

Summary

The Swedish welfare state stands on three legs – the provision of services, the provision of mandatory social insurance and the provision of income support. Income support benefits consist of either of two categories. The first is benefits for specific groups, such as parents or persons with functional disabilities. The second category consists of benefits designed to give basic income support with the aim of preventing poverty. This study examines the broad spectrum of benefits in the latter category with the aim of identifying problems and proposing changes that both simplify relatively complex benefit rules and increase economic efficiency in Sweden's provision of basic income support.

The study begins with an overview of the present order with mandatory insurance provided by the public sector complemented with income support benefits for specific groups and provision of basic income. This order of doing things is contrasted with two other orders that have commanded considerable attention in the literature – the basic income proposal, possibly combined with a flat tax, and lifetime welfare accounts. It is argued that even though these alternatives have attractive features in terms of economic efficiency, it would be practically impossible from both a political and a technical point of view to propose a full scale transition from the present order to either of these alternatives.

The study discusses the problems with the existing income support systems for people with limited means and formulates proposals for change. The proposals are aimed at simplifying rules so that they are easier to understand and administer. For working age persons the changes proposed aim to reduce or eliminate benefit rules that restrict labor supply and inadvertently create poverty traps.

The study presents three proposals. The first proposal involves the extra income support provided to old age pensioners and

persons receiving disability benefits. The old-age benefit is based on contributions paid into notional accounts and the amount of the disability benefit is based on earnings prior to the grant. Either short contribution histories in the case of the old age benefit or low or no earnings prior to the grant of disability lead to a low benefit. Persons in such circumstances are entitled to a minimum guarantee benefit, both as old-age pensioners and within the disability system. This is presently supplemented by a complicated three tier system of housing allowances, based on the individual's or family's income, estimated wealth and housing costs.

The study presents a proposal that is designed to replace the present three means-tested benefit system with a single means-tested benefit with a level of generosity that, together with the income guarantee, would prevent any old-age pensioner or recipient of disability insurance from needing to seek community provided social assistance. This new benefit would be a simplified means-tested benefit based on actual income from all sources. Fictive wealth and housing costs would no longer enter the calculation. This eliminates the present arbitrary – and for this reason unfair – wealth rules. It also simplifies the administration by doing away with the arduous process of determining whether a claimant has a right to a benefit, and if so how much, based on the necessarily arbitrary determination of wealth.

The new benefit redistributes money from persons with higher to persons with lower benefits, compared with the present rules, largely because persons (families) at the top are often persons with higher housing costs, which in the proposal are no longer a factor in determining the amount of the benefit.

The second proposal would affect working-age persons. Sweden presently has a housing allowance that can be claimed by persons 18-29, not living at home, and parents of children below 18 (20 for students) years of age, who live at home. The allowance is similar to that just described and is based on means-tested income, wealth and housing costs. A little over half of the recipients of this benefit are single mothers; another about 25 percent are families with two adults; and most of the remainder are students.

The problem with the housing allowance is that it is very inefficient. Since it tapers off gradually up into income levels well over the average it provides considerable incentive for a very large number of parents (mostly women) not to increase hours of work at the margin and over a large part of the income distribution. The

same argument applies, of course, to two parent households. The benefit is also administratively complicated. It is based on household income, housing costs, housing size and wealth that is cumbersome to administer and impossible for individual's to understand.

Sweden already has a universal child allowance that provides a specified amount per child. The proposal presented in this study is to replace the housing allowance with a supplement to the existing child allowance. This would go to single parents for up to three children. The proposal abolishes the possibility for two adults with children to receive a benefit. It also abolishes support for persons 18-29. For this group, if desired, the government could adjust the rules for allowances and loans for students. For all households together the effect of the new rules is marginal. However, this is not the case for individual households. For this reason the proposal includes a transition rule that protects the present level of benefits for current recipient households. To the extent that the new rule affects applicants negatively, those affected would be limited to new applicants.

Sweden's benefit of last resort is social assistance - income support provided at the municipal level. Social assistance is means-tested against all other kinds of income. The discussion in this study focuses on the 100-percent marginal trade-off between the benefit and income up to the ceiling. One possible solution to this would be to lower the level of the benefit and then taper off the benefit from this lower level. This is considered to be in conflict with a broad political consensus in Sweden, so another possibility is examined. This is to decrease the income tax for persons with the level of income equivalent to the social assistance level. This doesn't change the marginal effects associated with the present level of social assistance but it does affect the reservation wage of individuals, increasing the propensity to seek and take work for persons on social assistance. Of course, a more general measure designed to provide incentives to increase the supply of hours worked of low skilled (low income) persons would be to reduce taxes for an even broader low-income band, which would be even more preferable.