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POLICY POINT

Stay on target

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How best to help?

Everyone agrees the Government plays a critical role in helping New Zealand through the economic consequences of the Covid-19 global pandemic. But the best tools are not always clear. So far, assistance has focused on enhancing the benefit system, supporting people through required periods of self-isolation and backing firms to maintain employment.

All policy options will fail in different ways, but perfection is the wrong standard. The public sector has done admirable work in swiftly implementing new support schemes on tight deadlines and allowing the money to flow. But it is not enough. Many apparently viable companies are shutting down or laying off staff. Those workers will not be helped by current measures.

The difficulty in ensuring support reaches the vulnerable has led to renewed calls for a universal basic income (UBI). Sometimes touted as a replacement for all benefits, the UBI would provide each Kiwi with a minimum fixed income. It would replace the administrative costs of the current system with a simple cheque to everyone. Targeting would be replaced by universalism.

The arguments against the scheme during normal times are well-canvassed. It is impossible, through a UBI, to provide enough support to the worst off without creating crippling tax levels. Today, the worst-off receive benefits through multiple overlapping systems. Providing a UBI-level of support to everyone would be impossible. But failing to provide it would result in layering the contemporary benefit system on top of a UBI – cancelling out the key benefits of a UBI.

But could a UBI-like scheme work in a crisis? Rather than an income designed to replace all benefits, or one intending to be in place over a long period, could the Government simply provide a few thousand dollars to each person in the country, no strings attached, so everyone has the minimum cash necessary to get through the year?

Advantage: UBI?

A temporary and limited UBI has some advantages. It slices away administrative costs and could be delivered simply. While it is without strings, those with higher earnings would see a third of their UBI income clawed back through standard income taxes this year, and the rest paid back in future years as the debt to fund the payments is paid off. And it would help protect anyone who had fallen through the cracks of other systems.

But it does not solve the underlying trade-off of a UBI: giving everyone a lump sum does less good for those in the most need than targeted assistance. Even a one-off payment of only $5,000 per capita would cost $25 billion, less any amount clawed back through taxes this year, with the remainder paid off over time. Without better alternatives in this crisis, that could be a cost worth bearing. But better methods exist to target support where it does the most good.

Stay on target: employment support

This paper suggests a combination of initiatives to help avoid lay-offs and support firms to bounce back quickly when the pandemic eases.

While the Government's existing wage support measures are laudable, they have not prevented lay-offs and firm closures. It would be impossible and undesirable to prevent all closures, but we can design better alternatives that help viable firms to weather the storm. We suggest a model based on Germany's Short-Time Work scheme (STW).

The scheme allows companies to reduce worker hours while the Government tops up those workers' wages. That shift could sharply reduce the number of redundancies. While the scheme does not help those who are not in work, or who have already lost their jobs, it reduce future redundancies.

Additional policy changes could do more to boost employment. The Government should allow companies to defer 2020 taxes to a combined 2020-2021 tax year, enabling them to count current losses against future profits for a reduced tax burden. This would improve short-term cash flow and avoid shuttering.

The Government could also provide wage support to all firms equivalent to the increase in the minimum wage since 2017. This would maintain worker earnings while reducing the cost of labour to firms, not only helping to avoid lay-offs but also encouraging some employers to increase staffing levels.

Together, these policies will reduce the burden of the current crisis by sharing it more equitably through the overall tax system. But even this will not be enough. Proponents of the UBI correctly point out the benefit system must have stronger backstop support in a pandemic-induced recession.

Stay on target: Building a better backstop

This paper suggests measures which could provide substantial assistance to those seeing sharp reductions in earnings and difficulties in meeting fixed spending commitments.

The first is a change in tax. Everyone should be allowed to combine their 2020 and 2021 tax years, with a suspension of automatic tax withholding (PAYE) during this crisis to improve cash flow for individuals and families. If a person's earnings drop sharply in 2020, they could defer all tax payments to 2021. Revised tax thresholds for a combined tax year would encourage those whose earnings have not dropped to file their taxes as usual at the end of the current tax year. Again, this is an example of targeted support: those with sharper earnings reductions would get more assistance.

The Government could go further by setting a longer, optional tax year spanning the last two quarters of 2019, all of 2020 and all of 2021. Those electing to take the longer combined tax year would receive immediate rebates on taxes paid in the last two quarters of 2019. This structure would ensure anyone without substantial earnings reductions in 2020 face higher overall taxes if they chose to combine tax years, while those with substantial drops in income would benefit by merging the tax years.

Finally, New Zealand's student loan scheme could be broadened to all Kiwis as final backstop. The scheme allows students to borrow up to $231.92 per week in interest-free living costs: a little over $12,000 per year. It is paid back through the tax system, with payments starting when borrowers earn more than $19,760 annually.

During this crisis, and only during this crisis, every Kiwi should get access to the student loan scheme.

Individuals would be allowed to borrow up to the $12,000 annual cap. If the amount borrowed is less than their drop in earnings in 2020, relative to their earnings in 2019, the entire amount borrowed would be interest-free. Any amount borrowed in excess of that individual's drop in earnings would be subject to normal commercial interest rates – the interest rate that applies to student borrowers living overseas.

The scheme has obvious merits.

It is targeted: those experiencing real drops in income will be eligible and can easily opt in. It is administratively simple: existing systems can be used to administer it. Much of the administrative cost is backloaded: rather than assessing now whether anyone's drop in earnings is more or less than the $12,000 cap, it would automatically be assessed at the next tax filing period with interest applying on excess borrowing. This especially matters when administrative agencies will be scrambling to implement a range of initiatives.

It is less costly than a UBI and better assists those in the greatest need: instead of giving a small amount to everyone, all Kiwis could borrow to cover their income loss to a maximum of $12,000. And, while all borrowed money must be repaid, this is achieved slowly and automatically through the tax system on a subsidised interest rate.

Proponents of the UBI are correct about one big thing – existing schemes are insufficient for the problem at hand. But there are better solutions allowing more targeted assistance to those most in need. Why give high earners a transfer when the Government could do far more for those who have taken the largest hit?