Newsletter

June 2009

*The **Social Market Foundation** is an independent public policy think-tank, developing and advancing innovative solutions across a broad range of economic and social policy. We publish original research, hold seminars and debates in Westminster and beyond, and run a diverse programme of events at the three main party conferences.*

Since its foundation in 1989, the work of the SMF has been principally devoted to promoting the social market philosophy, which seeks to marry markets and social justice. It neither sees the market as a necessary evil nor as an end in itself but as a means to improve people's lives. It is underpinned by adherence to two key principles: first, a positive preference for market mechanisms, while recognising that a truly pro-market approach is often not a free-market one; and second, a belief that a sustainable market economy rests on social and political foundations that are widely regarded as fair. Our work aims to elucidate these ideas and to explain why the social market is a fruitful source of solutions to public policy problems.

For further information please contact the editor, Laura Tomlinson at ltomlinson@smf.co.uk

To be added to or removed from the newsletter distribution list please send a request to news@smf.co.uk

Social Market Foundation
11 Tufton Street
Westminster
London
SW1P 3QB
020 7222 7060
www.smf.co.uk

Welcome to the June edition of the newsletter

Whichever party forms the next government the theme will be dominated by a huge public spending squeeze. The impact of the financial crisis on the UK's fiscal position will be the fourth worst in modern times – behind the two world wars and the Napoleonic wars. For all think-tanks this necessitates a shift in the way we approach public policy recommendations. At the Social Market Foundation we have always had a focus on the need to reform services to improve delivery efficiency and further social justice. Now all policymakers will have to engage with a difficult debate about how to fix the fiscal fallout from the recession. Having spent over a decade focussing on how best the Government should spend growing tax revenues, political and public policy debate will now focus on addressing what principles should apply in the ruthless prioritisation of expenditure that is to come, and how to maximise the effectiveness of every pound spent.

In this edition

This SMF newsletter has a number of articles on a variety of topics:

Latest news

Research

Following April's Budget statement, the SMF published its response to the employment measures announced. The paper focuses on the central Government initiative in this area: guaranteed employment for all young people through a public job creation scheme, coordinated by local authorities. It highlights evidence from similar schemes which suggests that these programmes are not effective at maintaining participants' human capital, and, if delivered by local authorities, are unlikely to improve jobseekers' employment chances later on. Instead, the paper explores other options for fighting long-term unemployment during a recession. It reveals that the success of any given intervention is determined by the extent to which it caters for the particular needs of individuals. It concludes that a devolved, flexible approach will be key to tackling unemployment.

The SMF therefore recommends that the £1.2 billion earmarked by the Government for public job creation schemes would be better delivered through the payment-by-results framework of the Flexible New Deal. Its outcome-focused, tailored approach will be best suited to ensuring individual jobseekers receive the appropriate help and relevant training required to boost their long-term employment prospects. The paper also points out that current investment in the scheme is inadequate and argues that an extra £1.4bn per year will be needed in 2010 and 2011 just to maintain the level of spending per jobseeker. If these issues are ignored, the SMF believes there will be serious consequences for the unemployed in coming years. Follow this link to read the full article issued following the Budget http://www.smf.co.uk/flexible-new-deal-can-tackle-long-term-unemployment.

On 20th May the SMF launched its latest piece of research entitled Anglo-Flexicurity: Insuring Against Unemployment in the UK with renowned author and economist Robert Shiller speaking on the panel along with report author Dr Henry Kippin, SMF Associate Research Fellow, and Francesca Arcidiaco, Vice-President of Government Relations Europe, Genworth Financial. For more information on SMF's work in the area and a copy of the publication please go to http://www.smf.co.uk/anglo-flexicurity-two.html.

This work was kindly supported by Genworth Financial.

Other ongoing areas of research include public service commissioning and the future of childcare in Britain. For those organisations interested in getting involved with SMF research, or partnering with us, please contact our research team on 0207 222 7060 or info@smf.co.uk.

See page 7 for more details of our upcoming publications or visit www.smf.co.uk/research

Events

In March we hosted a panel debate looking at health in the workplace. The event was chaired by SMF Director Ian Mulheirn and included speeches from the Managing Director of Bupa UK and North America and Leela Barham, a health expert. Contributions to the panel debate came from Business in the Community, The Work Foundation, CIPD and David Furness, SMF Health Project Leader. The speakers addressed a large specialist audience of interested stakeholders including Dame Carol Black.

This event was made possible by the kind support of Bupa.

In April Lansons Public Affairs held breakfast briefing the day after the Budget in conjunction with the Social Market Foundation. At the breakfast Labour Treasury Select Committee MP Andy Love, Conservative City Circle Chairman Richard Spring MP, Liberal Democrat Treasury spokesman Lord Oakeshott and the SMF's Ian Mulheirn all spoke on the implications of the Budget. After the speeches the Westminster and City policy community reacted to the previous day's announcements and a lively discussion ensued.

On 21st May we held a lively panel discussion 'Short Changed: Are pensioners getting a good deal?' The Parliamentary Under-Secretary of State for Work and Pensions Lord McKenzie spoke along with Stephen Haddrill, ABI, Jane Vass, Age Concern England and Steve Kyle, Just Retirement Solutions. To see copies of Lord McKenzie's speech and forthcoming footage of the event please go to http://www.smf.co.uk/Short-Changed.html.

This event was made possible by the kind support of Just Retirement.

For details of upcoming events visit www.smf.co.uk/events or see page 11.

Conferences 2009

The Social Market Foundation is now tying down its fringe schedule for each of the party conferences in autumn this year. There are still opportunities for sponsorship available and we would be delighted to hear from anyone further who is interested in partnering with us. For information on our proposed themes this year please contact Laura Tomlinson ltomlinson@smf.co.uk or on 020 7227 4407 or see our website www.smf.co.uk/conf-2009

Westminster boardroom

The conference room at the Social Market Foundation is available to hire for meetings and seminars. It is an ideal venue for those seeking a location near the heart of government as we are situated within short walking distance of underground stations at Westminster, St James' Park and Victoria and just minutes from the Houses of Parliament and Whitehall.

For more information about how to book our boardroom and hire rates please contact SMF on 020 7222 7060 or see our website www.smf.co.uk/room-hire

We are also delighted to inform readers that Senior Research Fellow, Jessica Prendergrast gave birth in April to a healthy baby girl named Mabel.

Staff Appointments

We are pleased to announce the appointment of two new Senior Researcher Fellows. Joining us for 6 months' maternity cover Dr Sandra Gruescu comes to the SMF with a background of public policy research and consultancy and has recently been working with the German government on pensions and family policy. Her research will focus mainly on taxation of the family, child poverty and pensions policies. James Lloyd, who joins us permanently, has come from the International Longevity Centre and will mainly be looking into industrial policy, regulation, and wealth and assets policy.

Note from the Director

Ian Mulheirn

Director

In what was almost his parting act as Secretary of State for Work and Pensions, James Purnell saw through the last stages of radical reform to the welfare system by announcing the private and third sector winners of the Flexible New Deal contracts. These new contracts, where non-state 'providers' are paid for each person they get into employment, represent a real innovation in the delivery of public services. International experience and pilot evidence suggests that these reforms, correctly implemented, can produce better services for users at lower cost to taxpayers. Welfare reform therefore raises important questions about where else in public service provision the powerful tool of 'payment by results' might be deployed in the coming decade of a sharp public spending squeeze.

In the past, to put it crudely, the standard public service delivery model involved centrally-determined and state-provided services that were deemed to meet service users' needs. But figuring out 'what works' for service users is rarely simple. Across different public services from health and welfare to education and social care achieving the best possible outcome depends on individual service users' needs and many other things besides. A 'cookie-cutter' solution is therefore bound to fail either to meet need or to be cost-effective: flexibility and autonomy of service provision are crucial. But from the taxpayer's perspective, these things raise questions of accountability: in such a flexible system how do we know that money will be spent wisely to meet citizens' needs? One answer is when payments to those commissioned to deliver services follow identifiable positive outcomes.

Of course in many areas of public service, payment by results isn't that simple. For example, where the desired results from a given service are subjective, hard to define, or far off in the future, such an approach is inappropriate or unworkable. Where outcomes are more measurable, however, payment by results offers huge opportunities for better and cheaper service provision.

"Payment by results is particularly suited to reducing re-offending"

One of the most promising areas for deploying payment by results is in offender management. Despite a decade of Government investment to reduce re-offending, rates remain high. The most recent statistics released by the Home Office reveal that 67% of adults given a custodial sentence and 50% of those given a community sentence re-offend within two years. Re-offending rates for juvenile and young adult offenders are higher still: up to 78% for those aged 18-20, for example. As well as having serious implications for the life chances of offenders themselves, on the well-being of victims of crime, and more broadly on public perceptions of safety, re-offending is expensive. The Chartered Institute for Personnel Development has estimated an annual cost to the taxpayer of between £11bn and £15bn.

Government must move away from directly providing separate prison and probation services, neither of which faces strong incentives to innovate to reduce re-offending rates. And rather than negotiating Byzantine contracts with non-state providers stipulating, for example, the precise number of hours prisoners should be confined to their cells each day, the Government should focus on what matters and pay for that. In other words, Government should pay delivery organisations for each offender who has not re-offended within two years of release.

Payment by results is particularly well-suited to reducing re-offending for two principle reasons. First, even more so than in welfare-to-work, the desired public outcomes from offender management are clear and measurable. Second, paying by results deploys the profit motive to make prison operators, health, probation and welfare-to-work services join-up their provision to ensure that ex-offenders are helped to re-enter mainstream society rather than fall between the cracks.

Major practical questions remain about the implementation of such a system. For example: how does the profit motive can fit alongside probation's role to provide sentencing assistance to courts? And would a profit-driven system reduce political accountability or compromise public safety? Nevertheless, this 21st century tool of public service commissioning has the capacity to produce radical change, creating a more efficient criminal justice system that is capable of rehabilitating ex-offenders and reducing the scandalously high rates of re-offending that persist today.

Forthcoming Publications

Securing sustainable employment outcomes

Beth Foley and Rena Menne

Building on the SMF's 2008 report *The Flexible New Deal: Making it Work*, we will soon publish a follow up report examining job retention of those individuals previously receiving employment benefits. This project provides an overview of methods used to make employment more sustainable and discusses how these are embedded in the current system.

Many people are trapped in a cycle between benefits and work. 54% of Jobseekers' Allowance claimants have claimed at least once before. Of these, a fifth has claimed five or more times over the previous four years.[1] This means that a substantial group of people live with very unstable employment patterns and are prone to suffer from the scarring effects of a broken employment history.

Three main levers are used to increase employment retention: financial support, increasing human capital and personal advice. Our analysis shows that all three can make a difference, but fall a long way short of universal success. Specific programmes have different aims; bonus payments for retaining a job are, for example, fundamentally different from an Emergency Fund new employees can draw on in case something goes wrong, and so are classroom training and work trials. Whether any of these interventions are successful in increasing employment retention depends on whether the support matches the personal circumstances of the employee. Success therefore crucially depends on personalisation.

The current employment services system recognises this to some extent. Flexibility which enables advisers to offer personalised solutions has increased over recent years. The Flexible New Deal and the Jobcentre Plus reforms implemented in April 2009 are two recent examples where personal advisers have been given more discretion about how to support their customers. Jobcentre Plus advisers now have more opportunities to provide specialised support earlier on in the claim, while the Flexible New Deal will bring more room for private and third sector providers to help those furthest from the labour market. Under a largely out-come based payment system, providers can support jobseekers with whichever service they see fit.

This SMF report argues that these reforms point in the right direction but should be taken further. Flexibility should be increased, especially for Jobcentre Plus personal advisers who have much less leeway than their private and third sector counterparts. Jobseekers should

[1] Department for Work and Pensions, *Repeat Jobseeker's Allowance Spells*, by Hannah Carpenter (London: HMSO, 2006).

not receive services according to the benefit they are on, but according to their individual needs. To achieve this, services should be driven by outcomes, rather than processes, regardless of whether the public, private or third sector provides them.

To maintain a successful and accountable employment service system, these new flexibilities should be complemented by new measures to make revolving door employment more visible and introduce a new definition of what constitutes a successful outcome. If these safeguards are put in place, more flexibility will benefit all jobseekers and will support them to not loose touch with the labour market in difficult times.

The date for the launch of this report has yet to be confirmed. To reserve a space in advance please send a request to events@smf.co.uk. For more information about the SMF's work in this area please go to www.smf.co.uk/flexible-new-deal

This project has been made possible by the kind support of Remploy.

The NHS and the Financial Crisis: Not *what* to cut but *how* to cut.

Emerging conclusions from the SMF Health Project

David Furness

The full impact of the economic crisis is beginning to be understood in the public sector. For many months, public service providers seemed a million miles away from the US sub-prime mortgage market. But there is now an increasing realisation that the credit crunch has moved from a banking crisis to a full blown recession. The recently delivered Budget has given some indication of the long term damage to public finances. The picture is not a pretty one. From 2012, public spending will rise by only 0.7% per year. And while we do not yet know how that money will be divided up among the departments (and we can expect some fierce competition for scarce resources) it is clear that the Government's ability to invest in public services will be severely constrained for the foreseeable future.

Policymakers are on the lookout for 'big ticket' items to cut, so in public expenditure these are at a premium. And in the particular case of healthcare, the same is true. The bulk of health spending is the aggregation of millions of patient interactions with service providers – even capital expenditure on new building projects does not account for a large proportion of how the health service spends money. So it's not easy to cut out big chunks of the NHS budget to save money, explaining current government focus on efficiency.

But we should not kid ourselves. The public finances are in a terrible state, and efficiency savings simply will not be enough to sustain the quality of health services given the level of resources likely to be available to the NHS in the years to come. In his 2002 Treasury review, Derek Wanless concluded in his most optimistic projections for the NHS that real-terms spending increases of 4.4% per year would be necessary for the service to improve, and it is highly unlikely that increases of this sort will be available in the years ahead. So cuts seem inevitable, even in healthcare. And they will be cuts in services, not the cancellation of big projects.

Some attention has already been devoted to *what* to cut. But instead, we ought to focus much more on *how* cuts should be made. And the answer requires a radical rethink of the nature of the NHS. At the Social Market Foundation we are coming towards the final stages of a major report examining the future of the health system. A central conclusion of our work is that ever greater responsibility ought to be devolved to local Primary Care Trusts (PCTs). We have reached the end of the era of top-down central control in public services. And just as improvement cannot be driven from the centre, neither can decisions about where to make cuts in services. If cuts in services are determined centrally, there are real fears that public support for the NHS cannot be maintained. We have conducted some public opinion research in conjunction with Ipsos MORI exploring people's attitudes to resource constraints in the NHS. We found that people are much more likely to accept cutbacks if they feel involved in decision making and if decisions are properly explained to them. This is a job for local health commissioners – not central government.

But accepting the need for cuts to be led by local commissioners means a renegotiation of the NHS settlement. No longer will it be possible to pretend that the NHS is a nationally uniform service. Instead, local variation and local control will be the rule. This might entail a dramatic fall in the number of national targets, with genuine autonomy offered to local commissioners who have the key role of working with local people to create services that meet their needs. And, in response, accountability mechanisms should be strengthened to give local people a real voice in decisions about local services. So perhaps the central question for health policymakers in response to the economic crisis is not "What shall we cut?" but "How shall we make the right decisions about what to cut?" And the answer is that decisions should be made locally, not nationally; at the frontline, not central HQ.

As the lasting impact of the economic crisis becomes ever more apparent there are hard choices to make. The future of public services in this country does not look bright – there will not be much money to spend in the years ahead. And so it becomes ever more urgent that politicians are upfront and honest about inevitable cuts in services, and that local commissioners are genuinely empowered to make the cutbacks that will be needed if public services are to survive this current crisis.

The SMF Health Project has been a significant research project running over the past two years and now drawing to a close. The report is due to be published imminently but the date has yet to be confirmed. To be notified of details please send a request to events@smf.co.uk. For more information about the SMF's work in this area please go to www.smf.co.uk/health-project.

This project has been made possible by the kind support of BUPA, Pfizer, Standard Life Healthcare and NHS Connecting for Health.

Forthcoming Events

SMF at the NHS Confederation Conference: Preventative Healthcare and the Role of Pharmacies

Date:	08.00-09.00	Friday 12 June 2009
Venue:	Jury's Inn, 31 Keel Wharf, Liverpool, L3 4FN	

Chair: Rebecca Evans, Deputy Editor, Health Service Journal

Speakers: David Furness, SMF Health Project Leader
Jonathan Mason, National Clinical Director for Primary Care and Community Pharmacy, Department of Health
David Pruce, Director of Policy and Communications, Royal Pharmaceutical Society
Sue Sharpe, Chief Executive, Pharmaceutical Services Negotiating Committee

The Social Market Foundation is holding an exclusive breakfast roundtable during the NHS Confederation Conference in Liverpool. Taking advantage of this gathering of key stakeholders we would like to discuss issues relating to preventative healthcare and in particular the role of pharmacies in delivering public health interventions.

The NHS has often been criticised for being an 'illness' not a 'wellness' service. Better at treating the sick than keeping people well, the health service has in recent years focused much more on prevention rather than cure. Some interventions have focused on improved screening, while public health campaigns have encouraged individuals to improve their lifestyles. The drift of health policy is towards much more investment in prevention, with a new range of services available to patients. This shift in emphasis is embodied in the Pharmacy White Paper. There is now scope for pharmacists to play a larger role in primary and preventative healthcare, and for commissioners to develop a range of innovative new services. This breakfast roundtable will focus on how to build on the Pharmacy White Paper, particularly in the context of the crisis in public finances.

Key questions to be debated will include:

Government has been pushing for a greater role for pharmacy, either through locally enhanced or other models, for some years now - what are the barriers to this?

How can commissioners work more effectively with pharmacy to develop new services? How can we target necessary public health interventions like flu vaccines at high risk groups?

What role is there for the private sector to help progress these reforms?

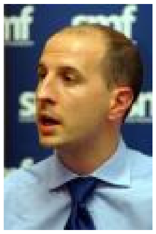
Can investment in prevention continue to be prioritised when public health budgets are under pressure?

Proceedings will open with remarks from senior stakeholders including David Pruce, Head of Policy at the Royal Pharmaceutical Society, Sue Sharpe, Chief Executive of the Pharmaceutical

Services Negotiating Committee and David Furness, Health Project Leader at the Social Market Foundation.

Breakfast will be provided.

This event is being kindly supported by Novartis Vaccines.
Spaces at this event are limited so please respond quickly, to reserve a place please contact events@smf.co.uk or call 020 7227 4412.



Building Bridges to a Better Society

New SMF Research

Dr Simon Griffiths

In the UK, several events have stoked controversy around migration in recent months. The Prime Minister's party conference claim that he wanted "British jobs for British workers" and the recent demonstrations over the use of foreign workers outside the site of the new Olympic stadium both indicate the unease that some sections of the public feel about migration. Unemployment and deprivation tend to make this unease more severe, giving rise to new concerns that the deepening economic recession will further threaten community cohesion. The Social Market Foundation's new project on migration and inclusion, which begins this month, is therefore coming at a particularly apposite time.

At the centre of the social market philosophy is the idea that a fair and successful market economy relies on a healthy civil society in order to function properly – one in which all members are included. The economic boom and greater European integration led to a sharp rise in the number of migrants, particularly from the EU, working in the UK. As the economic boom ended, so the unease in the wider UK population about migration levels rose. An inclusive civil society must now address the impact of migration on the UK. In some areas, we are entering a phase of 'super diversity'; around 300 languages are now spoken in London schools, for example. On the one hand, diversity on this scale can bring cultural vibrancy and economic benefits, but on the other presents a set of difficult and seemingly intractable challenges.

Getting the policy response to super-diversity right is crucial. Over the last few years, riots have occurred in Britain, Spain, the Netherlands, Denmark, Belgium and Russia. In all of these cases, ethnicity was a key factor. The 2001 British riots in Bradford, Oldham and Burnley made it clear to the government that their approach to multiculturalism was failing. This prompted a review, led by Ted Cantle, which found that people of different ethnicities were living "a series of parallel lives". As Cantle noted, "These lives often do not seem to touch at any point, let alone overlap and promote any meaningful interchanges. A Muslim of Pakistani origin summed this up: 'When I leave this meeting with you I will go home and not see another white face until I come back here next week'"

"Building social capital is not an easy task"

After the riots, the British government moved away from the *laissez-faire* approach to multiculturalism that it had previously adopted. Instead it was argued that the response to multiculturalism should be a cautious emphasis on commonality. ('Cautious' because it seems clear that a move to 'assimilationism' is also undesirable.) This means a new approach to migration and ethnicity. As Cantle observed, "virtually every modern multicultural city has not just dozens, but possibly hundreds of different communities now interacting. And we don't understand how they interact, or what stops them. So we have to develop new models."

Over the next few months the SMF is focusing on the notion of 'bridging' social capital to analyse migration and inclusion. The term was popularised by Robert Putnam in his book *Bowling Alone*. Social capital denotes a resource made up of social networks, norms, understandings and values which facilitate co-operation within or among groups. Bridging capital is the social 'glue' between different groups. This inter-group glue contributes to the cohesion of the community as a whole. At one extreme these habits could constitute sustained relationships between individuals or groups; at the other they could just be the mutual observation of politeness norms.

The SMF's research will look at how 'bridging' social capital can best be encouraged, focusing on the links between recent migrants and existing communities. Since super-diversity demands familiarity with the make-up and needs of particular communities, central government policy will not be the focus. Instead, the SMF will look at civil society's ability to build bridging social capital. It is civil society, so Oxford University's *Centre on Migration Policy and Society* (COMPAS) observes, that "provides a greater flexibility and ability to respond to changing needs on the ground. It can be well placed to recognise and respond to the cross cutting nature of migrants' needs."

Building social capital is not an easy task, and it may not be best-served by an immediate push for sustained, meaningful relationships. This is nicely illustrated in a story told by Onees Lodhi from the *Capital Community Foundation*. Lodhi relates how a Somali community group organised a camping trip for a group of Somali and Eastern European boys. When the community workers tried to set up a football match as an icebreaker, they found the boys reluctant to split from their groups and cross the ethnic divide. Attempts to split the boys up resulted in angry exchanges. Lodhi observes that "taking the boys outside their traditional comfort zones only served to fuel animosities rather than acting as a bridge to understanding". Building bridges without agreement from all groups may have the opposite effect to that intended.

Getting the recommendations right for civil society groups that build social capital, and governments that want to provide a framework where this can happen, will not be easy. It will be exciting to see how this research develops in the coming months.

For more information on the SMF's work on migration please contact sgriffiths@smf.co.uk. This project is made possible by the kind support of the Barrow Cadbury Trust.

Families and the tax system: Is there a case for joint taxation?

Dr Sandra Gruescu

One might like to think that the decision about whether to get married, as well as whether to have children would be a very private decision that actions of the state would not influence. But most people would admit that money, and especially the lack of it, plays a strong role in these matters. So it is not surprising that in recent years several studies have shown that the tax and benefits system not only influences the way we look for work but also decisions about the family. If the tax and benefits system advantages single-earner married couples you will likely find that more people get married. If, on the other hand, the tax-benefit system targets money on poor children, without regard to the number of adults in the household, society may see marginally more lone parent families. At the other end of the income scale an example of these potential influences is shown in the current Budget. The cut in tax relief on pension contributions, the clawing back of the personal allowance and the new 50 per cent tax rate for earners over £150,000, will make a high earning couple much better off if, for example, instead of the husband earning £200,000 and the wife nothing, the husband cuts his salary by half and the wife gets a £100,000 a year job as well. This will work because couples are taxed individually.

The introduction of individual taxation in 1990 and the abolition of the Married Couples Allowance, were positive steps for gender equality, removing the incentives for one partner to remain outside paid employment. Gordon Brown is a strong supporter of that change, saying in 1999 that he would "never allow the wife or partner to be regarded as the chattel" as had been the case prior to individual taxation. But the rise of tax credits as a major part of the tax benefit system reintroduces some of the 'first-earner advantage'.

"Ultimately, there is no such thing as a neutral tax system from the family's perspective."

The Conservative Party plans to end the "couple penalty" and "recognise marriage in the tax and benefit system". One way to do this would be the introduction of joint taxation of couples, as the following examples from the German and French system illustrate. Great Britain's tax system is geared towards the individual rather than the family with the underlying idea to remain on neutral ground. In comparison France has a pro-natalist way of taxing the family, whereas Germany's family taxation is modelled on the traditional ideal of a family with married parents.

In Germany the constitutional law protects marriage and family, which the tax law translates into joint taxation of married couples, regardless of any children. Married partners can choose to be taxed individually or decide to pool their incomes and apply the so-called income splitting, whereby their joint income is divided by two and the corresponding tax rate is applied to each of the two equal income shares. With the progressive tax rate the sum of these two is smaller than the sum of the tax which otherwise would have been paid on the two individual incomes. The implication is that the highest 'gain' can be made if one partner (in most cases the husband) earns rather a lot and the other partner (the wife) earns nothing. This is widely seen as a problem and a strong argument against income splitting exists as it deters mothers from rejoining the labour market after having had some time off to look after children. But an argument for income splitting is that married couples with different income distributions are treated equally. As married couples without children profit the most, and the splitting advantage carries less weight the more children the family has, 'family splitting', as has been adopted in France, is a possible alternative.

France is well known for its long tradition of a pro-natalist family policy with generous family allowances, strong support for working mothers and a tax system that rewards having children. As in Germany the family is seen as a household unit and is therefore taxable as such. For tax purposes the household income is added up. It is then divided by a divisor based on the size of the family. For married couples without children this takes the same form as income splitting in Germany, as the pooled income is divided by two. When children come into play the divisor is increased by 0.5 for the first and second child and by 1 for the third and each further child. The tax formula is then applied to the resulting income shares and summed up. By calculating the tax burden in this way children are acknowledged as dependents. As a result parents on an average income who have at least three children *de facto* do not pay tax.

Ultimately, there is no such thing as a neutral tax system from the family's perspective. Joint taxation as in Germany disincentivises second earners, with consequences for gender equality. Family taxation as in France goes further as it acknowledges the dependencies and financial strains once children are involved. In the UK raising the couple elements of tax credits would benefit couples but disincentivises second earners. Therefore, introducing a second earner element to tax credits would be a possible solution to ensure that couples are recognised in the tax system and gender equality is maintained.

For more information on SMF's work in this area please contact Sandra Gruescu at *sgruescu@smf.co.uk*..

Getting The Vote Out:

Behavioural Economics and the June Elections

Beth Foley

On 4th June, UK voters went to the polls for local and European elections. It was a vote taking place at a time of profound political shifts. Yet, despite this context, the results gave rise to now-familiar headlines bemoaning low voter turnouts. After 1998's historic low of 28%, turnout in local elections has hovered just above the 30% mark, with some wards recording figures as low as 12%. This trend is not confined to the UK: in recent decades falling turnout rates have been evident across the industrialised countries. The decline is concerning. Voting underpins the legitimacy of a democratic system, creating ties of accountability between government and the people. But, despite concerted efforts, governments have struggled to reverse the trend. Lessons from the discipline of behavioural economics suggest the problem lies in policymakers' inaccurate and incomplete understanding of people's behavioural motivations, largely due to an over-reliance on the tenets of rational choice theory.

Grounded in the assumptions of neo-classical economics, rational choice theory rests on two premises: that human beings are ultimately self-interested and that they make choices based on rational, cost-benefit calculations. In many cases, it has proved a useful predictive model and is used extensively in policymaking. However, it can yield questionable results when applied to issues such as voting. According to the 'rational' model, when deciding to vote, an individual would weigh up the costs (the time and effort involved in registering, gathering information about candidates and journeying to the polling station) against the direct benefits (the probability that her individual vote will prove decisive to the outcome). Given that this probability is infinitesimal, particularly relative to unavoidable costs involved, the 'rational' citizen would not make the effort to vote. When considered through the rational choice theory lens, then, the interesting question is not why so many choose *not* to vote but, conversely, why so many people actually do.

> "The interesting question is not why so many choose *not* to vote but, conversely, why so many people actually do"

Nevertheless, in keeping with the rational choice analysis, strategies proposed by government have aimed to reduce the perceived 'effort costs' of voting to make the cost benefit calculation more appealing. They include making electoral registration and the voting mechanism easier through online or postal options and making polling stations more accessible. There have even been moves to increase the direct benefits for voters through the use of concrete incentives, with the 2007 Councillors' Commission report controversially recommending the use of some form of financial reward.

Yet evidence from other fields suggests that individuals basing their decision to vote on monetary incentives would damage the important idea that the purpose of the vote should be to hold those in power to account. On the issue of voting – where motivations are as significant as the behaviour itself – it is clear that solutions presented by rational choice theory are neither practical nor politically palatable. On the other hand, the theory is also unable to explain why so many individuals do make the seemingly irrational decision to vote, particularly given the fact that voters tend to be over-represented amongst the most educated. This conundrum – or the 'paradox of voting' – was first elaborated by Anthony Downs in 1957 and raises questions about the explanatory power of rational choice theory.

What, then, actually influences the decision to vote or abstain? A number of studies highlight the role played by subconscious behavioural biases. Despite the 'rational' conclusion on the futility of voting, surveys consistently reveal that people do believe they should vote and have usually registered to do so. However, our tendencies to procrastinate or sideline future goals in favour of immediate desires, mean that – in the event of bad weather or a good programme on TV – our intentions may not be realised on polling day. Equally, individuals are not all forward-looking, rational decision-makers – we are continually swayed by the simple force of habit. Consequently, people tend to be serial voters or serial non-voters; decisions are often conditioned, not on the basis of the choices available at the upcoming election, but on whether an individual voted previously.

Yet, also emerging from the evidence is a widespread belief among the public in the importance of voting and a general intention to do so. The failure of the rational choice model to explain this apparent paradox stems from its disregard for the fact that people are not narrowly self-interested, socially detached entities. We remain acutely aware of the perceptions and actions of those around us, and our behaviour is continually informed by social norms. The act of voting, in particular, is bound up with social and cultural affiliations, often linked to a sense of history and the importance of the democratic process. A survey conducted after the 2005 general election found that 60% of voting participants believed it was their 'duty to vote'. Included in this idea of 'duty' are all the ethical and social considerations overlooked in models of strictly rational behaviour. What's more, policy founded on the idea of the strategic, self-interested individual is in danger of subverting many of these vital social and cultural drivers.

With low turnout a prominent feature of these latest elections, policymakers are once again under pressure to address the issue. But if their strategies are to prove more effective in reversing the trend, they must move beyond the narrow parameters of rational choice analysis. Addressing the issue of voter turnout, like many other policy challenges facing the UK, will require a much more nuanced model of human decision-making. Further exploration of the emerging lessons from behavioural economics would be a useful place to start.

For more information on the SMF's work on behavioural economics, please contact Beth Foley at bfoley@smf.co.uk. We are currently undertaking further research into this area – kindly supported by the Department for Communities and Local Government – which will be published later in 2009.