

Introducing a Basic Income system in Spain.

Feasibility and cost.

Paper prepared for the Basic Income European Network 10th Congress
Barcelona, 19-20 September 2004

Rafael Pinilla-Pallejà* and Luis Sanzo-González**

Correspondence: Rafael Pinilla-Pallejà. Área de Sanidad de la Delegación del Gobierno en Valencia. Sanidad Exterior. Muelle de la Aduana, s/n. Puerto de Valencia. 46024 Valencia (Spain).
rpinilla@sanidad.valencia.map.es

Acknowledgements: We are grateful for financial support from “Fundación Alternativas”. The findings, interpretations and conclusions expressed in this paper are of the authors and do not necessarily represent the views of the Ministry of Public Affairs, or the Basque Government.

This document includes results from Espasim Difusión V.!. Un modelo de micro-simulación para evaluar reformas del sistema de impuestos y subsidios en España" © Levy, Mercader y Planas, 2002. A description of EspaSim can be found at <http://selene.uab.es/espasim>. The authors of the software do not accept any responsibility derived from the analysis presented in this document.

* Ministry of Public Affairs, Valencia.

** Justice, Labour and Social Security Department. Basque Government, Vitoria.

Abstract:

We present the major lines of a basic income proposal for Spain has published by 'Fundación Alternativas' early in 2004. The main aim of our work is to promote economical and political debate about basic income in our country showing several options supported by data and arguments. The proposal includes a deep reform of fiscal and social protection systems. The reform would be implemented by an income flat-tax reform and includes a simple refundable tax credit for all.

We have used the micro-simulator EspaSim to analyse the feasibility and potential cost of such reform. Adjusting working and child benefit elements to reach some desired political goals the financial cost could be less than 2% of GDP and more than 70% of potential electorate would be directly benefited by the reform.

Resumen:

Presentamos a grandes rasgos una propuesta de renta básica para España que ha sido publicada por la Fundación Alternativas a principios de 2004. El principal propósito objetivo de nuestro trabajo es promover el debate político y económico sobre la renta básica mostrando diversas opciones apoyadas en cálculos y argumentos. La propuesta incluye una reforma profunda del sistema fiscal y de protección social. La reforma podría llevarse a cabo mediante un impuesto de tipo impositivo único que incluiría un crédito fiscal reembolsable para todos.

Hemos utilizado el microsimulador EspaSim para analizar la factibilidad y el coste potencial de este tipo de reforma. Ajustando las cantidades de la bonificación al trabajo y el subsidio a la infancia se pueden alcanzar las metas deseadas con un coste financiero que podría ser menor del 2% del PIB y más del 70% del electorado potencial sería beneficiario directo de la reforma.

1- Introduction

During the last years we have been working on a fiscal reform towards basic income in Spain. A working paper with the essential lines of our proposal was published early in 2004 with the support of the “Fundación Alternativas” (Sanzo-González and Pinilla-Pallejà, 2004). The main aim of this work is to promote political and economical debate about how we could reform the present tax and welfare systems to make them more appropriate to the changing world of the twenty-first century.

If we compare Spain with the main occidental European countries, it has a poorly developed welfare-state. The social spending is about 24% of GDP, 6% less than occidental European average (Calero and Costa, 2003). Thus, we still could increase our social expenditure. But in this years of “globalization” economic growth and efficiency are very important too.

Many theoretical papers point out that basic income guarantee could improve both social security and economic efficiency. In fact, we could think of basic income as a social innovation. Like a new technology, basic income could reduce some economic and administrative costs driving economy to a more healthy growth. But like technological innovation and any other innovations it means a serious challenge to the *status quo* and facing general scepticism. This is a major issue because basic income affects everybody and it is impossible to implement it against majority.

People need some time to learn and understand social innovations. For this reason we need to promote a well informed political and social debate. We need to explain ideas and arguments, but over all we need to produce sound data in order to support arguments and ideas. ¿What do we mean with basic income guarantee? ¿How much is this for us? ¿Do we have to pay more taxes?

In fact, there is not a simple answer to this questions. There are thousands of ways to implement a basic income scheme. So, the relevant questions are:

1- What kind of basic income scheme are we proposing to implement?

2- How can we reach this kind of guarantee?

2- Technical support for policy makers

These are not purely technical questions. People have much to say about this. But the design of a basic income scheme is also a technical and complex task. So, we need both social debate and technical studies working together in a probably long and winding process.

The basic income proposal we are presenting here is not a complete one. We do not think this is the basic income scheme “we must necessary” implement, but we certainly believe that it could be a good starting point to discuss our social future. With this proposal we want to help policymakers whose actions may have significant implications on the next decades to make systematic well-informed decisions.

A fiscal and welfare reform is an example of a class of problem requiring decision making under deep uncertainty. For this reason we propose to adopt a new quantitative approach to long-term policy analysis (LTPA) (in this paragraphs we follow Lemper, Popper and Bankes, 2003). This approach includes four key elements: 1. Consider large *ensembles* of scenarios, 2. Seek *robust* not optimal strategies, 3. Achieve robustness with *adaptability*, 4. Design analysis for *interactive exploration* of the multiplicity of plausible futures.

Robust decision-making tries to combine the best capabilities of humans and computers to address decision problems under conditions of uncertainty. Computer-guided exploration of scenarios can provide a prosthesis for the imagination helping to discover adaptive near term strategies that are robust over a large ensembles of plausible futures.

According to long-term policy analysis approach, in this paper we have used ‘EspaSim’ to simulate several tax reforms. ‘EspaSim’ is an integrated tax-benefit micro-simulation model for Spain. It is a software that allows the user to estimate the effect of different tax-benefit reform scenarios on the disposable income of individuals and families of a dataset. ‘EspaSim’ uses individual micro-data on income, expenditure and other

relevant variables from a dataset that is representative of the Spanish population. Given the characteristics, income and expenditure of individuals/families, EspaSim estimates the taxes/benefits that each individual should pay/get. This allows us to know, for instance, the government revenue under a specific tax scenario, who would win/lose with a certain tax-benefit reform, or what would be its effect on poverty or income inequality (Levy, Mercader-Prats and Planas, 2001).

3- A basic income scheme for Spain

In this section we present the main lines of the tax and welfare reform proposal we published early in 2004 (Sanzo-González and Pinilla-Pallejà, 2004). This proposal is based on four principles:

1. *Our goal is to guarantee a minimum income sufficient to satisfy basic needs.* In Spain there is not an official method to define poverty threshold. So we have taken “non contributive pensions within the Social Security System (NCP)” as a reference level to fix basic income goals. The levels we want to reach are (in 2003 €): 360 €/month for a person, 540 €/month for two persons (regardless age), and 110 €/month for each child or young dependent under 25 years old.

This quantities are quite modest, but enough to prevent poverty as we will see. Moreover, Spain is a large country with a quasi-federal state. We consider in this proposal a basic income scheme equal for all the country, but local government of local authorities could complement this federal income with a local basic income (Pinilla-Pallejà, 2002)

2. *The basic income scheme must improve employment.* Spain has a high unemployment rate (about 11% of active population) and unemployment is widely considered the most important social problem. So it is very important for our proposal some kind of working benefit. This benefit help us to explain that a basic income scheme is not a reform against paid work. On the contrary, our proposal is against unemployment.

3. *The management of basic income guarantee must be as simple as possible.* For this reason we have chosen a *flat income tax* with a negative income tax mechanism to pay basic income. There are three decisive reasons for this election:

- a) The negative income tax management helps us to achieve a balanced budget between tax collection and basic income expenditure.
- b) Basic income management by means of income tax allows us to ensure net progressiveness of the tax system.
- c) This is probably the best way to reduce tax evasion (tax evasion is more than 5% of GDP in Spain).

Negative income tax could present the known problem of pay delay in the case of poor people. But an individualised flat tax could allow us to compute and pay the income tax every month. This is very feasible in the Spanish case because income tax is worked out in personal terms not in family terms. So people who benefit of basic income rights could get their money every month without any delay.

4. *Basic Income guarantee must not substitute current social security benefits.* Basic Income would complement current social policies.

4- Financial cost and distributive effects

We have used the computer simulation program 'EspaSim' to try hundreds of different schemes. We have chosen one of them as an example of this simulation as follows (monetary figures are actualised to 2001 € because 'EspaSim' works with 2001's Spanish income structure):

Main characteristics of the reference basic income guarantee proposal:

A) Income Guarantee:

1. One person alone: 333 €/month or 4,000 €/year.
2. Two Persons: 500 €/month or 6.000 €/year.

3. Three Persons: Every adult 250 €/month or 3,000 €/year.
4. Any dependent person under 25 years 100 €/month or 1,200 €/Year.

B) Working Benefit: 2,000 annual reduction on taxable income.

C) Tax Rate: Flat tax of 38% on taxable income. The first 8,000 € of annual income and 2,000 € more in the case of working people do not pay tax. This way, a working person will not pay any tax on the first 10,000 €. Below 8,000 € operates the negative income tax at a 50% rate. Thus, earned income between 8,000 and 10,000 is tax-free.

D) Other social benefits: All the other social benefits remain without any change.

As we can see below in Table 1, this reform would have cost 15,051 million € more than current tax system in 2001 in Spain. This is a large figure, but in relative terms represented only 2.3% of GDP. The lesson to be stressed with this simulation is that *the overall amount to be financed is perfectly reachable in a few years without any tax burden increase*, in growing economy. Table 1 also shows that severe poverty would have virtually disappeared and relative poverty (percentage of people below 60% of median equivalent income) would have decreased from 19.8% to 10.9%. GINI coefficient (the most popular inequality index) would have decreased from 32.9% to 27.5%.

Table 1. Reference basic income guarantee proposal compared to current tax system

	Current system	Basic income proposal
Additional cost in million €		15,051
Additional cost in % of GDP		2.3%
Poverty line 60% median income	19.8%	10.9%
Poverty line 40% median income	7.8%	0.3%
Absolute poverty (4,000€ equivalent income)	7.8%	0.2%
GINI index	32.9	27.5
Percentage of losers		22.4%
Percentage of indifferent		7.2%
Percentage of winners		70.3%

Finally, although a tax rate of 38% can seem a very high one, we can see in Table 1 that 70.3% people would pay less taxes with this reform and only 22.4% would pay a little more.

5- A category by category approach

The case detailed above is just one possibility among several others. By modifying particular details, different results may be obtained. Those changes will be introduced as a result of the priorities of each society. Given that the additional cost over current system ranks rather high, changes to be introduced should be gradual if we want them to be implemented. For example, a basic income scheme can be introduced using a ‘category by category approach’. If this is the case, we have to carefully assess each of the steps to be taken at every stage. In order to select a strategy to implement a basic income scheme, the simulation programs can be very helpful again. For a better understanding of the effects of the different changes, we present Table 2, in which a sensitivity analysis between tax rates and the rest of items is shown:

Table 2. Sensitivity of reference basic income proposal to increments in tax rate

Tax rate	Cost*	Poverty**	GINI	Losers	Indifferent	Winners
37%	16,236	11.0%	27.7	19.5%	7.2%	73.1%
38%	15,051	10.9%	27.5	22.4%	7.2%	70.3%
39%	13,866	10.8%	27.4	24.4%	7.2%	68.4%
40%	12,680	10.8%	27.2	26.5%	7.2%	66.2%
41%	11,494	10.5%	27.0	28.5%	7.2%	64.3%
42%	10,309	10.4%	26.9	30.7%	7.2%	62.0%
43%	9,123	10.4%	26.7	32.9%	7.2%	59.9%
44%	7,937	10.3%	26.6	34.5%	7.2%	58.3%
45%	6,751	10.2%	26.4	35.7%	7.2%	57.0%

* Additional cost compared to current system tax in 2001 in Spain.

** Percentage of people with personal equivalent income less than 60% median income.

We could reduce financing cost increasing the tax rate. But this would mean the reform will have more ‘losers’ and less ‘winners’. In the reference scheme, for each 2% of better-off tax payers we need to increase the cost in 1,185 mill. € (approx.).

If we compare the Spanish social system with other European welfare systems we can observe three main failures. 1- Spain lacks of a general system of minimum income guarantee (although we have a significant rate of poverty). 2- Spain does not have any

universal child benefit (even though we have the least fertility rate in Europe), and 3- We have a persistent high unemployment rate in a relatively low active population. A basic income scheme could solve this failures, but usually we will need to implement it in a gradual way.

A gradual approach may take the form of quantitative gradualism starting with a partial basic income guarantee and increasing the amount of guaranteed income every year. This would be the case if we start guaranteeing half of minimum income goals. The main advantage of this option is that we can always control the cost increasing income guarantee little by little according to current possibilities every year. This kind of gradualism could seem easier to implement in financial terms, but only the most poor people would benefit for the change, and in political terms, it is very difficult to implement a policy that only benefits the most poor people. Moreover, this kind of minimalist path does not allow us to make up the deep reform we need to do in the present tax and social welfare systems.

On the other hand, a gradual approach could be qualitative or ‘category by category’. For example, we may propose to guarantee a minimum income for children, paid workers or unemployed people. This kind of gradualism could seem more difficult to implement in financial terms because it would affect large groups of people and would probably cost much more in one simple move. But if we want to reform tax and welfare systems to make them more appropriate for the world of the twenty-first century, this kind of gradualism affecting large proportions of population is our better option. Moreover, this kind of strategies have the advantage of promoting social participation and political debate. In order to facilitate well informed political debate we are going to present some more simulations.

Table 3. Sensitivity of reference basic income proposal to decrements in child benefit

yearly	monthly	Cost*	Poverty**	GINI	Losers	Indifferent	Winners
1,200 €	100 €	15,051	10.9%	27.5	22.4%	7.2%	70.3%
1,080 €	90 €	13,406	10.9%	27.7	24.6%	7.2%	68.1%
960 €	80 €	11,760	11.1%	27.8	27.3%	7.2%	65.4%
840 €	70 €	10,112	11.3%	28.0	30.5%	7.2%	62.3%

* Additional cost compared to current system tax in 2001 in Spain.

** Percentage of people with personal equivalent income less than 60% median income.

Table 3 shows the sensitivity of reference basic income proposal to changes in the child benefit element. We could reduce financing cost reducing child benefit amount. Every reduction in 10 €/month means saving 1,645 million € of public expenditure. But again this would mean the reform would have more ‘losers’ and less ‘winners’.

Table 4 shows the sensitivity of reference basic income proposal to decrements and increments in working benefit element (additional amount of tax-free earned income).

Table 4. Sensitivity of reference basic income proposal to changes in working benefit

Working benefit***	Cost*	Poverty**	GINI	Losers	Indifferent	Winners
1,000 €	11,306	10.3%	27.4	30.3%	7.0%	62.7%
1,500 €	13,217	10.5%	27.5	26.0%	7.2%	66.9%
2,000 €	15,051	10.9%	27.5	22.4%	7.2%	70.3%
2,500 €	16,809	11.1%	27.6	18.6%	7.3%	74.1%
3,000 €	18,498	11.3%	27.6	15.6%	7.3%	77.1%

* Additional cost compared to current system tax in 2001 in Spain.

** Percentage of people with personal equivalent income less than 60% median income.

*** Additional amount of tax-free income for ‘earned income’.

In this case, 500 €/year of tax-free earned income makes a difference of 1,800 million € in financial cost and a 3-4% variation in losers-winners percentages. Knowing this data policymakers can adjust the amounts of every category to achieve the political goals with the least financial cost.

Let us assume policymakers want to design a basic income scheme to reach the following goals: 1- virtual eradication of severe poverty, 2- reduction of income inequality, 3- improvement of the economic support for households with children, 4- improvement of working conditions to promote employment reducing the tax income burden on wages, 5- more than 70% of potential electoral support (percentage of losers must be less than 30%), 6- maximum tax rate of 42% (current maximum tax rate in Spain was 48% in 2001 and is 45% in 2004), 7- to reach all this goals at the least financial cost.

In Table 5 we show some policy combinations to meet these goals. Policy 2 is more workfare oriented, policy 3 is more family oriented and policy 1 is a balance between work and family support goals. All three policies would virtually eliminate severe poverty and reduce inequality with less than 30% of losers.

Table 5. Different policy combinations adjusting child and working benefits.

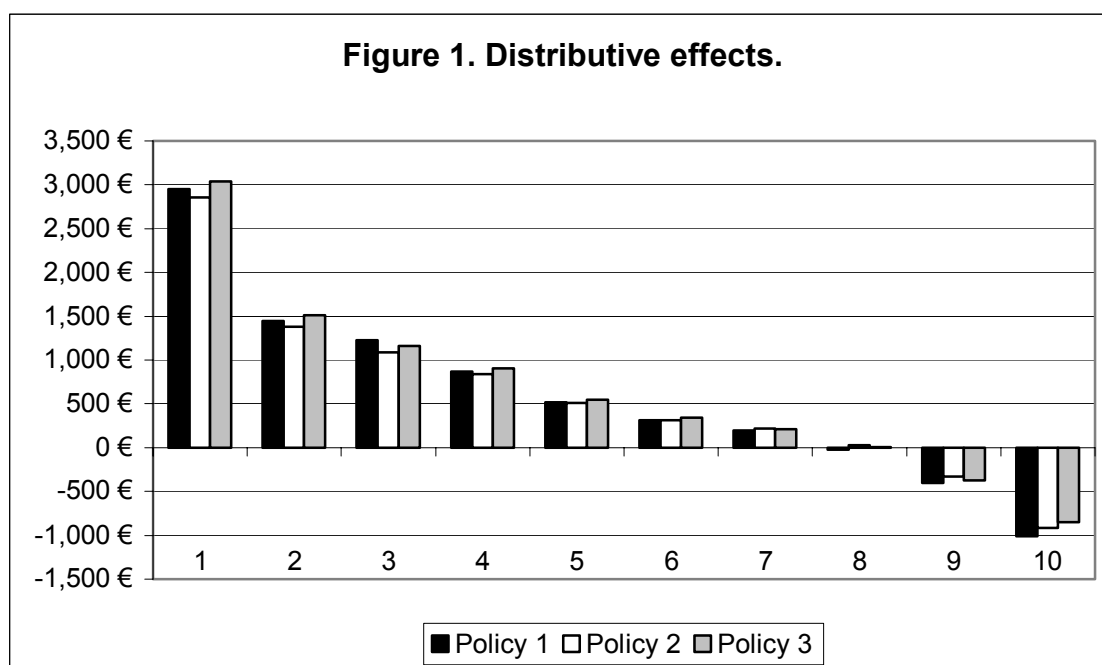
Policy	Working benefit***	Child benefit	Tax rate	Cost*	% GDP	Poverty**	GINI	Losers
1	2,500 €	1,080 €	42%	10,598	1.62%	0.3%	27.1	29.4%
2	3,000 €	960 €	42%	10,821	1.66%	0.3%	27.3	28.4%
3	2,000 €	1,200 €	41%	11,495	1.76%	0.3%	27	28.5%

* Additional cost compared to current system tax in 2001 in Spain.

** Severe poverty: percentage of people with personal equivalent income less than 40% median income.

*** Additional amount of tax-free income for 'earned income'.

Figure 1 shows distributive income effects of these policies for income deciles compared to current income distribution in 2001 in Spain.



6- Conclusions

A fiscal and welfare reform to introduce a basic income guarantee scheme is an example of a class of problem requiring decision-making under deep uncertainty. According to long-term policy analysis approach, in this paper we have used a computer program to simulate several tax reforms oriented towards basic income guarantee. By modifying particular details, different results may be obtained. These changes should be introduced as a result of the priorities of each society after a well informed political debate.

If we want to reform the tax and welfare systems to make them more appropriate to the world of the twenty-first century, a 'category by category' approach is just what we must try. In order to facilitate a well informed political debate, we have selected two large categories, families with under 25 dependents and working people, to simulate several basic income schemes. We have presented the main relevant effects: financial cost, potential political support, poverty and inequality.

According to the simulations, basic income guarantee could be a feasible policy to implement in Spain. We have shown that such a scheme could:

- 1- Meet the virtual eradication of severe poverty.
- 2- Achieve a significant reduction of income inequality.
- 3- Improve the economic support for households with children and other under 25 aged dependents.
- 4- Provide better conditions to promote full employment reducing the tax income burden on wages (specially for low paid workers).

The financial cost could be less than 2% of GDP and more than 70% of potential electorate would be directly benefited by the reform. All this is reachable implementing a flat tax rate of 42% (current maximum tax rate in Spain was 48% in 2001 and is 45% in 2004).

Bibliography

Adelantado, J. coord. (2000), *Cambios en el Estado del Bienestar. Políticas sociales y desigualdades en España*. Barcelona. Icaria.

Atkinson, A. B. And Bourguignon, F. (1990), “ The design of Direct Taxation and Family Benefits”, *Journal of Public Economics*, Vol. 41: 3-29.

Calero Martínez, J. y Costa Cuberta, M (2003), *Análisis y evaluación del gasto social en España*. Documento de trabajo 21/2003, Madrid, Fundación Alternativas.

Cantó, O.; Del Río, C. y Gradín, C. (2000), *La situación de los estudios de desigualdad y pobreza en España*. Universidad de Vigo, Mimeo.

Clark, M. A. (1999), *Report for Working Group on Basic Income*. Jamaica. New York.

Gobierno Vasco. (2000), *Encuesta de Pobreza y Desigualdades Sociales, 2000*. Departamento de Justicia, Trabajo y Seguridad Social, Servicio de Estudios y Régimen Jurídico, Vitoria-Gasteiz.

Healy, S and Reynolds B. (2002), “From Poverty Relief to Universal Entitlement: Social Welfare, Minimum Income and Basic Income in Ireland. BIEN 9th International Congress Paper, Geneva 12-14 September 2002.

Lerner, S. Clark C.M.A. and Needham, R. (1999), *Economic Security for all Canadians*. Between the lines, Toronto.

Lempert, R. J.; Popper, S. W. and Bankes, S. C. (2003), *Shaping the Next One Hundred Years. New Methods for Quantitative, Long-Term Policy Analysis*. RAND publications, Santa Mónica, CA. Available at www.rand.org

Levy, H., Mercader-Prats, M. y Planas, M. (2001) "An introduction to ESPASIM: A microsimulation model to assess tax-benefit reforms in Spain", *Brazilian Electronic Journal of Economics*, vol. 4:1, pp. 1- 23. <http://www.beje.decon.ufpe.br/>

Pinilla-Pallejà, R (2002a), *A Diversified Basic Income Scheme for Federal States and Multinational Communities*. Paper prepared for the Basic Income European Network 9th Congress. Geneva, 12-14 September. (08/09/02 revised version)
<http://www.nodo50.org/redrentabasica/descargas/Pinilla%20BIEN%202002.pdf>

Pinilla-Pallejà, R. (2002b), *Una propuesta de renta básica diversificada para el Estado Español*. Ponencia preparada para el II Simposio de Renta Básica. Vitoria, 14 de diciembre. http://www.nodo50.org/redrentabasica/descargas/RBIIsimposio_1.pdf

Pinilla-Pallejà, R. (2004) *La renta básica de ciudadanía. Una propuesta clave para la renovación del estado del bienestar*. Barcelona. Icaria.

Raventós, D. (1999), *El derecho a la existencia*. Barcelona. Ariel.

Raventós, D. Coord. (2001), *La renta básica. Por una ciudadanía más libre, más igualitaria y más fraterna*. Barcelona. Ariel.

Ruiz-Huerta, J, Martínez, R. y Ayala, L. (2001), “Mínimo exento, reforma fiscal y equidad: un análisis del caso español” *Hacienda Pública Española*. Monografía 2001.

Sanzo-González L. (2002a), “Poverty Measurement in the Spanish Basque Country: Statistics Improvements and Detection of Social Change” Manuscript. Basque Government. Vitoria-Gasteiz.

Sanzo-González L. (2002b). “Allocation universelle et garantie de ressources en Espagne et au Pays Basque”. BIEN 9th International Congress Paper, Geneva 12-14 September 2002. Disponible en www.basicincome.org

Sanzo González, Luis y Rafael Pinilla Pallejà (2004) *La Renta Básica. Para una reforma del sistema fiscal y de la seguridad social*. Documento de trabajo 42/2004. Madrid, Fundación Alternativas. Disponible en www.fundacionalternativas.com/laboratorio

Van Parijs P. (1995), *Real Freedom for all what if anything can justify capitalism*. Oxford. Oxford University Press.

Van Parijs P. (2000), “Basic Income: A Simple and Powerful idea for the 21st century” 8th International BIEN Congress Paper, Berlin, 6-7 October 2000. Available at www.basicincome.org

Van der Veen, R. Groot, L. y Lo Vuolo, R. eds. (2002), *La renta básica en la agenda: Objetivos y posibilidades del ingreso ciudadano*. Buenos Aires. Miño y Dávila.

Zubiri Oria, I. (2001), Las reformas fiscales en los países de la Unión Europea: causas y efectos. *Hacienda Pública Española*. Monografía 2001, (13-52).