A SOCIAL SAFETY NET FOR THE IMPACT OF TECHNICAL CHANGE: AN EVALUATION OF THE MYERS COMMITTEE'S ADJUSTMENT ASSISTANCE PROPOSAL

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FIGURE I 7
This paper assesses the "social safety net" proposal by the Myer's Committee Report on Technological Change as a program aimed to ameliorate the losses of individuals adversely affected by technical progress. The point is made that while the safety net is geared toward retrenched employees moving through the unemployment pool, much of the actual loss from unanticipated technical progress is taken as written down capital values by immobile factor owners tied to the old technology. In the end, the safety net amounts to little more than increased unemployment benefits which do not compensate many of the injured parties. Some of the arguments for treating certain factor owners asymmetrically are scrutinized and the experiences of Australia and the United States with similar trade adjustment assistance schemes are recounted.
I. INTRODUCTION

The basic conclusion of the Myers' Committee Report on Technological Change is that technical change is desirable and ought be permitted to take its unimpeded course; but although technical change benefits society at large, nevertheless some people are harmed by the introduction of new technologies, and these people ought be protected by a "social safety net." The general characteristics of the social safety net are that individuals made redundant by technological change would benefit from income support programs in the course of their adjustment to new employment, and the costs of compensation would be met jointly by the employers responsible for instituting the change which caused redundancy, and via government subsidisation by society at large which benefits from the change. The purpose of this note is to critically review the Myers' social safety net proposal. We should emphasise at the outset that the intent is not to provide a broad review of the various issues raised by the Myers Committee (for such a broad analysis of the Committee's proposals, see Michael Carter, forthcoming).

In section II we review the theoretical justification underlying any compensatory scheme. We view the Myers proposal as equity motivated and not as a problem of the "second best" or externality. Section III focusses upon identifying the gainers and losers from technical change and, in particular, we suggest that there are some holes in the safety net. In section IV, therefore, we assess some arguments for compensating some, but not all, losers from technical advance and in section V we conclude that the Myers proposal is essentially a call for higher
unemployment benefits and not at all a safety net for individuals harmed by technical progress. Section VI considers an aspect of the financing proposal. Finally, in section VII we recount some of the difficulties encountered by similar programs to encourage adjustment to international trade related changes in Australia and the United States.

II. WHY PROVIDE A NET AT ALL?

The Myers Committee proposes a "safety net" for retrenched employees. In particular:

"The Committee recommends that the government support the introduction of a two-part retrenchment compensation scheme that would include:

Provision in awards for:

* a period of notice before retrenchment
* monetary compensation for lost seniority and other accumulated credits only
* assistance to find alternative employment

The award provisions would have to be established by a test case. The Committee recommends that the Government sponsor such a case based on standards in general accordance with the NLAC guidelines.

A temporary income-maintenance scheme that would:

* be funded by the government and administered as a supplement to unemployment benefits
* provide for persons retrenched through no fault of their own to receive for a fixed period after retrenchment a fixed proportion of their weekly earnings averaged over the 3 months prior to retrenchment, up to a maximum of the national average weekly earnings for the preceding quarter

The period of income maintenance might vary from 1 month for persons who were employed by the same employer for 3 to 5 years, up to 6 months for persons who were so employed for 10 years or more. The rate of benefit might vary with the period of employment from 60% of weekly earnings as defined above to 75%. A loading might be added for persons with dependants." (p.182)

The Committee appeals to an equity argument in order to motivate the compensation by government and firms to those employees disadvantaged by technological change:
"The Committee is of the view that the community as a whole benefits from technological change as well as the employer and that such cost-sharing is therefore appropriate. Because the employer retains liability for significant payments, the scheme is not likely to be regarded as encouraging retrenchments." (p.182)

Income support schemes such as that recommended by the Myers Committee are quite common in situations where employees are believed to have suffered redundancy and unemployment because of the vagaries of exogenous forces over which they have no control. At the most general level, unemployment benefits are offered to compensate for the employment consequences of the business cycle; but there have also been more specific compensation schemes related to particular causes of unemployment, as for example compensation for a change in protective policy or to facilitate adjustment as a consequence of exogenous changes in world prices. However, notwithstanding these precedents, one can still ask: why compensate at all in the face of technological change? That is, what is the justification for a social safety net as proposed by the Myers' Committee?

Economic theory provides the well-known Pareto criterion for evaluating the worthiness of the introduction of a particular change: if at least somebody benefits and no one is harmed, a change is desirable. However, more often than not, someone is harmed, at which point one can apply compensation criteria to ask whether those harmed could be compensated to yield a net improvement. And if potential compensation does yield a net improvement, the further issue is whether compensation ought in fact take place if a change is to be justified, or whether it is sufficient that compensation be potentially possible. Adherence to the rule of actual compensation precludes change when the information costs of identifying gainers and losers are excessive.
The Myers' Committee social safety net proposal would appear to be an application of the actual as opposed to the potential compensation principle. One can appreciate the equity foundation for the actual compensation principle, and hence for the social safety net; but then the compensation scheme must embody the means of distinctly identifying those who ought finance the requisite transfers and those who ought be the recipients of the transfers. Any arbitrariness in identification would detract from the equity motivation underlying compensation.

Alternatively, one can take a broader perspective of government's responsibility for social welfare. Any number of different specifications of social welfare might imply redistributive transfers in the face of changes in income distribution generated by technical change. In particular, Max Corden (1974) has observed that governments generally tend to adopt a conservative social welfare function manifested in a reluctance to pursue policies which, notwithstanding their general benefit, harm specific groups in society. The Myers' Committee proposal for a social safety net fits into this scheme by providing income maintenance for individuals who, as a consequence of change, would otherwise suffer a fall in their incomes.
III IDENTIFICATION OF WHO GAINS AND WHO LOSES

Let us then accept the Myers' proposition that actual compensation ought to occur in the wake of technical change. If the gainers are to compensate the losers, we need to identify the individuals in each category. Begin with those who gain. Benefits derive from technical change, in that, as with any change in the economic environment, economic agents are confronted with new opportunity sets; for some individuals these sets will have expanded, with the market mechanism providing incentives to adapt to changed circumstances by seeking new optimizing equilibria. In particular, those firms introducing an innovation gain via either increased efficiency in utilization of existing factors or perhaps exploitation of previously non-utilized inputs. Competition may in time erode the rents associated with a particular innovationary activity. However, consumers gain via a reduced price for an existing product, a quality-adjusted reduction in price, or perhaps the introduction of a new product entirely - all changes which can be evaluated in terms of consumer surplus. So the gainers are the firms which earn rents as a consequence of an innovation, and consumers at large.

As for the losers, unanticipated new technology imposes losses on the individuals associated with the old technology in proportion to the inflexibility of the association. So factors of production inflexibly tied to the old technology lose the most, while those factors which can readily adjust to new employment lose the least.

One can categorize labor employed in conjunction with a technology about to be superceded into three categories; those individuals who notwithstanding the technical change retain employment associated
with the old technology, those individuals who are made redundant but are immediately able to find alternative employment at a comparable wage, and those individuals whom the technical change makes redundant but who do not find alternative employment and so enter the unemployment pool. It is only the last category of workers whom the Myers social safety net would encompass. Those workers who adjust immediately to other employment are mobile factors with minimal association with the old technology. The more technology specific individuals who stay behind do not physically adjust at all, but precisely because of their specific skills, with respect to the old technology, they might be expected to suffer a loss in income as the value of their specific human capital investment is written down. But they would fall outside of the social safety net.

On the other hand, in the presence of downward-wage rigidities (where the wage encompasses a return to specific human capital), employees tied to the old technology who stay behind and continue to operate in conjunction with that technology would not lose at all; but because of the minimum-wage, the technical change would give rise to unemployment. In Figure 1, $S$ is the inelastic supply of sector-specific labor and $w_1$ is the market-clearing real-wage with the old technology. The value of the marginal product of labor is given by $VMP_1$; as the consequence of the introduction of the new technology, $VMP_2$ is now the reduced value of marginal product and $w_2$ would be the new market-clearing wage. If the wage cannot fall below $w_1$, then the new technology leads to unemployment ($L_1 - L_2$). The social safety net would aid these latter workers - but if these unemployed workers are truly specific to the old technology, then they would become
permanent members of the unemployment pool. However, if the wage could fall, society would be saved the value of the output foregone indicated by the shaded triangle. The appropriate adaptation in the case of such factors specific to a superceded technology is to permit these factors to remain employed in conjunction with that technology so long as the value of their marginal product is positive. Equity may dictate a lump-sum income supplement but maintaining the previous market-clearing wage and providing compensation for those factors unemployed as a consequence of the technical change yields a socially inefficient outcome. Moreover, the social safety net reinforces the downward wage rigidity insofar as the social safety net is widely known to exist to cushion the income fall of those factors who become unemployed. One should further emphasize that the primary cause of unemployment here is not the introduction of the new technology, but rather the wage-rigidity itself.

The social safety net encompasses labor: but labor is not the only factor of production harmed by the introduction of new technologies. The owners of capital embodying old technologies have their incomes inexorably tied to these old technologies, and it is they, perhaps
more so than labor, who are harmed when a given technology is unexpectedly superceded. In particular, the owners of the capital comprising the investment of the marginal firm -- or the marginal division of a diversified firm -- will see the discounted present value of continuing to produce fall to zero, and consequently the firm will be shut down. An inframarginal firm employing a superceded technology will continue to operate, and as such will absorb the full extent of the capital loss. It is ironically the firm which fails that incurs the lesser loss. For example, the invention of the steamship imposed capital losses on owners of sailing vessels: owners of old (marginally economically efficient) ships went out of business, but owners of the newer, more efficient sailing ships took the loss and remained in business. Of course, the Myers social safety net would not have helped the owners of any sailing vessels, although it would have helped those seamen who spent some time unemployed while adapting their skills from trimming sails to shovelling coal.

There is then an evident asymmetry in the coverage provided by the proposed Myers social safety net to the losers from technical change. Those factors of production which adjust via the transition through the unemployment pool to new employment are caught in the net. However, those factors which adjust by writing down capital values and do not physically adjust precisely because of their ties to the old technology are not compensated.

IV JUSTIFICATIONS FOR THE ASYMMETRY IN THE NET

Are there, then, justifications for such an asymmetry in the social safety net? A number of considerations might be raised.

(i) Capitalists (or the owners of capital) introduce technical change, and therefore, presumptively there is no need to compensate capital. A variation of this proposition is that one does not hear the owners of capital complain about the technical change; complaints
are confined to labor. The implication is that the owners of capital must gain from technical change, with the losers confined to labor. One might, however, take issue with this line of argument. If all innovating decisions affecting a particular market were internalized, then one could indeed presume that by revealed preference for the types of technologies to be employed, the owners of capital are not harmed by decisions to innovate. But markets are not necessarily monopolistic, nor collusively organized. Competitive innovationary activity would harm those individuals with claims over capital invested in forms tied to old technologies. Such harmed owners of capital might simply have no recourse to 'complaint' about technical change while impacted labor might complain because firms are tied together in a competitive relation, in contrast to the cooperative relation of capital and labor in the production process. The difference in these relations does not imply that technical change harms individuals whose income is based on the sale of labor services, but does not harm individuals whose incomes derive from the returns to capital embodying superceded technologies.

(ii) Owners of capital have the means of spreading risk by diversification of their investments, and hence do not require the insurance provided by the social safety net; whereas such opportunities for risk-spreading are not available to individuals whose incomes derive primarily from the sale of labor services. That is, risk-averse owners of capital can reduce risk by appropriate portfolio adjustment, but labor is subject to an individability in the sales of its services, and hence is denied the opportunity of diversification. Still, the diversification option is not open to all individuals earning income from capital; for sufficiently small holdings of capital, indivisibilities become
important, and in particular, this is the case for 'small businesses' where the investment has been undertaken by self-employed persons. The provisions of the social safety net would cover a self-employed person impacted by technical change in the individual's guise as a labor input, but it would not cover the harm incurred by the individual as the consequence of the effect of technical change on the value of his capital investment.

Also, for many individuals home ownership represents a disproportionate share of their portfolios. If technical change reduces employment opportunities in a particular geographic area, then certain homeowners will take capital losses. Yet, as undiversified owners of place-specific capital, these individuals are offered no compensation.

(iii) It is difficult to provide a special safety net for owners of capital harmed by technical change because the source of a decline in the capital value of an enterprise can often not be identified. Since it is virtually impossible to distinguish between new technology induced losses and losses attributable simply to poor judgement or lackadasical management, insurance cannot be provided for owners of capital. However, similar informational problems about the source of income loss might also be expected to arise in the case of income earned from the sale of labour services. More generally, given the complexities of the general equilibrium system, a technical change in any one activity can permeate any number of industries indirectly linked to the industry wherein the change originally took place. In these indirectly impacted industries labor as well as capital may be harmed, but verification of the cause of income loss may be difficult. There is accordingly a general problem not particular to capital in the directly impacted industry in identifying the parties harmed by a technological change.
V. A SOCIAL SAFETY NET OR MERELY A PROPOSAL FOR VARIATION
IN THE NATURE OF UNEMPLOYMENT BENEFITS?

Appropriate certification of the parties harmed by technical change is a particularly troubling one in design of a compensatory scheme. Technical change is after all only one of many potential causes of a decline in the value of the marginal product of a factor of production. It is perhaps only the individual himself who knows whether he has suffered a real income loss, and then even he himself might be in doubt as to whether or not technical change in some industry linked via interindustry flows to his industry was at fault. Independently of the individual's awareness of the source of his loss, self-certification admits the above "moral hazard" problem -- i.e., the possibility of misrepresentation of the true cause of loss and foregone opportunities which might have been available to defray the loss. It is accordingly not surprising that the proposed Myers social safety net does not entail attendant attempts to identify the source of income loss (for labor, covered by the net), but rather compensation is independent of whether or not technological change was the indicated source of loss. In their own words,

"The Committee does not believe that it would be practical or equitable to distinguish between people who are retrenched for different reasons, and regards its recommendations (for compensation) as applying to all persons who are laid off through no fault of their own". (p.179).

So the social safety net, suggestively motivated to compensate individuals adversely affected by technological change, in the final analysis becomes but a general income maintenance scheme which complements unemployment benefits for whatever reason individuals are retrenched (p.181).
The suggestion is that informational difficulties require that the social safety net be cast in this overly wide manner if the net is to catch all those individuals retrenched, and consequently unemployed, because of technological change. But since it would appear that the social safety net is applicable to only those same individuals who are eligible for unemployment benefits (Myers, 1980), the net would be too narrow in not encompassing individuals legitimately adversely affected by technical change but not eligible for unemployment benefits; in particular, married women with employed husbands.

In summary then, with respect to coverage, the Myers Committee's proposed social safety net, which is ostensibly intended to provide compensation for individuals adversely impacted by technological change, is overly broad in being but a supplementary income maintenance scheme for only such individuals who are already eligible for unemployment benefits. But notwithstanding this overly broad coverage, the net's coverage is narrow in neglecting those individuals earning income from labor and not eligible for unemployment benefits, and is also narrow in not including individuals harmed by technological change and earning income from capital (both physical and human) tied to superseded technologies. The Myers' social safety net would appear to have little to do with a compensation motive for ameliorating the plight of individuals harmed by technical change, but rather merely constitutes a proposal for variation in the nature of unemployment benefits.
VI. THE INCENTIVE FOR ADJUSTMENT

One of the aims associated with a compensatory scheme in principle linked to technological change must be to facilitate adjustment by those factors that can adjust; that is, by factors not inexorably linked to an old technology. Quite naturally, it is mobile factors which have the option of adjustment, although retrenchment may mean that adjustment occurs via the transition through the unemployment pool. In contrast with standard unemployment benefits, the Myers Committee proposes that its income maintenance scheme be partially financed by those employers deciding upon the redundancy of a particular employee (p.182). Insofar as a redundancy decision is associated with technological change, this proposal essentially translates into a tax on innovating firms, and so impedes the adoption of new technologies.

The Myers Committee does not explicitly suggest an externality argument for the tax and economic theory does not pretend to understand the negative social ramifications of unemployment. If firms hire less than the socially optimal number of employees, then a subsidy, not a tax, is in order. If minimum wage rigidities cause unemployment, then the subsidy would simply mop up the unemployment caused by the unemployment's real source. There may be some second best justification for the subsidy to firms, to defray the wage bill, but there is no argument for slowing technical change in particular in order to internalize any social costs of unemployment.

By making it costly for the firm to dispense with unwanted employees, the proposal would further inhibit firms' hiring of labor in anticipation of future labor-saving innovations. And when a labor-saving technological change is introduced, the cost to the firm of laying off an individual worker drives a wedge between the value of that individual's marginal
product and his wage. Since for a mobile factor the wage earned would tend to be the same as that in alternative employment (if it were less, he would presumably change employment voluntarily), a loss is incurred through inefficient resource allocation, for the value of the marginal product in alternative employment exceeds that in current employment within the innovating firm.

By deviating from the standard unemployment benefits scheme in having their supplementary scheme internalize some of the costs of such benefits within the firm, the Myers' Committee proposal accordingly hinders the very adjustment to technological change which one might have supposed the scheme would seek to facilitate.

VII. COMPARISONS WITH TRADE-RELATED ASSISTANCE SCHEMES

There is a certain similarity between the general social benefit from technological change in conjunction with the adverse effects on some sub-segments of society, and the general social gains which accrue from liberalization of international trade in accompaniment with the specific harm suffered by previously protected interests. It may accordingly be instructive to briefly recount the experience of two trade-related income maintenance schemes, one instituted in Australia in the wake of the 1973 25 percent across-the-board tariff cut and the other a continuing trade adjustment assistance scheme in the U.S.

In Australia an income maintenance scheme, the Structural Adjustment Assistance Program, was instituted in conjunction with the 1973 across-the-board 25 percent tariff cut with the intent of providing compensation for losses incurred as a consequence of the reduction in tariff protection. The circumstances of such trade-related change are
similar to those of technical change, in that in both instances exogenous influences lead to changes in the value of the marginal product of factors of production - although in distinction to technical change, income changes due to reduced protection are the direct consequence of administrative decisions rather than following from market-induced decisions on the timing of introduction of new processes and products. The Structural Adjustment Assistance Program ran for some 18 months after the tariff cut, when it was discontinued. The scheme aimed principally at directly affected workers, with certification provided by employers' declarations that the cause of retrenchment for a particular individual was the tariff reduction. The main beneficiaries of the scheme were married women ineligible for unemployment benefits. While considerations relating to the perceived time period necessary for adjustment to the tariff cut underlay the discontinuation of the scheme, an important consideration was also the scheme's creation of a two-class system of unemployment benefits - a situation which the Myers Committee seeks to avoid or at least not exacerbate, by the limitation of income maintenance benefits only to those already eligible for unemployment benefits. The Structural Adjustment Assistance Program was also more comprehensive than the Myers Committee's proposed social safety net in that firms as well as employees were eligible for assistance; although the provisions for assistance to affected firms were much more limited than those relating to retrenched employees. - with very few firms actually availing themselves of assistance. Like employees, firms had to leave the industry (shutdown production) in which event they were eligible for subsidised management consultancy. However, one would expect the inframarginal specific factors of production comprising firms to take the losses associated with the reduction in tariff protection in the
form of reduced rents from continued production. Hence the Structural Adjustment Assistance Program, during its brief operation, also aided those factors of production which were sufficiently mobile to actually adjust by seeking alternative employment, but made no provision for those factors which, because of their industry-specific nature, could be potentially most harmed by a reduction in the price of their industry's output.²

More broadly based evidence on the operation of income maintenance schemes is provided by the 1962 U.S. Trade Expansion Act and the subsequent Trade Act of 1974. These Acts were similar to the Australian Structural Adjustment Assistance Program, in that they incorporated provisions for direct reallocation assistance to workers, firms and communities to mitigate the isolated adverse consequences of evolving international comparative advantage while at the same time securing the benefits of freer trade.³ U.S. adjustment assistance, like the proposed Myers Committee safety net, aims not at inframarginal (non-adjusting) workers, but at workers dislocated or made redundant by specific circumstances outside the scope of workers' discretion. The most serious problem with the U.S. Trade Adjustment Assistance Program would appear to be that of certification. It is generally acknowledged that the program instituted under the 1962 Trade Expansion Act was a failure. The criteria for worker certification were inflexible and stringent, and the time interval between injury and delivery of benefits was on average twenty-two months. Even though the 1974 Act liberalized the benefits and criteria for assistance, substantial uncertainty with respect to certification still persists, with the consequence that even relatively mobile labor groups prefer "escape clause" remedies. As with Myers Committee safety net, Trade
Adjustment Assistance offers no relief to firms and workers indirectly harmed by change. This has been proposed as an important source of resistance to the program.\footnote{1}

In common with the Myers Committee safety net, the Trade Adjustment Assistance program recognises that as the industrial structure changes, the pattern of skills demanded also changes, and the 1974 Trade Act includes some manpower training provisions specifically for trade impacted workers. However, from the standpoint of the economy as a whole, there is no evidence that subsidies to train "trade-related" unemployed workers does anything but displace other workers who would otherwise have been provided with the opportunity to participate in such training programs.

In distinction to the Myers Committee's proposed compensation scheme for the consequences of technical change, the U.S. Trade Adjustment Assistance Program subsidises affected employers (rather than taxing them by making them liable for some of the costs of adjustment by employees), and the Australian Structural Adjustment Assistance Program also accepted the principle of compensation to firms as well as employees. One may seek to explain the Myers Committee's proposal in terms of the differential effects of technical change and changes in an industry's international competitiveness. Technical change takes place within an industry and affects the manner in which inputs are combined to produce an industry's output; so now inputs within the industry displace previously employed factors of production. In contrast, with trade-related change the impact is on the whole industry, and all industry factors are affected. Hence non-discriminatory treatment for employers and employees under the Trade Adjustment Assistance Program, in that both are assisted, and the provisions covering affected firms under the Australian tariff-compensation scheme.
VIII CONCLUSION

There is no evident basis in the case of technical change to sustain the dichotomy of employers as the beneficiaries of change and a subset of employees (those retrenched) as the losers. The very factors which are adversely affected and do not adjust by leaving the industry potentially suffer greater losses than mobile factors. It does not appear appropriate to argue that the different underlying causes of change -- trade-related change in the one case and technical change in the other -- justify or explain the differential compensation treatment embodied in the Myers Committee social safety net and in various trade-related assistance programs. And it does not appear that the narrower Myers Committee safety net would constitute an adequate application of the Pareto principle for change with compensation in practice rather than in principle. The safety net proposed does not cover all those adversely affected by technological change. It does, however, cover labour already eligible for unemployment benefits and in particular those unemployed for reasons other than technological change.
FOOTNOTES

1. This is a static argument in the sense that we assume the individual cannot acquire new skills over time. In fact, if a worker has a sufficiently long time horizon, then he will presumably attempt to acquire a new set of skills which he calculates will eventually yield an income higher than welfare benefits.

2. See, for example, Priorities Review Staff (1975). Also, the survey findings of the Manpower Evaluation and Review Branch (1975) are consistent with this paper's theoretical analysis. In particular:

   "An impression that the recipients of income maintenance were to some extent marginal workers was gained from the fact that a relatively high proportion of them had been employed in the job from which they were retrenched for only short periods, and had suffered a period of unemployment in the 12 months prior to retrenchment." (p.29).

3. For an account of these programs see Murray and Egmond (1970), Leveson and Wheeler (1980) and Frank (1977).

REFERENCES


