
MX3A	59	64	108
MX1A2B	63	68	115
MX4A	64	69	116
MX2A2B	68	73	123
MXR	51	55	94
MX1AR	55	60	101
MX1BR	57	62	105
MX2AR	60	64	109
MX2BR	63	68	115
MX3AR	64	69	116
MX1A2BR	68	73	123
MX4AR	68	74	124
MX2A2BR	72	78	131

Notes: See Table 1 notes. AWE is for full-time adult male non-managerial employees mean = $576.80, median = $533.30, estimated lowest-decile = $317.00.
* The relevant maximum non-transfer-incomes by class are found in Table 2.

Sources: See Table 1

Median AWE. For *all* recipient categories, the top of weekly non-transfer-incomes ranges is more than 50 percent of *median* adult male AWE, and is 73 percent of the median adult male AWE for welfare recipients with a dependent spouse and four dependent children (78 percent, where rental-assistance is also received).

Lowest-decile AWE. Where the comparison is between the top of the non-transfer-incomes ranges and estimated mean for the *lowest-decile* of adult male AWE, only four recipient categories show EMTR estimates of *less than* 100 percent. All recipient categories with a dependent spouse and at least two dependent children face an upper range of non-transfer-incomes that *exceeds* the lowest-decile adult male AWE at May 1990. For example, for a married person with a dependent spouse and four dependent children (two aged under 13 years and two aged 13 years and over and in receipt of private rental-assistance), the upper range of non-transfer-income exceeds lowest-decile adult male wage earnings by 31 per cent.[8] That is, the BK section as illustrated in Figure 1 has a negative slope for these welfare recipients, and this negative slope extends to non-transfer-incomes that are greater than the mean for the lowest-decile of weekly earnings for adult males.

In short, welfare recipients in these categories face no increase or *reductions* in disposable incomes as they undertake market activity for hours giving earnings in excess of the "free area", and this often continues to be the case where full-time wage earnings exceed lowest-decile male AWE. Clearly this creates barriers for movement from welfare dependency to wage employment or self-employment that require reform.

5. Welfare Reform

Three key recognitions are necessary for the formulation of welfare reform. Namely -

- Welfare recipients may be "losers" rather than "choosers", and policies that are one-sided in harshness will evoke political backlash.
- Pervasive anti-competitive influences in the Australian labour market will not readily be reversed by legislative means, since reversal involves a process of complex changes in firms and in workplace organizations that will occur over time.
- Job growth through deregulation of minimum wages by legislative processes may occur slowly, with slow expansion of opportunities for low-wage employment.

Proposals for welfare reform raised in McGavin (1992) are designed to "linearize" the budget constraint between market and non-market activity, so that substitution of time from non-market activity to market activity leads to adequate increments in disposable incomes across the relevant ranges for activity choice. That is, they eliminate of the flat BK section of Figure 1 that occurs where increases in market labour activity bring little or even negative rewards for significant categories of recipients of state welfare transfer payments.

The proposals involve two key interacting changes, namely -

- substantial reductions in base-level transfer payments, *and*

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- eligibility for supplementary transfer payments for able persons that are proportional to payments for market labour activity (whether low-wage employment or fee-for-service self-employment).[9,10]

Thereby, the poverty trap section of the outside-market/inside-market allocation of activity is removed, and incentives operate to help able persons to move off or to reduce net welfare dependency (while at the same time *increasing* their disposable incomes). Under present arrangements, people who are capable of contributing to market production, consume market goods and services to which they have access through state welfare transfers, but contribute little to the production of these goods and services. The proposals are designed to reverse this "dependency culture" that is part of structural wage-unemployment in Australia,[11] so that able people have opportunities *and* incentives to contribute to market productive activity. The proposals involve "welfare that helps self-help" and aim to meet objectives of humanity, of economy, and of administrative and political practicability.

Assessing the impact of major structural changes in state welfare provision (and of taxation - see below) is assisted by sophisticated general-equilibrium modelling.[12] The results of such modelling exercises vary greatly according to complex assumptions employed, and it may be difficult with confidence to assess the specific numerical results generated by such studies (Head, 1990, p. 83). This suggests that reforms should be introduced on an announced-schedule that allows for experimental adaptation in implementation.

Successful implementation of welfare reforms also requires close integration of state welfare payments with a restructured taxation system that circumvents the problems of withdrawal of transfer payments as these are now encountered in creating poverty traps. These related reforms are now outlined.

6. Integration with Tax Reform

Taxation reform has first to target the withdrawal of tax-exempt state welfare transfers that cause EMTRs of 100 percent or more (Table 1). The effects of Medicare and Rebate Withdrawal Adjustments on raising EMTRs could be eliminated by incorporation of Medicare levy in a revised progressive-taxation scale[13] and by integrating inflation-adjustment of both the taxation-rate scale and state welfare transfer payments. Likewise, high EMTR effects of private rental assistance can be eliminated by the integration of state welfare transfers for additional child and private rental assistance with Family Assistance Supplement (FAS).

These reforms need to be combined with the introduction of a gradually-progressive revised income-taxation scale that provides for smooth transition from (a) positive net transfers to persons to (b) negative net transfers to persons (that is, from negative net taxes to positive net taxes). Introduction of a gradually-progressive scale would be eased by the reduction (or even the abolition) of the zero-rate taxation threshold.

Since the proposals combine expanded market labour activity with receipt of state welfare transfers, expansion in the numbers of people receiving state welfare transfers could occur. But gradually-progressive income-taxation means that increases in personal disposable incomes can occur along with reductions in *net* state welfare transfer payments to persons (compared with net state welfare transfers to persons under existing "free-area" and "shading-in" arrangements). That is, the number of persons receiving state welfare transfers may increase, but total state welfare transfers need not increase (or need not increase markedly). The proposed welfare arrangements are thus ones that "help finance welfare".[14] Where concerns arise about cumulation of people in state welfare dependency under a regime of gradual-transition from net positive to net negative state welfare transfers, these may be addressed by the flexible use of appropriate eligibility and duration conditions of the kind that apply under the "job-search-allowance" and "new-start" programs (Australia, 1990).

These reforms target for change those elements that are most significant for high EMTRs over ranges relevant for persons moving from welfare dependency to market labour activity. The following points summarize these reforms:

1. Remove the distinction between taxable and tax-exempt state welfare transfers (where appropriate, with adjustment in levels of previously non-taxable transfers).
2. Incorporate Medicare taxation [levy] in a revised progressive income-taxation scale for persons (thereby removing the 20 per cent Medicare phase-in range).
3. Integrate inflation-adjustment of the taxation-rate scale and of state welfare transfer payments (thereby eliminating the need for Rebate Withdrawal Adjustments, and thus removing EMTR components of 6.25 or 12.5 percent across the relevant adjustment ranges) (see Table 1 notes).
4. Integrate state welfare transfers for additional child and private rental-assistance with Family Assistance Supplement transfers, and integrate both with a multiple-step progressive-taxation scale providing for both vertical and horizontal equity.[15]

5. Use a gradually-progressive revised taxation scale so that rising negative transfers (taxes) progressively replace positive transfers (state welfare payments) to achieve

   both -

   (a) integration of taxation and state welfare transfer systems with gradual transition from net positive transfers to net negative transfers, and

   (b) continuous rise in disposable incomes with increases in market labour rewards (hourly earnings rates) and with increases in market labour activity (hours).[16]

6. Reduce - or even abolish - the taxation threshold (thereby assisting a gradual progressivity from a low bottom-of-scale taxation rate).

This tax-welfare framework is one where state welfare transfer payments are more clearly seen as "positive transfers" and taxes more clearly seen as "negative transfers". This allows increased focusing of wages-policy on market-activity or employment targets, and clearer focusing of changes in taxation and state welfare transfers on income-distribution targets.

7. Progress in Implementation of Welfare and Taxation Reform

Implementation of the Social Security (Poverty Trap Reduction) Act 1985 involving various amendments to the Social Security Act have ameliorated some welfare traps. Gallagher *et. al.* (1992, pp. 33,40f) instance the removal of the separate income tests for rent assistance and increase of pension "free areas" (July 1987), introduction of pensioner earnings credits (November 1987), extension of fringe benefits to those returning to wage jobs (June 1990), wage-employment entry payments (January and November 1991), and increases in pensioner rebates so that full-rate pensioners are not liable for tax. These changes have, however, concentrated on pensioner recipients and sole parent benefit recipients. The "free area" for persons receiving state welfare transfers for wage-unemployment has not changed from the weekly level of $30 set in May 1986, and earnings credits that allow averaging of incomes for purposes of determining state welfare transfers, have not been applied to recipients of wage-unemployment state welfare transfers.

Integration of child family payments for persons in receipt of state welfare transfers (including transfers for wage-unemployment) and for persons independently supporting themselves were foreshadowed in Australia (1988, p. 166), and implemented by the Social Security (Family Payment) Amendment Act 1992, with 1 January 1993 as the intended date of effect of legislation (see the "time line" in Appendix 2 of Gallagher *et. al.*, 1992). The effect of these changes is to combine various state welfare transfers for children[17] into a Family Allowance, with eligibility being governed by the age and number of children and income and asset tests, rather than by receipt of other state welfare transfers (Media Release of Minister for Family Support, Parliament House, 7 May 1992). This integration is expected to reduce EMTRs for persons moving from welfare dependency to earned income.

No significant changes affecting welfare trap EMTRs were announced in the 1992-93 Budget, and remedies are again sought in increased compliance administration (Australia 1992, p. 3.108f).

The *Fightback!* package of the Coalition Parties involves a major restructuring of income taxation and of taxation on goods and services that would significantly impact upon welfare trap EMTRs. Changes proposed include increasing the annual threshold for income taxation from $5400 to $7000 and reduction of the bottom-of-the-scale rate from 20 percent to 16.2 percent (Fightback 1991, p. 15). Increases in state welfare transfer payments are proposed to offset the effects of the introduction of goods and services taxation (GST) (Fightback 1991, p. 151). Implementation of these proposals would raise the income levels at which welfare traps occur and extend the range over which these welfare traps occur.

Overall, the significant reforms to reduce poverty and welfare traps introduced by the Government have been ameliorating the impact of high EMTRs. Further policy changes being considered by the Department of Social Security in the second stage of the Review of Poverty Traps raise the prospect of *separation* of taxation and social security systems, rather than more fundamental reforms for the *integration* of taxation and welfare reforms in Australia although the doubtful suitability of this separation for recipients of wage-unemployment and sickness allowance transfers is acknowledged (Gallagher *et. al.* 1992, p. 35).

The focus in the presentation of *Fightback!* concentrates on increasing private compliance costs incurred by recipients of state welfare transfers (which also involve increases in public costs for the administration of social security rather than focusing on altering the incentive structure of relative rewards between state welfare dependency and market labour activity (for example, Fightback 1991, p. 209f, and the tabulation of the Coalition and of the Government rules for Job Start Allowance by the Shadow Minister for Social Security, Parliament House, 24 July 1992).

8. Summing-Up

The integration of taxation and state welfare transfers, incorporating work-related incentives, forms the key relationship of income taxation reform with proposals for welfare state and labour market reforms. These taxation reforms are recognized as implying the need for a major widening of the tax base. For example, Head (1990) suggests the introduction of value-added taxation (incorporating appropriate compensatory arrangements for the effects of indirect taxation on subsistence components of consumer spending).[18] The purpose of this brief article is to highlight the need for reforms to target those elements of income taxation and state welfare transfers[19] that involve interactions that are most significant for high EMTRs and for high EMTRs extending across wide incomes ranges that include low-income earnings (such as lowest-decile adult AWE).

Notes

1 Hereafter termed "non-transfer-incomes".

2 For example, Podger *et. al.* 1980a,b, Edwards 1985, EPAC 1988, Freebairn *et. al.* 1988, SSR 1988, Saunders *et. al.* 1989, Bascand and Trengove 1990, and Gallagher and Ryan 1992. Gallagher *et. al.* 1992 gives EMTR calculations, by components, for Job Start Allowance and Sole Parent Pensioner recipients as at August 1991.

3 Subsequent AWE data in this paper are for full-time non-managerial male employees.

4 Gallagher *et. al.* (1992, p. 31) recognize this, but do not follow-through this recognition in their policy recommendations.

5 Shown in Tables as S1.

6 Shown in Tables as MX2A2B.

7 Shown in Tables as MX2A2BR.

8 See the last entry in Table 3 for MX2A2BR.

9 Separate supplementary payment provisions should apply for persons who by reason of age or incapacity are unable to engage in regular productive activity in the market.

10 Note that these supplementary transfers are *not* of the "workfare" kind (see, McGavin, 1992, p. 39f).

11 OECD (1992, p. xi) make the important observation also argued in McGavin (1992) that inappropriate state welfare policies contribute to high levels of structural wage-unemployment.

12 For example, Agrawal *et. al.*, 1990, and Piggott, 1990.

13 Gallagher *et. al.* (1992, p. 36) also note this.

14 Critics may note that the proposals may increase "churning" (government activity of taxing or negative transfers and positive state welfare transfers or negative taxing). This may be a price to be paid for achieving lower net transfers *and* inducements to increase market production of goods and services (through low-wage-employment and self-employment), with attendant spillover and multiplier effects.

15 Vertical equity objectives are met in the rate scale by the fact that more tax is paid by persons with a higher taxable-income than by those with relatively lower taxable-income (that is, by progressivity of the tax-scale). Horizontal equity is met by the use of rebates that enable recognition that a single-income family has reduced capacity-to-pay tax compared with a person without dependants who receives the same income.

16 The term "market labour rewards" includes rewards from self-employment (see McGavin, 1992, p. 39).

17 These transfers being Family Allowance, Family Allowance Supplement, Additional Pension and Benefit, and Guardian Allowance and Rental Assistance for Families with Children.

18 See Stephens (1990) for a critical assessment of flattening of the taxation rate-scale with introduction of indirect taxation and tax-rebates/transfer-payments for low-income and middle-income families.

19 In principle, these transfers include cash and in kind transfers although the examples given in this paper are for cash state welfare transfers (see Table 1 notes).

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