

**A REVIEW OF
THE COMMISSION ON SOCIAL WELFARE'S
MINIMUM ADEQUATE INCOME**

THE ECONOMIC AND SOCIAL RESEARCH INSTITUTE

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Tim Callan, Brian Nolan and Christopher T. Whelan

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GENERAL SUMMARY

Revisiting Adequacy

A central recommendation of the Commission on Social Welfare (CSW) in its 1986 Report was that all social welfare recipients should be entitled to a minimally adequate basic payment, which it estimated to be in the range £50-£60 per week for a single person in 1985. As an urgent priority, the Commission recommended that basic personal rates be brought up to £45 per week. Since the Commission reported, its estimates of minimally adequate income have played an important part in debates about the adequacy of social welfare support rates and in official policy statements.

This study, commissioned by the Department of Social Welfare, reviews the calculations of the minimum adequate rates using the CSW's methodologies and other appropriate methodologies; compares these calculations with current social welfare weekly payment rates and the CSW's rates updated in line with trends in the Consumer Price Index and net earnings and taking into account secondary benefits; evaluates the extent to which adoption of the newly calculated rates would improve the effectiveness of social welfare payments; analyses the likely impact of implementing the newly calculated rates on incentives to work; discusses the wider context of employment opportunities and economic efficiency; and considers the appropriate method of uprating payment rates in the future.

Neither the methods employed by the CSW and updated here, nor the alternative approaches discussed in this study, allow one to derive in an unproblematic, objective and scientific way estimates of income adequacy which would be universally acceptable and convincing. Statements about adequacy reflect judgements, values and attitudes: research cannot substitute for, but can inform, such judgements.

The CSW's starting-point was that "To be adequate, payments must prevent poverty, and in our view poverty must be judged in the light of actual standards of living in contemporary Irish society" (p. 123). Application of that criterion is inevitably imprecise, so this study aims to provide as many relevant pointers as possible rather than to arrive at a particular figure.

The Commission on Social Welfare's Methods of Estimating an Adequate Income

The CSW applied seven different methods to establish what would be an adequate income for a single adult living alone. Re-application of two of these methods with up-to-date data is not yet possible. The remaining five methods, applied to up-to-date data, produce estimates of the minimum adequate income for a single adult in 1996 from £75 to £96 per week – a wider range than 1985.

The CSW's methods have strengths and weaknesses. Three of these methods derive adequate income simply as some proportion of average earnings or income. This links adequacy directly and transparently to average living standards in the society, but the choice of a particular proportion of the average is essentially arbitrary, and the approach is stronger in assessing how adequacy has been changing over time than in deriving an adequate income at a point in time. The other CSW methods seek to identify official judgements about income adequacy from the income threshold for entitlement to a medical card, the level of tax allowances, and the wage minima set by Joint Labour Committees. It may not however be valid to infer judgements about adequacy from policy decisions on these instruments, which are in any case affected by, rather than independent of, the level of social welfare rates.

Other Perspectives on Adequacy

Alternative perspectives can also contribute to better informing official, political and societal judgements about adequacy. The main alternatives considered in this study are as follows:

Income poverty lines: based on the large-scale household survey carried out by the ESRI in 1994, a purely relative income adequacy standard for a single person set at 60 per cent of average equivalent household income would be about £81-86 per week in 1996 terms, while a standard set at 50 per cent would be about £68-72 per week. In the similar survey carried out in 1987, a very high proportion of households relying on Unemployment Assistance were below half average income, but their poverty risk had fallen by 1994.

Non-monetary deprivation indicators: for households relying on the various social welfare schemes, the percentage on low income and experiencing basic deprivation was mostly stable or fell between 1987 and 1994. There seems little prospect of identifying a specific income level below which people are deprived of what are generally regarded as necessities and above which they are not, or even a threshold below which deprivation escalates very rapidly.

Respondent's assessments: in 1987, households relying on social welfare and comprising a single adult themselves regarded a figure of about £58 per week as the minimum necessary to "make ends meet". By 1994, subjective evaluations of such households were that a minimum of about £80-87 per week was needed. The

income regarded as minimum by other household types generally rose to a similar extent over the period.

Budget standards: the study by Carney *et al* of the "costs of a child" concluded that in 1992-94 income support for teenagers was significantly below the basic minimum needed. The main strength of this approach is that people can concretely identify with the living standards incorporated in the consumption basket, the main weakness is the number of subjective decisions involved about what is included in an "adequate" consumption basket and to what standard.

Case studies: information from the Money Advice and Budgeting Service funded by the Department of Social Welfare provides an insight into the financial difficulties in which some (anonymous) households assisted by the service find themselves. However, one cannot draw direct conclusions about the adequacy of social welfare payments from these cases, since they have mostly been referred to the advice service precisely because of the unusual scale of their debts and financial difficulties.

Cross-country comparisons: comparing the relative generosity of social security systems across countries offers another perspective on adequacy, though fully valid comparisons are difficult and inferences for adequacy must be drawn with care. Irish social welfare rates are generally more generous relative to average earnings or income than those in the UK, but if anything below the average for EU countries as a whole.

Adequacy Estimates and Current Social Welfare Rates

The various approaches examined (the CSW's and others) produce estimates of the minimum adequate income for a single adult in 1996 ranging from £68 to £96 per week. The range recommended by the CSW as minimally adequate for 1985, when uprated simply in line with price changes to 1996, is £68-81. Uprating the CSW's range in line with net earnings in industry gives the much higher figures of £84-100, reflecting the growth in real take-home pay over the period.

The basic rates of payment for a single adult under the different social welfare schemes are currently (1996/1997) in the range £62-75 per week. Even the lowest rate, paid by short-term Unemployment Assistance and Supplementary Welfare Allowance, has reached the CSW's priority rate uprated in line with prices. However, these, and the £64.50 paid by Unemployment and Disability Benefits, are below the bottom of the CSW's recommended range uprated in line with prices, £68. Contributory Old Age and Widow's/Widowers pensions now pay above that figure, and so do non-contributory Old Age and Widow's/Widower's pensions if one includes the £6 living alone allowance. Since the bottom of the range of current adequacy estimates is also £68, the same conclusions apply using that as standard of comparison. Focusing only on the CSW's own methods the bottom of

the range of adequacy estimates is £75, and most schemes currently pay below that.

In 1985, the lowest social welfare rates fell much further below the bottom of the range the CSW then recommended. Short-term Unemployment Assistance and Supplementary Welfare Allowance were then only 64 per cent of the bottom recommended figure. Considerable convergence in rates has taken place since then, with priority given since 1986 to bringing up the lowest rates of payment. This has brought the lowest rates a good deal closer not only to adequacy benchmarks indexed to prices but also to those indexed to average net earnings. Support rates for the elderly, on the other hand, have lagged significantly behind real net earnings.

The most substantial social welfare increases since 1986 have been in the adult rate on which the CSW concentrated. The payment for adult dependants has increased less rapidly, and is down to about 60-62 per cent of the adult rate compared with over 70 per cent in 1985. This is in line with the CSW's recommended relationship between the two but that was not based on an in-depth examination of the issue.

In assessing the adequacy of the basic rate of cash transfers, additional cash payments and non-cash benefits also have to be taken into account, and these have increased in importance since the CSW reported. The most important are entitlement to medical card cover, assistance with heating and energy costs, and housing subsidies. These and other extra benefits could add up to 20 per cent to the value of basic cash support, which could make a considerable difference *vis-à-vis* adequacy benchmarks derived from, for example, average income. However, incorporating these benefits systematically in assessing adequacy is difficult, because entitlements vary a great deal by scheme and across households in different circumstances; assigning them a value is in some cases problematic (particularly for housing); and simply adding an average estimated value for these benefits to the basic payment rate is not particularly meaningful.

Assessing the Direct Impact on Poverty

Exploring the likely impact of increasing social welfare payment rates is a difficult and complex task. Changes in welfare rates, particularly those involving very substantial changes in relative terms, can have far-reaching implications not only for those dependent on welfare, but for the wider labour market and the economy in general. This study first looks at the impact of implementing alternative adequacy standards on income poverty on the basis of a technical assumption that there would be no change in behaviour – although it must be emphasised that possible impacts on incentives and behaviour are central to an overall assessment of alternative payment rates.

Four different payment rates are used, namely £68, £75, £82 and £90 for a single person per week in 1996 terms, with corresponding increases for adult and child dependants. The costs of implementing these payment rates are approximately £160m, £530m, £940m and £1,400m per annum respectively. These sums equate to tax rate increases (or tax cuts forgone) of about 1+ percentage points, 4 to 5 percentage points, 8 percentage points and 11 or 12 percentage points respectively in all tax rates (standard rate, top rate and marginal relief rate). Within this framework of analysis, with the £68 payment package just under half of the additional social welfare expenditure would reach its target, in the sense that it goes towards reducing income shortfalls for families below that income level; and the package would close about one-quarter of the aggregate poverty gap relative to that income standard. For the £75 per week package, about 55 per cent of the additional expenditure would go towards reducing the income shortfalls, and more than half of the initial income gap would be closed. At the highest standard considered (£90 per week), almost 60 per cent of the additional expenditure would be "on target" and about 70 per cent of the initial income shortfall would be reduced – again, on the technical assumption of no change in labour market or other behaviour.

Overall, the results indicate that increases in social welfare payments could, on the technical assumption of no change in behaviour, have a substantial impact on rates of income poverty – whether measured by the numbers falling below income poverty lines, or income shortfalls relative to that line. But a substantial proportion of the additional expenditure does not go towards reduction of poverty at the relevant income standard; and some of the income shortfalls are not amenable to reduction through increases in welfare payments as some individuals on low incomes find themselves ineligible for any scheme. The factors underlying this deserve further investigation, but complete effectiveness and efficiency would require pound for pound withdrawal of benefit above the target income standard, with very serious implications for incentives.

Assessing the Impact on Work Incentives

Given the overall budgetary constraints and, in particular, the net revenue which the tax-transfer system must generate to finance other government expenditures, there is a trade-off between the level of income support and the effective tax rates on income from employment. This trade-off is brought into sharp relief by simple tax-transfer systems, such as proposals for a basic income, but it is also inherent in more conventional systems including the current Irish tax-transfer system.

It comes as no surprise, then, that an increase in weekly social welfare payment rates from around £64 for a single person in 1996 terms to £90 would involve sharp increases in taxes (or tax cuts forgone) and a substantial worsening

of financial incentives to work. Following the increase in tax rates which it would entail, about 30 per cent of employees and 64 per cent of the unemployed would face replacement rates of more than 70 per cent, with the likely outcome being significant reductions in labour supply and employment and increased unemployment.

A more modest increase in social welfare rates, to a level of around £68 per week for a single person, would have a much smaller impact on work incentives. The proportion of employees facing replacement rates of over 70 per cent would rise from just under 16 per cent to just over 18 per cent, while the proportion of unemployed persons facing high replacement rates would rise from 31 per cent to about 39 per cent – but with most of the increase occurring in the 70 to 80 per cent replacement rate bracket. An increase in the payment rate to £75 would have a more substantial impact on work incentives, with over half the unemployed facing a replacement rate above 70 per cent.

The direction and scale of the impact of increasing social welfare rates on work incentives is reasonably clear from our analysis, but estimates of the likely behavioural response to such changes in incentives are not currently available, and are of central importance in establishing the crucial trade-offs between income support rates, employment and poverty. A number of approaches can offer helpful insights into these central questions, including the estimation and simulation of labour supply responses at micro-level, macroeconomic modelling, and, in time, approaches combining information from micro- and macroeconomic models.

Uprating Social Welfare Rates

Examination of the approaches to uprating social welfare rates publicly articulated by different Irish governments over the past twenty-five years reveals a number of consistent themes: the need to protect the value of social welfare payments for pensioners against inflation, concern about work incentive effects, the need for recipients to be able to afford a basic minimum standard of living, the desirability of recipients sharing in improvements in the living standards of the community, and affordability in terms of the state of the economy and the public finances.

If adequacy is to be assessed against the standards of the society at a given point in time, as the CSW envisaged, the target will move up over time as general living standards in the community rise, but there is wide scope for debate about the most appropriate indicators or reference points to employ. The information currently available for Ireland from which such indicators might be constructed is limited, but progress can still be made towards a more explicit public process of evaluating adequacy in uprating, as suggested in the European Council's Minimum Income Recommendation, employing available reference points such as changes in prices, net earnings and incomes. This would not imply that adequacy should be

the only consideration in uprating decisions. Indeed, a complementary process could focus on assessment of efficiency and incentives aspects. Both public debate and political choices about social welfare rates, adequacy and economic efficiency would then be better informed and necessarily more explicit about the hard choices involved.

Chapter 1

INTRODUCTION

In 1983, the Commission on Social Welfare (henceforth CSW) was established by the Minister for Social Welfare to review the operation of the Irish social welfare system. A central recommendation of the Commission in its 1986 Report was that all social welfare recipients should be entitled to a minimally adequate basic payment, which it was estimated would in 1985 be in the range £50-£60 per week for a single person. These figures were produced by applying a number of different methods which were intended to reflect conventional living standards in Irish society. As an urgent priority, the Commission recommended that basic personal rates be brought up to £45 per week. Since the Commission reported, its estimates of minimally adequate income have played an important part in debates about the adequacy of social welfare support rates, and its recommendation in this regard have featured in programmes for government and official policy statements. The 1994 Programme for Competitiveness and Work (PCW) noted that by the Budget of that year all social welfare weekly payments had reached the Commission's priority rates and at least 90 per cent of the Commission's main recommended rates, and promised further progress towards those rates.¹

The December 1994 policy agreement between the parties to the present government, "A Government of Renewal", stated that the ESRI would be commissioned to review the minimum adequate income rates recommended by the Commission on Social Welfare.² Under the terms of reference agreed between the Department of Social Welfare and the ESRI, this study is to:

- (1) Review the calculations of the minimum adequate rates, including equivalence scales, etc., using the CSW's methodologies and other appropriate methodologies which may have been developed subsequently, taking account of revised macroeconomic and other sources (including the ESRI's Household Income Survey of 1994).

¹ PCW para. 6.6 p. 62.

² Para. 114.

- (2) Compare these calculations with current social welfare weekly payment rates and the CSW's rates updated in line with trends in the CPI and net earnings in the period since the publication of the Commission's report. This evaluation should take into account secondary benefits (widely defined) in the context of defining adequacy.
- (3) Evaluate the extent to which adoption of the newly calculated rates would improve the effectiveness of social welfare payments in reducing income inequality compared with current rates and CSW rates as updated by the CPI.
- (4) Analyse the likely impact of implementing the newly calculated rates, taking account of secondary benefits, on incentives to work. Discuss the wider context of promoting employment opportunities and economic efficiency.
- (5) Consider the appropriate method of updating payment rates in the future.

This report presents the results of the study. It is structured as follows:

Chapter 2 reviews approaches to assessing minimum adequate income levels which have been adopted in the international research literature and their strengths and weaknesses; in doing so, the nature of the question and the difficulties which arise in answering it are brought out.

Chapter 3 describes the range of methods employed by the Commission on Social Welfare in arriving at minimum adequate income levels, and applies them with up-to-date data to derive the levels they would now produce.

Chapter 4 discusses and explores empirically what can be learnt about the adequacy of social welfare rates from other approaches using household survey data, notably the use of subjective assessments of survey respondents about income adequacy, relative income poverty lines and non-monetary indicators of deprivation.

Chapter 5 brings together the minimum adequate income calculations produced by the different methodologies, and compares them both with current social welfare rates and the CSW's recommended rates updated in line with the CPI or with earnings. The need to take non-cash benefits into account in assessing adequacy is also discussed at this point.

Chapter 6 then uses the ESRI tax-benefit model to carry out a static simulation of the effectiveness and efficiency of the additional social welfare expenditure implied by alternative adequacy estimates in reducing poverty.

Chapter 7 uses the tax-benefit model to examine the impact of alternative new rates on work incentives.

Chapter 8 considers the way social security payment rates are updated and the manner in which adequacy of these rates enters into the process.

Finally, Chapter 9 brings together the findings of the study and draws out their implications.

It is worth emphasising right at the outset that neither the methods employed by the Commission on Social Welfare and updated here, nor the alternative approaches which we also discuss, allow one to derive in an unproblematic, objective and scientific way estimates of income adequacy which would be universally acceptable and convincing. All the methods of addressing this issue currently in use have their problems, and the search for a methodology which can provide an unambiguous answer to the question "how much is adequate?" is in our view misguided. To be adequate, income must be sufficient to allow one to avoid poverty or live decently within one's community: the question of what constitutes adequacy, like poverty, is not amenable to "scientific" determination. Statements about adequacy reflect judgements, values and attitudes: research cannot substitute for, but can inform, such judgements. In the same manner, research can be enormously helpful in teasing out the complex inter-relationships between adequacy and economic incentives, and one of the aims of this study is to illuminate these issues. It does not however attempt to adjudicate on where the balance of advantage lies when the wider economic and distributional repercussions of providing particular levels of support to social welfare recipients are taken into account, since that is once again a matter for political decision. The results contained in this study are thus presented in the belief that alternative perspectives on the problem can contribute to better informing official, political and societal judgements about adequacy.

Chapter 2

MEASURING ADEQUACY

2.1 Introduction

This study is concerned with reviewing the adequacy of Irish social welfare income support levels. In this chapter we discuss what adequacy means and describe approaches which have been adopted to measuring it elsewhere. This sets the stage for the remainder of the study which focuses on the approaches to deriving minimum adequate income levels for Ireland adopted by the Commission on Social Welfare and some alternatives.

2.2 Defining Income Adequacy

Posing the question "Are social welfare levels adequate?" brings one straight to the central conceptual issue in assessing adequacy, "adequate *for what?*" The answer provided by the Commission on Social Welfare (CSW) was that "To be adequate, payments must prevent poverty, and in our view poverty must be judged in the light of actual standards of living in contemporary Irish society" (p. 123). In defining poverty in turn the CSW concurred with Townsend's definition that:

"Individuals, families and groups in the population can be said to be in poverty when they lack the resources to obtain the type of diet, participate in the activities and have the living conditions and amenities which are customary, or at least widely encouraged, or approved, in the societies to which they belong. Their resources are so seriously below those commanded by the average individual or family that they are, in effect, excluded from ordinary living patterns, customs and activities" (1979, p. 31).

The CSW thus saw poverty as exclusion from ordinary participation in society due to lack of income, took the position that it is possible in principle to estimate the level below which income should not fall to allow minimal participation in society, and identified that income level with adequacy of social welfare payments (p. 124).

Very much the same understanding of poverty and adequacy underlies the National Anti-Poverty Strategy (NAPS) currently being developed by the Irish government following the UN World Summit for Social Development held in Copenhagen in 1995. The NAPS Overview Statement discussion document put

forward the following working definition of poverty, to be refined in the course of drawing up the strategy:

"People are living in poverty, if their income and resources (material, cultural and social) are so inadequate as to preclude them from having a standard of living which is regarded as acceptable by Irish society generally. As a result of inadequate income and resources people may be excluded and marginalised from participating in activities which are considered the norm for other people in society" (NAPS, 1995, p. 3).

This identification of adequacy with income poverty lines is not universally accepted. Veit-Wilson (1987; 1994) for example argues that income poverty lines are scientific measures of the minimum incomes needed to take part in society, whereas social security rates should be assessed against a government's "minimum income standard", based on political decisions about the minimum politically acceptable level of living that government wants to ensure for all citizens. Findings from studies of poverty will inform decisions about such minimum income standards, but "the standard comes from the political decision and not from the scientific finding" (1994 p. 7), and could be above or below a poverty line. While this distinction helps to highlight the role which attitudes and values must play in decisions about adequacy, in practice one would have to agree with the conclusion reached by the Advisory Group set up by the Australian Government to advise on benchmarks for assessing the adequacy of social security there:

Should the government nominate an explicit income level as an "adequacy benchmark", the income level would be perceived as, *de facto*, an official poverty line. As such, it would be subject to scrutiny in relation to its strengths as a poverty indicator and would attract the expectation that the benchmark would constitute a level below which payments would not fall. ... for the purposes of public presentation, there is little prospect of maintaining a distinction between an explicit adequacy benchmark and an income poverty line (DSS, 1995, p. 6).

This does not mean that all those found at a particular point in time to have incomes below an adequate level will necessarily be experiencing poverty in the sense of inability to participate in the ordinary life of the community. As our own research for Ireland has highlighted, some of those on low income in a given week or month may be able to use other resources – such as savings – to avoid deprivation for a time, so low income alone without taking wider resources and income dynamics into account may not be a reliable indicator of inability to participate (Callan, Nolan and Whelan, 1993). This has implications for poverty measurement practice on which we have elaborated elsewhere (Nolan and Whelan, 1996), and also for the way adequacy of social welfare is assessed as discussed below. It remains true, however, that the core criterion against which the adequacy

of social welfare payments is assessed – by both the provider and the recipient – will be whether they are sufficient to allow recipients to avoid poverty. Application of that criterion is an inevitably imprecise exercise, given the nature of the information available and the diverse ways in which the problem can be approached. A research study like this can therefore hope only to provide as many relevant pointers as possible to help policy-makers in arriving at conclusions about adequacy, rather than to arrive at firm conclusions or recommendations about the level of social welfare support which would be adequate.

A similar conceptual starting-point is reflected in the 1992 Recommendation by the EU Council that member states recognise "the basic right of a person to sufficient resources and social assistance to live in a manner compatible with human dignity as part of a comprehensive and consistent drive to combat social exclusion" (Commission of the European Communities, 1992). The Recommendation states that social protection systems should be adapted as necessary according to a set of principles and guidelines. These include fixing the amount of resources considered sufficient to cover essential needs with respect for human dignity, taking account of living standards and price levels in the Member State concerned, for different types and sizes of households; in order to fix the amounts, reference should be made to appropriate indicators such as statistical data on average disposable income and household consumption, the legal minimum wage if it exists, and the level of prices in the Member State; and establishing arrangements for periodic review of these amounts, based on these indicators, in order that needs continue to be covered.

Like the Commission on Social Welfare, this recommendation is explicit that social protection has to be assessed against the standards of the society in question at a given point in time. Adequacy is in that sense relative since prevailing living standards differ across countries and change over time. Standards constructed to represent an "absolute" subsistence standard of living do have value in assessing adequacy at a point in time, as the CSW acknowledged, but over any prolonged period where real incomes are rising they will lose contact with the reality of expectations and perceptions of "needs", and therefore with what people see as adequate. In addition to assessment of adequacy at a point in time, then, one needs to develop appropriate benchmarks against which the evolution of social welfare support rates can be set or which can inform decisions about changes in those rates.

One also has to consider the time dimension in assessing adequacy at a point in time, in that an aspect of "adequate for what?" is "adequate for how long?". As already noted, households may be able to supplement current weekly income for a time by running down savings or by borrowing, and a level of social welfare payment sufficient to avoid poverty in the short term might not suffice for those

depending on it over a longer period. This is reflected in the current structure of social assistance rates, whereby a higher rate of Unemployment Assistance is paid to those who are in receipt long-term. The CSW took the view that this distinction between short-term and long-term needs was a logical corollary of the adequacy principle, but did not accept that this must be reflected in separate levels of payments. For the CSW, the minimally adequate income would not allow long-term recipients to budget for certain needs, notably energy costs, but these should be met by electricity/fuel allowance and by an additional payment on a quarterly basis (equivalent to the weekly value of child dependant allowances), not by adjusting the regular weekly payment. Leaving aside the merits of this policy stance, the point to be emphasised here is the need to be clear about the time horizon being adopted in assessing adequacy.

This example also brings out the importance of taking non-cash benefits into account in assessing the adequacy of cash social welfare payments. The standard of living of those depending on social welfare will of course depend not only on their cash payments but also on what these payments have to buy. This will be crucially affected by the extent to which the state provides goods and services directly or supplements cash income in other forms. Two distinct aspects have to be considered here. The first is the provision of goods and services by the state free or heavily subsidised to the community as a whole, which in the Irish case would involve most importantly education and general hospital health care. This sets the context in which the demands on cash incomes are determined, and any substantial changes over time in state provision affecting those relying on social welfare would have to be taken into account in assessing adequacy of cash transfers over time. (Differences across countries in this respect also greatly complicate cross-country comparisons of adequacy). The second aspect is that some of the state support to those on social welfare comes in the form of non-cash benefits, which are not received by (most of) the rest of the population and thus affect the living standards of recipients relative to the average in the society. These should be taken into account in assessing the adequacy of cash payments at a point in time, and any significant changes in the role of non-cash benefits should also be among the factors included in any examination of the evolution of cash payments over time.

As well as knowing "adequate for what?", one must know "adequate for whom?". Families and households differ in size and composition, and what will be adequate for a single person may not suffice for a married couple with dependent children. The assessment of adequacy thus inevitably leads one into the question of the relationship between "needs" and household size/composition, which is the appropriate "equivalence scale". Equivalence scales attempt to capture the income levels required by different family types to achieve the same standard of living or

"well-being", but there is no consensus among researchers about the best method for determining these scales and different methods give quite different results. The Commission on Social Welfare in its analysis concentrated on calculating a minimum adequate income for a single person, and recommended that the additional payment for an adult dependant should be 60 per cent of the rate for a single person, apparently on the basis that this was the standard figure in the literature (p. 196) – though in fact there is considerable variation in such estimates. In considering payments for dependent children the CSW noted that there was little recent research on equivalence scales for Ireland and the results of research elsewhere could not necessarily be readily applied, so a fully adequate unitary child income support payment could not be calculated (p. 295). This illustrates the difficulties faced in taking family size and composition into account in assessing adequacy: as we will see in the next section, it is a problem which is dealt with or skirted in different ways by the different methods of deriving estimates of adequate income.

2.3 Approaches to Deriving an Adequate Income Level

Since the core criterion against which adequacy is to be assessed is whether the income level is sufficient to allow recipients avoid poverty, there is a good deal of overlap between approaches to estimating an adequate income and methods of deriving an income poverty line. We now briefly review some of the main approaches which have been employed elsewhere to estimating an adequate income, as background to the CSW methods to be discussed in Chapter 3 and some alternative perspectives adopted in Chapter 4. A more detailed discussion of some of these approaches in the context of poverty measurement is contained in Callan and Nolan (1991) and Nolan and Whelan (1996).

The Budget Standard Approach

The most obvious way of deriving an estimate of what constitutes an adequate income is to specify first what an individual or family "needs", the minimum acceptable consumption basket, and then cost that consumption at current prices. The minimum income is thus the level required to purchase the basket of goods deemed by academics, social workers, social welfare administrators or politicians to be necessary to achieve a basic or minimum standard of living. This is the budget standard method, as employed by Rowntree in his pioneering British studies, taking as starting-point the specification and costing of a nutritionally adequate diet, and then specifying and costing requirements for other commodities or group of commodities, such as clothing, housing, and transport. Exercises of this type have been carried out in many countries and are directly taken into account in the setting of social security rates in for example Norway, Sweden and, until the early 1990s, Germany. An alternative employed in the original construction of the US official poverty standard was to take non-food expenditures

into account by simply multiplying the "necessary" food expenditure by a factor (of three) to arrive at the poverty line.

This budget standard method, on the face of it, has a number of appealing features. First, "minimum necessary" expenditures are being calculated in an apparently objective and scientific manner. Second, the content of the specified consumption basket can be readily spelt out and understood by a wide audience: as a recent Australian review puts it, "Through being explicit about consumption outcomes, the budget approach builds upon a common understanding of being poor. As such, it could achieve widespread credibility" (DSS, 1995, p. 23). Finally, it produces an income line which can be taken to represent a fixed basket of goods and services believed to represent the "bare necessities of life" (as Sawhill (1988) puts it in discussing the US line), which can then be indexed to prices so that progress against this fixed adequacy standard or poverty line over time can be monitored.

However, the extent and nature of the judgements being made in constructing the minimum basket need to be emphasised. Even for food, nutritional studies do not permit a precise estimate of what is "needed". For other expenditures, and to some extent for food as well, "needs" as defined by experts – both the commodities deemed to be necessities and the minimum quantity required – will be based on what are in effect social rather than scientific criteria, and with a significant degree of arbitrariness. (This would also be true if the basket of goods was selected by a sample of low-income households rather than by researchers.) Budget standard lines cannot be taken as representing requirements which are in any sense "absolute" or needed for subsistence, but the terminology employed can give a misleading impression. In addition, most budget standards have in practice made allowances for items which are not considered necessities, and for the fact that consumers do not actually allocate their expenditure "optimally": again the scope for judgement and arbitrariness is wide. As we shall see, judgement and arbitrariness also characterise a number of other commonly-used approaches to estimating an adequate income; in the case of the budget standards method, however, there is the danger that this may not be obvious, and so the results will be accorded a "scientific" status.

Costing a specified consumption basket does have a role to play in assessing the adequacy of social security support, while explicitly acknowledging that the "needs" involved are socially defined and that there is a substantial element of judgement and arbitrariness involved. For example, Piachaud's (1979) analysis of the cost of a specified consumption bundle for children in Britain showed that support rates for teenagers were less generous than those for younger children relative to their "needs", and Bradshaw and Morgan's (1987) costing of a basket of goods illustrated that those on social security could afford only "an extremely

restricted and dull lifestyle" (p. 14), with food consumption deficient in nutrition. Following the same approach the study of "The Cost of a Child" in Ireland by Carney *et al.* (1994) showed that in 1992 child income support levels for social welfare recipients (taking both CDAs and Child Benefit into account) were well below the cost of what was considered a basic minimum consumption basket for older children. We discuss what can be learned from the results of this Irish study, and from UK budget standard exercises, about the adequacy of Irish social welfare rates in Chapter 4.

The Food-Ratio Method

The food-ratio method of deriving income thresholds is based on the observation (first credited to Engel in 1895) that the proportion of income spent on food and other necessities tends to fall as incomes rise. Statistics Canada use the notion that the proportion of expenditure going on necessities (food, shelter and clothing) should not exceed some critical level to produce "low-income cut-offs". The Engel Curve relationship between the proportion spent on necessities and income, controlling for other relevant variables such as family size and location, is first used to estimate the income level at which different proportions of spending go on necessities on average. To derive an income adequacy threshold one then has to select the critical proportion for spending on necessities which should not be exceeded. In constructing the Low Income Cut-Offs the proportion used is simply the overall average percentage of household expenditures going on necessities plus an arbitrary figure of 20 percentage points: since 36 per cent of household expenditure went on food, shelter and clothing in the early 1980s, for example, the critical proportion was 56 per cent, and the income threshold was the level at which that proportion went on necessities on average.

This approach has the advantage of being based on observed spending patterns at a point in time, but faces serious problems. The definition of "necessities" raises many issues, since simply taking all expenditure on food, clothing and housing includes luxury items such as caviar and fur coats, and excludes other types of expenditures which might be considered necessities. The proportion of expenditure going on necessities varies widely at any given income level – Engel's Law holds only approximately – so a significant number of those below the derived income threshold will not be spending more than the cut-off proportion on necessities, while some of those above the line will be doing so. The choice of the critical proportion going on necessities from which the income thresholds are derived is essentially arbitrary. Further, in updating the thresholds over time a choice is faced between simply up-rating thresholds from a base year in line with the CPI, redoing the exercise regularly with up-to-date expenditure data to reflect changes in prices, real living standards and expenditure patterns, or some mix of the two leaving the choice between them to the user (Evans, 1991).

Subjective Evaluations of Minimum Income

When an adequate income is seen to be based on prevailing social standards, one apparently straightforward approach is to try to measure views in the population about minimum income needs, and base an adequacy standard on these views. This approach has been used to estimate what are termed consensual income poverty lines, and have been the subject of a substantial research literature. Respondents may be asked:

(i) how they would rate particular income levels for a list of hypothetical families of different composition (Dubnoff, 1985), or what income hypothetical families would require to reach different levels of living (Rainwater, 1974);

(ii) how they feel about their own current income level (Dubnoff, Vaughan and Lancaster, 1981);

(iii) what income they consider to be the minimum they themselves need to make ends meet (Goedhart, *et al.*, 1977);

(iv) what income levels they would consider, in their own circumstances, to be "very bad", "bad", etc., on a scale up to "very good" (van Praag, *et al.*, 1982).

These approaches have the significant advantage that the poverty or adequacy standard is updated within the method in line with the responses of those surveyed: no decision has to be taken external to the method itself about an up-rating procedure. Some evidence suggests that, when there is real income growth, survey respondents' evaluations of minimum incomes rise by more than the increase in prices alone but less than the full increase in real incomes. However, it is hard to see the standards produced by the more complex methods, emerging as it were from a "black box", being broadly understood and accepted. For example, Kapteyn and colleagues (e.g., Kapteyn, van de Geer and van de Stadt, 1985) use the responses to question (iii) above (the "minimum income question"), estimate their relationship with income and other relevant variables such as household size, and derive a poverty line as the point where, on average, actual income is equal to the stated minimum income needed. Critical assumptions are also involved about the way in which responses to the questions can be interpreted, for example, about the relationship between "making ends meet" and what the respondents, or most people in society, would regard as "adequate". Analysis of the way in which perceptions of the minimum income necessary evolve over time in different circumstances is valuable in itself, but does not provide a satisfactory basis for setting and uprating a societal adequacy standard. However, as we explore in Chapter 4, the responses of those relying on social welfare may provide useful insights into their own evaluations of the support levels currently prevailing.

Purely Relative Adequacy Standards

The view that adequacy has to be seen in terms of the standard of living of the society in question has led some to frame poverty lines or adequacy standards

explicitly, and purely, in terms of relative income. Customarily, this involves setting a poverty line or adequacy standard at a particular percentage of mean or median income or earnings, for example 50 per cent. This approach to deriving income poverty lines has been adopted in many recent studies (see, for example, Commission of the European Communities, 1981; O'Higgins and Jenkins, 1990; ISSAS, 1990; Hagenaaars *et al.*, 1994; Smeeding, *et al.* (1988) and Buhman, *et al.* (1988). However, regarding adequacy as socially determined still leaves room for diverse views about the precise nature of the relativity concerned and therefore the extent to which a purely relative approach to measuring adequacy is satisfactory. Most people would presumably be much less happy with its application over a period of recession than growth, and even in a steadily growing economy, do socially-perceived "needs" necessarily rise *pari passu* with average incomes? Considerable care needs to be exercised in applying the methodology to specific situations, and it may be more suitable for some than for others. It does have the considerable appeal of simplicity and transparency: it yields results which can be readily understood and serve at least as a starting point for the analysis of poverty and of adequacy. It is however more readily applied in measuring poverty than adequacy, simply because it does not produce a unique poverty line or adequacy standard because the choice of cut-off is arbitrary: there is in general no firm basis for the selection of any particular proportion of average income or earnings to serve as "the" poverty line or adequacy standard. In measuring poverty and the composition of the low-income population, the response can be to use a range of relative lines, allowing the sensitivity of the results to the precise location of the line to be assessed, as advocated by Atkinson (1985, 1987) and Foster and Shorrocks (1988a). This has been the approach employed extensively in our earlier work on poverty in Ireland in 1987, including comparisons with 1980 and 1973, and in our study comparing 1994 with 1987 (Callan *et al.*, 1996). When it comes to measuring adequacy of social welfare and estimating what would be an adequate income at a point in time, however, the fact that a purely relative approach has such a major element of arbitrariness is a major drawback. (This is again less serious when the aim is to assess trends in income adequacy over time, as discussed in later chapters).

The "Official Standards" Approach

Social security rates clearly cannot be used as a standard against which to assess their own adequacy (though they have sometimes been taken as an "official" poverty line by researchers). However, some have argued that other officially-sanctioned benchmarks, such as a minimum wage where that exists, can serve as a point of comparison or standard in assessing the adequacy of social security rates. The basic problem with such "official" benchmarks, however, is that they are not intended to be taken as official indicators of adequacy, being

established for other reasons and affected by other factors. We will develop this point in Chapter 3 when looking at this approach as employed by the Commission on Social Welfare.

Style of Living and Deprivation

The final approach to estimation of the level of income which would be adequate relies on analysis of patterns of living and deprivation and their relationship with income. Townsend's (1979) seminal study developed indicators of deprivation, where households lack an amenity or do not participate in activities which a majority of the population have, and sought to identify an income poverty line below which deprivation escalated, though many have been unconvinced by that exercise. Mack and Lansley (1985) measured deprivation indicators as socially prescribed necessities and use them directly in identifying the poor.³ Veit-Wilson (1994) argues that this research on deprivation indicators can serve as the basis for identification of the income level at which people can meet their basic needs:

The deprivation indicator method is probably the most reliable for giving us a direct picture of the lifestyle which people themselves define as minimally adequate, and also the income level which households in practice need in order to achieve it (pp. 26-7).

Our own work using 1987 Irish data has developed a methodology to first identify indicators of generalised deprivation, and to apply such indicators in combination with income thresholds in identifying those experiencing deprivation due to lack of resources (Callan, Nolan and Whelan, 1993, Nolan and Whelan, 1996). This demonstrates the value of information on non-monetary indicators, but also suggests that using such information to identify a minimum adequate income level, or even range, is very much more problematic than Veit-Wilson believes. As discussed in Chapter 4 below, this is principally because the relationship between deprivation and current income is rather looser than most discussions appear to assume.

2.4 Conclusions

This discussion has described briefly the main approaches employed elsewhere in measuring income adequacy, and has sought to bring out their strengths and weaknesses. It will be clear that no one method or approach has been widely accepted as the best, all have problems, and this uncertainty – even about the nature of the exercise and the appropriate role of research versus societal values and political decisions – must be acknowledged at the outset. None the less, the question is itself too important to ignore, and results from a range of methods can

³ Subsequent work in this area includes Townsend and Gordon (1988) for Britain, Mayer and Jencks (1988) for the USA, Muffels and Vrien (1991) for The Netherlands and Hallerod (1995) for Sweden..

contribute to the debate about adequacy. We therefore move on in the next chapter to describing the methods employed by the Commission on Social Welfare to estimate a minimum adequate income level for 1985, and then present the results of applying these methods to up-to-date data for the mid-1990s.

Chapter 3

THE COMMISSION ON SOCIAL WELFARE AND ADEQUACY

3.1 Introduction

The central recommendation of the Commission on Social Welfare on social welfare payment levels, that the basic weekly payment for a single person should be "in the range £50-60 in 1985" (p. 216), was based on the Commission's conclusion that the payment levels then prevailing were inadequate, and on the application of a number of different methods to estimate what would have constituted an adequate level. In concluding that payment levels were inadequate the CSW looked at a variety of evidence: the situation and perceptions of respondents in a survey carried out by the St. Vincent de Paul, views of administrators of the Supplementary Welfare Allowance, the results of studies of poverty by Roche (1984) and Rottman, Hannan *et al.*, based on the Household Budget Survey and some further data from that source produced for the Commission, the submissions which the Commission received, and meetings held with welfare recipients. The conclusion reached was that "for many recipients, particularly larger families and the unemployed, social welfare payments are inadequate or barely adequate to meet basic living costs, with little margin for extra expenses" (p. 168).

The conclusion that prevailing payment levels were inadequate did not in itself provide the Commission with a basis on which to recommend a level which would be adequate. The Commission saw the specification of a minimally adequate income as the most important issue to be dealt with, and sought to establish what would be an adequate minimum income for a single adult, "the level of income which would be sufficient to maintain a single adult in independent circumstances where there is no additional source of income, at a standard which is linked to living standards in society generally" (pp. 189-91). In the absence of a universally accepted method for deriving a minimum income, the Commission applied a number of methods and attempted to assess the range within which a minimum falls. The results were summarised as showing that "a minimally adequate income for one person, at 1985 prices, lies within the range £51-59 weekly" (p. 193).

In Section 3.2 of this chapter we describe in detail the different methods of deriving a minimal adequate income employed by the CSW and apply them to up-to-date data to produce the corresponding results for the most recent date available, which is 1994 or 1995. Section 3.3 then discusses the strengths and weaknesses of the methods, and conclusions are in Section 3.4.

3.2 The CSW Calculations of Minimum Adequate Income and Updated Results

The CSW applied seven different methods to derive a minimally adequate income, as described in detail in Appendix 9 of the Commission's Report. We now describe these methods and re-apply all but the first two with up-to-date data.

(1) The Food Ratio Approach

The CSW's first method drew on one applied by Roche (1984) in his study based on the 1980 Household Budget Survey (HBS), which he described as the food ratio approach. Roche categorised households in that sample into equivalent disposable income deciles, and calculated average food expenditure and average total expenditure per equivalent adult for each decile. For the fifth and sixth decile, total expenditure was 3.1 times food expenditure (i.e., $1/3.1=32$ per cent of expenditure went on food), and Roche applied this multiplier to the average amount spent on food by the bottom three deciles to arrive at a minimum adequate income per adult equivalent. The CSW substituted the slightly lower multiplier of 2.98, the ratio for the fifth decile rather than the average for the fifth and sixth deciles, and arrived at a minimum income figure for 1980. This was adjusted to 1985 prices in line with the CPI and the final result was a figure of £54.36.

The HBS is carried out by the CSO only every seven years. Data from the 1994 HBS have not yet been released, and so this method cannot be applied to up-to-date information as yet. In any case, as we point out in Section 3.3, this variant of the food ratio approach would produce rather peculiar results when applied over time, and so may not warrant recalculation.

(2) The Institutional Budget Method

This CSW method is based on the cost of maintaining an adult in prison. The average cost per prisoner of food, heat, light, laundry, recreation, and medical supplies but not any other costs such as salaries was calculated. A figure from the Household Budget Survey was then added to take into account housing and transport costs. Depending on the figure used for housing and transport, the resulting estimate was £51.63 or £56.03 in 1985 terms. This method does not in our view warrant recalculation, because the cost of maintaining someone in an institution has little bearing on the needs of those living in households, given the economies of scale which operate in providing for large numbers and the very different life-styles of those in ordinary households.

(3) Average Industrial Earnings Method

The third CSW method used *average earnings* of employees in transportable goods industries, on which the CSO publish regular quarterly statistics, as the benchmark. The net income for a single person corresponding to average gross earnings in 1985 was calculated by deducting income tax and PRSI, and half this figure was taken as the minimum adequate income for one person – which was deemed to be a conservative fraction. The figure this produced for 1985 was £58 per week.

In re-applying this method with up-to-date information, average earnings for industrial workers in Transportable Goods Industries from the CSO's Quarterly Industrial Inquiry were available up to June 1995. We have calculated net earnings by deducting the income tax payable by a single person, PRSI contributions and levies, and derived the minimum income figure as half that net earnings level for 1994. Using estimates for gross earnings in September and December 1995, the same exercise has been carried out for 1995. Table 3.1 shows the details of these calculations, and the up-dated results which show a minimum weekly income figure of about £90 for 1994 and an estimate of £94 for 1995.

Table 3.1: *Average Industrial Earnings Method of Deriving Adequate Income, 1994 and 1995*

	1994	1995
Average gross earnings ¹	13,547	13,844 ²
Single person's allowance	2,350	2,500
PAYE allowance	800	800
PRSI allowance	286	140
Taxable income	10,141	10,404
Income tax to be paid	3,146 ³	3,125 ³
PRSI and levies to be paid	1,049 ⁴	929 ⁴
Net earnings	9,352	9,790
Weekly equivalent	179.85	188.30
50 per cent of weekly net earnings = minimum adequate income	89.92	94.10

1 Average for all industrial workers (adult and non-adult rates of pay) in TGI.

2 Estimated by applying the per cent increase from June 1994 to June 1995, of 2.2 per cent, to September and December 1994 to estimate September and December 1995.

3 Income tax in 1994 is 27 per cent on 8,200 plus 48 per cent on remaining 1,941; in 1995 it is 27 per cent on 8,900 plus 48 per cent on remaining 1,504.

4 PRSI plus levies amount to 7.75 per cent of gross earnings in 1994; in 1995, an allowance of £50 per week applies for PRSI so PRSI is 5.5 per cent of the excess of £11,244, plus levies of 2.25 per cent still applying to total gross earnings.

(4) National Accounts Personal Disposable Income Per Capita

This CSW method took aggregate *personal disposable income* in the national accounts as the starting-point, 1983 data being the most up-to-date available at the time. The CSW took a rather convoluted approach to deriving a minimally adequate figure for a single adult from this aggregate (which in any case includes some income which does not accrue to households). As shown in Table 3.2, personal disposable income was divided by the number of persons in the labour force to give average personal disposable income per labour force member, a fraction of half was again applied, and an adjustment was made to allow for the non-labour force population using equivalence scales to arrive at a figure for a single person. The result, updated in line with prices to 1985, was a figure of £51.21 per week. (No justification for dividing by numbers in the labour force, and for this way of adjusting for household size, is given, and it is hard to see why this would be appropriate.)

Currently the most recent personal disposable income figure published by the CSO is for 1994, and Table 3.2 also shows our corresponding calculations for that year. The way the "aggregate equivalence measure" for the population not in the labour force was constructed is not clear from the CSW⁴ and the actual scale values employed are not given. We have been unable to reproduce exactly the aggregate adjustment factor implicit in the CSW figures, but have come reasonably close with a scale of 1 for each labour force participant, 0.6 for each person aged 15 or over and not in the labour force, and 0.37 for each child aged under 15. (That scale is employed by CSW in one of its other methods, method 7 described below). Using this approach we arrive at an estimated minimum for a single person in 1994 of £85 per week.

Table 3.2: *Personal Disposable Income Adequate Income Method, 1983 and 1994*

	1983	1994
Personal disposable income	£10663m.	£22018m.
Labour force	1,309,000	1,414,000
Personal disposable income per labour force member	£8145.9	£15571
Weekly equivalent	£156.65	£299.44
Half this average	£78.33	£149.72
Adjusted to single person using weighted aggregate equivalence measure	£44.54	£85.00
	updated to 1985 =	
	£51.21	

⁴ The CSW appendix simply states that "age differentiated equivalence proportions were multiplied by the total non-labour participants in the age group", ft. Table A9.4, p. 472.

(5) Official Standards

The fifth CSW method points to the income level below which an individual is entitled to a medical card, and the level of basic income tax allowances, as reflecting "in some way official judgements about income adequacy" (pp. 472-3). We will consider whether this is valid in Section 3.3, but here simply describe and re-apply the method. In 1985 the net (after income tax and PRSI) figure corresponding to the medical card limit for a single person was £54.98, and the weekly figure corresponding to personal income tax allowances for a single adult on PAYE was £53.58.

Re-applying these approaches with up-to-date data, the gross threshold income below which a single person living alone and aged under 66 is entitled to a medical card was £82.50 per week in 1994, £84.50 in 1995 and is £86.50 in 1996. As Table 3.3 shows, after payment of income tax and PRSI contributions these would come to a net figure of about £74, £78 and £81 respectively.

Table 3.3: "Medical Card" Method of Deriving Adequate Income, 1994, 1995 and 1996

	1994	1995	1996
Medical card threshold, single person living alone aged under 66	82.50	84.50	86.50
Annual equivalent	4,302	4,394	4498
Taxable income	866	954	1048
Tax payable	234.00	257.58	282.96
PRSI contributions	236.61	98.67	18.59
Net annual equivalent	3,831.39	4,037.75	4,196.45
Net weekly amount	73.68	77.65	80.7

The weekly equivalent of the income tax allowances of a single person, including PAYE and PRSI allowances, was unchanged at £66 in each of 1994, 1995 and 1996, as shown in Table 3.4. This reflects the fact that, although the personal allowances were increased in 1995 and 1996, at the same time the income tax allowance for full-rate PRSI contributors was reduced and then abolished, as the new allowance within the PRSI system itself was introduced at £50 per week in 1995 and then increased in 1996 to £80 per week. The stability of the income tax allowance is therefore somewhat misleading as an indication of the way the tax and PRSI systems combined operate.

However, an alternative indicator within the structure of the income tax system is the exemption limit below which a single person does not have to pay tax. By 1994 this was higher than the total of tax allowances, whereas in the mid-1980s when the CSW carried out its analysis the exemption limit was slightly

lower than total allowances. (The exemption limits have been set with an eye to work incentives, and thus are in fact influenced by the level of social welfare rates rather than representing an independent standard of adequacy, but as discussed when we come to the strengths and weaknesses of the various methods this is also true of the allowances.) As Table 3.4 also shows, the weekly amount corresponding to the annual exemption limit rose from £69 in 1994 to £71 in 1995 and £75 in 1996. At these levels, no PRSI contributions would currently be payable.

Table 3.4: *Tax Allowances/Exemptions Method of Deriving Adequate Income, 1994, 1995 and 1996*

	1994	1995	1996
Personal allowance	2,350	2,500	2,650
PAYE allowance	800	800	800
PRSI allowance	286	140	-
Total annual allowance	3,436	3,440	3,450
Weekly equivalent	66.08	66.15	66.35
Annual exemption limit for a single person aged under 66	3,600	3700	3900
Weekly equivalent	69.23	71.15	75

(6) Low Pay JLC Method

The CSW's sixth method takes the legal *minimum wage* rates set by Joint Labour Committees (JLCs) for certain sectors/occupations as an alternative "official" point of reference. Different minima are set by different JLCs and there is often considerable variation within a given JLCs recommendations, depending for example on the age, experience and skills involved. The CSW took the rate set for agricultural workers and calculated the net wage which would correspond to this gross weekly figure. A minimum adequate social welfare income was then calculated as either 70 per cent or 80 per cent of that figure – apparently on the basis that replacement rates higher than 80 per cent are taken as problematic from an incentive viewpoint – which produce estimates of £51.36 and £58.70 respectively.

In updating this method we, like the CSW, use the weekly JLC rate set for adult agricultural workers. As Table 3.5 shows, this is currently £143.48 per week, having been £137.24 for most of 1994 and 1995.⁵ Taking income tax and PRSI contributions into account, the table gives the derivation of the net weekly

⁵ This JLC set rates which applied from March 1994 and then from October 1995, so the former is used here for 1994 and 1995 while the latter is used for 1996.

pay which a single person on these gross earnings would receive. We see from the table that 80 per cent and 70 per cent of the net wage lead to a minimum adequate weekly income estimate for a single person of £77/88 in 1994, £79/90 in 1995 and £83/95 in 1996.

Table 3.5: *Minimum Wage/JLC Method of Deriving Adequate Income, 1994, 1995 and 1996*

	1994	1995	1996
Gross weekly minimum wage for adult agricultural worker	137.24	137.24	143.48
Annual equivalent	7,136.48	7,136.48	7461.00
Taxable income	3,700.48	3,696.48	4011.00
Tax payable	999.13	997.92	1,082.97
PRSI contributions	392.51	249.48	181.56
Net annual income	5,744.84	5888.60	6,196.47
Net weekly equivalent	110.48	113.24	119.16
80 per cent of net minimum	88.38	90.59	95.33
70 per cent of net minimum	77.33	79.27	83.41

(7) Average Household Incomes Method

The final CSW method took as reference point *average disposable household income* in the 1980 Household Budget Survey for different household types. The average income for households comprising a couple with two children was taken, uprated to 1985 prices, and alternative "replacement ratios" of 60 per cent and 65 per cent were taken. The resulting figures were converted to the corresponding figure for a one person household using an equivalence scale of 1 for the head, 0.6 for each other adult and 0.37 for each child, producing minimum incomes of £51.36 and £55.64 respectively. The same calculations for couples with one child gave higher figures.

The results from the 1994 Household Budget Survey are not yet available, as already noted, but similar results can be derived from the Living in Ireland Survey carried out by the ESRI in the same year, and we will employ these here to update this CSW method. The mean disposable weekly income for households comprising two adults and two children in that survey was £327, while the corresponding figure for households of two adults and one child was £305 per week. Table 3.6 shows how using the CSW procedure alternative estimates of a minimum adequate income for a single person can be derived from these mean incomes. (It is worth noting however that these two household types account for only 16 per cent of the households in the sample.)

The results show an estimate for minimum adequate income based on a couple with two children of either £84 or £91 per week, while once again those derived from mean income of a couple with one child are significantly higher.

Table 3.6: *Average Household Income Method of Deriving Adequate Income, 1994*

	<i>Based on Two Adults + Two Children</i>	<i>Based on Two Adults + One Child</i>
Mean disposable income	327.93	305.35
Adjusted to a single person basis ^a	140.14	155.00
Adequate income as 65 per cent of this figure	91.09	100.75
Adequate income as 60 per cent of this figure	84.08	93.00

^a using equivalence scale 1, 0.6, 0.37.

Summary of Results of Applying CSW Methods to Up-to-date Benchmarks

We now bring together in Table 3.7 the CSW's own key results from its various methods of estimating an adequate income for a single person for 1985 and those produced by re-applying the CSW's methods to up-to-date data. The CSW estimates for 1985 fell in the range £51-59 per week. We see that the 1994 estimates range from £66 to £91 per week, a much wider range (even taking the increase in the average level of the estimates into account). It is striking that the estimates based on the medical card income threshold or the tax allowances/exemptions show much lower percentage increases from 1985 to 1994 than those based on the JLC minima or purely relative earnings or income benchmarks. With the latter, the percentage increase in the level of the estimates between 1985 and 1994 is between 51 per cent and 66 per cent, and the estimated minimum adequate income for a single person is between about £85 and £90 per week. If the estimate derived from the tax allowances is replaced by that based on the tax exemption limit, which now seems more satisfactory within the logic of that method, the bottom of the range is £69 rather than £66. It is the £69-£91 range which we employ from this point on, and it remains a good deal wider than the CSW's 1985 range.

Table 3.7: *Summary of Results of Applying CSW Methods of Deriving Adequate Income, 1985 and 1994*

CSW Method Based On	Key Minimum Income Estimate Produced by CSW Methods £ per week		
	1985	1994	% Change
Food budget	54.36	na	
Institutional budget	51.36	na	
Average industrial earnings	58.00	89.92	55.00
National accounts average earnings	51.21	85.00	66.00
Medical card	54.98	73.68	34.60
Tax allowances/exemption limit	53.58	66.08/69.23	+23.3/29.2
Minimum wage	58.70	88.38	50.56
Average net household income	55.64	91.09	63.71

3.3 Strengths and Weaknesses of the CSW Methods

Having set out the various methods by which the CSW estimated the level of adequate income for a single person in 1985, and applied the same methods to up-to-date data, we now discuss the strengths and weaknesses of these approaches before looking at some alternatives in the next chapter. For this purpose we can divide the CSW's methods into three broad categories. The first covers the food budget and institutional budget methods. The second, which one might call the purely relative approach, covers the industrial wage, national accounts and the average household income methods. The third, the "official" approach, covers the medical card, tax allowance and minimum wage methods.

Budget Standard/Food Ratio and Institutional Budget Methods

In our general review of methodology in Chapter 2, we touched on the strengths and weaknesses of the budget standard and food ratio methods. What the CSW terms the "food budget" approach does not in fact implement either the conventional budget standard or food ratio approach described there. Unlike the budget standard method (such as the US official poverty line), it does not take as its starting-point an estimate of what expenditure on food is "needed": it simply starts with actual expenditure by low-income households on food. Having arrived at "necessary" food expenditure in a different way, the CSW then follows the US food budget method in simply taking the proportion of expenditure going on food for middle-income households as the appropriate benchmark. Adequate income is then what a household would need on average to be able to spend the actual amount going on food by low-income households but have the same proportion for

other expenditure as middle-income households. (In this the CSW simply adapted the approach developed by Roche (1984), which he called an "indirect method" of estimating consumption needs adapting the US approach (pp. 220-1)). The food-ratio approach implemented by Statistics Canada's Low Income Cut-Offs, on the other hand, calculates the income level at which a specified proportion spent on necessities is just reached on average: the crucial choice in that case is the critical proportion employed.

The CSW variant effectively assumes that low-income households (on average) prioritise expenditure on food and manage to reach an adequate level of food expenditure: their incomes would be adequate if this level of food expenditure could be accommodated within a higher level of overall expenditure, so that the proportion going on food was no higher than average. This may simply not be the case: food may not always be given absolute priority in this way (some prioritise regular bills, for example (Kempson, 1996)), and even if it is food expenditure may not reach "adequate" levels. Rather than being linked either to a level of expenditure held fixed in real terms (via indexation to the CPI), or to average incomes and living standards, the adequacy standard moves up as either the average expenditure of low-income households rises or the proportion of expenditure of middle-income households going on food declines. Further, there is a critical flaw in the method. Unless the proportion of expenditure going on food for the lower parts of the distribution is the same as for the middle, (which is likely to come about only if the bottom half of the income distribution were entirely flattened out), it will always produce a figure for adequate income which is above the actual income of those towards the bottom of the income distribution. While the proportion of expenditure going on food may itself serve as an indicator of average living standards, this method of deriving an adequate income level is neither clearly rooted in a subsistence-type estimate of "necessary" food spending nor is it transparently relative, and produces a target which is well-nigh impossible to hit.

We have already mentioned the weaknesses in what the CSW call the institutional budget method, which are in our view so severe that it did not warrant reworking for this study. The method calculates the cost of maintaining a prisoner, in terms of food, clothing, laundry, heating, medical care etc., and adds on an estimate for expenditure on housing and transport. However, the cost of maintaining someone in an institution has little bearing on the needs of those living in households and the cost of meeting those needs. First, those living in ordinary households have very different life-styles from those in prison, and (thankfully) have the opportunity to meet needs other than physical maintenance which even the most stringent approach to defining needs and adequacy would recognise. Second, the cost of providing food, heat, etc., in an institutional setting will reflect

economies of scale not available to those purchasing for a single household. Thus costs of maintaining someone in an institutional setting have little or no relevance to what constitutes an adequate income for the non-institutional population.

Purely Relative Approaches

The second group of CSW methods attempt to derive an adequate income simply as some proportion of average earnings or incomes. This purely relative approach is applied to three distinct benchmarks – the average industrial wage, average personal disposable income from the national accounts, and average household income for particular family types from a household survey. This general approach to deriving a measure of income adequacy has the important advantage of transparency: it is clear that adequacy is being linked directly to average living standards in the society, and moves up over time in line with that average. However, the same problem facing relative income poverty lines looms even larger in this context: the adequacy standard is derived as a proportion of the average, but the choice of a particular proportion is essentially arbitrary. In using relative income poverty lines to measure changes in poverty over time this can be dealt with by using a variety of lines and seeing which conclusions continue to hold across this range, but in measuring adequacy this is rather less satisfactory. The CSW take half net earnings as one estimate of adequate income, for example, and arrive at a figure for 1985 of £58 per week. If all we can actually say is that an adequate income lies between 40 per cent and 60 per cent of net earnings, the range this produces using the CSW's figures is between £46 and £70 per week. This may be an accurate reflection of our state of knowledge, but does not provide a firm basis for assessing the adequacy of payment levels at a particular point in time.

The arbitrariness of the choice of proportion to use in applying a purely relative method is illustrated by the fact that the CSW use 50 per cent as the proportion in deriving an adequate income from average earnings and personal disposable income, but 60 per cent and 65 per cent when the benchmark is average income for a couple with two children. This is justified by the CSW on the basis that as the latter "is a family income rather than that of a single person, a replacement rate as low as 50 per cent might be unduly restrictive" (p. 474), but the figure derived from average household income is in fact then adjusted using equivalence scales to a single person basis. One could also question the consistency across methods in applying the 50 per cent cut-off both to average earnings, where no adjustment is made to take dependants into account, and to average income per labour force participant from the national accounts which is then "adjusted to a single person" basis using equivalence scales. The key point is that alternative equally reasonable choices would produce quite different results. (The same is true of the use of 70 per cent or 80 per cent as the proportion when

the benchmark is the minimum wage, which falls into our third group of methods.) The fact that the CSW's various methods gave 1985 results concentrated in a particular range thus partly reflects the choice of proportions to apply to different benchmarks.

Applying the purely relative method to different benchmarks also begs the question as to which benchmark is the most appropriate. This in turn depends on what aim one has in mind. If the aim is linking adequacy firmly to general living standards, a broad measure of household income would seem the most satisfactory (although in focusing on disposable income an element of circularity creeps in since social welfare itself constitutes a substantial and varying proportion of household income). Alternatively, the view that social welfare rates must be linked with what is available from work could justify a narrower focus on earnings (though the use of average earnings in industry where only a minority of employees work simply reflects data availability). An important issue in using earnings as benchmark, however, is that increases in average earnings over time come about because of a combination of rising pay levels for specific occupations and the changing composition of the labour force towards higher skill levels and thus an increasing proportion of relatively well-paid jobs. Employees in low-skilled occupations benefit only from the first of these, and using the overall earnings average as the reference point for social welfare will overstate the improvement in the position of such employees: an alternative reference point of earnings in particular occupations would therefore also be useful. More generally, different indicators may give different results, both at a point in time and in measuring changes over time, and it is therefore necessary to be clear about how they are to be interpreted and the implications for measuring adequacy. Arbitrariness in the choice of proportion to use in deriving adequacy standards may not itself be as severe a problem in assessing changes over time as in attempting to measure adequacy at a point in time, because in that context the priority is simply to establish the way adequacy standards have been moving. The purely relative approach is thus in our view rather stronger in assessing how the adequacy of social welfare rates has been changing over time than in estimating what constitutes an adequate income at a point in time.

"Official" Methods

The third group of CSW methods, which employ the "official" approach, use the medical card income threshold, the total income tax allowance and minimum wage set by JLCs as benchmarks for income adequacy. This suffers from two major weaknesses. The first is that in each case one can question the extent to which these can reasonably be interpreted as reflecting "in some way existing official judgements about income adequacy" (CSW, pp. 472-3). The medical card threshold is the income level below which it is officially considered one cannot

afford to, or at least should not have to, pay for health care, but this does not mean that it can be taken as an indication of the income required to meet needs more generally. In the case of income tax allowances/exemption limits, not only ability to pay but also the possible impact on work incentives via the balance between incomes in and out of work come into play in decisions about where income tax starts to be paid, (and the state of the public finances and the revenue needs of the Exchequer play a central role in decisions about all the parameters of the tax system). In the same way, the fact that there is now an income threshold of £188 per week below which the Health and Employment and Training levies are not payable primarily seems to reflect concerns about rewarding work, and one could not reasonably interpret the (net equivalent of that gross) figure as an official judgement on income adequacy (particularly since it does not differentiate by family size). Finally, in setting minimum wages the various JLCs presumably take adequacy into account, but the wages available in other sectors/occupations and the relationship between earnings and unemployment compensation also play a part – so social welfare rates themselves influence the wage minima, and those minima may be increased precisely to widen the gap between them and unemployment compensation. In addition, as the CSW made clear, the minima set by the different JLCs vary a great deal and it is by no means obvious which rate to concentrate on, so a substantial element of judgement/arbitrariness enters into the method.

The second weakness in seeking to interpret any of these figures as an "official" view about income adequacy is that there is in fact an alternative benchmark for what is regarded officially as a minimum adequate income. When the Supplementary Welfare Allowance (SWA) scheme was introduced in the mid-1970s, its aim was explicitly stated to be to guarantee a standard basic minimum income, for those whose income from other sources is inadequate to meet their needs. The rates of payment under SWA thus themselves constitute the official benchmark most explicitly and directly linked to adequacy. They obviously could not be used as a basis on which to assess the adequacy of social welfare rates: since SWA has the lowest weekly rates of any social welfare scheme, the only conclusion one could reach is that all social welfare rates are always adequate by definition. This brings us into Wonderland with Alice, where words mean what one says they mean, but it brings out the fundamental flaw in the general approach of looking for an "official" benchmark against which to assess adequacy: since current official views about adequacy have played a major part in determining the income support rates actually paid, they cannot provide a basis on which to assess those rates.

Equivalence Scales

The final point to be made about the CSW's methods and results, which applies across the three different groups, relates to the treatment of the thorny issue of how best to take into account differences in needs due to differences in household size and composition. In attempting to derive an adequate income for a single adult from household expenditure or from the average income of a two-adult two-child household, the food budget and household income methods adjust to a single-person basis using equivalence scales. However, the scales used in the two methods are quite different. The food budget results are based on the work of Roche (1984), who built in a scale of 1 for the household head, 0.75 for each other adult, and 0.45 for each child aged under 18, Roche (1984, p. 73). The analysis of HBS average incomes, on the other hand, uses a scale of 1 for the head, 0.6 for each other adult, and 0.37 for each child aged under 14: differences of this magnitude could significantly affect the results, and we cannot be sure in any case that the "right" scale lies within this range. It is not clear which scales were used in deriving an adequate income figure from national accounts personal disposable income, the third method where such an adjustment was made, but it does not seem to have been either of these two. As we have already noted, in this case it is not in fact clear why an equivalence-based adjustment was made to average income per labour force member, when no such adjustment was made to average industrial earnings or to the minimum wage in arriving at an adequate income for a single adult.

The problem this highlights has a number of dimensions. The CSW highlighted how little was known about the relative needs of households of different sizes and compositions, and this prevented it from coming to firm conclusions about what constitutes a minimum adequate income for children. Its recommendations on child income support were that:

(1) the payment for children through CDA's should be rationalised to £10 per child in 1985 terms (p. 202), which represented an averaging on a neutral cost basis of range of rates payable in 1985;

(2) there should be a quarterly supplementary payment for those relying on social welfare in the long term of one week's CDA (p. 217); and

(3) a rate for universal children's allowance/Child Benefit was not specified, but the higher rate in force from the introduction of CB in April 1986 should be maintained or improved in real terms (p. 298), with supplementary CB payments for older children, of £5 per month for those age 12 or over or alternatively those aged 13 or over (p. 299).

The absence of an examination of what would be an adequate level of support for children meant that a clear recommendation about child income support rates,

to go alongside the recommendations on support rates for adults, could not be made – a serious drawback.

Second, a firm recommendation was made about the appropriate relationship between the payment rate for a single person and that for a couple: "The appropriate payment for a couple should be 1.6 times the personal rate" (p. 217). This was put forward with little supporting discussion, on the basis that "the 0.6 is the standard measure referred to in the literature on adult equivalence scales" (p. 196). However, quite a diversity of scales is in fact employed in the research literature or built into official rates, certainly a range from 0.5 to 0.7, although 0.6 is most commonly used in the UK. The strength of the conclusion reached by the CSW on a precise relativity between the needs of a couple versus a single person is not therefore based on an in-depth analysis of the international research literature or the Irish situation. Finally, the CSW sought to deal with the absence of a consensus about equivalence scales by concentrating on estimating an adequate income for a single person, but as we have seen some of the methods used themselves necessarily build in scales, which may influence the results: the problem is not so easily finessed.

Some research on equivalence scales in an Irish setting has been carried out since the CSW reported by Conniffe and Keogh (1988), based on the 1980 Household Budget Survey and focusing on the costs of children. The results suggested that young children cost considerably less than older children, that there are substantial economies of scale for younger children, and that social welfare support rates in 1987 fell short of the estimated costs of children in most instances. The methodology employed produces absolute cost figures, which can be updated in line with prices and the changing pattern of consumption across commodity types, and are deducted from total household income to arrive at income adjusted for household composition (see also Conniffe, 1992). The implications of employing this procedure, rather than the customary procedure of dividing income by a set of equivalence scales, have been examined empirically with the 1987 ESRI survey data in Nolan and Farrell (1990). The budget standards study of the costs of a child by Carney *et al.*, to be discussed in Chapter 4, has also added to our knowledge in this area. None the less, it remains the case that there is no consensus internationally about the best way to estimate the "needs" of one type of household *vis-à-vis* another, and that equivalence scales covering a wide range are in common use. It is therefore important to explore this issue and not to assume that, given an estimate of what constitutes an adequate income for a single adult, one can simply read off the corresponding figures for different family types. It is also worth noting the implicit assumption that resources are in fact shared within the household so that each member reaches the same standard of living. The distribution of resources within the household is a topic about which little is

known, though Cantillon and Nolan's (1996) analysis of the 1987 ESRI survey suggests that differences in the extent of deprivation between spouses at least are quite limited. In any case, mal-distribution within the household would mostly have implications for the best way to deliver income support (such as who in the household receives payment), rather than for the overall amount considered adequate for the household.

3.5 Conclusion

In this chapter the methods employed by the CSW to derive a minimally adequate income have been described and re-applied to up-to-date data, and their strengths and weaknesses have been assessed. The CSW applied seven different methods to establish what would be an adequate income for a single adult living independently in 1985 terms, and the results produced a range from £51 to £59 per week. Judging re-application of two of these methods to be unwarranted, we presented up-dated results from the remaining five for the most recent date available. All these could be recalculated for 1994, when the minimum adequate income figure for a single adult fell in a much wider range than 1985, from £69 to £91 per week. We extrapolate these figures to 1996 and discuss them in detail in Chapter 5, but were concerned at this stage to point up the strengths and weaknesses of the various CSW methods.

Three of the CSW methods we have up-dated here derive an adequate income simply as some proportion of average earnings or income. This general approach links adequacy directly and transparently to average living standards in the society, so adequate income moves up over time in line with that average. However, the choice of a particular proportion of the average as adequate is essentially arbitrary, and the fact that the CSW's methods gave results concentrated in a particular range partly reflects the choice of different proportions to apply to different benchmarks. This purely relative approach is thus stronger in assessing how adequacy of social welfare rates has been changing over time than in deriving an adequate income at a point in time.

The other CSW methods seek to identify alternative "official judgements about income adequacy" from the income threshold for entitlement to a medical card, from the level of tax allowances, and from the wage minima set by Joint Labour Committees. The main problem with these methods is that it may not be valid to infer judgements about adequacy from the policy decisions made about these instruments, which are in any case affected by rather than independent of the level of social welfare rates.

Given the problems we have identified with the methods of deriving an adequate income employed by the CSW, the obvious question is whether there is a better way. This indeed is the challenge issued by the Commission itself in presenting its results:

It should be emphasised that the calculations ... are not based on any agreed statistical procedure or theoretical foundation as, ultimately, in our view, any calculated minimum will be somewhat arbitrary. We recognise that the approach adopted may well be open to criticism. However, in the absence of any explicit official criteria and because of the limitations of available data we had no option but to attempt to establish a minimally adequate income. Not to have done so would, in our view, have been a serious omission. Furthermore, if our approach is considered to be deficient then an acceptable alternative should be provided (pp. 193-4).

We do not claim in this report to have an alternative methodology which allows one to derive in an unproblematic, objective and scientific way estimates of income adequacy which would be generally acceptable and convincing. This should come as no surprise, since we have argued earlier that this is an unattainable goal. We do pursue, in the next chapter, some alternative perspectives on the problem which, like the CSW's methods, can contribute to better informing official, political and societal judgements about adequacy.

Chapter 4

ALTERNATIVE PERSPECTIVES ON ADEQUACY

4.1 Introduction

In this chapter we look at a number of alternative perspectives on adequacy, employing data obtained in two large-scale household surveys carried out by the ESRI: the 1987 Survey on Income Distribution, Poverty and Use of State Services, and the 1994 Living in Ireland Survey. (These surveys have been described in detail elsewhere: see Callan, Nolan *et al.*, 1989 and Nolan and Callan (eds.) for the 1987 survey, and Callan *et al.*, 1996 for the 1994 survey.) We first take advantage of the availability of micro-data to investigate in greater depth than the CSW the purely relative approach to deriving an adequate income. We thus look in Section 4.2 at using household incomes or individual earnings in these surveys as a benchmark for deriving estimates of what constitutes an adequate income. In Section 4.3, we employ the survey data to explore empirically the extent to which households receiving or relying on payments from different social welfare schemes fall below relative income poverty lines, and the extent to which this changed between 1987 and 1994.

We then move in Section 4.4 to the use of non-monetary indicators of deprivation. As we saw in Chapter 2, some have seen the use of such indicators as the most promising direction to pursue in trying to measure income adequacy (see, for example, Veit-Wilson, 1994). The two surveys contain a range of information on aspects of life-style and deprivation, and we have devoted a good deal of effort in earlier work to developing their use. Here we use this information to examine the extent to which households in 1987 and 1994 receiving or relying on payment from different social welfare schemes were below income poverty lines and experiencing what we have called basic deprivation. We go on to consider whether such non-monetary indicators can permit the identification of an adequate level of income or the range within which an adequate level falls.

Respondents in each of the ESRI surveys were asked their own views as to what was the minimum income needed by their household to "make ends meet". In Section 4.5 these responses are used to throw some light on the attitudes of those relying on social welfare about income adequacy.

In Section 4.6 we move away from the survey-based analysis to discuss the results of the application of the budget standard method to Irish data by Carney *et al.* (1994), which focused on the costs of children, and also what can be learned from UK budget standard exercises with a broader scope. Section 4.7 presents some evidence on the types of financial problems facing social welfare recipients who seek assistance from Money Advice Centres funded by the Department of Social Welfare. Section 4.8 looks at the relative generosity of Irish social welfare rates compared with the UK and other EU countries. Finally, Section 4.9 brings together the conclusions.

4.2. Survey-based Relative Income/Earnings Benchmarks

As we have seen in Chapter 3, the CSW applied a purely relative approach to deriving measures of income adequacy from a number of different benchmarks – average industrial earnings, average personal income from the National Accounts, and average disposable income for specific household types from the Household Budget Survey. Since we have available micro-data on a representative sample of households, we can apply this approach more systematically and in greater depth to benchmarks based on average income for all households or earners. This allows us, *inter alia*, to explore the sensitivity of these results to the equivalence scale employed, an issue we highlighted in Chapter 3.

Average household disposable income in the 1994 Living in Ireland survey was £280 per week. We first convert this to average income per adult equivalent with a scale that allows 1 for the household head, 0.66 for each other adult, and 0.33 for each child – the approximate scale implicit in the social welfare system's Unemployment Benefit and Assistance and Supplementary Welfare Allowance schemes in 1987, which we employed in much of our research on the 1987 survey data. With that scale, as Table 4.1 shows, average disposable income per adult equivalent was £129 per week in 1994. A purely relative income poverty line or adequacy standard for a single person set at 60 per cent of this figure would thus be about £77 per week, while a standard set at 50 per cent would be about £64 per week. The CSW, in deriving an adequacy standard from average household income in the HBS, had to rely on published data and could not equalise household income directly, so it took the average for households with two adults and two children, and applied an equivalence adjustment to that average. This will not necessarily give the same result as equalising individual incomes and then averaging, even for that household type. Further, average equivalent income for that particular household type in 1994 is higher than the average for all households (with the equivalence scale just described). Taking the two-adult/two-child household type rather than the overall average gives average income per equivalent adult of £141 per week, and as Table 4.1 again shows, the 60 per cent standard would be £85 and the 50 per cent standard £70 per week.

Table 4.1: *Alternative Estimates of Adequate Income Based on Mean Income/Earnings, 1994*

	<i>Mean Equivalent Income</i>	<i>Adequate Income for Single Adult</i>
All in 1994 sample, child aged < 14, 1/0.66/0.33 equivalence scale	£129	60 per cent = £77 50 per cent = £64
Two adult/two child households in 1994 sample, child aged < 14, 1/0.66/0.33 equivalence scale	£141	60 per cent = £85 50 per cent = £70
All in 1994 sample, child aged < 18, 1/0.7/0.5 equivalence scale	£121	60 per cent = £73 50 per cent = £60
All in 1994 sample, child aged < 14, 1/0.6/0.37 equivalence scale	£132	60 per cent = £79 50 per cent = £66
All in 1994 sample, child aged < 14, 1/0.6/0.31 equivalence scale	£134	60 per cent = £80 50 per cent = £67
All in 1994 sample, child aged < 18, 1/0.6/0.31 equivalence scale	£137	60 per cent = £82 50 per cent = £68
Average net industrial earnings from QII, no equivalisation	£180	50 per cent = £90
Average net earnings of all employees in 1994 sample, no equivalisation	£193	50 per cent = £96

The equivalence scale adopted also matters, as the table goes on to illustrate. If instead of 1/0.66/0.33 we use 1/0.7/0.5, then the average equivalent income across all households is £121 rather than £129. Thus the 60 per cent and 50 per cent standards are lower, at £73 and £60 respectively. If, on the other hand, one uses the equivalence scale of 1/0.6/0.37 employed by the CSW to derive average equivalent income for two-adult/two-child households from the HBS, the average income per equivalent adult across all households in 1994 is a good deal higher, at £132, so a 60 per cent standard for a single person is £79 per week and a 50 per cent one is £66. As we will discuss in detail in Chapter 5, the equivalence scale implicit in Unemployment Benefit and Assistance has changed somewhat since 1987 and is now closer to 1/0.6/0.31. Equivalising with that scale, the mean is slightly higher than with the 1/0.66/0.33 scale and so the 60 per cent line is £80 and the 50 per cent line is £67 per week. Finally, the definition of a child versus an adult in applying the equivalence scales also matters. So far, we have followed the approach adopted in much of our work with the 1987 survey data, taking a child to be under age 14 in order to allow comparison with the CSO's Household Budget Surveys,⁶ the age cut-off also implicit in some of the CSW's methods. However, if one instead takes a child to be under age 18 and then applies the 1/0.6/0.31 scale,

⁶ Nolan and Farrell (1990) looked at the impact on relative income poverty in the 1987 survey of various alternative equivalence scales and ways of defining a child.

the 60 per cent line would be ££82 and the 50 per cent line would be £68.50. This illustrates that the estimate of an adequate income level produced by this general approach is significantly affected by the choice of equivalence scale and the way it is applied.

The more important and essentially arbitrary choice in applying a purely relative approach to deriving an adequate income is of course which proportion of the average one takes. The CSW, in deriving such an estimate from average equivalent household income, used 60 per cent and 65 per cent; common practice in studies applying relative income poverty lines is to use 50 per cent and 60 per cent (and sometimes also 40 per cent).⁷ Using the 1/0.66/0.33 equivalence scale, choosing 50 per cent of average equivalent income produces an adequacy estimate of £64 per week as we have seen, whereas 65 per cent of that figure is £84. In the context of evaluating the adequacy of current social welfare rates, this represents a world of difference as we shall see in Chapter 5. The point to be emphasised is that, within the purely relative approach itself, there is nothing to say that 50 per cent is appropriate and 65 per cent is not, or vice versa: justification for focusing on a particular proportion must come from a source external to the method, such as in-depth investigation of the living standards being attained by households on these income levels.

The CSW, as we have seen, also applied the purely relative approach to an earnings benchmark to derive an estimate of adequate income. The figure used is average earnings of employees in industry, with income tax and PRSI contributions calculated by applying the parameters of the tax/PRSI code to average gross earnings. Only a minority of employees work in industry, however, so it is worth looking at the wider coverage across all sectors of employment provided by the 1994 Living in Ireland Survey and their reported net earnings. For the 3,450 employees in the sample, average weekly earnings net of income tax and PRSI contributions was £193 per week, as shown once again in Table 4.1. The average net industrial earnings figure produced in Chapter 3 when up-dating the CSW's calculations to 1994 was £180. The CSW, in deriving an adequate income estimate from that figure, took 50 per cent: applying this to our slightly higher overall average net earnings figure would give an estimate of £96.5 rather than £90 per week. Once again, of course, the selection of 50 per cent as the

⁷ While these percentages are most often applied to mean income in such studies, some use the median instead, which is invariably lower than the mean: in such cases when a 60 per cent standard is applied, the resulting poverty standard will be closer to 50 per cent of mean income.

appropriate proportion to apply to average earnings is essentially arbitrary.⁸

4.3 Assessing the Adequacy of Social Welfare via Relative Income Poverty Lines, 1987 and 1994

Since ability to avoid poverty is a central element in income adequacy, as discussed in Chapter 2, one way of assessing whether social welfare income support levels are "adequate" is to look at the extent to which those relying on social welfare for their current income fall below relative income poverty lines. Without having to identify a particular income line as "the" poverty line, using a range of lines and comparing the position of households relying on different social welfare schemes gives an indication of the relative effectiveness of these schemes in providing the support required to avoid income poverty. Our earlier analysis of the situation of those relying on different social welfare schemes in 1987, described in Nolan *et al.* (1994), provides us with a benchmark against which changes since the CSW Report can be assessed using the survey data for 1994.

Many of the households in receipt of social welfare support also have incomes from other sources, and some are also receiving payment from more than one scheme. (A household is defined as a group of persons who live together, share some form of communal "kitty" or other budgeting arrangement, and usually meet together at least once a week for a common meal: it is therefore rather broader than the nuclear family of adult or couple with dependant children if any.) Here we want to make comparisons across schemes and are primarily interested in households depending on the scheme in question. It is therefore necessary to focus on those households which are largely reliant on particular social welfare schemes, and for current purposes we take this to be the case where payments from the scheme account for more than 50 per cent of household disposable income.⁹ In Table 4.2 we first show the overall percentage of households in the 1987 sample in receipt of payment from each of the main schemes, the proportion of these households who are reliant on these payments, and thus the proportion of households in the sample depending on the schemes. The percentage of households in the sample in receipt of payment broadly reflects the numbers in receipt in the population at the time, with the largest numbers in receipt of Unemployment Benefit (UB) and Unemployment Assistance (UA), contributory and

⁸ The CSW regarded 50 per cent of earnings as "a conservative figure given that replacement ratios in excess of 80 per cent are taken as problematic from an incentive point of view" (p. 471), but many employees will of course have earnings considerably below the average and thus replacement rates produced by setting unemployment compensation at half average earnings would be well above 50 per cent for them.

⁹ A household might not be reliant on any one scheme in this sense, but still receive more than half its income from social welfare. Such households are incorporated when we progress to the analysis of those dependent on social welfare overall.

non-contributory Old Age Pension (OAP); given the numbers involved, one can be much more confident in using the sample to analyse the situation of, for example, households receiving UA than those receiving Supplementary Welfare Allowance (SWA).

Table 4.2: *Households Receiving from/Relying on Social Welfare Schemes, 1987*

	<i>% Of All Households Receiving Under Scheme</i>	<i>% Of Recipient Households "Reliant" on Scheme</i>	<i>% Of All Households "Reliant" on Scheme</i>
Unemployment Benefit	8.0	42.3	3.4
Unemployment Assistance	13.4	48.1	6.4
Disability Benefit	4.9	42.1	2.1
Invalidity Pension	3.5	56.0	2.0
Old Age Contr. Pension	8.9	70.2	6.2
Old Age Non-Contr. Pension	10.0	49.0	4.9
Widow's Contr. Pension	4.3	47.0	2.0
Widow's Non-Contr. Pension	1.6	39.2	0.6
Deserted Wife's Allowance	0.4	76.6	0.3
Unmarried Mother's Allowance	0.9	36.6	0.3
Supplementary Welfare Allowance	1.0	23.4	0.2
Disabled Person's Maintenance Allowance	1.7	27.6	0.5

There was considerable variation across schemes in the extent to which recipient households were *reliant* on the scheme, in the sense outlined. About half the households receiving UA, Old Age Non-Contributory Pension, and Widow's Contributory Pension rely on these payments. For UB and DB the corresponding figure is 42 per cent, but for Widow's Non-Contributory Pension, Unmarried Mother's Allowance and especially Disabled Person's Maintenance Allowance (DPMA) the proportion of recipients relying on the scheme is lower. (The percentage of SWA recipients depending on that scheme is only 23 per cent, but this is due to the fact that many are in receipt of once-off payments or top-ups rather than the full weekly rate available under that scheme). By contrast, more than half the recipients of Invalidity Pension, 70 per cent of those receiving Contributory Old Age Pension, and over three-quarters of households receiving Deserted Wife's Allowance were relying on those payments. This reflects among

other things the fact that most recipients of, for example, Deserted Wife's Allowance did not have any other adult in the household, but a significant number of recipients of Unmarried Mother's Allowance were living in their parents' household.

Table 4.3 then shows for 1987, for all households receiving payment from a particular scheme and for only households relying on the scheme, the percentage falling below the 50 per cent and 60 per cent income poverty lines using the 1/0.66/0.33 equivalence scale. Income poverty rates were considerably higher for households relying on each scheme than for all households receiving payment from that scheme, which is as one would expect.¹⁰ Poverty rates were highest for the

Table 4.3: *Percentage Of Households Receiving/Relying On Social Welfare Schemes Below Relative Income Poverty Lines, 1987*

	% of the Households Receiving Scheme Below Relative Income Line		% of the Households Relying on Scheme Below Relative Income Line	
	50 % Line	60 % Line	50 % Line	60 % Line
Unemployment Benefit	25.4	45.6	53.8	79.1
Unemployment Assistance	46.8	61.0	83.4	92.4
Disability Benefit	24.7	42.3	53.7	80.3
Invalidity Pension	10.4	51.3	13.4	81.0
Old Age Contr. Pension	0.9	11.8	1.3	15.1
Old Age Non-Contr. Pension	11.2	28.2	18.6	46.4
Widow's Contr. Pension	3.1	20.0	4.6	31.0
Widow's Non-Contr. Pension	11.2	38.7	23.7	86.2
Deserted Wife's Allowance	30.1	63.0	39.3	82.3
Unmarried Mother's Allowance	20.6	58.2	18.0	100.0
Supplementary Welfare Allowance	38.8	76.4	100.0	100.0
DPMA	22.2	38.5	50.5	100.0

¹⁰ The figures presented in Nolan *et al.* (1994) Table 3.11 for poverty risks by scheme were incorrectly described as applying to households relying on, but in fact were for all households receiving, each scheme.

schemes which in 1987 had the lower rates of support, notably UA. Almost half the households in receipt of UA were below half average income, compared with about one-quarter of those receiving UB and DB, only about 10 per cent of those relying on Non-Contributory Widow's and Old Age pensions and hardly any of those on Contributory Old Age Pension. Poverty rates were higher at the 60 per cent income line, though only a small minority of households receiving Contributory Old Age or Widow's pensions were below that line. Focusing on households relying on the various schemes, poverty rates were generally significantly higher. Particularly striking is the finding that almost all the households relying on UA, SWA, and Deserted Wife's and Unmarried Mother's Allowances were below the 60 per cent income poverty line.

We now present the corresponding results for 1994, from the Living in Ireland Survey. Table 4.4 shows that, for the most part, the percentage of households receiving, and relying on, the various schemes is similar to 1987. The percentage in receipt of UA has risen and that in receipt of UB has fallen, as the administrative statistics on numbers of recipients would lead one to expect. (Note that Unmarried Mother's Allowance has been integrated into the broader Lone Parent's Allowance.) The one serious problem with the coverage of the 1994

Table 4.4: *Percentage of Households Receiving Payment from and Relying on Social Welfare Schemes, 1994*

	<i>% All Households Receiving Scheme</i>	<i>% Recipients "Reliant" on Scheme</i>	<i>% All Households "Reliant" on Scheme</i>
Unemployment Benefit	4.9	30.3	1.5
Unemployment Assistance	14.7	51.6	7.6
Disability Benefit	3.1	29.6	0.9
Invalidity Pension	3.1	46.3	1.4
Old Age Contr. Pension	8.2	67.4	5.5
Old Age Non-Contr. Pension	9.3	57.3	5.3
Widow's Contr. Pension	6.1	56.1	3.5
Widow's Non-Contr. Pension	2.1	55.9	1.2
Deserted Wife's Benefit/Allowance	1.4	68.4	1.0
Lone Parent's Allowance	4.0	57.5	2.3
Supplementary Welfare Allowance	0.2/0.8	20.6/15.9	0.04/0.1
DPMA	2.8	34.2	1.0

survey is that the very small numbers in receipt of a regular weekly basic SWA payment does not allow meaningful results to be derived for such households. Even when all those in receipt of SWA – whether basic payment, rent/mortgage supplement or special or exceptional needs allowance – are included, this comes to less than 1 per cent of sample households.

Table 4.5 shows the position of the households receiving or relying on the various schemes in 1994 *vis-à-vis* 50 per cent and 60 per cent relative income poverty lines, again with the 1/0.66/0.33 equivalence scale. Compared with 1987, poverty risks for households receiving or relying on these payments have fallen for UB, and for UA with the 50 per cent line. Those receiving Old Age or Widow's pensions or Invalidity Benefit, on the other hand, saw a significant increase in the risk of relative income poverty. While UA still has the highest poverty risk among the schemes on which very substantial numbers rely, it no longer stands out so starkly from the rest of the major schemes. This reflects the significant divergence across schemes in the rate of increase over the period, with payment rates converging over time, as will be documented in the next chapter.

Table 4.5: *Percentage of Households Receiving/Relying On Social Welfare Schemes Below Relative Income Poverty Lines, 1994*

	<i>% of Households Receiving Scheme Below Relative Income Line</i>		<i>% of Households Relying on Scheme Below Relative Income Line</i>	
	<i>50 % Line</i>	<i>60 % Line</i>	<i>50 % Line</i>	<i>60 % Line</i>
Unemployment Benefit	20.2	35.8	48.5	84.4
Unemployment Assistance	41.6	61.7	69.5	90.7
Disability Benefit	21.4	35.6	57.2	80.2
Invalidity Pension	32.6	51.3	66.1	91.0
Old Age Contr. Pension	2.5	33.5	1.6	45.40
Old Age Non-Contr. Pension	18.6	56.2	30.4	85.2
Widow's Contr. Pension	9.4	47.9	16.5	75.0
Widow's Non-Contr. Pension	33.6	59.0	57.2	91.0
Deserted Wife's Benefit/Allowance	41.3	64.2	59.1	75.7
Lone Parent's Allowance	48.0	64.3	74.5	85.2
Supplementary Welfare Allowance	31.8/44.3	86.5/76.0	100/45.8	100/45.8
DPMA	25.1	51.2	58.8	82.0

The sensitivity of these results to the equivalence scale adopted has also been examined, using the alternative scales employed in our previous research on the 1987 survey, viz. 1/0.7/0.5 and 1/0.6/0.4. The broad pattern of risks across the schemes produced by the 1/0.66/0.33 scale holds when these alternative scales are used, though some of the risk levels are indeed sensitive to the choice of scale. For example, the risk at the 60 per cent line for those in receipt of contributory Old Age Pension is 33 per cent with either the 1/0.66/0.33 or the 1/0.6/0.4 scale, but only 18 per cent with the 1/0.7/0.5 scale. Similarly the risk at the 50 per cent line for those households receiving or relying on Invalidity Pension is much lower with the 1/0.7/0.5 scale than either of the others. This reflects the fact that where the rates paid by the social welfare scheme in question are close to a particular income poverty line, even relatively small variations in the line can make a major difference to the measured risk. The main features of the pattern of risk across the schemes is however unaffected by varying the equivalent scales across this range.

4.4 Assessing Adequacy of Social Welfare via Non-monetary Indicators of Deprivation

While the risk of income poverty facing households relying on social welfare offers one perspective on adequacy, ideally one would like to be able to describe in some detail the living standards of such households so that people could decide for themselves whether these were acceptable, and thus whether social welfare income support levels were "adequate". Small-scale in-depth studies of households depending on social welfare offer valuable insights into their living standards and life-styles (e.g., O'Neill, 1992; Kempson, 1996) but it is difficult to judge the extent to which one can generalise from their findings. We can however look at a number of specially-designed non-monetary indicators of living standards/deprivation for households in the large-scale representative samples carried out by the ESRI in 1987 and 1994. Information obtained in these surveys allows us to examine the extent to which households relying on social welfare for their current income are experiencing basic forms of deprivation. Comparing the position of households relying on different social welfare schemes gives some indication of the effectiveness of these schemes in providing the support required to avoid such deprivation. Once again our earlier analysis of the situation of those relying on different social welfare schemes in 1987, described in Nolan *et al.* (1994), provides us with a benchmark against which changes since the CSW Report can be assessed using the survey data for 1994.

The eight indicators of what we have in earlier work termed "basic deprivation" (see Callan, Nolan and Whelan 1993; Nolan and Whelan 1996), on which we concentrate here, are as follows:

- having to go without heat through lack of money;
- having to go without a substantial meal all day;

in arrears on electricity/gas/rent/mortgage, had to go into debt or pawn something to meet ordinary living expenses, or received help from charity;
 not being able to afford new not second-hand clothes;
 not being able to afford a meal with meat, chicken or fish every second day;
 not being able to afford a warm waterproof overcoat;
 not being able to afford two pairs of strong shoes;
 not being able to afford a roast or equivalent every week.

Most of the adults in each household were posed the set of questions relating to these indicators, but here we utilise the responses of the household head if available, or the spouse of the head if not, as representative of the situation of the household. For the 1987 survey Cantillon and Nolan (1996) compared the responses of husbands and their wives and found a high degree of concordance between them, though wives do seem marginally more likely to report deprivation. A household where the head (or spouse if head's responses are not available) reports experiencing any of these eight forms of deprivation we consider to be experiencing "basic deprivation".

Once again we first describe the pattern found in 1987, and then the corresponding results for 1994. Table 4.6 presents, for the households receiving/

Table 4.6: *Households Relying on Social Welfare Schemes Below Income Poverty Lines and Experiencing Basic Deprivation, 1987*

	<i>% of Households Receiving Scheme Below Income Line + Experiencing Basic Deprivation</i>		<i>% of Households Relying on Scheme Below Income Line + Experiencing Basic Deprivation</i>	
	<i>50% Line</i>	<i>60% Line</i>	<i>50% Line</i>	<i>60% Line</i>
Unemployment Benefit	16.5	29.3	34.8	50.9
Unemployment Assistance	34.5	44.6	64.1	71.8
Disability Benefit	18.1	26.8	38.6	47.9
Invalidity Pension	6.8	38.5	8.6	62.0
Old Age Contr. Pension	0.8	5.4	1.2	7.4
Old Age Non-Contr. Pension	4.5	10.0	6.9	14.8
Widow's Contr. Pension	2.8	13.3	4.6	20.5
Widow's Non-Contr. Pension	9.1	36.6	18.5	80.9
Deserted Wife's Benefit/Allowance	19.6	42.8	25.6	55.9
Unmarried Mother's Allowance	15.6	53.2	18.0	100.0
Supplementary Welfare Allowance	32.8	55.5	74.4	74.4
DPMA	14.1	28.5	31.2	73.8

relying on each social welfare scheme in 1987; the percentage below the 50 per cent and 60 per cent relative income poverty lines *and* experiencing basic deprivation¹¹. For the most part, the pattern of poverty rates based on income lines alone, described in the previous section, holds when we look at the percentage below the income lines *and* experiencing basic deprivation. Perhaps the most striking aspect is the very high proportion of those relying on UA, Widow's Non-Contributory Pension and Unmarried Mother's Allowance who fell below the 60 per cent line and were also experiencing basic deprivation.

Our main interest here, however, is in the extent to which this pattern had changed by 1994. Table 4.7 shows the corresponding results from the Living in Ireland survey. In contrast to the comparison in the previous section of numbers

Table 4.7: *Households Relying on Social Welfare Schemes Below Income Poverty Lines and Experiencing Basic Deprivation, 1994*

	% of Households Receiving Scheme Below Income Line + Experiencing Basic Deprivation		% of Households Relying on Scheme Below Income Line + Experiencing Basic Deprivation	
	50% Line	60% Line	50% Line	60% Line
Unemployment Benefit	12.4	21.7	31.6	53.5
Unemployment Assistance	26.2	40.0	46.0	61.1
Disability Benefit	8.0	18.6	20.5	39.4
Invalidity Pension	19.0	27.0	40.2	50.4
Old Age Contr. Pension	0.0	7.2	0.0	9.6
Old Age Non-Contr. Pension	4.6	14.7	6.6	21.4
Widow's Contr. Pension	3.6	19.3	5.9	26.7
Widow's Non-Contr. Pension	12.2	20.0	22.6	32.1
Deserted Wife's Benefit/Allowance	26.1	47.4	37.2	52.2
Unmarried Mother's Allowance	31.0	42.2	49.4	53.7
Supplementary Welfare Allowance	20.6/ 38.9	75.2/ 61.9	100/ 45.8	100/ 45.8
DPMA	14.8	29.0	31.7	48.4

¹¹ As in the previous section, note that the results for 1987 presented in Nolan *et al.* (1994), Table 3.11, refer to households receiving rather than (as stated there) relying on the various schemes.

below the relative income lines alone, the percentage below these lines and experiencing basic deprivation is seen to fall more often than rise over the period. Although for many schemes there is no marked difference between 1987 and 1994, for households receiving or relying on UA and DB there was a sharp fall in the percentage below the income lines and experiencing basic deprivation. The same is true of Widow's Non-Contributory Pension with the 60 per cent income line. The opposite is the case with Widow's Contributory Pension, however, where the percentage below the 60 per cent line and experiencing basic deprivation rose; for Invalidity Pension, an increase in risk was seen with the 50 per cent but not the 60 per cent line. The general pattern, though, is one where a stable or falling risk of being below the relative lines and experiencing basic deprivation is most common.

Using non-monetary indicators in this way to see the extent to which those currently receiving social welfare are experiencing deprivation provides one benchmark against which the adequacy of *current* social welfare rates can be assessed: the finding that a significant proportion of recipients are having to do without what the population generally considers to be necessities is clearly an important input into such an assessment. However, as we saw in Chapter 2 some have argued that deprivation indicators can serve the more ambitious goal of identifying the level of income which *would* be widely considered adequate. This belief goes back to Townsend's (1979) influential British research using non-monetary indicators. Constructing a summary deprivation index, he hypothesised that there would be an income level (varying with household size and composition) below which deprivation "escalated disproportionately". His own results, he claimed, tentatively supported the notion that there was indeed such a income threshold. This has been a controversial claim, however, rejected by Piachaud (1981; 1987) and Mansfield (1986), but supported by Desai (1986). More recently, Veit-Wilson (1994) has drawn on the work of Mack and Lansley (1985), who measured deprivation in terms of enforced absence of items or activities which most people regarded as necessities, to argue that non-monetary indicators could provide the basis for a Minimum Income Standard:

The most democratic and effective approach is to ask the population what it considers to be the minimum necessities which no one should be without, and then discover the income levels at which different household types acquire them. (1994, p. iii).

While this is an appealing notion, our in-depth analysis of non-monetary deprivation indicators in the 1987 ESRI survey does not support optimism about its prospects of success as a strategy for identification of a minimum adequate income. The relationship between scores on summary deprivation indices and household income using that data has been examined in Callan, Nolan *et al.*

(1989), Callan, Nolan and Whelan (1993) and Nolan and Whelan (1996). These studies show that many factors other than current income affect deprivation scores, notably previous experiences of household members in the labour market but also such long-term factors as social class background. This means that a straightforward relationship between deprivation scores and current income (adjusted to take size and composition into account) is not to be expected. In turn, this makes highly problematic the identification of an income level, or even a relatively narrow income range (as Veit-Wilson acknowledges as more realistic), below which income is clearly inadequate because people are seen to be deprived of necessities and above which it is adequate because they are seen to not be deprived of those necessities.

In order to appreciate this it is necessary to spell out how relatively modest the observed relationships between household income and life-style measures actually are. This is particularly true where we employ individual indicators of deprivation. However, even where we aggregate items into summary indices and distinguish between dimensions the conclusion holds true. As in previous work we distinguish the basic deprivation dimension described earlier, a secondary dimension relating to such items as cars, telephones and leisure activities, and a housing dimension consisting of items related to housing quality and facilities. The correlation between the log of equivalent household income and the basic deprivation index in the 1994 survey is -0.3; the correlation with secondary deprivation is slightly higher at -0.4, while that with housing deprivation is lower at -0.2.

These levels of correlation are in line with our previously published findings from the 1987 survey (see especially Nolan and Whelan, 1996). In-depth analysis of the additional factors determining life-style deprivation using that dataset (Nolan and Whelan, 1996, Chapter 5) showed that income was only one of a number of factors affecting life-style deprivation, and demonstrated the influence of factors related to long-term resources and the manner in which a household has arrived at its present position. The role of such factors helps to account for the – at first surprising – finding that the basic and housing indices, made up of items possessed by most households and regarded by most as necessities, are less highly correlated with income than the secondary dimension, which includes items much less widely held and less universally regarded as necessities. The housing items are of a type that would be accumulated over a longer period, so that stage in the life-cycle and permanent income play a particularly important role. Current income is therefore less important than for the items of current consumption which make up the majority of those in the secondary index. The items in the basic deprivation index, though also relating largely to current consumption, represent rather more extreme forms of deprivation than the secondary items. People probably go to considerable lengths, drawing not only on current income but also

on savings and accumulated resources and on available support from extended family and friends, to avoid these forms of deprivation. It is thus precisely in the case of the items in the secondary index such as holidays, presents and nights out, which represent more discretionary spending, that we observe the strongest relationship with current disposable household income.

It is not necessary for present purposes to repeat that in-depth analysis with the 1994 survey data. What we do wish to emphasise is the implication that current income is likely to be more strongly associated with deprivation the more closely it corresponds with overall command over resources – in other words, the fewer other resources households have to fall back on. In particular, we might expect that households reliant on social welfare will differ from those receiving but not reliant on social welfare first in the extent of deprivation being experienced but also in the degree to which such deprivation varies by income level, because they are more likely to have run down savings, etc., and thus be entirely reliant on current income. We therefore now look at the relationships between current income, deprivation and social welfare status (i.e., whether not receiving, receiving not reliant, or reliant on social welfare).

Table 4.8 shows the extent of variation in each of the life style dimensions by social welfare status. Those receiving but not reliant on social welfare experience levels of deprivation about twice as high on average as those not in receipt of social welfare. Those reliant on social welfare, in turn, experience levels of deprivation which are about twice as high as those receiving but not reliant. Simply distinguishing those not receiving/receiving but not reliant/reliant on social welfare accounts for 12 per cent of the variation in basic deprivation, 24 per cent of the variation in secondary deprivation, 9 per cent for housing and 22 per cent of the variation in the overall index.

Table 4.8: *Mean Scores on Different Life-Style/Deprivation Indices for Households Not Receiving/ Receiving/Reliant on Social Welfare, 1994*

	<i>Households in sample</i>			<i>Proportion of Variance Explained</i>
	<i>Not Receiving Social Welfare</i>	<i>Receiving but Not Reliant on Social Welfare*</i>	<i>Reliant on Social Welfare*</i>	
	<i>(mean score on index)</i>			
Basic deprivation index	0.17	0.40	1.17	0.12
Secondary deprivation index	1.00	1.79	3.00	0.24
Housing deprivation index	0.10	0.30	0.65	0.09
Overall deprivation index	1.17	2.32	4.32	0.22

* Households receiving more than half their income from social welfare transfers (excluding Child Benefit) are taken to be reliant on social welfare.

In Table 4.9 we explore the patterns of deprivation for the individual items entering the basic deprivation index which underlie such differences. This shows for example that only 1 per cent of households not receiving social welfare is unable to afford a meal with meat, chicken or fish every second day, but this figure rises to almost 4 per cent of those in receipt but not reliant on social welfare and to almost 10 per cent of those reliant on social welfare. The corresponding figures for a warm waterproof overcoat are 1, 5 and 12 per cent respectively; and for two pairs of shoes the figures are 1, 5 and 16 per cent. Strikingly similar differences across these three groups of households are observed for the other basic items.

Table 4.9: *Percentage of Households Not Receiving/Receiving/Reliant on Social Welfare Experiencing Enforced Lack of Different Basic Deprivation Items, 1994*

	<i>Households in sample</i>		
	<i>Not Receiving Social Welfare</i>	<i>Receiving but Not Reliant on Social Welfare*</i>	<i>Reliant on Social Welfare*</i>
	<i>% Experiencing Enforced Lack of Item</i>		
Meal with meat, etc.	1.0	3.6	10.1
Warm overcoat	1.2	5.2	12.2
Two pairs of shoes	1.3	4.7	15.5
Roast joint or equivalent	2.0	5.3	15.8
New clothes	1.4	5.1	17.8
Manager lacks food	2.1	3.9	18.0
Manager lacks heat	0.8	1.0	8.8
Debt problems from everyday needs	2.1	3.9	18.0

* Households receiving more than half their income from social welfare transfers (excluding Child Benefit) are taken to be reliant on social welfare.

For the reasons outlined, not only is social welfare status correlated with the experience of deprivation but the relationship between income and deprivation is dependent on welfare status. Concentrating now on those households reliant on social welfare, Table 4.10 looks at the relationship between income decile and deprivation. Once again the distinctive nature of housing deprivation is shown by the absence of any systematic relationship with income. For the other two dimensions a gradual decline in deprivation is observed across the bottom three deciles – which cover an income range running up to £72 per week per adult equivalent. However, no further reduction occurs the fourth and fifth deciles – which extend from £72 to £94. Finally, a further significant drop occurs for the sixth decile and beyond. Focusing on basic deprivation, this means that the

MINIMUM ADEQUATE INCOME

Table 4.10: *Mean Deprivation Scores by Equivalent Income Decile for Households Reliant on Social Welfare*

	<i>Decile 1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>	<i>6 +</i>
	<i>(< £58)</i>	<i>(£58<65)</i>	<i>(£65<72)</i>	<i>(£72<81)</i>	<i>(£81<94)</i>	<i>(£94+)</i>
	<i>Mean Score on Index</i>					
Basic deprivation	1.9	1.4	1.0	0.9	1.0	0.4
Secondary deprivation	4.1	3.4	2.6	2.4	2.8	1.9
Housing deprivation	0.7	0.7	0.5	0.8	0.7	0.4
Overall deprivation	5.9	5.0	3.7	3.8	4.1	2.5

average score falls from 1.9 in the bottom decile to 1.0 in the third decile. It then remains effectively unchanged for the fourth and fifth decile before falling to 0.4 for the sixth decile and above.

In Table 4.11 we set out this relationship for the individual basic deprivation items, again for households reliant on social welfare. We see for example that the percentage of households unable to afford a meal with meat, chicken or fish every second day declines from 15 per cent in the first decile to 8 per cent in the third decile. For a warm waterproof overcoat the numbers suffering enforced absence drops from 20 per cent in the first decile to 13 per cent in the second decile and to 10 per cent in the third decile. It then remains constant before falling to 6 per cent for the sixth decile and above. Close to one quarter of those concentrated

Table 4.11: *Percentage Experiencing Enforced Lack of Basic Deprivation Items by Equivalent Income Decile for Households Reliant on Social Welfare*

	<i>Decile 1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>	<i>6 +</i>
	<i>(< £58)</i>	<i>(£58<65)</i>	<i>(£65<72)</i>	<i>(£72<81)</i>	<i>(£81<94)</i>	<i>(£94+)</i>
	<i>% Enforced Lack</i>					
Meal with meat, etc.	14.6	10.8	8.3	8.0	13.8	2.9
Warm overcoat	20.4	12.8	10.4	10.3	10.7	5.8
Two pairs of shoes	22.9	16.3	16.5	12.9	13.5	5.3
Roast joint or equivalent	23.2	21.1	12.3	11.5	14.7	6.5
New clothes	25.0	19.5	13.7	17.8	18.3	7.8
Manager lacks food	14.6	11.8	7.8	6.8	4.7	1.5
Manager lacks heat	30.0	24.4	15.6	13.6	10.9	3.0
Debt problems from everyday needs	38.7	23.7	12.2	10.9	10.0	11.7

in the bottom decile are also unable to afford two pairs of strong shoes, a roast joint or its equivalent or new rather than second-hand clothes. Fifteen per cent of households managers in the bottom decile reported that there was a day in the previous two weeks when they did not have a substantial meal due to lack of money, and 30 per cent that they had to go with heating during the last year through lack of money, i.e., that they had to go without a fire on a cold day, or go to bed early to keep warm or light the fire late because of a lack of fuel. These figures are almost halved by the third decile and then decline gradually. Finally, almost four out ten households found in the bottom deciles report debt problems arising from day-to day needs, this falls to 12 per cent by the third decile and very little variation is observed thereafter.

Overall then across the range of basic deprivation items those households relying on social welfare and located in the bottom decile are consistently identified as experiencing distinctive levels of deprivation. A general picture emerges whereby such deprivation is dramatically reduced as one moves from the first to the third decile. Thereafter income tends to have little effect until one reaches those households lying at or above the sixth decile at which point we can identify a group of households who have a deprivation profile which is very close to those households receiving but not dependent on social welfare.

From a descriptive point of view these results paint a striking picture of the hardships experienced by low-income households reliant on social welfare in 1994. The question remains of what we can reasonably infer about the impact of changes in income levels on such households. If we could shift households in the bottom two deciles, below £65 per adult equivalent, into the £65-72 income range which comprises the third decile would we observe reduction in deprivation on the scale observed in our cross-sectional analysis? One would have to doubt it. It seems more likely that the households which are distributed across the bottom three deciles differ from each other in many ways other than current income. Effectively, even the households dependent on social welfare differ not only in terms of current income but also in the ways in which they have arrived at their current situation, and so we cannot attribute all the differences in observed deprivation simply to income levels at the time of the survey. It would therefore be hazardous to extrapolate from our results to a conclusion about the likely effects on deprivation of increasing the incomes of those below £65 per adult to above that level. None the less, documenting the levels of deprivation being experienced by such households is particularly valuable in that it provides a concrete insight into the living standards social welfare affords them, on which basis those involved in the policy process can form a view as to whether current support rates are adequate.

4.5 *The Views of Social Welfare Recipients about Income Adequacy*

In the 1987 and 1994 ESRI household surveys, respondents were asked the following question:

In your opinion, what would be the very lowest net weekly income that your household would have to have in order to make ends meet, given the present circumstances and composition of your household?

This constitutes the "minimum income question" on which one of the approaches to deriving consensual income poverty lines described in Chapter 2 is based. For the reasons outlined there, we see some serious difficulties in using the responses to questions of this type of households throughout the income distribution to derive an income poverty line or an income adequacy standard. Among the difficulties we noted that even if there is a consensus throughout the society about what constitutes basic "necessities", a minimally acceptable way of life, people in the middle and upper parts of the income distribution may not have a clear perception of how much money it takes to reach that living standard. Further, respondents are explicitly (and deliberately) being asked their evaluations of how much they need to make ends meet *in their own present circumstances*, which may not reflect what they would more broadly consider an adequate income for a household of that composition. However, these subjective evaluations have particular relevance in the present context if we focus on households which are in fact currently depending almost entirely on social welfare. Then, the responses provide some direct evidence on whether those depending on social welfare consider it to be enough to "make ends meet", and if not how much would be enough.

Earlier, we used the cut-off that households receiving particular social welfare schemes were deemed to be largely reliant on the scheme in question if it constituted more than half the household's income. Now we want to focus firmly on households depending almost entirely on social welfare overall, but will not be distinguishing particular schemes. We therefore now look at the households in the 1987 and 1994 surveys in which at least *two-thirds* of total current weekly gross income was coming from social welfare transfers (other than Child Benefit). This was the case for 29 per cent of the 3,293 households in the 1987 survey and a slightly higher percentage, 32 per cent, of the 4,040 households in the 1994 survey. For these households depending on social welfare, disposable income and subjective evaluations of the minimum income needed to make ends meet – which we will refer to as stated minimum income – can be compared. It makes most sense to do so for distinct household composition types, since we know that household size and composition will affect both actual income and perceptions of needs. In doing so we distinguish composition types not only in terms of numbers

of adults and children (aged under 18), but also whether the adults are "elderly" – aged over 65 – or not, and use only categories for which there were at least 10 cases in the 1994 survey. We take the minimum income response of the household head as representative of the household.¹² Table 4.12 shows for 18 separate household size/composition types the mean stated minimum income, mean actual

Table 4.12: *Views of Different Household Types Depending on Social Welfare about Minimum Income, 1987*

	<i>Minimum Income Stated</i>	<i>Mean Reported Net Income</i>	<i>Mean Minimum as % of Mean Reported</i>	<i>Number of Cases</i>
	<i>£ per week</i>			
1 elderly	59.20	56.47	104.8	118
2 elderly	106.48	99.89	106.6	112
1 adult	56.56	43.93	128.8	42
2 adult	96.11	81.78	117.5	48
3 adult	111.45	110.67	103.4	21
4 adult	119.18	148.11	80.5	6*
1 adult 1 elderly	86.31	85.65	100.8	62
1 adult 2 elderly	110.99	126.16	88.0	34
2 adults 1 elderly	126.69	111.09	114.0	17
1 adult 1 child	75.04	60.35	124.3	8*
1 adult 2 children	80.84	75.31	107.3	6*
2 adults 1 child	98.96	86.45	114.5	37
2 adults 2 children	117.71	96.18	122.4	56
2 adults 3 children	122.01	108.85	112.1	47
2 adults 4 children	137.90	125.2	110.1	29
2 adults 5 children	132.40	120.57	109.8	17
3 adults 1 child	153.08	120.81	126.7	4*
3 adults 2 children	144.88	123.84	117.0	11

Child = aged under 18.

* very small number of cases in sample

¹² In about three-quarters of sample households this was a man; however, there were not substantial systematic differences between spouses in responses to this question.

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income, the former as a percentage of the latter,¹³ and the number of cases in the sample in the category on which these results are based, all from the 1987 survey. Table 4.13 shows the corresponding results for 1994.

Table 4.13: *Views of Different Household Types Depending on Social Welfare about Minimum Income, 1994*

	<i>Minimum Income Stated</i>	<i>Reported Net Income</i>	<i>Mean Minimum as % of Mean Reported</i>	<i>Number of Cases</i>
	<i>£ per week</i>			
1 elderly	79.11	71.93	110.0	200
2 elderly	137.63	130.44	105.5	153
1 adult	87.17	64.14	135.9	72
2 adult	145.53	114.23	127.4	55
3 adult	176.55	169.54	104.1	14
4 adult	249.80	228.38	109.4	10
1 adult 1 elderly	140.84	125.53	112.2	61
1 adult 2 elderly	194.65	191.59	101.6	15
2 adults 1 elderly	195.42	182.90	106.8	17
1 adult 1 child	124.99	91.26	137.0	18
1 adult 2 children	144.88	104.18	139.1	16
2 adults 1 child	168.52	129.48	130.2	32
2 adults 2 children	168.24	143.47	117.3	45
2 adults 3 children	180.81	161.68	112.8	49
2 adults 4 children	219.29	178.99	122.5	29
2 adults 5+ children	208.30	188.55	110.5	10
3 adults 1 child	175.28	180.89	96.9	10
3 adults 2 children	216.95	189.35	114.6	11

Note: Child = under 18.

¹³ Note that this is not the same as calculating minimum/actual income for each household and taking the mean of this ratio, but the differences are not major in this instance.

The results for 1987 show that the amount regarded as the minimum needed to get by varies systematically with household composition type and with household income, as one would expect from previous studies (including our own using the 1987 data – see Callan, Nolan *et al.*, 1989, Ch. 6). In most cases, mean stated minimum income exceeds mean actual income, but the percentage by which it does so varies a good deal. The household types with actual incomes closest to their stated minima were those comprising elderly persons, whether alone or with other adults, while those comprising a single adult or a single adult with a child were furthest from their stated minima. A crude overall average across all households depending on social welfare would indicate that minimum income exceeded actual income by about 10 per cent.

The average stated minimum income of single-person households – whether elderly or not – was about £57-59 per week in 1987. If one indexes the range of £51-£59 identified as minimally adequate for a single person by the CSW for 1985 by the CPI, the corresponding range for 1987 is £55-£63. The subjective evaluations of minimum incomes by single-person households depending on social welfare are therefore consistent with the CSW's conclusions about an adequate income for such households at about the same time. As far as the needs of a single person versus a couple are concerned, the mean stated minimum income of households depending on social welfare and comprising two non-elderly adults was 1.7 times that of corresponding single-adult households, while for households of two elderly persons the ratio was 1.8 times that of single elderly households. Subjective evaluations of "needs" by those depending on social welfare thus reflect greater needs for a couple relative to a single person than the 1.6 adopted by the CSW.

Compared with the equivalence scales produced by other methods or built into social welfare payment rates, the impact of children on stated minimum incomes is rather low. Couples with one child have a mean stated minimum only marginally higher than couples with no children, the mean then jumps for those with two children but is then little higher for three children. Taking an average over couples with 1-4 children, the implicit equivalence scale taking a single adult as 1 is that a child adds only 0.19 to a household's needs, whereas conventional equivalence scales often employ values of at least 0.3. This is a well-known feature of subjective evaluations, found consistently by consensual poverty line methodologies (see, for example, Hagenaaars, 1986; Van Praag and Van der Sar, 1988; Kapteyn Kooreman and Willemsee, 1988) including our own analysis of the subjective evaluations of the entire 1987 sample (Callan, Nolan *et al.*, 1989, Chapter 6). It is thus unsurprising that it is again reflected here in the responses of those depending on social welfare. The interpretation and substantive implications of this general pattern are matters of dispute in the literature, and it is not our

intention to deal with them at length here. The costs incurred when one has children are offset by the benefits attached in terms of satisfaction, "happiness" or "utility" probably contribute to the flatter equivalence scales produced by subjective evaluations than by other methods. However, in assessing adequacy and setting social welfare rates the concern of policy-makers is rather the material living standards which income support allows parents and children to attain.

The most interesting aspect of the subjective evaluations in the present context is that we now have comparable data available for 1994, shown in Table 4.13, so the evolution of perceptions of minimum income needs by those depending on social welfare can be studied. A similar general pattern to 1987 can be seen, in that mean stated minimum income again exceeds mean actual income for most household types, with the elderly having the smallest gap and households comprising a single adult and a single adult with a child having particularly large gaps. Overall, the gap between actual and stated minimum income has not narrowed since 1987, despite the relatively substantial real increases in what were the lower rates of social welfare payment implemented over the period (as described in detail in Chapter 5). For the most part, the amount regarded as a minimum needed to make ends meet appears to have risen in line with actual incomes. Focusing on single adult households, the mean stated minimum income is now £87 per week for non-elderly adults and £79 for single elderly persons.

The gap between the mean stated income of couples and those of one-person households has narrowed slightly, with the former being 1.74 times the latter for the elderly and 1.67 times for non-elderly adults. The pattern for the additional impact of children is somewhat different to 1987, with one child now having a major impact but couples with two children having the same stated minimum as those with one. However, again taking an average over couples with 1-4 children, the implicit equivalence scale for children taking a single adult as 1 is in fact the same as 1987, with each child adds 0.19 to a household's needs on average. Children in lone-parent families add a good deal more to stated minimum income needs, it should be noted: averaged over 1 and 2-child cases in 1994, each child increases the stated income needs of a single adult by about 0.33. (The number of "1 adult with children" household cases in the 1987 sample was very small indeed, as highlighted in Table 4.1.)

It would be unwise to read too much into the responses to the "minimum income question", particularly since the precise manner in which such a question is formulated can affect the way people interpret and respond to it. Responses varied considerably even within household types and concentrating on those relying on social welfare, the variance of minimum income being about twice that of actual incomes for most household types. It is clear from these results and from analysis elsewhere of this type of data, that the current income of a household is itself a

major influence on the amount which is seen by the household as the minimum necessary to make ends meet. Thus, while households relying on social welfare say that an income about 10 per cent higher than their current income would be enough to make ends meet, households which are actually receiving that higher income do not generally regard it as enough to make ends meet. Indeed, it is only when household income is well above the average that stated minimum income "needed" is on average equal to actual income. Households not relying on social welfare thus had mean incomes which were on average about three times as high on those relying on social welfare, but their mean stated minimum income was about twice as high. This brings out the extent to which expectations and perceptions of "needs", far from being fixed or exogenous when it comes to setting income support rates, are influenced both by those rates and by incomes in society more generally. However, in providing an insight into the perceptions of those relying on social welfare, these results are a valuable complement to other perspectives on the way income adequacy has evolved since 1987.

4.6 Results from the Budget Standard Method

So far this chapter has focused on what can be learnt about adequacy from the analysis of available Irish household survey data. It is now useful to look at the alternative route offered by the budget standard approach. We therefore set out in some detail the results of a recent Irish study adopting that approach specifically focused on children, as well as recent UK studies with the broader remit of producing budgets for a range of different household types.

Carney *et al.* (1994), in a study for the Combat Poverty Agency, applied the budget standards approach to estimating the "cost of a child" for Ireland in 1992. They specified and costed the basket of goods and services they considered to constitute a basic minimum, including food, clothes, schooling costs, and limited spending on recreation. They found that the costs associated with rearing a child differed considerably depending on the age of the child: estimated costs were nearly twice as high for teenagers as they were for young children. In 1992 prices, the estimated basic minimum cost for a child aged 0-6 was about £21 per week, whereas for someone aged 7-12 it was £28.50 and for someone aged 13-18 it was about £37. It is worth noting that Conniffe and Keogh's (1988) study of the costs of children using Household Budget Survey data for 1980 also suggested that older children cost substantially more than younger ones (and that there were substantial economies of scale with respect to number of children). However both studies concentrate on direct costs, whereas the costs of obtaining childcare if both parents work outside the home, not taken into account, are greatest for younger children.

Except for the youngest age group, the amounts estimated by Carney *et al.*, as a basic minimum were well in excess of the total income support then provided for

a child to those relying on social welfare through Child Benefit and Child Dependant Allowance. The study also presented estimates of the costs per child of attaining a "modest but adequate standard", which were £7-£13 per week higher than the basic minimum standard. This included a more varied diet, some additional educational expenses, and extra spending on toys and presents. Taking this as the standard of comparison, state support was inadequate even for young children, and even taking into account increases in support rates in 1993 and 1994.

No similar Irish study has been carried out applying the budget standards method to producing an estimate of adequate income for adults. It is therefore worthwhile to describe the results of such an exercise carried out for the UK by Bradshaw and colleagues at the University of York in the late 1980s-early 1990s (summarised in Bradshaw, 1993). This involved teams of researchers preparing budgets at a very fine level of detail for separate commodity groups – housing, food, fuel, clothing, household goods and services, personal care, transport, leisure goods and services. The content of these budgets was based on expert advice, recommended standards of official bodies, previous budget studies, actual consumption patterns, and the views of focus groups. The budgets are intended to represent a "modest but adequate" standard, though the difficulty of defining what this means is acknowledged. Budgets were constructed for six different family types, and vary depending on whether the household is an owner occupier or local authority tenant and whether they own a car or not. The various elements of the budgets were costed at different points in the late 1980s-early 1990s and the results were uprated to 1993 prices.

Table 4.14 shows the summary budgets for the six household types for tenants, where all households except the pensioner own a car. These are valuable in conveying both the breakdown of the budgets across the different commodity groups, and the relativities between the different types of household. Housing, food and transport make up more than half the budget for each household type except the lone parent, which is an outlier because one-fifth of its budget goes on childminding costs (assuming the parent works full-time outside the home). As a result of those costs, the total budget for a lone parent with two children is only marginally below that for a two-adult household with the same number of children (and of the same ages). The total budget for a pensioner is below that for a single non-elderly adult only because the former is assumed not to own a car: although the budgets also differ somewhat across the other items, these differences balance out.

In terms of the implied equivalence scales, these "modest but adequate" budgets suggest that a couple requires about 1.4 times the income of a single adult, significantly less than incorporated in many scales in common use and those implicit in either UK or Irish social security rates. (An alternative way of putting

Table 4.14: UK "Modest but Adequate" Budget Standards for Different Household Types, 1993

	Household Type					
	Single Adult	Single Pensioner	2 Adults	2 Adults, 2 Children Aged 4, 10	2 Adults, 2 Children Aged 10, 16	1 Adult, 2 Children Aged 4, 10
	UK£ per week					
Housing	33.0	43.4	36.0	47.8	47.8	43.8
Food	26.7	19.5	40.0	59.0	70.1	39.4
Fuel	5.8	8.6	7.2	14.7	15.0	13.3
Alcohol	7.8	5.0	13.4	13.4	13.4	5.6
Clothing	6.6	6.1	14.1	28.1	29.8	21.6
Household Goods	8.9	13.9	17.0	29.6	30.5	28.1
Household Services	5.4	3.4	8.5	8.4	10.1	5.7
Personal care	3.7	3.3	8.7	10.8	13.5	7.6
Motoring	22.3	-	33.3	36.0	35.5	33.8
Fares	3.3	4.9	5.4	10.7	13.3	5.2
Leisure goods	6.2	6.5	8.5	15.5	15.8	15.2
Leisure services	10.8	5.5	20.4	17.4	22.2	11.7
Childminding	-	-	-	26.8	6.6	64.9
Total	151.4	120.0	212.3	318.1	323.5	295.8

Source: Bradshaw (1993) Table 11.2, p. 174.

the same point is that a single adult needs rather more relative to a couple.) As far as children are concerned, the standard for a couple with two children aged 4 and 10 is 50 per cent higher than that for a couple without children. Expressed as a proportion of the budget for a single adult, the implicit equivalence scale for each child is 0.35. This falls within the range of about 0.3-0.4 which encompasses the figure for a child incorporated in many widely-used scales, but is striking in suggesting that there is little difference between a child and an extra adult. The budget for a couple with two children aged 4 and 16 is marginally higher, with an implicit scale value for the older child of 0.39; while this is even closer to the value for an extra adult, older children do not cost much more than younger ones overall (unlike in Carney *et al's* Irish study) because additional household expenditure on food and leisure is largely offset by lower child-minding costs.

Having drawn up these modest-but-adequate budget standards, Bradshaw's team then sought to adapt these to a "low cost" level, without presenting any

in-depth justification for doing so. This involved adjusting the budgets by reducing the number of items included, increasing the assumed lifetime of some items, and assuming that the lowest prices available are obtained for each item. The low-cost budgets produced by this exercise for three household types come to between half and two-thirds of the modest-but-adequate budgets for those types seen above. One cannot, of course, simply apply standards developed for the UK to Ireland, but it may be of interest none the less to uprate these UK£ figures for the early 1990s to the mid-1990s by indexing to the increase in prices there, and then convert them to IR£ terms using Purchasing Power Parity-based conversion factors. The figures this produces are £55 per week for a pensioner living alone in local authority housing, £151 per week for a couple with two children, and £117 for a lone parent with two children. (The lone parent is now assumed not to be in employment so presumably saves substantially on child care compared with the modest-but-adequate budget.) If the same relativities between a couple with two children and a single adult shown by the modest-but-adequate standards apply, the low cost figure for a single non-elderly adult would be about £71 per week. The "modest but adequate" budget for such an individual, on the other hand, would be at least one-and-a-half times that figure.

What weight should one place on the results of such budget standard exercises? One great advantage of the method is that it is straightforward and, at least in principle, transparent. Through an explicit setting out of the consumption basket, it can tap into common understanding of what adequacy means, and is therefore potentially credible and convincing to a wide audience. However, the precision of the eventual consumption basket and costings can obscure the large number of subjective decisions, relating to what is included and to what standard, many of which are essentially arbitrary. The difficulty in deciding whether a particular consumption basket would then be regarded by most people as "adequate" is demonstrated by the fact that Carney *et al.*, present both "basic minimum" and "modest but adequate" budgets – implying that the basic minimum is not adequate? Similarly Bradshaw *et al.*, invest enormous effort into producing modest-but-adequate standards for the UK, and then undermine the whole exercise by adjusting these in a fairly *ad hoc* way to arrive at the considerable lower "low cost" figures. The budget standards approach has a clear value in demonstrating what a given level of income can buy, even given stringent budgeting and careful management, and thus in supporting a case that a particular level of income support is "inadequate". Like other approaches, when employed to say what an adequate level of income or support would then be it faces much more severe difficulties. It is not the degree of arbitrariness involved which distinguishes budget standards from other approaches, which as we have seen also generally fall back on what are essentially arbitrary benchmarks such as a particular proportion of

average income. With the budget standard method, however, there is the danger that the extent of judgement being exercised is not obvious on the surface, and so the results may be accorded a "scientific" status which they do not deserve – and which practitioners would not claim for them. Budget standards are also time- and resource-consuming to establish and maintain, but with a clear understanding of their strengths and weaknesses can contribute to the assessment of adequacy of social security rates. As the Australian DSS review on adequacy (1995) already mentioned puts it, budget standards are essentially illustrative and should not be seen as an attempt to define an adequate standard of living, but rather to outline the financial consequences of a specified and defined living standard (p. 46): as such they have a clear value.

4.7 Case Studies from Money Advice Centres

Another perspective on the finances of low-income households and how they make ends meet is provided by information now becoming available from the Money Advice and Budgeting Service, through which the Department of Social Welfare funds centres in a number of locations around the country providing confidential assistance with the management of household finances. Individuals and families may be referred to the service by, for example, the Community Welfare Officer, social workers, local government officials or voluntary agencies, or may simply approach the service on their own initiative. As a valuable input into the present study the Department of Social Welfare asked five of these centres to prepare ten anonymised case studies each, to illustrate the type of problems with which people presented themselves and how the service sought to assist them.

These case studies provide a vivid picture of the scale of the financial difficulties which some households face. Most of the cases have arrears and/or debts to pay off, in some instances very substantial ones indeed. As a result, much of the weekly income coming into the household is pre-committed to keeping creditors at bay and the remainder generally goes on food and gas/electricity. Even so arrears/debts are often mounting and the financial situation is clearly unsustainable, there is little or no prospect of being able to cope with the debts – by the time the case is referred to the advice centre, eviction or legal proceeding for recovery of debt may be looming.

The advice centre generally seeks to develop with those seeking help a structure within which a certain proportion of their income is to be set aside each week to meet arrears and debts, while at the same time negotiating with creditors to agree on regular instalment payments to clear those debts. Very often this appears to be on the basis that the creditor writes off a significant proportion of the debt in return for some regular payment. The centre may also advise people as to their social welfare entitlements and explain their position and prospects to the Community Welfare Officer, and/or put them in touch with charities who may

make a contribution to helping them escape their present predicament. The aim is to put people in a position where, having extricated themselves from debt, they are budgeting within the constraints of their current income. While one could not use the case studies as a basis for calculating a success rate for the service in those terms, for a substantial proportion of the cases supplied it is hard to see how those seeking advice could attain a sustainable situation on their own: the imbalance between income and outgoings, and the scale of accumulated debt, is simply too great.

It is also interesting to note the types of household the advice service deals with most often, and the nature of the financial difficulties in which they find themselves. A very substantial proportion of the case studies are lone parents: in one of the centres (in Dublin) this was true of eight out of the ten cases provided. The other most common family type among the case studies, though much less common than that, were couples with very large families – of up to nine children – on UA or DPMA. The nature of the financial problems with which people presented to the advice centre varied, but commonly included rent arrears on local authority housing, arrears on gas, electricity or telephone, inability to service loans from financial institutions including credit unions, and the need to make payments to legal or illegal moneylenders. What is most striking, however, is the extent of the variation across the cases on roughly similar income levels in the size of debt they have accumulated.

Great care has to be exercised in drawing any inferences about the adequacy of incomes or social welfare rates generally from the experiences of the money advice and budgeting service as illustrated by these case studies. The first and most compelling reason for this is that those dealt with by the services are not in any sense a representative sample of the generality of low income households or social welfare recipients: on the contrary, they are a highly selective group, for the most part referred to the service precisely because of the scale of their financial difficulties. The assumption would have to be that their level of financial difficulty is if anything more atypical than typical: many people not seen by the service might still be experiencing less profound but none the less severe difficulties, but we simply cannot safely extrapolate from the experience of the service's clients. Less importantly, we are not in a position to assess directly even the extent to which the case studies are representative of all those helped by the service, though centres were asked to provide material on "typical" cases.

The other central difficulty in learning about adequacy from such case studies is that one could actually use them to support very different conclusions, at either end of the spectrum. On the one hand, it could be argued that the scale of the debt which some of the service's cases are seen to have accumulated while on social welfare, and their patent incapacity to cope with this debt on their current levels of

support, provide clear evidence that support rates are entirely inadequate (for them). On the other hand, cases where the advice and budgeting service is in fact successful in stabilising a household's financial situation could be seen as evidence that it is not support rates which are inadequate, but rather families' budgeting and financial management skills – so priority should be given to helping improve those skills. In the absence of information about how the case studies came to build up their debts, it is really not possible to assess whether better management would have been sufficient to allow them to avoid that situation. Unforeseen circumstances such as illness or family trauma clearly contributed in some cases, and in others the clients were psychiatric patients or suffering from depression, making it very difficult for them to cope. Some households clearly manage better than others on similar incomes, not only because of differences in their management skills but also because of differences in support available from family and friends. However, the situations people find themselves in by the time the advice service is involved are also a product of long-term processes such as detachment from the labour market and family breakdown: understanding the trajectories by which they arrived at their present plight is crucial to assessing the implications.

However they got into debt, many of the case studies were clearly not going to be able to extricate themselves without significant assistance – both financial assistance and advice. This provides the justification for investment in the advice and budgeting service, but not for any broader conclusions about adequacy or about the potential for improving financial management among low income households or social welfare recipients more generally. Harking back to our analysis of indicators of deprivation in the 1987 and 1994 surveys, it is worth recalling that going into debt for current household expenses was one of the indicators of basic deprivation we employed, and that a substantial proportion of those relying on social welfare and towards the bottom of the income distribution reported having such debt problems. Similar information on the households in the 1994 Living in Ireland survey will also be available from follow-up surveys for subsequent years (as part of the European Household Panel Survey), so it will then be possible to study how debt problems emerge over time for particular households and relate this to labour market, family and other experiences. Such analysis could usefully be complemented by a tracking of the experiences over time of those availing of the money advice and budgeting service.

4.8 An International Perspective

An indirect but valuable perspective on the adequacy of Irish social welfare rates is provided by comparisons between the relative generosity of support rates – relative to average earnings or household income – here and elsewhere. Making such comparisons on a truly consistent and comprehensive basis is notoriously

difficult, because of the complexity of social protection systems (cash and non-cash) and the differences in their modes of operation from country to country. This is an issue which would greatly benefit from more research in Ireland and at EU level, but to give a flavour of what it can tell us we first present some comparisons between Ireland and the UK, and then draw on results produced by the Commission in the Report on Social Protection to also make broader comparisons with the average for EU member states.

Table 4.15 shows selected benefit/assistance rates for Ireland and the UK in 1994, for a single adult, adjusting for exchange rate differences. We see that social assistance rates for those of working age are now a good deal higher in Ireland, as are unemployment benefit rates. In the case of contributory social welfare pensions for the elderly the basic rate is also a good deal higher in Ireland, though many UK recipients receive an earnings-related supplement, while means-tested pensions are lower in Ireland.

Table 4.15: *Selected Benefit Rates, Ireland and UK, 1994*

	<i>Ireland</i>	<i>UK</i>	<i>UK</i>
	<i>IR£</i>	<i>UK£</i>	<i>IR£ (adjusted for PPP)</i>
<i>"Safety net" for those aged:</i>			
18-24	58.90	36.20	37.45
25-64	58.90	45.70	47.28
65-74	61.00	63.95	66.16
<i>Social insurance benefits</i>			
Unemployment Benefit	61.00	45.45	47.03
Old age pension	71.00	57.60 ^a	59.60

^a Basic rate without earnings-related supplement.

This comparison of rates is against a background where average earnings in Ireland are lower than the UK, so expressed as a proportion of average earnings the gap between Ireland and the UK for most rates is even wider. This can be seen in Table 4.16, where we see for example that unemployment compensation for a single adult is about 35 per cent of average net earnings in Ireland compared with only 23 per cent in the UK. Although Child Benefit is higher in the UK, this would not be enough to offset the gap in adult rates for most families. However, the table also shows that comparison with the UK gives a very different picture to comparison with other countries. While Irish social assistance rates relative to earnings are not far below the EU average, social insurance rates are very far below that average. The UK thus affords a particularly low level of support in relative terms compared with other EU members, although the comparison with the

Table 4.16: *Selected Benefit Rates as % of Average Net Earnings, Ireland, UK and EU Average, 1994*

	<i>Ireland</i>	<i>UK</i>	<i>EU Average</i>
Unemployment assistance	35	23	42
Unemployment Benefit	35	23	61
Short-term Ill	32	28	69
Disabled	35	32	50
Lone Parents	44	38	40
Child Benefit (2 children)	4	9	12
Old age pension (social insurance)	42	44 ^a	75
Widow aged 30, 2 children	58	53	64
Widow aged 50, no children	36	31	55

^a Typical case including earnings-related supplement.

Source: Social Protection in Europe 1993, Chapter 4.

UK is of course particularly important given the links between the two labour markets.

An alternative if limited source of comparative data on the relative generosity of income support levels across countries is provided by the various studies which have sought to measure replacement rates for the unemployed, for example the recent OECD Jobs Study. This sought to derive replacement rates for unemployed persons at different durations and in different dependency positions, on as consistent as possible a basis across countries. Benefit or assistance entitlement was then taken as a percentage of the gross average industrial wage, though the impact of using net earnings for the average replacement rate across the various durations and dependency situations was also examined. A selection of the results for Ireland and some other EU countries are given in Table 4.17.

The figures have to be heavily qualified for a variety of reasons, but the overall pattern is of some interest in showing Ireland to have replacement rates higher than the UK, Italy and Greece but similar to or lower than many other EU member states. Income support levels for the unemployed are everywhere set with an eye to incentives as well as adequacy, and institutional structures and traditions differ markedly across countries (with for example insurance-based support determined by previous earnings levels in many instances). It is not therefore valid to draw strong conclusions from such comparisons as to the views prevailing in each country about what constitutes an adequate payment in relative terms.

Table 4.17: *OECD Estimates of Unemployment Replacement Rates for Various Countries, 1991*

	<i>Benefit/Assistance as Percentage of Average Gross Earnings</i>				<i>Average</i>	<i>Average Using Net Earnings</i>
	<i>First Year</i>		<i>Second Year</i>			
	<i>Single</i>	<i>With Dependent Spouse</i>	<i>Single</i>	<i>With Dependent Spouse</i>		
Ireland	38	52	26	41	29	37
Belgium	52	52	36	52	43	57
Denmark	73	74	61	67	52	60
France	58	58	37	37	37	48
Germany	37	41	33	36	28	43
Greece	44	53	4	4	17	23
Italy	7	8	0	0	3	5
The Netherlands	70	70	56	56	51	58
Portugal	65	65	37	40	34	42
Spain	70	70	30	30	33	41
UK	19	31	17	27	18	23

Source: OECD Jobs Study, Part II, Table 8.1 and Appendix Table 8.B.1.

None the less, it is of interest that Ireland's social welfare rates for this particular contingency are if anything low relative to average earnings in a comparative EU perspective – though the UK is of course particularly relevant from an incentives point of view given the close links between the two labour markets. Work incentive considerations only affect a sub-set of social welfare recipients, of course, with the elderly being the most substantial group for whom they have little direct relevance. (In the Irish case, only about one-third of social welfare recipients are in receipt of unemployment-related payments.)

4.9 Conclusions

In this chapter we have used data from large-scale household surveys carried out by the ESRI in 1987 and 1994 to throw light on the adequacy of social welfare. The purely relative approach to deriving adequacy estimates was first explored using data on household incomes and individual earnings in the 1994 Living in Ireland survey. Average household disposable income in the survey was £280 per week. Converting this to average income per adult equivalent with a scale that allows 1 for the household head, 0.66 for each other adult, and 0.33 for each child, and counting those aged under 14 as children, produces average disposable income per adult equivalent of £129 per week. A purely relative income poverty line or adequacy standard for a single person set at 60 per cent of this figure would thus be about £77 per week, while a standard set at 50 per cent

would be about £64 per week - in 1994 terms. If instead one uses another common scale, namely 1/0.7/0.5, then the 60 per cent and 50 per cent standards are lower, at £73 and £60 respectively. On the other hand, using the scales implicit in current unemployment-related support of 1/0.6/0.31 and counting a child as under 18, the lines would be higher at £68 and £82 respectively. Even over a quite narrow range of equivalence scales the estimate of an adequate income level is significantly affected by the choice of scale and the way it is applied, which given our state of knowledge is essentially arbitrary over a significant range.

The more important and essentially arbitrary choice in applying a purely relative approach is of course which proportion of the average one takes. The CSW, in deriving such an estimate from average equivalent household income, used 60 per cent and 65 per cent; common practice in studies applying relative income poverty lines is to use 50 per cent and 60 per cent (and sometimes also 40 per cent). Within the purely relative approach itself, there is nothing to say that 50 per cent is appropriate and 65 per cent is not, or vice versa: justification for focusing on a particular proportion must come from a source external to the method.

We then looked empirically at the extent to which households receiving or relying on social welfare payments from the various schemes in 1987 and 1994 fell below relative income poverty lines for each year. In 1987, a very high proportion of households relying on Unemployment Assistance or SWA were below half average income. Income poverty rates at the higher, 60 per cent income line were also high for those relying on UB, DB, Invalidity Pension, Widow's Non-Contributory Pension or Deserted Wife's Allowance. By 1994, the most notable changes were that poverty rates using the 50 per cent income line had fallen for those relying on UA or UB, but those relying on Old Age Pensions saw a substantial increase in risk with the 60 per cent line.

The adequacy of the various schemes was also assessed using a combination of relative income poverty lines and non-monetary deprivation indicators. The results for 1987 showed that, for the most part, the risk of being below the income lines and experiencing basic deprivation varied across schemes in the same way as risks with the income lines alone. By 1994, however, there had been a significant fall in the percentage of households relying on UA who fell below the income lines and experienced basic deprivation. The general pattern was that a stable or falling risk of being below the income lines and experiencing basic deprivation was much more common than an increasing risk. In-depth analysis of non-monetary deprivation indicators in the 1987 ESRI survey does not support optimism about the prospects of identifying a minimum adequate income as that below which people are deprived of what are generally regarded as necessities and above which they are not deprived of those necessities.

The income which households relying on social welfare believed was the minimum they needed to "make ends meet" in 1987 and 1994 was then analysed. The results showed that in 1987 households relying on social welfare and comprising a single adult regarded a figure of about £58 per week as the minimum necessary, which was in the range identified by the CSW as constituting a minimum adequate income. By 1994, subjective evaluations of such households were that a minimum of about £80-87 per week was needed to make ends meet. The income regarded as minimum by other household types generally rose in the same manner over the period. The equivalence scales implicit in the responses of different household types were also examined in some detail: as in other studies using these subjective evaluations, these implicit scales were much flatter than those produced by other methods, in other words the additional needs of larger compared with smaller families were substantially lower.

The main findings of an Irish application of the budget standards approach, estimating the "costs of a child", were also discussed. The study concluded that as of 1992-94 income support for teenagers was significantly below the basic minimum needed. Since no comprehensive Irish budget standards study of households more generally has been carried out, the results of a recent UK study were discussed in some detail. This contained a number of interesting findings about, for example, the needs of one household type versus another, and also provided important insights into what is involved in a full-blown budget standards exercise. The strengths and weaknesses of the budget standard approach were brought out in discussing these studies. The main strength is the extent to which people can concretely identify with the living standards incorporated in the consumption basket, the main weaknesses is the number of subjective decisions which are involved about what is included in an "adequate" consumption basket and to what standard. The main potential of budget standards is not to define what constitutes an adequate standard of living, but rather to outline the financial consequences of a specified and defined living standard and thus provide a point of reference in assessing the adequacy of current income support rates.

Case studies of those assisted by the Money Advice and Budgeting Service funded by the Department of Social Welfare were also discussed. These provide a direct insight into the financial difficulties in which some low-income households find themselves. Most of the cases have significant arrears or debts so that much of their weekly income goes on keeping creditors at bay. The advice service very often sought to put the family's finances on a stable footing by negotiating a partial write-off of these debts in return for some regular repayment. The biggest single group among the case studies comprised lone parents. One cannot draw conclusions about the adequacy of social welfare payments for the generality of recipients from these case studies, since they have mostly been referred to the

advice service precisely because of the unusual scale of their debts and financial difficulties.

Cross-country comparisons of the relative generosity of social security systems also offer a valuable perspective on adequacy, though obtaining data on which to make fully valid comparisons is difficult. The results presented suggested that Irish social welfare rates were more generous relative to average earnings or income than those in the UK, but were if anything below the average for EU countries as a whole.

Chapter 5

ADEQUACY AND SOCIAL WELFARE RATES

5.1 Introduction

In this chapter we first bring together in Section 5.2 the estimates of minimum adequate income levels produced by the various approaches described in Chapters 3 and 4, for 1994, 1995 and 1996. In Section 5.3 we compare these with the rates recommended as adequate by the CSW for 1985, updated in line with prices or alternatively in line with earnings. Section 5.4 then compares the various up-to-date estimates of what would be adequate, and the CSW's uprated recommendations, with current social welfare rates. Section 5.5 contrasts this with the situation in 1985. Section 5.6 considers the equivalence relationships between different family types implicit in current rates and the way these have changed since the CSW. Section 5.7 discusses the role of non-cash benefits and the impact which taking them into account has on assessment of the adequacy of cash income support levels. Section 5.8 brings together the conclusions.

5.2 Alternative Estimates of Adequate Income 1994-96

In Chapter 3 the different methods employed by the CSW to estimate an adequate income for a single adult were applied to up-to-date data, producing estimates for 1994 and, in some cases, 1995 and 1996. In Chapter 4 the stated minimum incomes needed to "make ends meet" and average disposable income or net earnings in the 1994 Living in Ireland survey were used to produce alternative estimates for that year. In Table 5.1 we bring these estimates together; where estimates applying to 1995 or 1996 are not available, these are extrapolated from 1994 or 1995 by uprating in line with the CPI. (The average level of the CPI rose by 2.5 per cent in 1995, and current forecasts for 1996 are that it will rise by 1.75 per cent¹⁴). This is a conservative up-rating procedure from a relative point of view, but over such a short period this will not significantly affect the levels of the estimates.

¹⁴ The latest ESRI *Quarterly Economic Commentary* (September 1996) and the Central Bank (*Quarterly Bulletin*, Autumn 1996) each forecasts an increase of 1.75 per cent in the CPI for 1996.

Table 5.1: *Alternative Estimates of Minimum Adequate Income, Single Person, 1994, 1995 and 1996*

<i>Method Based On</i>	<i>Minimum Income Estimate for a Single Adult for</i>		
	<i>1994</i> <i>£ per week</i>	<i>1995</i> <i>£ per week</i>	<i>1996</i> <i>£ per week</i>
<i>CSW Methods</i>			
average industrial earnings	89.92	94.10	95.75*
national accounts average earnings	85.00	87.16*	88.70*
medical card	73.68	77.65	80.70
tax exemptions	69.23	71.15	75.00
minimum wage	77.33/88.38	79.27/90.59	83.41/95.33
average net household income for 2 adult/ 2 child household: 60 per cent/65 per cent	84.08/91.09	86.22/93.40*	87.75/95.0*
<i>Other Methods</i>			
stated minimum income, single person households depending on social welfare: elderly/non-elderly	79.17/87.17	81.18/89.38*	82.6/90.95*
stated minimum income, 2 adult/2 child households depending on social welfare	72.02	73.85*	75.11*
average net household income, all households: 50 per cent ^a	64.5/68.5	66.14/70.21*	67.5/71.5*
60 per cent ^a	77.4/82.2	79.36/84.25*	80.75/85.75*

* extrapolated from previous year using CPI.

^a Range because of variation in equivalence scales and age cut-off for child shown in Table 4.1.

Focusing on the estimates for 1996, there is very considerable variation across the different methods, the full range being from £68 to £96 per week.¹⁵ This is rather wider than the range produced by the CSW's methods for 1985, both because the CSW methods give a wider range (from £75 to £96) in 1996 and because other methods are included and the half average equivalent household income calculation serves to extend the range down to £68.

5.3 Comparison with the CSW's Recommended Rates, Up-rated

We can now compare these alternative estimates of what constitutes an adequate income with the rates recommended by the CSW, updated to take

¹⁵ Note we have used the adequate income estimate based on the tax exemption limit rather than tax allowance since, as discussed in Chapter 3, that seems more satisfactory within the logic of that method.

changes in prices into account. In addition to recommending that the basic weekly rate for a single adult should be in the range £50-60, estimated to be minimally adequate in 1985, the CSW recommended that as a matter of priority that rate should be brought to £45 – which we will refer to as the CSW "priority rate". The Commission also recommended that the rate for a couple should be 1.6 times that for a single adult. We therefore show in Table 5.2 the evolution of the CPI since 1985, and the CSW's priority and recommended rates for a single adult and a couple, all up-rated in line with the CPI for each year from 1985 to 1996.

Table 5.2: *CSW Priority and Recommended Rates, Uprated in Line with CPI, 1985-96*

<i>Year</i>	<i>CPI</i>	<i>Priority Adult Rate</i>	<i>Priority Couple Rate</i>	<i>Basic Adult Rate (Bottom/Top of Range)</i>	<i>Basic Couple Rate (Bottom /Top of Range)</i>
1985	100.0	45.00	72.00*	50/60	80/96*
1986	103.8	46.71	74.74	51.90/62.28	83.04/99.65
1987	107.1	48.20	77.11	53.55/62.28	85.68/99.65
1988	109.4	49.23	78.77	54.70/65.64	87.52/105.02
1989	113.8	51.21	81.94	56.90/68.28	91.04/109.25
1990	117.6	52.92	84.67	58.80/70.56	94.08/112.90
1991	121.4	54.63	87.41	60.70/72.84	97.12/116.54
1992	125.1	56.30	90.07	62.55/75.06	100.08/120.10
1993	126.9	57.10	91.37	63.45/76.14	101.52/121.82
1994	129.9	58.46	93.53	64.95/77.94	103.92/124.70
1995	133.2	59.94	95.90	66.60/79.92	106.56/127.87
1996 ^f	135.5	60.99	97.58	67.77/81.32	108.42/130.11

* Couple rate = (1.6 times adult rate); ^f = forecast.

We see that if simply maintained in real terms, by 1996 the CSW's priority rate had reached £61 per week for a single adult and £98 for a couple. The Commission's recommended rates for 1985 were a range rather than a single figure, and by 1996 that range was £68-81 per week for a single adult and £108-130 per week for a couple. Compared with the various estimates in Table 5.1 of what would constitute an adequate income for a single person in 1996, the CSW recommendations held constant in real terms cover a narrower range. Whereas the uprated CSW range is £68-81 per week, the 1996 estimates of an adequate income are in the £68-96 range, with all but one £75 or higher. This is unsurprising given that many of the methods link adequacy directly to average earnings or incomes, which grew significantly over the period in real terms.

An alternative simple uprating procedure would be to link the CSW's original recommended levels to real net earnings. The CSO's quarterly series on average industrial earnings provides a consistent regular benchmark which can be used for this purpose, though only a minority of employees are covered. To arrive at the net equivalent of this gross earnings series one has to subtract income tax and PRSI contributions, and the former will differ depending on whether the employee is single or married. We therefore calculate the net earnings of a single person corresponding to average gross industrial earnings for 1985 and, using forecast earnings for the second half of 1995 and 1996, for 1996. (This is in fact what is involved in the application of the CSW's "average industrial earnings" method in Chapter 3 covering 1994 and 1995.) Forecast net average earnings for 1996 is about 68 per cent higher than the corresponding figure for 1985 – whereas the overall increase in the CPI over that period is about 36 per cent. This is the result of a rise of 51 per cent in gross average earnings, and a less rapid rise in income tax and PRSI payable at that earnings level. If the CSW's priority rates were linked directly to net earnings, they would therefore reach £76 for a single person and £120 for a couple; the CSW recommended range uprated in the same way would reach £84/100 for a single person and £134/160 for a couple.

5.4 Adequacy Estimates and Current Social Welfare Rates

We now look at the rates of income support currently being paid under the different social welfare schemes in the light of the various estimates of income adequacy which have been discussed. The first point of reference adopted is a comparison with the CSW's priority and recommended rates uprated in line with prices. As shown in Table 5.3, the rates of payment for single adults aged under 80 are now in the range £62.40-£75. Those aged 66 or over and living alone receive a further £6 living alone allowance, and those aged 80 or over receive a further £5 age allowance with the schemes relevant to those age groups. If one focuses on the basic weekly rate for someone aged under 66, the lowest current weekly rate of £62.40 (payable with SWA and short-term UA) is just above the CSW's priority rate up-rated to 1996 in line with prices, which was £61. So the priority rate uprated in line with prices has now been reached even by those lowest-paying schemes.

The £62.40 per week paid by those schemes is still well below the bottom of the CSW's recommended range uprated in line with prices, which is £68. That level is currently reached or exceeded only by contributory OAP and Widow's or Widower's Pension, though for persons aged 66 or over in receipt of the living alone allowance this would also be the case for non-contributory OAP and Widow's Pension. The personal rate payable under long-term UA, UB and DB, at £64.50, lies between the uprated CSW priority rate and the bottom of the

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Table 5.3: *Current Rates of Social Welfare by Scheme and CSW Recommended Rate Up-rated by CPI, 1996*

<i>Scheme</i>	<i>Personal Rate</i>	<i>With Adult Dependant^a</i>	<i>Personal Rate</i>	<i>With Adult Dependant^a</i>
	<i>£ per week</i>		<i>% of CSW Recommended Rate (Bottom of Range), Up-rated by CPI</i>	
<i>Social Insurance:</i>				
Contributory Old Age Pension (under 80)*	75.00	128.90 (66 or over)	110.1	118.3
Widow's/Widower's Contributory Pension, Deserted Wife's Benefit (under 66)*	68.10	-	100.0	-
UB/DB	64.50	103.00	94.7	94.5
Invalidity Pension under 65	66.20	109.80	97.2	100.8
66 under 80*	75.00	118.60	110.1	108.8
<i>Social Assistance:</i>				
Non-contributory. OAP (under 80) *	64.50	103.00	94.7	94.5
Widow's/Deserted Wife's/ Prisoner's Wife's Non-contributory Pension (under 66)*	64.50	-	94.7	-
UA short-term	62.40	100.90	91.6	92.6
UA long-term	64.50	103.00	94.7	94.5
Supplementary Welfare Allowance	62.40	100.90	91.6	92.6
CSW priority rate	60.99	97.58		
CSW recommended rate (bottom of range)	67.77	108.40		

^a Under 66 unless otherwise stated.

* Living Alone Allowance of £6.00 payable with these schemes to those aged 66 or over and living alone; £5 higher rate or allowance for those aged over 80 payable with all schemes catering for that age group.

recommended rate range. Short-term UA and SWA currently are 92 per cent of the bottom of the recommended range up-rated by prices.

For a couple, the rate of income support currently paid ranges from £100.90 to £128.90 per week. Once again, the lowest (short-term UA and SWA) rate is just above the up-rated CSW priority rate of £98, and the slightly higher rate of £103 paid by UB, DB and long-term UA is below the bottom of the CSW recommended

range of £108. The implicit equivalence scale built into the UB/DB/long-term UA rates now is that a couple needs 1.6 times the personal rate, the scale recommended by the CSW, while for short-term UA/SWA the implicit scale is slightly higher at 1.62, so the rate for a couple is closer to the CSW recommended rate than that for a single adult. (As discussed in the next section, this implicit scale for a couple versus a single adult has changed markedly since 1985.) The rate paid to a couple aged under 80 in receipt of contributory Old Age Pension significantly exceeds the bottom of the recommended rate – indeed it approaches the top of that range – whereas the rate received by a couple on non-contributory OAP is the same as UB/DB/long-term UA, and thus below the bottom of that range.

Most of the estimates of what constitutes an adequate income for a single person lie above the bottom of the uprated CSW recommended rate, all but one of those estimates being £75 per week or more. It follows that most of the current social welfare personal rates for a person aged under 80 lie well below those estimated adequacy levels, the only exceptions being contributory Old Age Pension and Invalidity Pension for someone aged 66-79, both of which are £75. For those aged 80 or over, Widow's/Widower's Pension and Deserted Wife's Benefit are close to that level, at £73.10 per week. (This of course implicitly makes the assumption that those in receipt of Invalidity Pension, and those aged 80 or over, have "needs" which are the same as other adults – whereas the social welfare system more reasonably assumes their needs are greater). On the other hand the lowest adequacy estimate from Table 5.1, based on 50 per cent of average net equivalent household income (and the 1/0.66/0.33 equivalence scale), was actually the same as the bottom of the updated CSW range – at £68 per week – and current UB/DB/long-term UA rates are not far short of that figure.

5.5 Social Welfare Rates in 1985 and Changes 1985-96

In discussing the rates of social welfare currently being paid *vis-à-vis* updated CSW adequacy benchmarks, it is important to review how these rates have changed since the CSW reported. Table 5.4 shows the rates being paid in 1985 and compares these with the bottom of the CSW's recommended range. Only contributory OAP reached the bottom of the recommended minimum adequate range at the time. Non-contributory OAP for a single adult was 88 per cent of the bottom of the recommended range, which was close to the priority rate. UB and DB were less than 80 per cent of the bottom of the recommended range, 88 per cent of the priority rate. Long-term urban UA was 70 per cent of the bottom of the recommended range, 78 per cent of the priority rate. Short-term rural UA and SWA were only 64 per cent of the bottom of the recommended range for a single adult, which was 71 per cent of the priority rate. Thus, most schemes paid rates for a single adult very far below the recommended range. The rates paid for a

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couple in 1985 were not as far below the CSW's recommended range, because the equivalence scale implicit in the level of support then paid for a couple versus a single adult were in fact rather more generous than the 1.6 recommended by the CSW, as detailed in the next section.

Table 5.4: *Social Welfare Rates and CSW Recommended Rate in 1985*

Scheme	Personal Rate	Person+Adult Dependant	Personal Rate	Person+Adult Dependant
	<i>£ per week</i>		<i>as % of CSW Recommended Rate (bottom of range), uprated by CPI</i>	
<i>Social Insurance:</i>				
Contributory OAP (under 80)	51.40	89.75 (aged 66 or over)	102.8	112.2
Widow's contributory pension /Deserted Wife's Benefit (under 66)	46.25	-	92.5	-
UB/DB	39.50	65.10	79.0	81.4
Invalidity Pension under 66	45.30	74.70	90.6	93.4
66 or over	46.20	76.20	92.4	95.2
<i>Social Assistance:</i>				
Non-contributory OAP (under 80)	44.00	88.00 (i.e. 2 personal rates)	88.0	110.0
Widow's non-contributory pension (under 66)	43.15	-	86.3	-
UA urban long-term	34.95	60.15	69.9	75.2
UA rural short-term	31.75	54.80	63.5	68.5
SWA	31.75	54.80	63.5	68.5
CSW priority rate	45.00	72.00		
CSW recommended rate (bottom of range)	50.00	80.00		

By 1996, as we have seen, the priority rate uprated in line with prices had been reached by all schemes. This reflects the fact that, in line with the Commission's recommendations, priority has been given since 1986 to bringing up what were then the lowest rates of payment. Focusing on the rates for adults without dependants, those on contributory or non-contributory old age pension have seen their rates rise by about 7 per cent in real terms between 1985 and 1996.

UB and DB rates rose by 20 per cent, but the increases in UA and SWA have been very much higher again. For UA the increase was 40/44 per cent for short-term recipients and 35/40 per cent for long-term recipients,¹⁶ and SWA adult rates rose by 44 per cent in real terms. Thus the divergence in rates across schemes has narrowed very considerably. The very substantial increase in what were the lower-paid schemes in real terms has been enough to bring them up to the CSW priority rate indexed to inflation.

It has also brought rates a good deal closer to adequacy benchmarks indexed to average earnings rather than prices. As we have seen, the net figure corresponding to average gross industrial earnings rose by 68 per cent in nominal terms between 1985 and 1996, while prices rose by 36 per cent, implying a real increase of 23.5 per cent. This quite rapid rise in real net earnings has been substantially exceeded by the rate of increase implemented for the lowest-paying schemes, of 44 per cent. The result is that, whereas in 1985 the SWA personal rate was 55 per cent of the adequacy estimate produced by the CSW's average industrial earnings method, in 1996 the SWA rate was 65 per cent of that estimate. (That method produces the highest adequacy estimate for 1996 of any of those implemented, so the point being made here relates not to the level of SWA versus the adequacy estimates, but the fact that the former has risen a good deal more rapidly than the latter over the 1985-96 period.) Support rates for the elderly, on the other hand, have lagged significantly behind real net earnings. Growth in average net equivalent household income has however been rather slower than growth in earnings, so support rates for the elderly have not lagged far behind that overall average.

5.6 Social Welfare Payment Rates and Implicit Equivalence Scales

In addition to giving priority to increasing what were the lowest payment rates in 1985, the most substantial increases in rates since then have been for the case on which the CSW concentrated, namely a single adult. Increases for child and more particularly for adult dependants have been lower, with the result that the equivalence scales implicit in social welfare rates at present are rather different to those in 1985. Table 5.5 shows that, taking the rate for a single adult as 1, UA and SWA paid an extra 72 or 73 per cent of that rate for an adult dependant. UB, which had a significantly higher rate for a single adult than UA or SWA at the time, paid considerably less extra for an adult dependant in proportionate terms, at 64 per cent of the single adult rate. By 1996, however, UB and long-term UA were paying only 60 per cent extra for an adult dependant, while SWA was down to 62 per cent extra. This is in keeping with the CSW's recommendation that a couple

¹⁶ The lower figure is based on a comparison of the urban UA rate in 1985 with the 1996 rate while the higher one compares the rural rate in 1985 – subsequently abolished – with 1996.

should receive 60 per cent more than a single adult. That recommendation was not itself supported by an in-depth examination of the issue on the part of the Commission: the report simply states that

If the basic payment for a single person is 1 then the appropriate scale is 0.6 for the related adult. The 0.6 is the standard measure referred to in the literature on adult equivalence scales (p. 196).

A wide range of values is in fact found in the literature and in social security rates internationally, though the 0.6 value is most commonly used in the UK. Since the CSW reported, no research on the needs of couples versus single adults specific to the Irish context has become available.

Table 5.5: *Equivalence Scales Implicit in Social Welfare Rates, 1985 and 1996*

1985	<i>Proportion of Single Adult Payment Rate</i>				
	<i>Extra Adult</i>	<i>First Child*</i>	<i>Second Child*</i>	<i>Third Child*</i>	<i>Average for Child 1-3*</i>
Unemployment Benefit	0.64	0.31	0.34	0.29	0.31
Unemployment Assistance (long-term)	0.72	0.33	0.36	0.3	0.33
Unemployment Assistance (short-term)/ Supplementary Welfare Allowance	0.73	0.34	0.38	0.32	0.35
1996					
Unemployment Benefit	0.6	0.3	0.3	0.32	0.31
Unemployment Assistance (long-term)	0.6	0.3	0.3	0.32	0.31
Unemployment Assistance (short-term)/ Supplementary Welfare Allowance	0.62	0.31	0.31	0.33	0.32

* Includes Children's Allowance/Child Benefit.

As far as children are concerned, the changes since the CSW in the equivalence scales implicit in the structure of rates have been less substantial. There has however been a concerted policy of implementing the Commission recommendation to reduce the variety of different rates for dependent children which operated in the mid-1980s: rates then differed not only by scheme but by number of children, the highest rate being paid for the second child. Table 5.5 shows, as a proportion of the rate for a single adult, the total support paid for each of the first three children by UB, long-term UA and short-term UA/SWA plus in each case the weekly value of monthly Children's Allowance (as it then was).

Relative to the rate for a single adult, the additional payment for a child ranged between 38 per cent and 29 per cent of the single adult rate. By 1996, this variation had been eliminated almost entirely, with the rate for each dependent child irrespective of size of family being £13.20 across all these schemes.¹⁷ Child Benefit, as Children's Allowance has become, does retain some variation, however, with a higher rate being paid for the third and subsequent child than for the first two. The overall average rate of support for children is now about 31 or 32 per cent of the single adult rate, which represents a small reduction since 1985 in the case of UA and SWA.

As mentioned in Chapter 2 the CSW did not make an explicit recommendation about the appropriate relativities between social welfare rates for adults and children, in the absence of Irish research on equivalence scales. However, the Commission did talk in terms of rationalising child dependant additions (CDAs) on a neutral cost basis to £10 per week in 1985 terms (p. 202), and maintaining or improving children's allowance/Child Benefit. In 1985 the latter, universal, payment was £15.05 per month or about £3.50 per week per child. Adding that amount to a £10 CDA, total support per child relying on social welfare would then be £13.50 per week, 27 per cent of the £50 bottom of the Commission's recommended range of £50-60 for a single adult. The current implicit equivalence scale for children could therefore be regarded as, if anything, generous relative to that envisaged by the CSW, though it must be emphasised that their main recommendation in this context was that research be carried out on equivalence scales for children in an Irish setting.

As described in Chapters 3 and 4, research on the cost of children in Ireland has been carried out by Conniffe and Keogh (1988) using Household Budget Survey expenditure data and by Carney *et al.* (1994) using the budget standard methodology. These studies provide valuable insights into the expenditure patterns and costs associated with children, including the variation in child costs by age which the Commission itself in fact emphasised. However, because they each produce estimates of the costs of children in absolute terms, their results cannot readily be converted into the form we have been discussing here, where child costs are expressed as a proportion of those for an adult, since the proportion they make up will then depend crucially on the value chosen for the single adult as a point of comparison. The use of absolute versus proportional scales is discussed in depth in Nolan and Farrell (Chapter 5), and that discussion will not be repeated here. For present purposes it suffices to note that the equivalence scales for children currently incorporated in Irish social welfare rates are not out of line with those in

¹⁷ Higher rates than this are however now paid with Widow's and Widower's Pensions, Deserted Wife's Benefit and Allowance, and Lone Parent's Allowance.

operation in the UK, and that strong Irish evidence in favour of an alternative has not yet been produced.

5.7 Adequacy and Additional Payments/Non-Cash Benefits

In assessing the adequacy of the basic rate of cash transfers, one must take into account the availability of other forms of assistance to recipients, either in the form of additional cash payments or non-cash benefits. The CSW, in discussing the adequacy of the rates being paid in 1985, noted that the important additional payments at the time – pay-related benefit and living alone allowance – and non-cash benefits such as free electricity, fuel and travel make continuing additions to the incomes and living standards of some recipients (p. 191). The main extra benefits currently in place are summarised in Table 5.6.

Curiously, the Commission did not mention the value of entitlement to a medical card, which constitutes a significant non-cash benefit for those relying on social welfare. This may be because it is not tied to social welfare receipt, being available to other low-income households. However, it is relevant in the context of adequacy benchmarks derived from average earnings or average household equivalent income, since earners/households at those averages will not be entitled to a medical card but those relying on social welfare will. It is not easy to give a value for medical card entitlement since the amount a particular individual saves will depend on the extent to which they utilise the health services in a given year. Various methodologies have been implemented elsewhere to value such benefits (see Callan, Nolan *et al.*, 1989, Ch. 9 for a discussion), but these face particular problems in the area of health care. In the illustrative figures on replacement rates regularly prepared by the Department of Finance a figure of about £100 per person per annum is currently employed, estimated on the basis of the average cost of providing GMS services. Since those with a medical card are also exempt from certain charges for hospital care the value to those covered may be slightly higher, but a figure of £2 per week would probably not be misleading in terms of order of magnitude.

Apart from medical card entitlement, the major *non-cash* benefits currently available to some social welfare recipients as shown in Table 5.6 are free travel, free television licence, school meals and butter vouchers. Free travel is available to all those aged 66 years or over, whether in receipt of social welfare or not, and also to those under 66 and in receipt of Invalidity or Blind Person's Pension or DPMA.¹⁸ It is therefore mainly relevant to assessing the adequacy of these payments or OAP, and it is difficult to place a value on this entitlement since again it varies greatly depending on use. It is possible however to calculate the average

¹⁸ Widows/widowers aged 60-65 whose spouses held a free travel pass may also qualify if receiving certain social welfare payments.

Table 5.6: *Extra Benefits Available to Some Social Welfare Recipients, 1996*

<i>Benefit</i>	<i>Value £ Per Week to Those Receiving</i>	<i>Groups Eligible for Benefit</i>		
		<i>Elderly</i>	<i>Non-elderly Long-term</i>	<i>Non-elderly Short-term</i>
Medical card	£2 per person	yes	yes	yes
Free travel	£1.27 per person	yes	no (except with disabilities)	no
School meals	na	na	some	some
Back-to-school allowance	£0.83/£1.12 per child	na	if below specified income limit	
Butter vouchers	£0.12 per person	yes if on social assistance		
Fuel allowance	£2.50 per household	yes	yes	no
Electricity allowance*	£2.50 per household	yes	some	no
Free TV licence	£1 per household	yes	some	no
Telephone rental allowance	£2.83 per household	yes	some	no
Rent/Mortgage Supplement	£12.50 per household on average	some	some	some
Local Authority Differential Rents	£7.50 per household on average	some	some	some
Exceptional Needs Payments	na	some	some	some

* Natural gas or bottled gas allowances available as an alternative.

cost to the state of providing the benefit per beneficiary. In 1995 the cost to the state was £31 million and there were 474,132 individuals for whom free travel passes had been issued, so the average expenditure per beneficiary was £66 per year or £1.27 per week. Entitlement to a free television licence, in some cases black and white and in others colour, is linked to entitlement to cash fuel allowances (discussed below). A black and white licence currently costs £44 and a colour one £62, so the entitlement is worth about £1 per week. The provision of school meals to national school pupils deemed to need them varies greatly from area to area and cannot be readily valued. In 1995 total expenditure by the Department of Social Welfare on school meals was £733,000, but the number of beneficiaries is not published. People who receive social assistance payments are entitled to butter vouchers, which are issued automatically to recipients and can be used towards the cost of butter. Claimants receive 2 per month plus 2 for each

dependant, each voucher being worth 52 pence, so the average value per week is about 12 pence per person.

As far as additional *cash* payments are concerned, we have already noted (in Table 5.3) the living alone and age allowances payable with some social welfare schemes and directed towards the elderly. As well as these, Table 5.6 shows that a fuel allowance is available to someone who is dependent on a long-term social welfare or health board payment and is "unable to provide for their own heating needs". The rate currently payable is £5 per week from mid-October to mid-April.¹⁹ Free Electricity Allowance is payable to those in receipt of Old Age, Retirement, Survivors, Widow's (Non-contributory) or Invalidity pensions, Lone Parent's Allowance, DPMA, living alone or with dependent spouse/children or carer. The allowance covers normal standing charges and 1,500 free units of electricity each year: rather than receiving a cash amount, the beneficiaries simply see the relevant amount deducted from their ESB bill. The total value of this allowance at present is £132.50 per year or an average of £2.55 per week.²⁰ Natural Gas Allowance is an alternative to the Electricity Allowance for people who are connected to a natural gas supply, and Bottled Gas Allowance is an alternative for those not connected to an electricity or natural gas supply but who would otherwise qualify. Telephone Rental Allowance is available to the same group of recipients who qualify for Electricity Allowance, and covers the normal rental charges and 20 free call units in each two-month billing period – again the amount is paid directly by the Department of Social Welfare to Telecom and the beneficiary simply sees a credit on their bill. At current charges this is worth £147 per annum or £2.83 per week to beneficiaries.²¹ The back to school clothing and footwear allowance (of £55 per second-level pupil and £40 per primary-level pupil) is payable to families below specified income limits each year. Finally, exceptional needs payments are made to people on social welfare or health board payments on a once-off basis, to help with once-off payments for items such as furniture and household equipment: the average benefit per beneficiary over a year is not available.

As well as these cash payments, substantial extra assistance is also received for housing costs by some social welfare recipients, either as a cash payment or in the form of reduced rents. A small number of tenants (about 800) affected by de-control of rents in the early 1980s receive Rent Allowance, to an amount which depends on means and on the gap between their old and new rent. Far more benefit from Supplementary Welfare Allowance Rent or Mortgage Supplements, and from

¹⁹ Those living in Dublin or Cork receiving fuel allowance, and certain others, are entitled to an extra £3 per week smokeless fuel allowance.

²⁰ The current standing charge is £20 per year and the rate per unit is 7.5 pence.

²¹ Telecom charges are currently £10 per month for the line, £1.10 per month for standard equipment, and 11.5 pence per call unit.

the fact that local authority tenants are charged differential rents, depending on their incomes. About 80,000 households currently benefit from SWA Rent and Mortgage Supplements, and the average amount per recipient is about £650 per year or £12.50 per week.²² As far as local authority differential rents are concerned the amounts involved vary greatly from area to area and household to household. About 92,000 households currently benefit and the average amount of the explicit subsidy (i.e., the amount by which rents of beneficiaries are below standard local authority rents) per beneficiary appears to be about £400 per annum or £7.50 per week. To the extent that local authority rents generally are below market rents, this may understate the true subsidy involved, but it is difficult to estimate the additional effective subsidy involved and to take into account that all local authority tenants share in that element of the benefit.

Since few of these additional benefits will be available to the earner on average earnings or the "typical" household on average (equivalent) income, and the amounts involved can be substantial relative to basic social welfare cash weekly payments, it is essential that they be taken into account in comparing adequacy estimates derived from average earnings or income and the support available to those depending on social welfare. This is difficult to do, however, because the descriptions of the schemes make clear that the groups benefiting vary across schemes and within those covered the benefit in some cases varies across households. Table 5.6 seeks to bring out that in broad terms the extra benefits are most significant for the elderly or those with disabilities, since they are targeted by free travel, free electricity and telephone, also benefit from fuel allowance and free TV licence, and are also likely to have a medical card. Leaving aside housing-related subsidies, the non-elderly receiving long-term social welfare payments are eligible for most of the extra benefits, though not free travel, but those on short-term payments are likely to benefit only from medical card entitlement. Given the complexities involved, we will simply illustrate the level which extra benefits might come to relative to basic cash payments for some hypothetical cases – an elderly couple, a family relying on UA, and a family relying on UB. First, though, the question of the appropriate treatment of housing-related payments has to be discussed.

Where social welfare recipients are receiving help with their rent or mortgage, either directly through Rent or Mortgage Supplement or indirectly through differential rents, this can add substantially to the basic cash payment a family is receiving. The average weekly benefit per beneficiary household for Rent/Mortgage Supplement is £12.50, but some of course receive considerably larger amounts. For those who benefit, the supplement is therefore significant

²² Since the supplement is not always received all year, the actual average weekly payment being received may be higher.

relative to their weekly cash support levels, which might be about £130-£140 for a family on UA. However, this assistance with rent or mortgage is intended to ensure that income after payment of housing costs is not less than the cash SWA rate less a specified amount. Thus, the explicit intention is to bring those who receive these supplements, who have exceptional housing costs, in line with other social welfare recipients in terms of income after housing costs: it would not be valid to simply add the average supplement to the basic cash payment to measure their living standards. On the other hand, if we are comparing social welfare recipients with households on average income, some of the latter will also have exceptionally high housing costs with which they are not receiving assistance.

Turning to local authority differential rents, the numbers involved and the average amount of benefit are again substantial, and in that case the relationship between the level of housing costs and the size of the benefit it is not as clear. The argument for adding that benefit to cash payments in making a comparison between beneficiaries and households on average income may therefore be stronger than in the case of rent/mortgage supplement. This is what we shall do in one of our illustrative cases, but is still unsatisfactory. The extent of variation in housing costs across parts of the country and across households on similar income levels is such that a more satisfactory approach would be to treat housing costs separately, and then focus on the adequacy of social welfare excluding the element going on housing in covering non-housing costs. (Although this distinction was not incorporated in the CSW's methods of deriving an adequate income, it would be consistent with the Commission's recommendation that a separate Housing Benefit be set up to cover housing costs.) An in-depth analysis of housing expenditures at household level, beyond the scope of this study, would be required to implement this approach, so we fall back on a simple example using the average saving to local authority tenants on differential rents.

In Table 5.7 we therefore show the value which extra benefits might have for three illustrative cases: a couple on non-contributory Old Age Pension, a couple with four children on long-term Unemployment Assistance, and a couple with two children on Unemployment Benefit. All three have medical card cover, but otherwise there are important differences across the cases in the extra cash and non-cash benefits from which they will benefit. The pensioner couple benefit from free travel, butter vouchers, fuel and electricity allowance, TV licence and telephone rental; they are assumed not to be in reduced rent local authority housing. In that case the total estimated value of extra benefits would be about £16 per week, which if added to their basic OAP would bring their weekly "income" from £103 to £119. This would make a considerable difference when social security support is compared with the CSW's recommended rates. Indexed by the CPI up to 1996, the bottom of the Commission's recommended range for a couple

Table 5.7: *Illustrative Cases Including Extra Benefits Available to Social Welfare Recipients, 1996*

<i>Benefit Received</i>	<i>Illustrative Case</i>		
	<i>Elderly Couple on Non-contributory OAP (under 80)</i>	<i>Couple with 4 Children on Long-term UA</i>	<i>Couple with 2 Children on UB</i>
	<i>Value £ per week</i>		
Basic cash payment	103.00	155.80	129.40
Medical card	4.00	12.00	8.00
Free travel	2.54	-	-
School meals	-	-	-
Back-to-school allowance	-	3.90	1.95
Butter vouchers	0.24	0.72	-
Fuel allowance	2.50	2.50	-
Electricity allowance	2.50	2.50	-
Free TV licence	1.00	-	-
Telephone rental allowance	2.83	-	-
Local Authority Differential Rents	-	7.50	-
Total value of extra benefits	15.61	29.12	9.95
Basic + extra benefits	118.61	184.92	139.35
Extra as % of basic payment	15.16	18.69	7.69

was £108 and the top was £130 (Table 5.2). The inclusion of non-cash benefits therefore serves to bring the support received by the pensioner couple up from below the bottom of the recommended range to the middle of that range – though still below the figures which would be produced by most of the methods applied to benchmarks for the mid-1990s.

Before assigning too much weight to such a conclusion, it has to be noted that simply adding the value of the extra benefits to the basic payment in this way assumes implicitly that the elderly have the same needs as any other social welfare

recipients. In fact, however, some of these extra benefits are targeted at the elderly precisely because of the presumption that they have special needs, for example in terms of heating. The same point may be made about other groups depending on social welfare long-term, who receive extra cash and non-cash support because they are thought to have needs which are not fully taken into account in the basic rate. As against that, the household on average income being used as one standard of comparison in assessing adequacy has to meet all their needs out of that income.

Again this points one back towards the way in which the adequacy standards are derived. Ideally that exercise would incorporate differing needs for different contingencies, taking into account age, duration of dependence and special needs arising from location, illness, etc. A simple standard differentiating only by family size and composition is therefore an extremely crude one, and the results presented here have to be seen in that light.

With that caveat in mind, it is still of interest to compare the relative importance of extra benefits across our three illustrative cases. Table 5.7 shows that the couple with four children relying on long-term UA would receive a basic payment of £156 per week. In addition to the value of the medical card, they benefit from back-to-school allowance and butter vouchers and are assumed to benefit from fuel and electricity allowances. For the purpose of illustration we also assume that, unlike the other two cases, they are local authority tenants with reduced rent because of their income, worth the average figure already described of £7.50 per week. This brings the total estimated value of their extra benefits to £29 per week. By contrast, the table also shows that a couple on UB with two children and not benefiting from local authority differential rents would have total extra benefits of about £10, with £8 of that total coming from the assumed value of medical card cover and the remainder from the back-to-school allowance. Whereas the extra benefits constitute 15 per cent of the basic income support received by the pensioner couple and 19 per cent for the family on long-term UA, then, the corresponding figure for the family on UB is 8 per cent.

The additions to the basic payments discussed in this section are now a good deal more important than they were in the mid-1980s, and this extension clearly needs to be taken into account in assessing the evolution of income support rates since the CSW reported. However, entitlements to these extra benefits vary a great deal by scheme and across households in different circumstances, and assigning them a value is in some cases problematic, particularly for housing. In examining the impact of alternative social welfare policy options on poverty and on work incentives in the next two chapters we do not therefore attempt to incorporate these extra benefits, confining attention to the impact of changes in the basic weekly rates of payment. Given the manner in which they have grown in importance over the past decade, in our view the time is ripe for an in-depth examination of the

role of these additional benefits versus basic weekly payments and of the relative merits of cash versus non-cash provision.

5.8 Conclusions

This chapter first brought together the estimates of minimum adequate income levels produced by the various approaches described in Chapters 3 and 4. These produced 1996 figures for a single adult ranging from £68 to £96 per week – a considerably wider range than produced by the CSW for 1985. These were compared with the rates recommended as adequate by the CSW for 1985, updated in line with prices or alternatively in line with earnings. The range recommended by the CSW as minimally adequate for 1985 was £50-60, and uprated in line with price changes the corresponding figures for 1996 would be £68-81. Uprating the CSW's original range in line with net earnings in industry gives the much higher figures of £84-100, reflecting the growth in real take-home pay seen over the period.

The various up-to-date estimates of what would be adequate, and the CSW's uprated recommendations, were then compared with current social welfare rates. The basic rates of payment for a single adult under the different schemes are now in the range £62.40-75. Even the lowest rate, paid by short-term UA and SWA, has reached the CSW's priority rate uprated in line with prices. However these, and the £64.50 paid by UB/DB, are still below the bottom of the CSW's recommended range uprated in line with prices. Contributory Old Age and Widow's/Widower's pensions now pay above that uprated CSW figure, and so do non-contributory Old Age and Widow's/Widower's pensions if one includes the £6 living alone allowance.

Most of the estimates of what constitutes an adequate income for a single person produced by the various methods discussed in Chapter 4 are well above the bottom of the CSW recommended range up-rated by prices, all but one being £75 per week or more. Most current social welfare personal rates lie well below that figure, the only exceptions being contributory Old Age Pension and Invalidity Pension. (For someone aged 80 or over, Widow's/Widower's Pension and Deserted Wife's Benefit are close to that level.) On the other hand the outlier among the adequacy estimates was that based on 50 per cent of average net equivalent household income, which was actually the same as the bottom of the updated CSW range – at £68 per week – so current UB/DB/long-term UA rates are not far short of that figure.

It is also important to emphasise how far the social welfare rates being paid in 1985 fell below the bottom of the range the CSW then recommended. Only contributory OAP reached the bottom of that range, non-contributory pension for a single adult was 88 per cent of the bottom, UB/DB were about 80 per cent, long-term UA was 70 per cent, and the lowest rates then payable, for short-term

UA and SWA, were only 64 per cent. Considerable convergence in rates has taken place since then. Increases in social welfare since 1986 have given priority to bringing up what were then the lowest rates of payment. Single adults on contributory or non-contributory old age pension have seen their rates rise by about 7 per cent in real terms, UB and DB rates rose by 20 per cent, but the increases in UA and SWA have been between 35 per cent and 44 per cent. This has brought the lowest rates a good deal closer not only to adequacy benchmarks indexed to prices but, for the lowest paying schemes, also to those indexed to average net earnings. Average net industrial earnings rose by 23 per cent in real terms, but this quite rapid rise was substantially exceeded by the rate of increase implemented for the lowest-paying schemes. Support rates for the elderly, on the other hand, have lagged significantly behind real net earnings. Growth in average net equivalent household income has however been rather slower than growth in earnings, so support rates for the elderly have not lagged so far behind that overall average.

In addition to giving priority to increasing what were the lowest payment rates in 1985, the most substantial increases in rates since then have been for the single adult case on which the CSW concentrated. Increases for child and more particularly for adult dependants have been lower, with the result that the equivalence scales implicit in social welfare schemes now look rather different to 1985. For UA and SWA, the extra payment for an adult dependant in 1985 came to about 72 per cent of the rate for a single adult, whereas by 1996 that figure was down to 60-62 per cent. The latter is in line with the relativity recommended by the CSW, but that recommendation was not based on an in-depth examination of the issue. A marginal decline in the payment for children (including Child Benefit) relative to the personal rate has also been seen.

In assessing the adequacy of the basic rate of cash transfers, other forms of assistance available to recipients either in the form of additional cash payments or non-cash benefits also have to be taken into account. Such additional cash and non-cash benefits have increased in importance since the CSW reported. The various benefits involved and the types of recipient entitled to receive them was set out, and an attempt was made to assign each a value. The most important were seen to be entitlement to medical card cover, assistance with heating and energy costs, and direct or indirect housing subsidies. These extra benefits are most important for the elderly and long-term social welfare recipients. Some illustrative examples showed that extra benefits could add as much as 20 per cent to the value of basic cash support. This could clearly make a considerable difference in the assessment of the overall value of support *vis-à-vis* adequacy benchmarks derived from, average income, for example. However, entitlements to these extra benefits vary a great deal by scheme and across households in different circumstances,

assigning them a value is in some cases problematic, particularly for housing, and simply adding an average estimated value for these benefits to the basic payment rate is not particularly meaningful. The extended role of these benefits does clearly need to be taken into account in assessing the evolution of income support rates since the CSW reported, and ways of taking them fully into account in the derivation of adequacy standards need to be developed.

Chapter 6

ASSESSING THE DIRECT IMPACT ON POVERTY

6.1 Introduction

In this chapter and the next one, we explore the likely impact of an increase in social welfare payments to levels in the range identified in earlier chapters. This is a difficult and complex task. Changes in welfare rates, particularly those involving very substantial changes in relative terms, can have far-reaching implications not only for those dependent on welfare, but for the wider labour market and the economy in general. In order to explore these issues, we have broken down the task into five stages: costing the changes, financing issues, assessing the direct impact on poverty, assessing the impact on incentives, and assessing the wider labour market and economic implications. The first three stages are considered in this chapter, while the two later stages – which are central to the assessment of the overall impact – are explored in the next chapter.

In this chapter, we identify the approximate cost of the additional expenditure and, for reasons discussed later, construct a revenue-neutral package by raising the standard and top rates of income tax to generate the revenue to cover the increase in expenditure. Under the technical assumption that there are no behavioural responses to the changed incentives, we examine the direct impact of this revenue-neutral package on measures of poverty.²³ In particular, we consider by how much head count measures of poverty would fall if social welfare rates were increased. We also consider how much of the additional welfare expenditure would go towards reducing the extent by which families and households fall below the relevant income standard; and how much of this income shortfall would be reduced by the policy package. In the next chapter we explore the impact of the revenue-neutral policy packages on work incentives,

²³ In reality, one would expect some behavioural and labour market changes to occur in response to changes in social welfare and tax rates of the type considered here, but we abstract initially from such responses, returning to these issues in Chapter 7. It is not, at present, possible to perform an analysis of the type undertaken here incorporating such behavioural and labour market responses, but the possibilities of doing so in future are considered in Chapter 7.

which can be used to give some indication of the likely behavioural responses to the package.

We begin, in Section 6.2, with a discussion of the methodology employed in our analysis. Section 6.3 presents our cost estimates and the reasons for undertaking further analysis in the context of revenue-neutral packages. Section 6.4 shows the direct impacts of packages delivering alternative target rates in terms of head counts of poverty. Section 6.5 deals with the effectiveness and efficiency of the increased social welfare expenditure in reducing the aggregate income shortfall, relative to a number of different adequacy or poverty standards. The main findings and conclusions are drawn together in Section 6.6.

6.2 Methodology

In order to assess the likely impact of higher social welfare rates on the incidence of income poverty, we must be able to simulate the tax and benefit position of a representative sample of households. This is done using *SWITCH*, the ESRI tax-benefit model (a brief description of the model is given in the box; for more details see Callan, O'Donoghue and O'Neill, 1996). The dataset on which the model is based was gathered in 1987, but has been uprated to represent the situation in 1996. The uprating procedures capture some of the key changes in population characteristics between 1987 and 1994 (smaller family sizes, and registered unemployment)²⁴, as well as income growth and changes in tax and social welfare rates over full 1987 to 1996 period. This means that the social welfare and tax rates presented in the simulations can be compared with current rates.

In earlier chapters we have seen that the application of the methods used by the Commission on Social Welfare, and some additional methods, could yield a much wider range of values in 1996 terms than was the case in 1986. At the lower end of the scale, two methods – half of average income per adult equivalent and uprating of the CSW's minimum £50 per week figure in line with the CPI – produce figures of approximately £68 per week in 1996 terms. Two other methods suggest a figure of about £75 per week – coincidentally, about 55 per cent of mean income per adult equivalent. Uprating the CSW's topmost rate (£60 per week in 1986 terms) in line with the CPI yields a figure of £82 per week, which is close to the estimate produced by the 60 per cent relative poverty line. At the top end of the scale we find a number of methods produce figures of between £85 per week and £95 per week. We examine a package based around the £90 per week mark.

²⁴ In the time available it was not possible to extend the uprating of population characteristics to 1996, but changes in the past two years have been small compared to those over the 1987 to 1994 period.

These figures of £68, £75, £82 and £90 are chosen simply to represent the wide range of values which arise from the application of the different methods: they span that wide range in a convenient fashion, in steps of between £7 and £8. We refer to the £68 per week figure as the 50 per cent relative income line, and to the £82 figure as the 60 per cent relative income line, as these are commonly used in measurement of poverty elsewhere.

SWITCH, the ESRI tax-benefit model
Simulating Welfare and Income Tax Changes

Changes in the level and structure of taxes and benefits can have complex and far-reaching effects on the incomes and effective tax-cum-benefit withdrawal rates of different families. *SWITCH*, the ESRI tax-benefit model, simulates the amounts of social welfare entitlements, and the income tax and PRSI liabilities for a representative sample of households in order to capture the direct effects of social welfare and income tax changes. Details of the model's structure and operation are given in Callan, O'Donoghue and O'Neill (1996), Callan, O'Neill and O'Donoghue (1995) and Callan, O'Donoghue and O'Neill (1994). These studies show that the 1987 survey data on which the model is based have good coverage of the income tax base and the social welfare client population.

The model first estimates the social welfare entitlements and tax liabilities of each family in the nationally representative household survey under a baseline tax and social welfare policy regime – in the present study, this is given by the 1996/97 tax and social welfare regime. Then, the same calculations are undertaken for a policy reform – such as higher rates of social welfare, as explored in this study. This allows the gains and losses for each family in the sample to be identified. If a reform is to be self-financing, the gains and losses for individual families must balance out. The modelling process allows us to identify tax rates which ensure that the reforms are “revenue-neutral”; and gives us a picture of the overall effects of the reform on different types of family and at different points in the income distribution.

There is, of course, a margin of error attached to the estimates of expenditure and tax revenue from the model. The size and importance of this margin of error vary depending on the questions of interest. In the present context, it seems likely that the model-based estimates tend to overstate the tax rate increases required to finance higher social welfare payment rates. For this reason, we indicate a range of tax rate increases required to finance the packages modelled.

The Commission on Social Welfare favoured further Irish research on the issue of equivalence scales – a need met in part by the work of Conniffe and Keogh (1988). There was, however, an equivalence scale implicit in the Commission's recommendations, which favoured an adult dependant allowance

(ADA) of 60 per cent of the personal rate, and a minimum child dependant addition (CDA) of £10 per week, which, together with the rates of child benefit envisaged by the Commission,²⁵ implied an equivalence scale for children of between 23 per cent and 28 per cent – somewhat lower than the 33 per cent implicit in the combination of child benefit and the CDA rate for Unemployment Assistance current in 1986. The 60 per cent weighting for ADAs has, in effect, been implemented. Rates for children have also been streamlined, with the combination of child benefit and CDAs for most schemes now amounting to about 30 per cent of the payment rate for a single adult.

In setting an income adequacy target, the issue of what equivalence scale is to be chosen is, of course, an important one. But in the present context, our aim is to evaluate the impact of alternative income targets, with the key concern being the *level* of the income target. For this reason, we concentrate in our analysis on a single equivalence scale close to that implicit in the current system, i.e., 1 for the first adult in a family, 0.60 for an adult dependant, and 0.30 for dependent children.²⁶ Thus, in exploring the targets for revised and updated income adequacy targets, we have used these implicit weights.

In order to gauge the impact of a policy change, we consider the direct effects of the change on two key measures of poverty. The *head count* measure is the proportion of persons (adults and children) who fall below the relevant income standard. Here we focus on head count measures of poverty for persons, as the question of how many persons fall below a given income poverty line is of most fundamental interest; an added advantage is that this gives us comparable measures whether the analysis is based on incomes measured at household or at "family unit" level. The *aggregate poverty gap* is a money amount, the aggregate of the income shortfall for each person below the relevant income standard. For each of these measures, we consider the impact of the change in question (a rise in the basic payment rate to £68, £75, £82 or £90) against each of the income standards (the 50 per cent and 60 per cent relative income lines, represented by the £68 and £82 income standards, as well as the £75 and £90 income standards). In this way, we are able to consider the direct impact of policy on poverty as measured by the widely used 50 per cent and 60 per cent relative income poverty lines; and also to assess the direct impact of policy in achieving its more specific income maintenance goals, defined by the target social welfare rates themselves.

²⁵ The Commission on Social Welfare recommended certain real increases in Child Benefit, which, taken together with the £10 per week CDA, would have brought the total child payment to just under £14 per week. This would be about 28 per cent of a basic payment of £50 per week, but only 23 per cent of a payment rate of £60 per week.

²⁶ The same equivalences are used at household level, i.e., 1 for the first adult in a household, 0.6 for other adults and 0.3 for dependent children.

We consider analyses both at household level, and at a "family unit" or "tax unit" level which corresponds more closely to the way in which tax and social welfare policies operate: a "tax unit" is defined as a single person or married couple, together with dependent children – aged under 15, or in full-time education at any age. This definition of a child is somewhat different from that used in other poverty analyses, but corresponds quite closely with the definition of a "child dependant" in the social welfare system.

In order to assess the impact of a policy change the new or "reform" policy option must obviously be simulated; but the baseline situation must also be simulated. Table 6.1 compares head count measures of poverty at household level based on 1994 survey data, using social welfare receipts and tax payments recorded in the survey, and estimates based on the uprated 1987 data, using simulated social welfare entitlements and income tax liabilities. In general, the (uprated) modelled results are about 5 to 6 percentage points lower than the results found in the 1994 Survey. Proportionately, this difference is most important at the lowest poverty line.

Table 6.1: *Model-based Estimates of Income Poverty Compared With 1994 Survey Results*

<i>Proportion of Mean Equivalent Income</i>	<i>Poverty Line (1994 values)</i>	<i>1994 Survey (Recorded Tax and Social Welfare)</i>	<i>1994 Estimates (Modelled Tax and Social Welfare)</i>
		%	%
40%	£52 per week	6.8	1.5
50%	£65 per week	20.9	15.9
60%	£78 per week	34.2	28.5

Notes: Proportion of persons living in households falling below relevant poverty line.

Three main factors contribute to the differences shown in the table. First, the estimates are based on entirely different datasets – the 1987 dataset, uprated to 1994 levels, as against the 1994 survey. Second, there are differences in the definition of "children" which could be of importance. The model-based estimates treat all those aged under 15, and all those in full-time education, as dependent children; the 1994 survey counts all those aged over 14, whether or not they are in full time education, as adults rather than children. Third, the model-based estimates use simulated social welfare entitlements and tax liabilities rather than those recorded in the survey. The contributions of these different factors could, in principle, be examined; but it is clear that the simulated baseline is close enough to the "actual" 1994 situation to allow a broad assessment of the impact of policy changes at the 50 per cent and 60 per cent relative income poverty lines. The model can be thought of as capturing at least

three-quarters of those below these income standards. But the model-based estimates of the numbers falling below the 40 per cent line are so low (capturing only 1 in 5 of those below the line) that analysis of impacts on poverty at that level could be misleading. Thus, we concentrate our model-based analysis on income standards which are at least as high as the 50 per cent relative income line.

6.3 Costing and Financing of Social Welfare Increases

There are, of course, many different ways of delivering and financing income supports at the adequacy standards derived in earlier chapters. For example, child income support is currently provided through a mix of child-dependant additions for welfare recipients, a smaller payment per child as a universal and untaxed child benefit, and targeted supports for low income earners with children. An increased payment could be provided through a similar structure, or could be introduced in conjunction with structural reforms such as a taxable child benefit. Reform of tax/transfer structures is, of course, an ongoing concern, but in what follows, we concentrate on packages which stay close to the current structures, in order to concentrate on issues concerning the level of social welfare payments and taxes.

The lowest income adequacy target we simulate is £68 per week for the personal rate, £40.80 for the ADA, and £20.40 for the combination of CDA and Child Benefit. The highest target is £90 per week for the personal rate, £54 per week for the ADA, and £27 for the combined CDA/Child Benefit rate. Two intermediate targets (of £75 and £82 per week for the personal rates, with appropriate adjustments to the ADA and CDA rates) are also examined.

The Family Income Supplement scheme (FIS) has aimed at ensuring that work is financially rewarding for individuals with children, who might otherwise see little or no financial reward from taking up or remaining in employment. In exploring the impact of higher social welfare rates for the main schemes (Unemployment, Old Age, Illness and so on) it seems appropriate to consider corresponding alterations to the income limits for FIS. The income limits have been changed so that a couple with children, currently qualifying for FIS, would see an increase in their FIS entitlement equal to the combined increase in the personal rate, ADA rate, and CDA rate for a family of the same size currently qualifying for Unemployment Assistance.

This total package of social welfare increases is then costed on the technical assumption of no behavioural change, which implies that employment and unemployment rates are unaffected. The social welfare costs are detailed for each of the income adequacy targets in Table 6.2. In addition, the table shows the extent of the tax cut which could be financed by this amount of revenue (or the extent of the tax increase required to raise this revenue). These tax rate

calculations are based on equal percentage point increases in the standard and top rates of income tax.²⁷ Other financing mechanisms are, of course, possible, but this simple one can be used to gain insights into the broad impact of such a package.

Table 6.2: *Costs of Alternative Social Welfare Payment Rates*

<i>Income Standard (per week)</i>	<i>Increase in Social Welfare Expenditure (per annum)</i>	<i>Tax rate increase/ tax cut forgone (percentage points)</i>
£68	£161m	1.3-1.5
£75	£528m	4.2-4.9
£82	£940m	7.5-8.6
£90	£1,396m	11.1-12.6

Note: Calculations include costs of increases in personal rates, adult dependant additions, child dependant additions and Family Income Supplement income limits (assuming full take-up). Tax rate calculations are based on equal percentage point changes in standard, top and marginal relief tax rates and on the technical assumption of no behavioural change.

A £68 per week income target requires an increase in social welfare expenditure (including corresponding FIS increases) of about £160m per annum. This amount of revenue could finance a cut of about 1.4 percentage points in each of the main income tax rates (standard, top rate and marginal relief rate) over the level that would obtain in the absence of such a social welfare increase. An additional £7 on the basic payment rate (with proportionate increases in ADAs and CDAs) leads to an additional cost of almost £370m. The additional cost for a further £7 (bringing the payment rate to £82) is over £400m per annum. The additional cost is lower for the rise from £68 to £75 than for the rise from £75 to £82, as some rates are already close to or above the £75 target, while very few are close to or above the £82 rate. A £90 per week target would require a very substantial increase in social welfare spending of close to £1,400m per annum – close to 40 per cent of existing spending. If revenue of this magnitude were required, tax rates would have to be about 11 or 12 percentage points higher than in the absence of such a social welfare increase. While we defer more detailed consideration of incentive effects to the next chapter, it is clear that income tax increases of this magnitude could be expected to have a substantial impact on behaviour, particularly in the labour market. Thus, the assumption implicit in the present chapter, of no behavioural response to the tax and social

²⁷ The marginal relief rate is also increased by the same amount: to do otherwise could lead to inconsistencies in the system.

welfare package must be treated as a technical one, rather than a prediction of what would actually happen.

It is worth clarifying at this point how these estimates of cost, and of tax rate increases or tax cuts forgone, should be related to longer-term discussions of budgetary strategy. In recent years, budget changes have seen real increases in social welfare, or tax cuts in real terms, costing in the region of £200m per annum on a full-year basis. The Expert Working Group on the Integration of the Tax and Welfare Systems (TWG) noted that, on reasonable assumptions regarding economic growth and the growth in other public expenditure, similar resources might be available in future years for improvements in the tax/transfer systems. A key concern expressed by the TWG, was that best use be made of such resources, with year-to-year budgetary choices being made in the context of a coherent medium-term strategy. For this reason, the TWG considered a "resource envelope" of about £1,000m over a five-year period, in assessing alternative packages designed to improve work incentives. This overall resource envelope is very relevant to any discussion of real increases in social welfare payment rates, including increases towards any of the adequacy standards summarised in the previous chapter.

It is important to recognise, however, that economic growth is the driving force giving rise to increased resources for the tax/transfer system. It is growth in incomes from market sources which would give rise to increased tax yields at fixed rates, and would therefore permit tax cuts and/or welfare increases. But this growth in individuals' and households' incomes implies that adequacy standards based on a proportions of mean income (such as the average earnings, national accounts or relative poverty line approaches) would themselves be growing. Adequacy standards which are based on a relative concept are not fixed in real terms. They would advance at the same time, and for the same underlying reason, as the resources available to the tax/transfer system.

A more detailed consideration of the issues involved in uprating adequacy standards is deferred until Chapter 8. But the point that must be stressed is that if the adequacy standards identified here are thought of as fixed in relative terms, then they are best evaluated in terms of resources available in the current situation. Additional resources brought by economic growth can help in meeting standards which are fixed in real terms, but will be of much less benefit in meeting standards which are set in relative terms.²⁸

²⁸ There is some benefit from growth, even if the adequacy target is set in relative terms. Without growth, real and relative increases in social welfare rates can only be financed by higher effective tax rates. With growth, real or relative increases in social welfare rates could be financed by allowing the growth to generate higher tax revenues at fixed tax rates. For example, if allowances and bands were indexed to prices, while real earnings advanced, tax rates would be constant at the same real earnings levels, but

It is for this reason that our analysis focuses on packages which are "revenue-neutral" in terms of the direct tax/transfer system. Within this revenue-neutral framework, increases in social welfare rates must be financed by higher tax rates. In practical terms, it may be more likely that real or relative increases in social welfare rates would be financed by allowing economic growth to generate higher tax revenues at fixed tax rates. The policy debate would then be about the way in which the fruits of economic growth are to be distributed. It may be useful to think in terms of a baseline scenario for 5 years hence: this might include indexation of benefits, tax allowances and tax bands with respect to earnings rather than prices. Policy options could then be measured against this baseline, as well as against the current situation. For example, achievement of an adequacy target expressed in relative terms might involve a *fall* in tax rates relative to the current situation, but a *rise* in tax rates relative to the baseline scenario of indexation to earnings. While this approach (a baseline scenario of indexation to earnings for 5 years hence, with other policy options expressed as variations from this scenario as well as compared with the current situation) has many attractions, it is complex to construct and to interpret – disadvantages which, given the time constraints, have ruled out its application to the questions at hand. The simpler "revenue-neutral" procedures adopted here can capture most of what the more complex analysis would show. The "revenue-neutral" analyses can be interpreted as showing the impacts – direct impacts on poverty measures, and impacts on work incentives – of aiming for alternative adequacy standards, relative to a scenario in which the resources required are applied instead to cutting income taxes.

6.4 Impact on Head Counts of Poverty

We consider the effects of implementing the alternative adequacy standards in terms of their direct impacts on the numbers below these targets themselves. (These are shown in the diagonal boxes in Table 6.3).

When analysis is undertaken at tax unit level, about 23 per cent of persons are found to have incomes below the £68 per week standard in 1996. An increase in the minimum social welfare payment rate to £68 per week would, under the assumption of no behavioural change, reduce this proportion by about three-quarters, to under 6 per cent. About 30 per cent fall below the £75 income standard. Once again, the direct impact of an increase in the payment rate to this £75 level would be a reduction of about three-quarters in this proportion. The direct impacts of packages involving higher rates are somewhat attenuated, as the negative impacts of tax increases on taxpayers initially above the relevant income standards come into play. At the £82 income standard about 35 per cent of persons are initially below the standard; a package involving a payment rate

growth in real earnings would generate increased revenue.

of £82 reduces this figure by just over two-thirds. Almost 42 per cent of the population fall below the £90 per week income standard. An increase in the social welfare payment rate to that level would reduce that proportion by just under two-thirds, to about 16 per cent.

Table 6.3: *Estimated Impact of Higher Social Welfare Rates on Head Counts of Poverty: Tax Unit Level Analysis*

<i>Adequacy Standard</i>	<i>Baseline 1996</i>	<i>With £68 Payment</i>	<i>With £75 Payment</i>	<i>With £82 Payment</i>	<i>With £90 Payment</i>
£68	23.0	5.6	4.2	3.5	2.8
£75	29.7	28.7	7.7	4.6	4.0
£82	34.7	33.7	30.9	11.0	5.7
£90	41.6	38.9	36.2	34.1	13.5

Notes: Equivalence scale: 1 for first adult in tax unit, 0.6 for second adult, 0.3 for dependent children.

Table 6.4 shows the results of the corresponding analysis conducted at household level. Initial rates of poverty are lower than for the tax unit analysis, as, on balance, the implicit assumption of sharing of resources between tax units within a household tends to bring more people above these income standards. The direct impacts of payment rates on head counts of those falling below the relevant income standard are also greater. Head counts of poverty measured in this way fall by between 75 and 80 per cent of their original values. Typically, at both household and tax unit levels, an increased payment has little impact on the head count of poverty measured by a higher income standard; and increases in payment rates beyond the standard have relatively small further impacts on this measure of poverty. This reflects in large measure the nature of the head count measure of poverty, which focuses solely on income changes which involve a movement from below the poverty line to above it (or vice versa). Later analyses focusing on the aggregate poverty gap (or income shortfall relative to the income standard) move beyond this narrow focus.

In the next section we will consider the impacts on the aggregate poverty gap, which allow a more precise quantification of the effectiveness and efficiency of the alternative policy packages in their direct impacts on poverty.

Table 6.4: *Estimated Impact of Higher Social Welfare Rates on Head Counts of Poverty: Household Level Analysis*

<i>Adequacy Standard</i>	<i>Baseline 1996</i>	<i>With £68 Payment</i>	<i>With £75 Payment</i>	<i>With £82 Payment</i>	<i>With £90 Payment</i>
£68	12.5	2.4	1.2	1.0	0.4
£75	17.1	15.7	3.3	1.6	1.2
£82	22.7	20.8	17.0	5.3	2.2
£90	29.9	27.3	23.1	19.4	7.5

Notes: Equivalence scale: 1 for first adult in tax unit, 0.6 for second adult, 0.3 for dependent children.

6.5 *Impact on Aggregate Poverty Gap*

How effective are the social welfare increases under consideration in reducing the aggregate poverty gap? And how much of the increase in social welfare spending goes towards reduction of the aggregate poverty gap? These are the questions to which we now turn. The answers, of course, depend on the precise poverty line cut-off which is used. For this reason, we examine the impact of the alternative social welfare packages at a range of income standards.

First, we define the measures used in answering these questions more precisely. The concepts of marginal poverty reduction effectiveness and marginal poverty reduction efficiency are defined as follows:

$$\text{Effectiveness} = 100 \times \frac{\text{BaselinePovertyGap} - \text{ReformPovertyGap}}{\text{BaselinePovertyGap}}$$

$$\text{Efficiency} = 100 \times \frac{\text{BaselinePovertyGap} - \text{ReformPovertyGap}}{\text{IncreaseInSocialWelfareExpenditure}}$$

The effectiveness construct measures the extent of the reduction in the aggregate poverty gap (the sum of the income shortfalls of all those below the income poverty line) as a proportion of the initial poverty gap, in order to answer the question "by how much has a policy change reduced poverty?". The efficiency construct has a different focus. It measures the reduction in the poverty gap as a proportion of the increase in social welfare expenditure. Some of the increased expenditure goes to individuals initially below the poverty line or adequacy standard and helps to bring their incomes up towards that standard. It is this expenditure which is regarded as being "on target". If the payment increase brings an individual's income from below the poverty line to a level above the poverty line, that part of the increase which raises income above the poverty line or adequacy standard is regarded as an inefficient "spillover" in the

Beckerman (1979) framework. Also regarded as inefficient is any increased payment going to individuals whose incomes were already above the relevant income standard. Tax increases associated with higher welfare payments may also reduce the "target efficiency" of the package.

These measures can be seen as an adaptation of Beckerman's (1979) concepts of the poverty reduction effectiveness and poverty reduction efficiency of social security expenditures to a consideration of changes at the margin. An earlier application of this approach for Ireland can be seen in Callan and Nolan (1992); but we are not aware of any corresponding results for other countries.

Table 6.5: *Estimated (Marginal) Poverty Reduction Efficiency of Higher Social Welfare Rates: Tax Unit Level Analysis*

Adequacy Standard	With £68 Payment	With £75 Payment	With £82 Payment	With £90 Payment
£68	47	20	13	9
£75	65	55	33	24
£82	71	67	56	40
£90	80	73	66	58

Notes: Equivalence scale: 1 for first adult in tax unit, 0.6 for second adult, 0.3 for dependent children.

Table 6.6: *Estimated (Marginal) Poverty Reduction Effectiveness of Higher Social Welfare Rates: Tax Unit Level Analysis*

Adequacy Standard	With £68 Payment	With £75 Payment	With £82 Payment	With £90 Payment
£68	25	35	41	47
£75	19	54	60	64
£82	13	42	65	70
£90	10	32	52	70

Notes: Equivalence scale: 1 for first adult in tax unit, 0.6 for second adult, 0.3 for dependent children.

The results are presented in Table 6.5 (marginal poverty reduction efficiency) and Table 6.6 (marginal poverty reduction effectiveness). Looking first at the results on the target efficiency of the payments, we see that at any given standard – for example, the £82 per week figure – the lowest of the payment levels is the most efficient. While 71 per cent of the £68 payment would go towards those with incomes which remained below the £82 standard, only 40 per cent of the highest, £90 per week payment would reduce the income

shortfall in this way. This result is unsurprising: the £90 payment rate is itself above the £82 standard. An alternative perspective is to examine the efficiency of the expenditure in terms of the implicit target i.e., to treat the target payment as defining the poverty line and poverty gap. Evaluating each payment against its *own* adequacy standard, we find that the three higher payments are about equally efficient, with 55 to 58 per cent of the expenditure being "on target"; for the £68 payment, the efficiency measure is somewhat lower, at 47 per cent.

The results on effectiveness show some interesting differences depending on the level of the adequacy standard. At the £82 line, we find that an increase in payments from the 1996 levels to £68 per week reduces the initial poverty gap by about 13 per cent. An increase of a further £7 per week reduces the gap by another 30 percentage points, with a further increase of £7 (bringing the payment up to the adequacy standard of £82) reducing the gap by a further 23 percentage points. But an increase of £8 beyond the adequacy standard (to the £90 per week level) has a much more limited impact – a further reduction by about 5 percentage points.

At the £68 per week income standard, the pattern is quite different. The increase in payment to £68 per week reduces the initial gap by 25 per cent. A further increase of £7 per week leads to a reduction by an additional 10 percentage points in this case. Further increases of £7 and £8 per week (to the £82 and £90 per week levels) yield reductions of about 6 percentage points in the initial income shortfall in each case.

An alternative perspective is to look at the effectiveness of the alternative payment rates in terms of meeting the adequacy standards they represent. Here again we find a distinct difference between the lowest of the payment rates considered, and the others. The effectiveness of the payments in reaching the "own standard" ranges from 54 per cent to 70 per cent for the three higher rates (£75, £82 and £90 per week), but is only 25 per cent in the case of the £68 per week standard.

Many social welfare rates are already close to the £68 per week level. What the present analysis suggests is that a good deal of the aggregate gap between existing incomes and an adequacy standard of £68 per week cannot be reduced simply by increasing social welfare payment rates to that level. This may be because the persons below this income level are not in receipt of social welfare – for example, some self-employed would fall into this category – or because they would not receive the full rates of payment – for example, those young people living in the parental home, whose social welfare payments may be restricted due to their parent's incomes. But at higher adequacy standards, the potential scope for welfare payments to bridge the gap – *before any account is taken of labour market responses* – is greater.

While tax and social welfare policy operates, in the main, at individual and family/tax unit level, poverty is often thought of and measured in terms of households. For this reason, we have also conducted an analysis of marginal poverty reduction effectiveness and efficiency at household level (Appendix 6.1). We find that the levels of efficiency are a good deal lower at household level – reflecting the fact that the social welfare system focuses mainly on the family and individual levels, rather than on household level. However, the level of poverty reduction effectiveness is a good deal *higher* under household level analysis (reflecting the lower initial income shortfall at household level). The patterns of effectiveness and efficiency at household level and tax unit level are rather similar.

6.6 Conclusions

We have explored the potential impact of packages involving four different social welfare payment rates, ranging from £68 per week – the bottom of the range of adequacy targets found in earlier chapters – to £90 per week, close to the top of the range. The policy packages we examined include increases in FIS income limits, designed to maintain work incentives for families with low incomes relative to their needs. We found that the costs of payment rates at £68, £75, £82 and £90 per week were approximately £160m, £530m, £940m and £1,400m per annum. These sums equate to tax cuts forgone or tax rate increases of about 1 percentage points, 4 to 5 percentage points, 8 percentage points and 11 or 12 percentage points respectively in all tax rates (standard rate, top rate and marginal relief rate). These calculations are based on a technical assumption that there would be no change in behaviour associated with the package. Possible impacts on incentives and behaviour will be considered in the next chapter, and should be borne in mind when interpreting the results from this chapter.

Within this framework of analysis, we find that for the £68 payment package, just under half of the additional social welfare expenditure would go towards reducing income shortfalls relative to that £68 target; and the package would close about one-quarter of the aggregate gap relative to that income standard. For the £75 per week package, about 55 per cent of the additional expenditure would go towards reducing the income shortfalls, and more than half of the initial income gap would be closed. At the highest standard considered (£90 per week), almost 60 per cent of the additional expenditure would be "on target" and about 70 per cent of the initial income shortfall would be reduced – again, on the technical assumption of no change in labour market or other behaviour.

Overall, the results indicate that increases in social welfare payments could, on the technical assumption of no change in behaviour, have a substantial impact on rates of income poverty – whether measured by the numbers falling below

income poverty lines, or income shortfalls relative to that line. But a substantial proportion of the additional expenditure does not go towards reduction of poverty at the relevant income standard; and some of the income shortfalls are not amenable to reduction through increases in welfare payments as some individuals may find themselves ineligible for any scheme (e.g., some farmers and low income self-employed). The factors underlying this are deserve further investigation at national level. International comparisons would also be helpful in understanding the practical bounds on poverty reduction effectiveness and efficiency of social security systems. Complete (100 per cent) effectiveness and efficiency would require not only that everyone below the line should receive a payment, but also the strictest of means tests (pound for pound withdrawal of benefit) at the target income standard; this in turn would have very serious implications for the effects on work incentives. The primary motivation for the analysis of effectiveness and efficiency is simply to assess the potential performance of the tax/transfer system in delivering alternative levels of income support. It is not centrally addressed to the question of determining what that level of support should be; but could be used to guide improvements in the delivery of a given level of support, in conjunction with analyses of incentives to which we now turn.

Appendix 6.1: Household Level Analysis of Marginal Poverty Reduction Effectiveness and Efficiency

The income tax and social welfare systems operate with a number of different units of assessment. For some purposes (e.g., qualification for some social insurance benefits) it is the individual's own circumstances (contribution record etc.) which are relevant. For others (e.g., amounts of many social insurance and social assistance benefits) it is family circumstances which matter. Household circumstances may also enter the reckoning in some instances (e.g., the "benefit and privilege" rules applying mainly to young single people living in the parental home). In measuring poverty or adequacy, there are arguments to be made in favour of different units of analysis. The tax unit or narrow family unit (individual or couple together with dependent children) has been the unit used within the present chapter. But there is also an argument that one should examine the effects of potential policy changes on poverty as measured at household level – the unit most commonly employed in studies of poverty.

The aggregate income shortfall measured at household level will be smaller than that at family unit level for two reasons. First, consider what happens when a household comprises two units, one of which has an income below the standard and one above. The average income may lie above or below the standard, so that the head count of poverty may rise or fall; but the total income shortfall must be reduced, as the income of the unit above the standard offsets at least some of the gap experienced by the other unit. Second, in performing this analysis we are operating not only with the same basic income standard, but with the same equivalence scale; the standard at household level is therefore lower, to the extent that some adults receive an implicit weighting which is lower in the household level analysis (the additional adult weighting being 0.6 of the first adult) than in the tax unit level analysis (where the first adult in each tax unit receives a weight of 1).

This lower income shortfall at a given income standard implies that for any given level of poverty reduction efficiency, the household level analysis will show higher effectiveness than the tax unit level analysis. (Mathematically, the measure of target effectiveness can be expressed simply as the target efficiency times the additional expenditure *as a proportion of initial poverty gap*). In our analysis the amount of additional expenditure depends only on the level of payment, and not on the level at which the analysis is conducted; but expenditure *scaled by the initial poverty gap* does, of course, depend on the level of the analysis, with poverty gaps tending to be smaller at the household level.

Of course, the level of efficiency will not tend to be the same for household and tax unit levels of analysis. The social welfare system operates mainly at

either individual or tax unit level, with household elements of means-testing forming a much more limited part of the system. This being so, one would expect that efficiency levels at any given standard will be lower in household based analysis. Effectiveness may, however, be either higher or lower, since it is the product of two factors subject to opposing influences: efficiency is lower, but the lower initial income shortfall (or poverty gap) means that the amount of expenditure scaled by the income shortfall is higher. What our analysis can show is the extent to which efficiency is lower, and the net effect of this factor and of the lower initial income shortfalls on effectiveness.

Table 6.7: *Estimated (Marginal) Poverty Reduction Efficiency of Higher Social Welfare Rates: Household Level Analysis*

<i>Adequacy Standard</i>	<i>With £68 Payment</i>	<i>With £75 Payment</i>	<i>With £82 Payment</i>	<i>With £90 Payment</i>
£68	20	8	5	3
£75	33	26	16	11
£82	42	37	29	20
£90	55	47	40	34

Notes: Equivalence scale: 1 for first adult in tax unit, 0.6 for second adult, 0.3 for dependent children.

Table 6.8: *Estimated (Marginal) Poverty Reduction Effectiveness of Higher Social Welfare Rates: Household Level Analysis*

<i>Adequacy Standard</i>	<i>With £68 Payment</i>	<i>With £75 Payment</i>	<i>With £82 Payment</i>	<i>With £90 Payment</i>
£68	54	70	80	84
£75	30	81	87	91
£82	20	59	86	92
£90	16	45	68	88

Notes: Equivalence scale: 1 for first adult in tax unit, 0.6 for second adult, 0.3 for dependent children.

Tables 6.7 and 6.8 report the results of a household level analysis for efficiency and effectiveness respectively. As expected, levels of efficiency are lower under the household level analysis than for the tax unit level analysis – the extent of the difference varying between 24 and 29 percentage points for efficiency evaluated at the "own" standard (the diagonal boxes). Despite the fall in efficiency, the payments emerge as much more effective in reducing income shortfalls in this household level analysis (again, focusing on effectiveness in

meeting the adequacy standard implicit in the payment rate, as highlighted in the diagonal boxes). Effectiveness levels are between 18 and 29 percentage points *higher* than in the tax unit level analysis.

The patterns of efficiency and effectiveness remain similar to those in the tax unit level analysis, when we focus on results where the payment levels are evaluated in terms of their own adequacy yardstick (the diagonal boxes). Efficiency in terms of the own yardstick rises with the level of payment (while it must, necessarily, fall in terms of a fixed yardstick). Effectiveness is much greater for the three highest payment levels, ranging roughly between 80 and 90 per cent for the £75, £82 and £90 rates, while effectiveness is again a good deal lower for a payment rate set at the lowest of the adequacy standards (£68 per week).

Chapter 7

ASSESSING THE IMPACT ON WORK INCENTIVES

7.1 Introduction

We now turn to the impact of the packages described in the last chapter on work incentives. We begin by setting out in broad terms the nature of the trade-off between adequacy and work incentives (Section 7.2). The measures used to assess the impact on work incentives (described in Section 7.3) are informed by this discussion. In Sections 7.4 to 7.6, we present estimates of the impact on three key groups in turn. Sections 7.4 and 7.5 deal with the impact on work incentives facing the unemployed and those who are employees; while Section 7.6 is concerned with the impact on the incentive to take up paid employment facing those who describe themselves as engaged in home duties. Section 7.7 considers the overall impact on incentives and discusses the wider context of promoting employment opportunities and economic efficiency. The final section draws together the results and reconsiders the broader context of the trade-off between rates of income support and financial incentives to work.

For reasons discussed in the preceding chapter (Section 6.3), the analysis is conducted on a revenue-neutral basis. It is recognised that this is not, in fact, the context in which the adequacy standards identified earlier would be likely to be implemented: if social welfare payments were to be increased relative to average incomes, the change would be more likely to take place in a context of economic growth – a context in which the many adequacy standards based on average incomes would also be growing. But, as discussed in Section 6.3, the revenue-neutral analysis captures a key element of the trade-off between higher social welfare rates *relative to average incomes*, and the incentive to work. In the analyses conducted in this chapter, the tax rate increases assumed necessary to finance the packages are at the higher end of the ranges quoted in the previous chapter, i.e., 1.5 percentage points on all income tax rates for the lowest, £68 per week target and 12 percentage points for the highest, £90 per week target rate. Thus, the deterioration in incentives which would arise from the packages could be somewhat less than that shown here. On the other hand, the analysis is conducted on the basis of complete take-up of Family Income Supplement – a

factor tending to understate any deterioration in incentives. The offsetting nature of these influences should make the overall picture a reasonable representation of the association between higher payment rates and work incentives.

The way in which a given level of income support is financed and provided can, of course, make a significant difference to the effects on work incentives: some methods of providing a given level of support will be more damaging to work incentives, and others less so. In the packages analysed here any increase in social welfare payment rates would continue to be delivered and financed by unchanged structures. Thus, the analysis does not deal with restructuring of social welfare or taxes to minimise the damage to incentives, such as was considered by the Expert Group on the Integration of the Income Tax and Social Welfare Systems (1996). Improvements to the financing and delivery structures, designed to provide the required level of support with minimal damage to work incentives, should, of course, be sought – whatever the level of income support is to be. But when improvements in the financing and delivery systems have been exhausted, there remains a trade-off between the level of income supports provided and the strength of the financial incentive to work.²⁹ It is this form of trade-off which is the focus of the present chapter.

7.2 Adequacy and Work Incentives

A key concern in setting rates of social welfare payments is the impact they have on incentives to work, and on the wider labour market. Much of the discussion of these issues tends to focus on income maintenance payments for those who are unemployed, and the balance between in-work income and out-of-work income for this group. The issues involved are much broader. Other key groups who may be particularly responsive to changes in benefit rates, and associated changes in taxes, include those who are in the pre-retirement age groups, married women who are not engaged in paid employment, lone parents and potential migrants. There are, of course, some groups of welfare recipients for whom work incentive issues are of much less importance. Many pensioners and those who are ill or disabled are wholly dependent on a social welfare payment, and not in a position to supplement it with income from employment.³⁰ For simplicity, in our initial discussion of the nature of the relationship between income support levels and work incentives, we follow the usual practice in presenting the issues in the context of incentives affecting the balance between

²⁹ There are efficiency arguments for income support: the introduction of a scheme of income support for the unemployed may help to improve job search and allow better matching. In some circumstances, therefore, increases in the level of payment could improve the efficiency of the labour market.

³⁰ In some instances, the labour supply of a spouse or partner of an ill, disabled or elderly social welfare recipient may be affected by the level or structure of the payment.

employment and unemployment. Our focus is on the *financial* incentive to work, reflecting the fact that this study is designed to deal with issues concerning the level of social welfare payments. There are, of course, many other factors which enter into individuals' and families' decisions about work. OECD (1996) notes that many people would work even if they would get more money receiving benefits – perhaps because the job was seen as a first step towards higher earnings, for the social status of being employed, or for the individual's sense of self-worth. But financial incentives still matter, in a number of respects. Even if many people would seek work when the net reward to employment is small, more would seek work if the net reward (over and above the income available when unemployed or out of the labour market) is greater.

What are the mechanisms underlying between the trade-off between the level of income supports provided and the strength of the financial incentive to work? Simple economic models – which, as Atkinson and Micklewright (1991) point out, take little account of the details of benefit administration – suggest that unemployment benefits may create an option "an option of leisure and low income, which some people choose in preference to full-time work with a higher income" (OECD, 1994). But higher benefit levels may affect unemployment in several other ways, as the OECD study goes on to point out:

- higher benefits may tend to raise recipients' perceptions of the minimum acceptable wage (or "reservation wage"). Higher reservation wages may result in longer unemployment durations, which directly raise the level of unemployment, and have negative indirect effects (including greater skill losses and a greater risk of long-term unemployment)³¹;
- higher benefits may reduce the cost of becoming unemployed, leading those in employment to take greater risks – individually or collectively – in dispute or bargaining situations;
- higher benefits may lead to increased employment in risky or seasonal employments; a shift in the composition of employment towards these industries or occupations can also lead to higher unemployment.

It is clear that these mechanisms are potentially important. The precise extent of their importance is, however, an empirical question. The report of the Expert Working Group on the Integration of the Income Tax and Social Welfare Systems contains a review of much of the literature on the implications of work incentives for employment (Appendix 5 of *Integrating Tax and Social Welfare*).³² The evidence from international sources can best be described as

³¹ Again, the nature of benefit administration – and, in particular, the degree to which benefits are conditional on acceptance of job offers – can affect the extent to which benefit levels influence unemployment levels through this mechanism.

³² A part of this review deals with mechanisms such as those described above; here we focus on the review of the empirical evidence.

mixed. For example, the OECD's (1994) cross-country study concludes that high unemployment countries which significantly reduce work disincentives arising from benefit entitlements may experience a considerable improvement in their unemployment situation within a few years. On the other hand, Atkinson (1993) concludes that while studies of the UK, Germany, Sweden and Denmark have found evidence that benefits and the taxes needed to finance them have contributed to reductions in labour supply,

"the predominant impressions are

- (a) the small size of many (but not all) of these effects;
- (b) that it is the labour supply of women, particularly married women and lone mothers, which is more likely to be reduced, and
- (c) the lack of consensus about many aspects, and qualifications which surround many estimates of the magnitude of disincentives".

The mixed nature of the international results, their sensitivity to different specifications, and their dependence on the particular context makes it all the more important that empirical research on these issues be undertaken which addresses the specific Irish context – including Irish institutions, benefits, tax rates and structures. But the research base on these issues for Ireland is not at present sufficient to permit a quantification of the employment impact of complex changes such as are involved in providing and financing the social welfare payment packages under consideration here (an issue to which we will return in Section 7.7). Most of the Irish studies reviewed in *Integrating Tax and Social Welfare* are based on time-series evidence, and rely on very simple measures of policy – such as the average income tax rate, or what is termed a "replacement rate".³³

Measures of replacement rates constructed using time-series data on unemployment compensation per recipient, and net income per worker – as used in Browne and McGettigan (1993) – can diverge substantially over time from the behaviour of average replacement rates based on actual or hypothetical family circumstances. (Callan, Nolan and O'Donoghue, 1996 find that over the 1987 to 1994 period, the Browne-McGettigan measure fell by almost 6 percentage points, while the other measures rose by 1 percentage point). This could well distort estimates of the impact of changes in replacement rates on employment and unemployment.

While precise quantification of the impact of policy packages on employment and unemployment is not yet possible, we can provide information which helps to inform judgements on the likely impacts. In doing so, we draw on

³³ The replacement rate is the ratio of net income when out of work to net income when in work; for more details on the measurement of replacement rates at individual level, see Section 7.3.

some findings from the international literature on labour supply responses to changes in taxes and transfers. As noted earlier, results in such studies can vary across countries, and can be sensitive to changes in the specification of the model or the construction of the dataset used for estimation. A number of results, however, seem to be relatively robust, and are supported by a great many studies:

- Married women's labour market participation tends to be more responsive to economic incentives than that of married men or most single people.
- Greater than average responsiveness to financial incentives may also be found among lone parents (with child care costs as a central element of the financial calculations) and the pre-retirement age groups.
- Most of the potential response in total labour supply arises from decisions about whether or not to take up (or remain in) a job, rather than decisions about hours of work.³⁴ This would include decisions about part-time as well as full-time work.

These international findings suggest that particular attention should be paid to the measurement of incentives relevant to decisions about employment as against non-employment, including unemployment. As will be seen, the balance between income in and out of paid work is generally measured by replacement rates (or average tax rates). Marginal tax rates are more relevant for decisions about changes in hours, which may account for rather less of the potential labour supply response.

In the Irish context, two additional factors should also be taken into account in assessing possible responses to tax/transfer policy changes. The first is that, as pointed out in *Integrating Tax and Social Welfare*, "high [replacement rates] and tax rates can also have an impact on the choice between work in the formal economy or in the black economy". The recent CSO study of the Live Register and Labour Force Survey sheds some light on this issue. It reports that, after adjustments for sample design, non-response, and individuals not listed as resident at the address given on the Live Register, 11 per cent of those on the Live Register and usually resident at the addresses shown described themselves as engaged in full-time employment. Further analysis of the unique CSO dataset is needed to assess the extent to which this phenomenon represents a response to high replacement rates. Are those who are "working and claiming" facing high replacement rates? Or are other factors more important in explaining the extent of the phenomenon? Answers to these questions would help to assess the extent to which disimprovements in work incentives lead to a decline in the regular

³⁴ For example, a recent survey (Blundell, 1992) notes that "it is usually felt that the response to tax reductions in terms of working hours by prime-aged men is small and possibly negative, with working hours probably determined in some collective manner".

economy in favour of irregular activity.³⁵ The measures of incentives most relevant to the "working and claiming" phenomenon highlighted in reactions to the CSO study are those relating to the net reward from full-time work in the regular economy: precisely those used in the present study.

A further mechanism of potential importance in the Irish context is the response in terms of migration flows. As with employment decisions, financial incentives are only one element in the complex processes determining migration decisions. But tax and welfare changes can affect the level and composition of gross inflows and outflows. If rates of benefit and tax in Ireland are increased, then potential emigrants and return migrants may find Ireland less attractive if they are likely to be in employment, but more attractive if their risk of unemployment is high. This perspective suggests a need to monitor incentives beyond the national context, taking into account incomes when employed or unemployed in other relevant countries – with the UK being a prime example.

In the next section we outline the measures of work incentives which are applied in the present study. Sections 7.4 to 7.6 show the immediate impact of these payment packages on work incentives. In Section 7.7, we return to a discussion of the broader issues involved in the trade-offs between income support levels, employment and poverty, informed by the results on work incentives presented in the earlier sections.

7.3 Measures of Work Incentives

The discussion in the previous section emphasised that the potential labour supply response to tax/transfer policy changes arose mainly from decisions concerning participation in the paid labour market as against non-participation, or acceptance versus rejection of job offers. The measures of work incentives relevant to such decisions relate to the balance between family income when an individual is not in paid employment, and the income the family would have if the individual were employed full-time in the paid labour market.

For those who are not currently in employment (the unemployed and those in home duties) it is necessary to predict the wage that the individual would receive if in employment. While many analyses focus on jobs at the average industrial wage (or some fixed proportion of that wage), we use the detailed information available in the ESRI's 1987 dataset to predict the wage which each individual is likely to be able to command in the labour market. The predictive characteristics

³⁵ All tax and transfer systems need some controls and checks on compliance. The optimal degree of administrative effort may well vary with tax and benefit rates. For constant effort, rule-breaking behaviour is likely to rise the higher are effective tax rates and benefit withdrawal rates. A higher effort may therefore be worthwhile – but since enforcement of rule is costly, a system with higher effective taxes is still likely to end up with a more rule-breaking behaviour.

include educational qualifications and past labour market experience. The predictions are based on the wage equations estimated by Callan and Wren (1994), which distinguish between single and married men and women.³⁶ A key feature of the predictions is that time spent out of the labour market or unemployed tends to reduce the wage the individual can command. The average predicted wage for the unemployed is about two-thirds of the average industrial wage.

Given the predicted wage, family income when in employment can be simulated using the tax-benefit model. The balance between family income when the individual is in paid employment and that when the individual is unemployed or in home duties is then summarised by the *replacement rate*, i.e., the ratio of disposable family income when the individual is unemployed or in home duties, to the disposable income the family would have if the individual took up full-time paid employment. Policy changes which improve the net gain from taking up employment lead to a reduction in replacement rates; while policies which reduce the net gain from taking up employment lead to increases in replacement rates.

The replacement rates measure can also be applied to those who are already in employment. In their case, the gross income from employment is known, but the income they would receive if unemployed must be simulated. This is done by simulating the Long-Term Unemployment Assistance which the individual would receive, given his or her family situation, if he or she became unemployed.

The replacement rate measure used in this study can be thought of as concerned entirely with cash income. They do not take account of the non-cash benefits and additional payments discussed in Section 5.7. In particular, it should be noted that the financial balance between work and unemployment may be affected by considerations such as the potential loss of a medical card³⁷, the loss of rent/mortgage supplement or increased rent under a differential rent scheme operated by a local authority. Replacement rates which take account of the value of such secondary or non-cash benefits would tend to be higher. The focus here is on changes in replacement rates in response to changes in cash benefits and taxes, rather than changes in non-cash or secondary benefits. For this purpose, measures of cash replacement rates can be expected to give useful results.

³⁶ The unmeasured labour market characteristics of the unemployed and/or those not in the paid labour market may be inferior to those of labour market participants; the procedures adopted do not take account of this factor.

³⁷ Recent policy changes allowing the retention (for up to three years) of medical cards by long-term unemployed individuals taking up a job, are aimed at facilitating the transition to employment at a critical juncture.

Replacement rates are designed to give information on the incentives to take up or remain in a full-time job. *Marginal effective tax rates* are more relevant to decisions concerning hours of work and work effort e.g., decisions on whether or not to seek or accept overtime hours. This is principally of relevance to those who are in employment, and our analysis focuses on the impact of policy packages on the marginal tax rates of those in employment. The marginal effective tax rates measured here include the individual's marginal income tax rate (whether standard, top rate or marginal relief rate) as well as the rates of employee PRSI contributions and Levies. The benefit withdrawal rate for Family Income Supplement (FIS) is also included; but no other social welfare withdrawal provisions are included in the marginal effective tax rate measures.

Further details of the measures used in this analysis can be found in Callan, Nolan and O'Donoghue (1996).

7.4 Work Incentives for the Unemployed

Table 7.1 shows the estimated impact of the policy packages involving alternative rates of social welfare payment on replacement rates facing those who are unemployed and in receipt of Unemployment Benefit or Unemployment Assistance.

Table 7.1: *Estimated Impact of Alternative Social Welfare Payment Rates on the Distribution of Replacement Rates for the Unemployed*

<i>Replacement Rate Category</i>	<i>Baseline 1996</i>	<i>With £68 Payment</i>	<i>With £75 Payment</i>	<i>With £82 Payment</i>	<i>With £90 Payment</i>
0 <10	0	0	0	0	0
10 <20	1	1	0	0	0
20 <30	6	5	4	3	1
30 <40	12	11	7	4	3
40 <50	11	11	11	10	8
50 <60	15	13	11	11	11
60 <70	24	20	16	17	15
70 <80	24	30	38	36	29
80 <90	5	6	8	11	20
90 <100	2	3	6	7	9
>100	0	0	0	2	5
All	100	100	100	100	100

The results show a general upward shift in replacement rates for each of the policy packages of increased social welfare rates. In principle, a full-scale labour supply model could be estimated and simulated to assess the likely effects of this

change in work incentives,³⁸ but this would require a major programme of research. When, as is common in debates in other countries, such a model-based analysis is not possible, the debate tends to focus on the extent to which policy changes affect the incidence of "high" replacement rates – often those above 70 or 80 per cent. Implicit in this focus is the view that individuals with high replacement rates are those whose decisions are most likely to be strongly affected. The replacement rates calculated here are purely in terms of basic cash benefits, and do not take account of any secondary or non-cash benefits (such as medical cards, differential rent schemes, or rent/mortgage supplement under the Supplementary Welfare Allowance scheme). Inclusion of such secondary/non-cash benefits would tend to raise the replacement rates for many of the unemployed above the levels examined here.³⁹ For this reason we regard the 70 per cent level as a more appropriate cut-off in identifying the group facing high replacement rates.

Under the baseline 1996 policy, about 31 per cent of the unemployed have replacement rates above 70 per cent – a cut-off widely used to indicate a "high" replacement rate. Under the package involving a £68 payment rate, this proportion increases to 39 per cent of the unemployed. At a £75 payment rate, over half of the unemployed would face replacement rates above 70 per cent, with 56 per cent facing these rates at an £82 payment rate.

The effect is, not surprisingly, even more substantial when the payment rate is increased to £90. Under this policy about two-thirds of the unemployed face a replacement rate of over 70 per cent. The £90 payment rate is closest to the adequacy standard derived from the average industrial earnings method. It will be recalled (Chapter 3, Section 2), that this method involved taking half of the net income (after income tax, PRSI and levies) available to a single person with a job at the average industrial wage. The average wage that can be expected by those who are unemployed (on the basis of their qualifications and experience) is about two-thirds of the average wage, but with some individuals facing wages well below these levels. When the level and structure of child income supports are also taken into account, along with increases in taxes required to finance the welfare increases, it is not surprising that payments at this £90 rate involve such a high incidence of high replacement rates. Such a dramatic shift in the financial incentives facing the unemployed must be expected to have sizeable

³⁸ For a general discussion of this strategy, and an application to the specific case of lone parents in the UK, see Walker (1996). In the Irish context, work of this type was undertaken by Callan and Van Soest (1996), which examined the effects of alternative tax treatments of married couples on the labour supply of husbands and wives.

³⁹ The payment packages examined do not involve changes to the structure of secondary benefits.

consequences for labour market behaviour. We will return to the question of overall labour market impact in the Section 7.7.

7.5 Work Incentives for Employees

Table 7.2 shows the impact of the policy packages on replacement rates facing employees. Focusing in particular on those with "high" replacement rates, we find that under the baseline 1996 policy, about 17 per cent of employees faced replacement rates of 70 per cent or more. Under the £68 payment package, this proportion rises to about 18 per cent, and under the £75 payment package, to 21 per cent: the increases are concentrated on those with replacement rates between 70 and 80 per cent. A payment rate of £82 involves a more substantial increase in the proportion facing high replacement rates, from 17 per cent to 25 per cent. A £90 payment package again has the most substantial effect, increasing the proportion facing "high" replacement rates to almost 30 per cent of employees.

Table 7.2: *Estimated Impact of Alternative Social Welfare Payment Rates on the Distribution of Replacement Rates for Employees*

<i>Replacement Rate Category</i>	<i>Baseline 1996</i>	<i>With £68 Payment</i>	<i>With £75 Payment</i>	<i>With £82 Payment</i>	<i>With £90 Payment</i>
0 <10	7	6	5	5	4
10 <20	7	6	5	5	4
20 <30	14	13	11	8	7
30 <40	16	16	15	14	12
40 <50	16	16	15	15	14
50 <60	13	14	16	16	17
60 <70	10	10	11	13	14
70 <80	10	11	13	15	16
80 <90	4	4	4	4	7
90 <100	2	2	3	3	3
>100	1	1	1	3	3
All	100	100	100	100	100

Note: Estimates based on higher range of tax rate increases/tax cuts forgone from Table 6.2.

Table 7.3 shows the impact of the policy packages on marginal effective tax rates facing those in employment. The marginal effective tax rate calculations incorporate the individual's marginal rate of income tax, as well the rates of employee PRSI and Levies and the benefit withdrawal rate on Family Income Supplement for those entitled to it. The £68 payment rate package involves an

increase in the standard, top and marginal relief tax rates of about 1¼ percentage points. This affects over 400,000 standard rate taxpayers and about 300,000 top rate taxpayers. A smaller number of cases – about 15,000 find themselves facing substantially higher marginal effective tax rates: most of these are individuals who now qualify for Family Income Supplement payments, and now face a 60 per cent withdrawal rate on top of their existing income tax and PRSI rates.

The £75 payment package has a more substantial impact on marginal tax rates. It requires a tax rate increase (or tax cut forgone) of close to 5 percentage points, affecting top rate and standard rate taxpayers. In addition, over 100,000 families face a marginal effective tax rate rise of more than 10 percentage points – due mainly to the increase in the role of FIS associated with the higher welfare payments.

Table 7.3: *Estimated Impact of Alternative Social Welfare Payment Rates Marginal Effective Tax Rates for Employees*

<i>Increase in Marginal Effective Tax Rate</i>	<i>With £68 Payment</i>	<i>With £75 Payment</i>	<i>With £82 Payment</i>	<i>With £90 Payment</i>
1 to 5 % points	874	848	0	0
5 to 10 % points	0	0	825	0
Over 10 % points	15	112	196	1,114
All	889	960	1,021	1,114

The £82 and £90 payment rate packages gives rise to much more dramatic impacts on the distribution of marginal tax rates. Under the £82 payment rate package, the standard, top and marginal relief rates of income tax each rise by 8 percentage points. Over 800,000 tax units face marginal effective tax rate increases of about 8 percentage points, with about 200,000 facing increases of over 10 percentage points. Under the £90 payment package, well over a million tax units face increases in marginal effective income tax rates of over 10 percentage points – with the vast majority facing a marginal rate increase of more than 12 percentage points. Once again, these figures illustrate the nature of the trade-off, at any given level of resources, between tax rate increases (or tax cuts forgone) and welfare increases. The issue of possible labour market responses is discussed in more detail in section 7.7, but it is clear that disimprovements in the financial incentive to work on the scale associated with the £90 payment rate would have unfavourable effects on the economy's employment performance.

7.6 Incentives to Participate in the Paid Labour Market

Table 7.4 shows the impact of the policy packages on replacement rates facing those who describe themselves as engaged in home duties. Replacement

rates tend to be quite high for this group even in the baseline situation. A number of factors contribute to this.⁴⁰ First, a high proportion of those in home duties are married women whose husbands are in employment. Even if the tax liabilities of husbands and wives were strictly independent, this can lead to quite high replacement rates where the husband has a substantial income, and particularly where the potential wage of the wife is substantially below that of the husband. For couples where the wife has had a long spell out of the labour market during the child-bearing and child-rearing years, this is not untypical. The income-splitting provisions in the income tax code reinforce this tendency to high replacement rates, as second earners, in effect, face the same marginal tax rates as the first earner as soon as purely employment related allowances (such as the PAYE and PRSI allowances) are exhausted.

Table 7.4: *Estimated Impact of Alternative Social Welfare Payment Rates on the Distribution of Replacement Rates for Persons Engaged in Home Duties*

<i>Replacement Rate Category</i>	<i>Baseline 1996</i>	<i>With £68 Payment</i>	<i>With £75 Payment</i>	<i>With £82 Payment</i>	<i>With £90 Payment</i>
0 <10	0	0	0	0	0
10 <20	0	0	0	0	0
20 <30	0	0	0	0	0
30 <40	2	2	1	1	1
40 <50	6	5	4	3	3
50 <60	13	12	10	10	9
60 <70	29	28	26	24	19
70 <80	31	33	36	36	38
80 <90	18	18	19	21	22
90 <100	2	2	3	4	6
>100	0	0	0	1	2
All	100	100	100	100	100

Withdrawal of social welfare benefits contribute to high replacement rates for other groups of those in home duties: women whose husbands are in receipt of unemployment or sickness payments may find that the net contribution of

⁴⁰ It should be noted that the replacement rate calculations do not take account of the impact of childcare costs. These can be expected to reduce further the net financial reward from employment. But the results shown can be expected to give a good indication of the effects of social welfare and tax increases on the incentives facing this group.

earnings to family income is sharply reduced by the withdrawal of adult dependant and the partial withdrawal of child dependant payments to their husbands. While the incentives facing lone parents have been somewhat improved, withdrawal of benefit can also contribute to high replacement rates for this group.

In total, 51 per cent of those engaged in home duties face replacement rates of over 70 per cent under the baseline policy. This figure rises to 53 per cent under the £68 payment package, 58 per cent under the £75 package, 62 per cent under the £82 package, and to 68 per cent under the £90 per week payment package. Married women are known to be particularly responsive to changes in work incentives in most countries. Ireland is no exception, as shown by a number of studies. (Callan and Farrell, 1991; Murphy and Walsh, 1996; Callan and Van Soest, 1996). Thus, a significant response – mainly involving a reduction in married women's participation – could be expected to the packages involving payments of £75 or more.

7.7 Work Incentives and Employment

The nature of the impact on work incentives of four alternative payment rate packages has been examined in the preceding sections. Summing up, it is clear that the direction of the impact on work incentives is reasonably clear. Each of the packages involves some deterioration in work incentives. The deterioration involved in the payment package of £68 is relatively small, reflecting the fact that many social welfare rates are already close to that level. An increase from current levels to £75 has a greater impact, with over half of the unemployed facing replacement rates in excess of 70 per cent. An increase in the payment rate to £82 has a modest further impact on the numbers facing high replacement rates (above 70 per cent), but raises the numbers facing replacement rates above 80 per cent. The deterioration involved in the highest payment rate examined (£90) is the most dramatic, with about two-thirds of the unemployed facing cash replacement rates of over 70 per cent, and about one-third facing a replacement rate above 80 per cent.

The direction of the likely responses and effects of these changes in incentives is also reasonably clear. Given the nature of the impact on work incentives, most economic models would predict a fall in effective labour supply, tending to raise wages and reduce employment. Other things being equal, some shift away from work in the regular economy towards work in the irregular economy could also be expected.

While the direction of responses is reasonably clear, the size of the likely response cannot be predicted with any certainty: the evidence on this crucial question is very mixed. In what follows we set out considerations which are relevant in assessing these issues. We conclude by outlining a framework which

helps to draw together the different elements involved, and clarify how further progress could be made in developing the knowledge base to inform policy decisions in the future.

Responses to the deteriorations in work incentives identified in earlier sections have potentially important implications for the ultimate impact of increased social welfare rates on poverty. The assessment in the previous chapter concentrated on the first-round or "cash" impacts on poverty, before any behavioural responses were taken into account. Falls in labour force participation or increases in registered unemployment arising from behavioural responses imply that the impact on poverty would be *less* than these "cash" impacts suggest. Some individuals who are initially in employment would, after responses and feedback effects are taken into account, be either unemployed or out of the labour market, and would therefore have lower incomes than the "static" analysis suggests. Some would move from incomes above particular poverty lines or adequacy standards to incomes below such standards, or find that their income shortfall had increased. Increases in tax rates beyond those examined in the analysis of "first-round" impacts would also weaken the impact on poverty, to the extent that the burden fell on low income households.

One key element in assessing the impact of implementing the alternative payment rates is establishing the appropriate benchmark scenario. In our analysis of incentives, we concentrated on a very simple package of measures, including an unchanged tax-benefit structure, and a revenue-neutral financing package via changes in standard and top rates of tax. This certainly helps in identifying some of the differences between the packages in terms of their impact on work incentives. But a fuller evaluation must take account of the fact that implementation of any such target social welfare rate is likely to be phased in over a period of time, during which the economic and social structures of society are changing quite rapidly. This is not simply a question of income growth, but includes such factors as demographic trends – including falls in the dependency ratio – and shifts in the educational composition of the labour force. Even when one makes allowance for the relative nature of many of the adequacy targets, such changes in the economic and social background could make a significant difference to the work incentive implications of alternative adequacy targets.

The focus of this study is on social welfare payment levels, so it is natural that in discussion of the incentive impact of policy changes we should focus on the impact of benefit changes on replacement rates. But one should not lose sight of the fact that high replacement rates reflect benefit levels relative to potential earnings. There is scope for policy to affect the level of potential earnings for those facing the highest replacement rates. A minimum wage is sometimes canvassed as an anti-poverty measure, but in this respect, it is not well targeted.

Even if employment were unaffected by a minimum wage, most of the income gains would accrue to low paid individuals in households which are above the 60 per cent relative income poverty line (Callan and Nolan, 1992). In addition, there is the risk that a general minimum wage may crowd out some low wage employment. Alternative policy measures for improving the earning potential of target groups, such as investment in education and (re-)training may, however, have a more significant role to play in an overall strategy.

Figure 7.1: *Social Welfare, Taxation and the Labour Market*

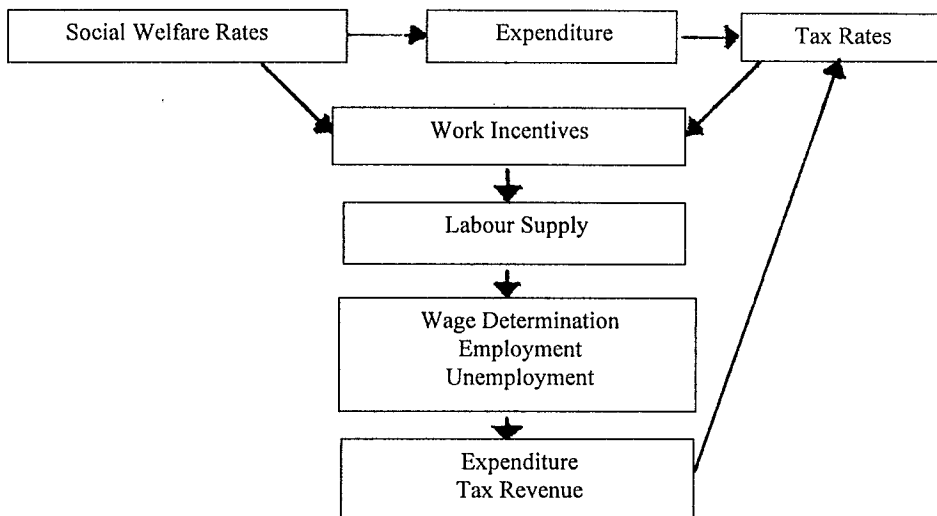


Figure 7.1 helps to clarify some of the main links between social welfare payment rates, taxation and employment.⁴¹ Changes in social welfare rates have direct implications for expenditure; expenditure increases must ultimately be financed by changes in taxation. The combination of changes in social welfare rates and tax rates can have a substantial impact on financial incentives to work, as seen already. The response to these changes in terms of individual decisions regarding job search, acceptance or rejection of job offers, and hours of work alters labour supply, which in turn feeds into the process of wage and employment determination. Changes in employment and unemployment have further implications for public expenditure and tax revenue, which may require further changes in tax rates. Such changes would again affect work incentives,

⁴¹ Other aspects of public policy also have an impact on expenditure and the balance between income taxes and other sources of tax revenue. For example, an improvement in work incentives might be brought about by a reduction in taxes on labour and the introduction of a "carbon tax", as considered in Fitz Gerald and McCoy (1992).

employment and unemployment until all adjustments had taken place (technically, until the process converged).

Microsimulation models are well suited for the analysis of the impact of changes on expenditure, taxation and work incentives. The microsimulation approach can also be extended with labour supply models to deal with the labour supply responses (as, for example, in Callan and Van Soest, 1996). Macroeconomic models, which take account of labour supply, labour demand, the nature of wage and employment determination, and the links between the labour market and the wider economy are needed to complete the feedback loops. But in order to deal with these wider issues, macro-models work with a simpler representation of the tax and welfare systems, and use very limited information to represent changes in welfare rates and the impact on work incentives.

In the present study, our brief has been to analyse the likely impact of implementing the adequacy standards on work incentives – a task for which the ESRI's microsimulation model is best suited; and to discuss the wider context of promoting employment opportunities and economic efficiency. We have outlined the main channels by which the alternative packages would tend to influence employment and the great degree of uncertainty about the magnitudes of the various responses involved. There is certainly a need for more detailed examination of these issues. Three approaches offer the prospect of greater insights into the critical trade-offs between income support rates, work incentives, employment and unemployment:

- (1) Estimation of individual and family labour supply responses to tax and welfare changes would allow microsimulation of the impact of policy changes which included estimated behavioural responses.
- (2) Exploration using a macroeconomic model of the impact of changes in simple representations of average tax and benefit rates, relative to an appropriate baseline scenario.
- (3) Analysis of policy changes using a micro-to-macro model, which sought to combine the best elements of each of the other two approaches.

In view of the difficulties involved in analysing the trade-offs between income support levels, work incentives and the broader economic effects, total reliance should not be placed on any one of these approaches: each needs to be pursued with care, with the micro-to-macro approach building on the work done by the other approaches.

7.8 Conclusion

Given the overall budgetary constraints, and in particular, the net revenue which the tax-transfer system must generate to finance other government expenditures, there is a trade-off between the level of income support and the

effective tax rates on income from employment. This trade-off is brought into very sharp relief by simple tax-transfer systems, such as proposals for a basic income (see Callan, O'Donoghue and O'Neill, 1994); but it is also inherent in more conventional systems including the current Irish tax-transfer system.

It should come as no surprise, therefore, that an increase in social welfare payment rates, from a base of around £64 per week in 1996 terms, to a level of £90 per week (with corresponding increases in adult and child dependant rates) should involve sharp increases in taxes, and a substantial worsening of financial incentives to work. For example, the £90 per week payment package involves a tax increase (or tax cut forgone) of 12 percentage points in the standard and top tax rates, affecting upwards of 800,000 individuals; and would lead to a situation in which about 30 per cent of employees, and 63 per cent of the unemployed would face replacement rates of more than 70 per cent. In our view these dramatic changes in the financial incentives to work would lead to significant reductions in labour supply and employment, and increased unemployment.

A more modest increase in social welfare rates, to a level of around £68 per week, would have a much lesser impact on work incentives. It could be financed by an increase in tax rates (or a tax cut forgone) of about 1 per cent. The impact on the distribution of replacement rates would be much less dramatic. The proportion of employees facing "high" replacement rates (over 70 per cent) would rise from just under 16 per cent to just over 18 per cent, while the proportion of unemployed persons facing high replacement rates would rise from 31 per cent to about 39 per cent – but with most of the increase occurring in the 70 to 80 per cent replacement rate bracket. An increase in the payment rate to £75 would have a more substantial impact on work incentives, with over half of the unemployed facing a replacement rate above 70 per cent.

In the present context, we see the analysis of work incentives as a crucial part of the overall assessment of adequacy of payment rates. Any assessment of adequacy which fails to take account of the impact on incentives runs the risk of focusing on payment rates which could be unsustainable. We have seen that the £90 per week payment rate, in the present economic context, involves very substantial deterioration in financial incentives to work. This, in turn, could lead to reductions in employment and a diminution in the tax base which would create a requirement for *further* increases in taxes.

Comparisons with other countries may be of particular value in helping to assess the nature of the trade-off between income support rates, employment and overall rates of poverty. An initial study (Callan and Sutherland, 1996) of developments in Irish and UK tax/transfer policies brings out the fact that payment rates under the UK safety net (Income Support) have fallen

substantially as a proportion of average income, while payment rates under the corresponding Irish schemes (Supplementary Welfare Allowance and Unemployment Assistance) have increased relative to average income. The outcomes associated with these policy choices are also described, though it must be remembered that many other factors contributed to the outcomes. Unemployment rates (measured on a Labour Force Survey basis) rose in both countries, but the increase was greater in Ireland than in the UK. But overall rates of income poverty rose sharply in the UK, while remaining roughly constant or rising much more slowly in Ireland.

An overall assessment of adequacy and incentives to work is required. Only this approach can be geared to delivering the required level of support with minimal damage to work incentives. For example, increases in replacement rates for those currently facing the lowest replacement rates may involve little or no damage to work incentives. Similarly, increases in replacement rates for individuals who are unlikely in any event to be able to take up employment - including many recipients of pension and illness payments - may have little impact on the wider labour market. But further increases in replacement rates for those who are actual or potential labour market participants, and are already facing high rates, may have more serious consequences in terms of the overall labour market impact.

A precise estimation of the labour market impact of alternative policy packages is not within our remit, and would, indeed, require a major programme of research. It should be pointed out, however, that the packages analysed here are simply one possible way of delivering the "target" level of income support, working within the existing policy structures. While *all* delivery systems will face a trade-off between the level of income support provided and the effective tax rate on employment, there may well be alternatives superior to the current system, and to the particular packages analysed in this report.⁴² In the search for such alternatives, detailed comparisons with the tax-transfer systems in operation in other countries could be of considerable benefit. Issues for investigation should include not only the level and structure of payments, but the structure of benefit withdrawal and the structure of entitlement to (and withdrawal of) non-cash benefits.

⁴² The work of the Tax and Welfare Group (TWG), *Integrating Tax and Social Welfare* is very relevant in developing policy packages aimed at improving work incentives and/or improving income support with minimal damage to work incentives. But the framework used in the TWG analysis of policy packages incorporates scope for tax reductions arising from economic growth. Income growth would tend to raise most of the adequacy standards considered in this report, so that this framework is not suitable in the present context, as noted in Chapter 6.

Chapter 8

ADEQUACY AND UPDATING SOCIAL WELFARE RATES

8.1 Introduction

In addition to reviewing the calculation of minimum adequate social welfare rates and assessing the impact of newly-calculated rates on effectiveness and incentives, the terms of reference for this study include a consideration of the appropriate method of updating payment rates in the future. This is the topic of this penultimate chapter. We first look in Section 8.2 at the manner in which the issue of updating has been addressed in recent years. In Section 8.3 we then consider the relationship between adequacy and updating and draw out some implications for appropriate procedures. Section 8.4 summarises the main conclusions.

8.2 Approaches to Updating Social Welfare Rates

The approach publicly articulated by different Irish governments over the past twenty-five years to updating social welfare rates from one year to the next has varied a good deal, both in content and in the extent of explicit pre-commitment involved. Without attempting a comprehensive survey, it is useful to refer selectively to public statements of policy over the period to illustrate the main themes, which as we shall see tend to recur although with significant changes in emphasis. Our aim is not to describe what different governments actually did with respect to social welfare rates or to evaluate their policies against the stated objectives, but simply to draw out the terms in which those objectives were stated.

The political parties which came into government in 1973 had promised in a pre-election statement to make financial provision for "improving and extending the social welfare ...services". That government implemented increases in social welfare rates in its first budget which the Minister for Finance's budget statement described in the following terms:

The increases ...go far beyond covering the increases in the cost of living ... and also go a long way towards bringing these various payments, particularly pensions and children's allowances, into line with those in neighbouring countries (pp. 17-18).

By 1976-77, however, the impact of the first oil crisis on the economy and the public finances led to a marked change in emphasis from the same government. With inflation accelerating the stated policy at budget time was to concentrate on maintaining the real value of payments. Concern about incentives to work were also expressed with the introduction of a provision that an unemployed person's income from benefits could not exceed 85 per cent of his after-tax income immediately prior to unemployment.

With the change of government in 1977 the stated policy changed markedly once more. The National Development Plan 1977-80 produced by that government set out the commitment to maintain the living standards of social welfare recipients by adjustment at least in line with the cost of living, while devoting special attention to those with little or no income other than their weekly social welfare payment. The 1980 budget of that government talked in terms of "major improvements in the incomes of the less well off", and even as the extent of the crisis in the public finances came to be acknowledged its 1981 Budget stated that:

The Government intend that those in need should not suffer by reason of changing economic conditions over which they have little or no influence. The [Budget] measureswill not only prevent this happening but will, in fact, improve further and significantly the position of those dependent on social welfare payments.

The general stance on updating adopted by the government in office from 1982 to 1987 was unusually explicit. As well as the commitment to establish a Commission on Social Welfare, the programme for government on which the parties contested the election stated that:

Unemployment Benefit and Disability Benefit will be kept in line with increases in take-home wages and salaries. Expenditure on other social benefits will be maintained in the light of inflation so that, even if a drop occurs in the immediate purchasing power of better-off groups in the community, the living standards of the section of the community dependent on social welfare payments will be maintained (p. 19).

Throughout the life of that government budgets made reference to the need to protect pensioners and other long-term beneficiaries from the effects of inflation, and as unemployment soared concern was regularly expressed from a work incentive point of view about the relationship between short-term benefits and disposable earnings from work. Several budgets also justified extra increases for those on long-term UA in terms of the hardship imposed by the increase in long-duration unemployment.

The Commission on Social Welfare reported in 1986, with its recommendations on minimum adequate rates of support. It was some time

before these became the explicit focus of official policy commitments, though the Commission's emphasis on the need to give priority to increasing the lowest rates could have had some impact on the Programme for National Recovery agreed between the social partners in 1987. This set out the policy that:

The Government will maintain the overall value of social welfare benefits and within the resources available will consider special provision for greater increases for those receiving the lowest payments (p.13).

The subsequent Programme for Economic and Social Progress agreed in 1991, by contrast, while reiterating the commitment to continue to protect social welfare rates against inflation, also included the commitments:

to move by 1993 to the priority level of rates recommended by the Commission on Social Welfare.

Thereafter, to increase social welfare rates further and progressively, in accordance with the recommendations of the Commission on Social Welfare, as the resources of the economy grow (p. 22).

The 1993 Programme for Government agreed between the Fianna Fail and Labour parties relied on the same two points of reference, protection against inflation and the CSW's recommendations. Its commitment was to at least maintain the real value of social welfare payments and protect the incomes of pensioners, and "to continue the implementation of the recommendations of the Commission on Social Welfare". The Programme for Competitiveness and Work agreed by the social partners in 1994 expanded on these themes, the stated policy being to continue to at least maintain the real income position of those on social welfare and to make further progress towards the Commission on Social Welfare's priority and main recommended rates, though it cautioned that "Such progress will have regard to the capacity of the economy and the Budget to support the increase in expenditure". The PCW also stated that "Care will be taken to promote employment maintenance and growth through ensuring an adequate incentive on the part of unemployed people to take up work."

The agreement at the end of 1994 between the parties forming the current government contained a general commitment to the maintenance and development of the social insurance system. Subject to the availability of resources, the following areas with relevance to uprating were among the stated priorities:

Increasing the rate of disability and unemployment benefit towards the main rate recommended by the CSW;
commissioning the ESRI to review the minimum adequate rates recommended by the CSW;

developing the further integration of the tax and social welfare systems in the context of the work of the Expert Working Group on that topic.

A commitment was also given to work towards a basic income system for children.

The stated objectives of Budgets in 1995 and 1996 have included protecting the spending power of social welfare recipients, moving towards a basic income for children, helping the long-term unemployed obtain work, making the social welfare system more work-friendly, and improving the position of families, pensioners and carers. This range of objectives, as well as the commitments enshrined in the Programme for Competitiveness and Work which runs until the end of 1996 are, therefore, those articulated most recently as underlying policy on uprating.

This review of the objectives underlying uprating of social welfare rates as articulated by different Irish governments over the past quarter-century brings out a number of consistent themes, though the balance between objectives has varied a good deal over time. The first and most commonly-accepted aim is to protect the value of social welfare payments, particularly for pensioners, against inflation. This emerges as a "core value", in good times and in bad: pensioners in particular should not see their real living standards fall even if those of the rest of the community are declining for a time. The need for such protection is not necessarily viewed as axiomatic for social welfare recipients more generally, however. The approach taken by the government of the early/mid-1980s differentiated between long-term and short-term recipients, with rates of support for the latter linked to take-home pay rather than prices – at a time when prices were expected to rise more rapidly. This also reflected the second consistent theme, namely concern about work incentive effects. Throughout the period reviewed, reference has regularly been made in setting rates for the unemployed to the need to maintain a differential between income when unemployed and income in work. While this is a prominent feature of the debate about adequacy at present, it is worth noting how regularly it has recurred over the entire period back to the mid-1970s.

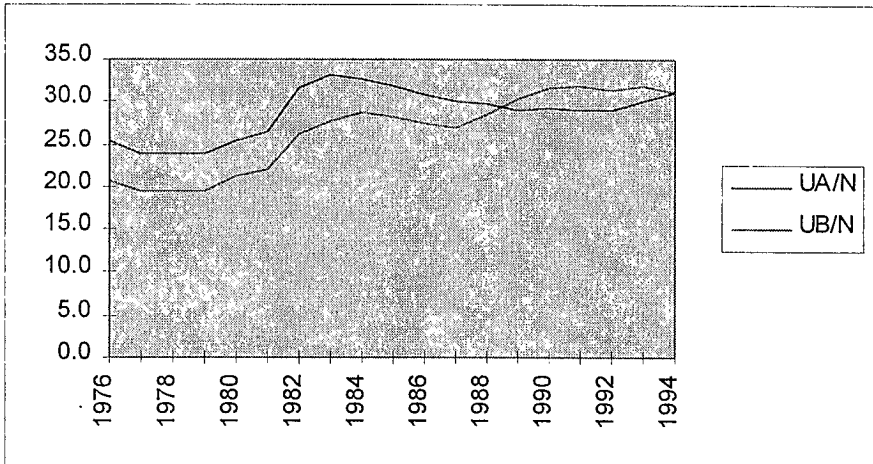
A third theme is that social welfare payments should be increased over time to reach levels which would be adequate or would enable recipients to afford the basic minimum standard of living. Since the CSW reported, this has most often been put with reference to the Commission's recommended rates, but had been made in more general terms in earlier years. It is not however possible to glean with any precision the notion of adequacy underlying such formulations, in particular whether it relates to a standard held constant in real terms or moving up over time as average incomes rise. A fourth theme, naturally more prominent in good times than in bad, is the desirability of social welfare recipients sharing

in such improvements in the living standards of the community as a whole. Finally, throughout the period rates increases have been related to affordability in terms of the state of the economy and the public finances. The reference in the PCW to "the capacity of the economy and the Budget to support the increase in expenditure" is a typical example, and typically open to differing interpretations as to what is "affordable".

Having seen the way in which uprating decisions have been presented, it is useful in concluding this section to briefly illustrate the relationship these decisions have actually produced between two key variables: basic social welfare rates for the unemployed and net take-home pay. The unemployed are of particular interest in this context because incentive aspects loom larger for them than for most other categories of social welfare recipients, and so the balance between the various objectives in setting support rates is particularly delicate. Figure 8.1 shows that in the mid-1970s the support provided to a single man by Unemployment Assistance and flat-rate Unemployment Benefit came to about 20 per cent and 25 per cent respectively of the average take-home pay of an adult male in industry. From 1979 to 1990 UA (long-term) then rose significantly faster than average take-home pay, and by the latter date had reached about 30 per cent of average male take-home pay. Flat-rate UB, by contrast, rose only up to 1983 and then declined, falling below UA from the late 1980s. Since 1990 UA has been rather stable as a proportion of average take-home pay while UB has risen so that by 1994 they were each paying the same rate. (We have not taken into account Pay-Related Benefit payable with UB throughout the period though now phased out, because although it clearly had major implications for incentives our focus here is on the annual uprating of the basic rates). By the end of the period, both UB and UA came to about 30 per cent of average male take-home pay, representing a significant upward shift compared the relationship which held in the mid-1970s, particularly in the case of UA.

This example illustrates the manner in which the mix of objectives and constraints feeding into uprating decisions have produced significant changes in a relationship which is central to both adequacy and incentive effects. It demonstrates *inter alia* that a policy of linking rates increases directly to take-home pay would in fact have involved lower rates increases over the past twenty years than those actually implemented. This is of particular relevance to our discussion in the next section of how best to incorporate adequacy considerations explicitly into the uprating process.

Figure 8.1: *The Relationship Between Unemployment Compensation and Take-Home Pay, Single Man, 1976-1994*



8.3 Adequacy and the Updating Process

Having described the way in which the updating of social welfare rates has been approached over the past twenty-five years, we now turn to how this crucial element in social welfare policy might best be approached in the future. In doing so it has to be emphasised that both the level of social welfare rates at any point in time and changes in these rates over time are matters of societal choice exercised through the political process. There are multiple and sometimes conflicting objectives to be taken into account in decisions about rates: adequacy itself is only one element and cannot be set apart from considerations of efficiency and the desired degree of redistribution. What social science research can contribute, however, is important insights into the implications of different choices and different ways of approaching the issue. We therefore seek to bring out how the CSW's concept of adequacy, if adopted unambiguously and wholeheartedly, might be taken into account explicitly in the decision-making process.

If one's notion of adequacy is that it represents an absolute standard which remains fixed over time, then taking this into account in updating social welfare rates is rather straightforward. Having defined such a target, updating boils down to two elements as far as adequacy is concerned. The first is ensuring that rates keep up with increases in prices, and the second is deciding how quickly the target level of support in real terms is to be attained (assuming it has not already been reached, in which case the goal would be simply to keep up with prices). Arguably, this is the way in which some public articulations of policy towards

rates increases in the past could be interpreted, and it certainly represents the manner in which the rates recommended by the CSW have tended to be employed – as a target which moves upwards over time only in line with prices. As previous chapters have made clear, however, this is clearly inconsistent with the Commission's underlying approach to adequacy.

If adequacy is instead to be assessed against the standards of the society in question at a given point in time, as the CSW envisaged, and thus what is considered adequate changes over time as those standards change, then taking it into account in uprating will necessarily be a good deal more complex. Rather than representing a fixed target in real terms, the target will move up over time as general living standards in the community rise. However, many questions remain to be tackled as to the nature of that relationship and how it is best incorporated into the decision-making process. Most importantly, what indicators of "general" living standards are most appropriate, and how is the adequacy standard to be linked to those indicators?

While the CSW was unambiguous in adopting a relative concept of poverty and of adequacy, the different methods by which it attempted to implement this concept and derive a minimum adequate income for a point in time involve assumptions about the relationship between adequacy and various benchmarks over time. Most obviously, taking a proportion of average net earnings or disposable income as an estimate of adequate income assumes that the adequacy standard will move upwards over time step for step with take-home pay or average income per head. Other CSW methods imply different assumptions. For example, basing the adequacy standard on "official" benchmarks such as the medical card income threshold or minimum wages involves a less direct but none the less significant link to changes in average earnings/income over time. The institutional budget method makes a rather different implicit assumption, linking the adequacy standard to costs of meeting needs which may or may not change over time, but this is the exception among the CSW's methods.

The 1992 "Minimum Income" Recommendation by the EU Commission provides an important point of reference in considering the process by which adequacy standards can be uprated over time. As described in Chapter 2, the Recommendation states that social protection systems should be adapted as necessary according to a set of principles and guidelines. These include fixing the amount of resources considered sufficient to cover essential needs with respect for human dignity, taking account of living standards and price levels in the Member State concerned, for different types and sizes of households. In order to fix the amounts, reference should be made to appropriate indicators such as statistical data on average disposable income and household consumption, the legal minimum wage if it exists, and the level of prices in the Member State.

Member States are also encouraged to establish arrangements for periodic review of these amounts, based on these indicators, "in order that needs continue to be covered".

Considering this Recommendation in the Irish context, what is striking is the very limited extent to which the suggested indicators have been *explicitly* taken into account in assessing adequacy and updating social welfare rates. The review in Section 8.2 made clear that in general the rate of increase in prices has been the key "hard" point of reference in official articulations of policy, with other aspects covered by much vaguer formulations such as references to "general improvements in living standards". If the CSW's relative concept of adequacy is to be fully incorporated into policy-making, an essential step is therefore to have available and explicitly make use of specific indicators of trends in general living standards. This would also be central to the implementation of the Minimum Income Recommendation.

Data currently available for this purpose are extremely limited. The only official data on earnings and incomes available with sufficient frequency to be of use are the figures produced quarterly by the CSO on average earnings in industry from the Quarterly Industrial Inquiry, and those in the annual National Accounts on aggregate incomes from different sources and total personal disposable income. Both have limitations in the context of monitoring trends in earnings or incomes generally. The QII covers only industrial employment, where a minority of employees work, and the published information relates to average gross earnings but not their distribution – which as discussed below is also relevant to updating. Information on individual earnings does not in any case tell us what is happening to household living standards, since the latter depends also on how earners and those in receipt of other income sources are grouped together, with their dependants, in households. The national accounts income aggregates cover the whole economy and include income from self-employment and property as well as earnings, but can serve as the basis for only the crudest estimate of average income per head, with no means of taking into account the way this income is distributed among households of differing compositions. Data on household incomes are produced from the Household Budget Survey but this is at present only carried out every seven years. The European Community Household Panel Survey being carried out by the ESRI for Eurostat will provide *inter alia* annual estimates of household incomes for a large sample for some years from 1994, but it is not clear at this point how long that survey will continue.

Improvements in the range of indicators of trends in earnings, household incomes and general living standard are therefore required if the updating process is to include an explicit assessment of adequacy in the light of those trends. One

can point, for example, to the data available in the UK on both earnings and household incomes. The New Earnings Survey provides a detailed picture of individual earnings and hours worked for a very large sample of employees. This means that not only measures such as average and median earnings, but also the level of earnings of those at different points in the earnings distribution, are available on an annual basis. The annual Family Expenditure Survey and more recently the specially-designed Family Resources Survey provide in-depth information on household incomes, so that mean and median household equivalent incomes and the distribution of that income can be derived in a variety of ways. This provides the basis for the annual official report on Households Below Average Income, which sets out the evolution of the position of households towards the bottom of the income distribution relative to both income standards that are held constant in real terms and ones that move over time in line with the average for all households.

This type of detailed annual information about earnings and household incomes would provide the range of indicators needed to properly monitor trends in living standards and serve as benchmarks in setting adequacy standards. Both individual earnings and household incomes are relevant points of comparison, and it is important that in each case one knows more than simply how the average is changing because different distributional patterns may have different implications. If average earnings are increasing because top earnings are rising very rapidly but earnings in the bottom half of the distribution are actually stagnant, for example, this may be regarded in a different light to an upward shift in the entire distribution giving the same increase in the mean. Even if one did not wish to distinguish between these situations in assessing adequacy, it would certainly be necessary to do so in considering the work incentive effects of raising social security rates, and so the distributional information would be an important input into the up-rating process more broadly.

Other approaches to assessing adequacy at a point in time discussed in this study, including the budget standard methodology, the analysis of views of survey respondents on the income needed to "make ends meet", and the study of the extent of deprivation among those relying on social welfare, could also serve as an input to this process.⁴³ They would be particularly valuable if applied with sufficient regularity to allow changes over time to be monitored accurately, though not necessarily each year. Consultation with those relying on social welfare, and with voluntary and statutory agencies dealing with recipients, would also provide an important input.

⁴³ Each of these methods faces problems, as we have made clear, but taken together may be a useful input into assessing changes in an adequacy standard.

While improving the information base in this way is extremely important, progress can still be made towards a more explicit process of evaluating adequacy in uprating using the data currently available. Changes in consumer prices, in average take-home pay and in average income per head excluding social security transfers provide three indicators to which specific reference could be made in assessing how an adequacy standard was changing over time. Using these indicators in the way suggested in the Minimum Income Recommendation to regularly and publicly review changes in what constitutes an adequate income in the Irish setting would be a major step forward, and would in itself highlight the need for more comprehensive information. Implementing such an explicit assessment of the way in which an adequacy standard is changing over time does not imply either that the standard itself has to be derived as a fixed proportion of average earnings or income, or that adequacy will then be the dominant consideration in making decisions about the way rates are actually uprated. It would probably be generally agreed that, at a minimum, the adequacy standard would move up in line with prices to maintain its real value in terms of purchasing power. Beyond that, there would be scope for differing judgements about the nature of the adequacy standard and its relationship with average earnings or income. What would be different is that the judgements involved would have to be formulated and presented with some precision, rather than largely left implicit as is currently the case.

Conclusions as to how the adequacy standard has changed since social security rates were last altered would be a major, but by no means the only, input into the up-rating decision. Our review of approaches to uprating brought out that the key elements acknowledged as entering into uprating decisions have encompassed affordability and efficiency considerations as well as adequacy ones, and this would of course continue to be the case. One of the most explicit statements an Irish government has made about its approach to uprating in recent years, that (in 1982) pensioners were to be protected against inflation but short-term benefits for the unemployed were to be increased only in line with increases in take-home pay, expected to rise less than prices, helps to make this point. This differentiation was not because the adequate level of payments was thought to be changing in a different way for these two groups, but rather because of work incentive considerations. In the same way, no government could be expected to introduce an explicit link between for example pension levels and earnings on adequacy grounds alone, in the absence of a credible policy for how this expenditure was to be financed in the light of demographic and economic projections. (Thus recent UK debates on that topic have revolved around adequacy and affordability implications of different up-rating procedures for pensions.) The result of adopting a more explicit process for evaluating changes

in adequacy over time thus leaves it entirely open to the political process to produce different judgements about what constitutes adequacy, and different decisions about the balance between adequacy and other objectives.

8.4 Conclusions

This chapter has considered the way in which social welfare rates are uprated from one year to the next, and in particular how adequacy considerations enter into these decisions. Looking at the approach to uprating social welfare rates publicly articulated by different Irish governments over the past twenty-five years showed that, despite a good deal of variation in content and in the extent of explicit pre-commitment, there were a number of consistent themes. The first and most commonly-accepted aim was to protect the value of social welfare payments for pensioners against inflation, and where possible to extend the same protection to others relying on social welfare. The second consistent theme was concern about work incentive effects. A third theme is adequacy: rates should be increased to the point where recipients can afford the basic minimum standard of living. A fourth theme was the desirability of social welfare recipients sharing in improvements in the living standards of the community as a whole. Finally, throughout the period rates increases were set in the context of affordability in terms of the state of the economy and the public finances. The interaction of these objectives and constraints over the twenty years from 1976 was shown to have produced a significant increase in basic support rates for the unemployed as a proportion of take-home pay in industry.

How should this crucial element in social welfare policy be approached in the future? We have emphasised that both the level of social welfare rates at any point in time and changes in these rates over time are matters of societal choice exercised through the political process, and that adequacy itself is only one element and cannot be set apart from considerations of efficiency and the desired degree of redistribution. The point of departure for the present study is the CSW's concept of adequacy, and our focus in this chapter has been on how that notion of adequacy, if wholeheartedly embraced, might be taken more fully and explicitly into account in the uprating process.

The manner in which the rates recommended by the CSW have tended to be employed in uprating – as a target which moves upwards over time only in line with prices – is clearly inconsistent with the Commission's underlying approach to adequacy. If adequacy is to be assessed against the standards of the society in question at a given point in time, as the CSW envisaged, the target will move up over time as general living standards in the community rise. However, many questions remain to be tackled as to the nature of that relationship and how it is best incorporated into the decision-making process. Most importantly, what indicators of "general" living standards are most appropriate, and how is the

adequacy standard to be linked to those indicators? The information currently available for Ireland from which such indicators might be constructed is extremely limited, and we have highlighted priorities for development in that area. These include more regular and comprehensive data on earnings and household incomes and their distribution, and on other non-monetary indicators of general living standards.

However, progress can still be made towards a more explicit process of evaluating adequacy in updating using the data currently available. Changes in consumer prices, in average take-home pay and in average income per head excluding social security transfers provide three indicators to which specific reference could be made in assessing how an adequacy standard was changing over time. Using these indicators in the way suggested in the European Commission's Minimum Income Recommendation to regularly and publicly review changes in what constitutes an adequate income in the Irish setting would be a major step forward, and would in itself highlight the need for more comprehensive information. Implementing such an explicit assessment of the way in which an adequacy standard is changing over time does not imply either that the standard itself has to be derived as a fixed proportion of average earnings or income, or that adequacy will then be the dominant consideration in making decisions about the way rates are actually updated.

Chapter 9

CONCLUSIONS

9.1 Revisiting Adequacy

A central recommendation of the Commission on Social Welfare in its 1986 Report was that all social welfare recipients should be entitled to a minimally adequate basic payment, which it was estimated would in 1985 be in the range £50-£60 per week for a single person. These figures were produced by applying a number of different methods which were intended to reflect conventional living standards in Irish society. As an urgent priority, the Commission recommended that basic personal rates be brought up to £45 per week. Since the Commission reported, its estimates of minimally adequate income have played an important part in debates about the adequacy of social welfare support rates, and its recommendation in this regard have featured in programmes for government and official policy statements.

The present study has been commissioned by the Department of Social Welfare. Its aims are to review the calculations of the minimum adequate rates using the CSW's methodologies and other appropriate methodologies; compare these calculations with current social welfare weekly payment rates and the CSW's rates updated in line with trends in the CPI and net earnings and taking into account secondary benefits; evaluate the extent to which adoption of the newly calculated rates would improve the effectiveness of social welfare payments; analyse the likely impact of implementing the newly calculated rates on incentives to work; discuss the wider context of employment opportunities and economic efficiency; and consider the appropriate method of uprating payment rates in the future.

It was emphasised at the outset of the study, and bears repeating, that neither the methods employed by the Commission on Social Welfare and updated here, nor the alternative approaches discussed, allow one to derive in an unproblematic, objective and scientific way estimates of income adequacy which would be universally acceptable and convincing. All the methods of addressing this issue currently in use have their problems, and the search for a methodology which can provide an unambiguous answer that everyone will accept to the

question "how much is adequate?" is in our view misguided. Statements about adequacy reflect judgements, values and attitudes: research cannot substitute for, but can inform, such judgements. The results contained in this study are thus presented in the belief that they can contribute to better informing official, political and societal judgements about adequacy, and to improving the process whereby social welfare rates get set.

9.2 Defining and Analysing Adequacy

Posing the question "Are social welfare levels adequate?" brings one straight to the central conceptual issue in assessing adequacy, "adequate *for what?*" The answer provided by the Commission on Social Welfare (CSW) was that "To be adequate, payments must prevent poverty, and in our view poverty must be judged in the light of actual standards of living in contemporary Irish society" (p. 123). The CSW thus saw poverty as exclusion from ordinary participation in society due to lack of income, took the position that it is possible in principle to estimate the level below which income should not fall to allow minimal participation in society, and identified that income level with adequacy of social welfare payments (p. 124). Very much the same understanding of poverty and adequacy underlies the National Anti-Poverty Strategy (NAPS) currently being developed by the Irish government following the UN World Summit for Social Development held in Copenhagen in 1995. The core criterion against which the adequacy of social welfare payments is assessed – by both the provider and the recipient – will be whether they are sufficient to allow recipients to avoid poverty. Application of that criterion is an inevitably imprecise exercise, given the nature of the information available and the diverse ways in which the problem can be approached. Our approach has been that a research study like this can hope only to provide as many relevant pointers as possible to help policy-makers in arriving at conclusions about adequacy, rather than presenting firm conclusions or recommendations about the level of social welfare support which would be adequate.

The standard of living of those depending on social welfare will clearly depend not only on their cash payments but also on what these payments have to buy. This will be affected by the extent to which the state provides goods and services directly or supplements cash income in other forms. Non-cash benefits to social welfare recipients which are not received by (most of) the rest of the population will affect the living standards of recipients relative to the average in the society, and need to be taken into account if adequacy is being assessed *vis-à-vis* that average. Valuing these benefits and imputing that value to recipients is however problematic.

Another important issue in assessing adequacy is that families and households differ in size and composition, and what will be adequate for a single

person may not suffice for a married couple with dependent children. The assessment of adequacy thus inevitably leads one into the question of the relationship between "needs" and household size/composition, which is the appropriate "equivalence scale". There is no consensus among researchers about the best method for determining these scales and different methods give quite different results. The Commission on Social Welfare concentrated on calculating a minimum adequate income for a single person, and recommended that the additional payment for an adult dependant should be 60 per cent of the rate for a single person, apparently on the basis that this was the standard figure in the literature – though in fact there is considerable variation in such estimates. In considering payments for dependent children the CSW noted that there was little recent research on equivalence scales for Ireland and the results of research elsewhere could not necessarily be readily applied, so a fully adequate child income support payment could not be calculated.

The main approaches employed elsewhere in measuring income adequacy include the construction of budget standards, the food ratio method, reliance on subjective assessments of survey respondents, seeking to identify an official view about adequacy from policy parameters such as the level of minimum wages, derivation of purely relative thresholds from average income or earnings, and analysis of the observed relationship between income and non-monetary indicators of deprivation. The review of these methods presented in Chapter 2 sought to bring out their strengths and weaknesses. It will be clear that no one method or approach has been widely accepted as the best, all have problems, and this uncertainty – even about the nature of the exercise and the appropriate role of research versus societal values and political decisions – must be acknowledged rather than obscured. None the less, decisions have to be made and will be made via the political process about adequacy, and results from a range of methods can contribute to the debate which feeds into this process.

9.3 The Commission on Social Welfare's Methods of Estimating an Adequate Income

The methods employed by the CSW to derive a minimally adequate income were first described and re-applied to up-to-date data. The CSW applied seven different methods to establish what would be an adequate income for a single adult living independently in 1985 terms, and the results produced a range from £51 to £59 per week. Re-application of two of these methods with up-to-date data was not possible until the results of the 1994 Household Budget Survey are available, and in any case was judged to be unwarranted given fundamental problems with the two methods. We presented updated results from the remaining five for the most recent data available. All these could be recalculated for 1994, when the minimum adequate income figure for a single adult fell in a

much wider range than 1985, namely from £69 to £91 per week. Upated to 1996, the corresponding range is £75 to £96.

As well as re-applying the CSW's methods, it was important to examine their strengths and weaknesses in some depth. Three of the CSW methods updated here derive an adequate income simply as some proportion of average earnings or income. This general approach links adequacy directly and transparently to average living standards in the society, so adequate income moves up over time in line with that average. However, the choice of a particular proportion of the average as adequate is essentially arbitrary, and the fact that the CSW's methods gave results concentrated in a particular range partly reflects the choice of different proportions to apply to different benchmarks. This purely relative approach is thus stronger in assessing how adequacy of social welfare rates has been changing over time than in deriving an adequate income at a point in time.

The other CSW methods seek to identify alternative "official judgements about income adequacy" from the income threshold for entitlement to a medical card, from the level of tax allowances, and from the wage minima set by Joint Labour Committees. The main problem with these methods is that it may not be valid to infer judgements about adequacy from the policy decisions made about these instruments, which are in any case affected by rather than independent of the level of social welfare rates.

9.4 Other Perspectives on Adequacy

Given the problems noted with the methods of deriving an adequate income employed by the CSW, the obvious question is whether there is a better way – which was indeed the challenge issued by the Commission in presenting its results. Some alternative perspectives on the problem were therefore employed in the belief that they, like the CSW's methods, could contribute to better informing official, political and societal judgements about adequacy.

Data from large-scale household surveys carried out by the ESRI in 1987 and 1994 were used to throw light on the adequacy of social welfare in a number of different ways. First, the purely relative approach to deriving adequacy estimates was explored using data on household incomes and individual earnings in the 1994 Living in Ireland survey. Average household disposable income in the survey was £280 per week, and converting this to average income per adult equivalent with a scale that allows 1 for the household head, 0.66 for each other adult, and 0.33 for each child and counting a child as under 14 produces average disposable income per adult equivalent of £129 per week. A purely relative income poverty line or adequacy standard for a single person set at 60 per cent of this figure would thus be about £77 per week, while a standard set at 50 per cent would be about £64 per week. These figures were seen to be sensitive to the equivalence scale employed; for example, a scale closer to that currently implicit

in income support for the unemployed, of 1/0.6/0.31, and counting a child as under 18 would produce a 60 per cent standard of £82 and a 50 per cent one of £68 per week for a single person, an even more important and essentially arbitrary choice in applying a purely relative approach is which proportion of the average one takes. The CSW, in deriving such an estimate from average equivalent household income, used 60 per cent and 65 per cent; common practice in studies applying relative income poverty lines is to use 50 per cent and 60 per cent. Within the purely relative approach itself, there is nothing to say which figure is appropriate.

We looked empirically at the extent to which households receiving or relying on social welfare payments from the various schemes in 1987 and 1994 fell below relative income poverty lines for each year. In 1987, a very high proportion of households relying on Unemployment Assistance or SWA were below half average income. Income poverty rates at the higher 60 per cent income line were also high for those relying on UB, DB, Invalidity Pension, Widow's Non-Contributory Pension or Deserted Wife's Allowance. By 1994, the most notable changes were that poverty rates using the 50 per cent income line had fallen for those relying on UA or UB, but those relying on Old Age Pensions saw a substantial increase in risk with the 60 per cent line.

The adequacy of the various schemes was also assessed using a combination of relative income poverty lines and non-monetary deprivation indicators. The results for 1987 showed that, for the most part, the risk of being below the income lines and experiencing basic deprivation varied across schemes in the same way as risks with the income lines alone. By 1994, however, there had been a significant fall in the percentage of households relying on UA who fell below the income lines and experienced basic deprivation. In general, a stable or falling risk of being below the income lines and experiencing basic deprivation was much more common than an increasing risk. In-depth analysis of non-monetary deprivation indicators in the 1987 ESRI survey does not support optimism about the prospects of identifying a minimum adequate income below which people are deprived of what are generally regarded as necessities and above which they are not deprived of those necessities, or even a threshold below which deprivation escalated very rapidly.

The income which households relying on social welfare believed was the minimum they needed to "make ends meet" in 1987 and 1994 was also analysed. The results showed that in 1987 households relying on social welfare and comprising a single adult regarded a figure of about £58 per week as the minimum necessary, which was in the range identified by the CSW as constituting a minimum adequate income. By 1994, subjective evaluations of such households were that a minimum of about £80-87 per week was needed to

make ends meet. The income regarded as minimum by other household types generally rose in the same manner over the period. The equivalence scales implicit in the responses of different household types were also examined in some detail: as in other studies using these subjective evaluations, these implicit scales were much flatter than those produced by other methods, in other words the additional needs of larger compared with smaller families were substantially lower.

The main findings of an Irish application of the budget standards approach, estimating the "costs of a child", were discussed. The study concluded that as of 1992-94 income support for teenagers was significantly below the basic minimum needed. Since no comprehensive Irish budget standards study of households more generally has been carried out, the results of a recent UK study were discussed in some detail. This contained a number of interesting findings about, for example, the needs of one household type versus another, and the variation across types in the composition of the commodity baskets specified also provided important insights into what is involved in a full-blown budget standards exercise. The strengths and weaknesses of the budget standard approach were brought out in discussing these studies. The main strength is the extent to which people can concretely identify with the living standards incorporated in the consumption basket, the main weaknesses is the number of subjective decisions which are involved about what is included in an "adequate" consumption basket and to what standard. The main potential of budget standards is not to define what constitutes an adequate standard of living, but rather to outline the financial consequences of a specified and defined living standard and thus provide a point of reference in assessing the adequacy of current income support rates.

Case studies of households assisted by the Money Advice and Budgeting Service funded by the Department of Social Welfare provided another perspective on the situation of some low-income households. These provide a direct insight into the financial difficulties in which some households find themselves. Most of the cases have significant arrears or debts so that much of their weekly income goes on keeping creditors at bay. The advice service very often sought to put the family's finances on a stable footing by negotiating a partial write-off of these debts in return for some regular repayment. The biggest single group among the case studies comprised lone parents. One cannot draw conclusions about the adequacy of social welfare payments for the generality of low-income households or social welfare recipients from these case studies, since they have mostly been referred to the advice service precisely because of the unusual scale of their debts and financial difficulties.

Cross-country comparisons of the relative generosity of social security systems also offer another perspective on adequacy, though obtaining data on which to make fully valid comparisons is difficult and inferences for adequacy must be drawn with care. The results presented suggested that Irish social welfare rates were generally more generous relative to average earnings or income than those in the UK, but were if anything below the average for EU countries as a whole.

9.5 Adequacy Estimates and Current Social Welfare Rates

The estimates of minimum adequate income levels produced by the various approaches, updated from 1994 or 1995 where necessary, produced 1996 figures for a single adult ranging from £68 to £96 per week – a considerably wider range than produced by the CSW for 1985. These were compared with the rates recommended as adequate by the CSW for 1985, updated in line with prices or alternatively in line with earnings, as summarised in Table 9.1. The range recommended by the CSW as minimally adequate for 1985 was £50-60, and updated in line with price changes the corresponding figures for 1996 would be £68-81. Up-rating the CSW's original range in line with net earnings in industry gives the much higher figures of £84-100, reflecting the growth in real take-home pay over the period.

The various up-to-date estimates of what would be adequate, and the CSW's updated recommendations, were then compared with current social welfare rates, again as summarised in Table 9.1. The basic rates of payment for a single adult under the different schemes are currently (1996/1997) in the range £62.40-75. Even the lowest rate, paid by short-term UA and SWA, has reached the CSW's priority rate updated in line with prices. However these, and the £64.50 paid by UB/DB, are still below the bottom of the CSW's recommended range updated in line with prices. Contributory Old Age and Widow's/Widower's pensions now pay above that updated CSW figure, and so do non-contributory Old Age and Widow's/Widower's pensions if one includes the £6 living alone allowance.

Most of the estimates of what constitutes an adequate income for a single person are well above the bottom of the CSW recommended range updated by prices, all but one being £75 per week or more. Most current social welfare personal rates thus lie well below that figure, the only exceptions being contributory Old Age Pension and Invalidity Pension. (For someone aged 80 or over, widow's/Widower's Pension and Deserted Wife's Benefit are close to that level.) The outlier among the adequacy estimates was that based on 50 per cent of average net equivalent household income, which was actually the same as the bottom of the updated CSW range – at £68 per week – and current UB/DB/long-term UA rates are not far short of that figure.

Table 9.1: *Alternative Estimates of Minimum Adequate Income and Selected Social Welfare Rates, Single Person, 1996*

	<i>1996</i> <i>£ per week</i>
<i>Minimum Income Estimate for a Single Adult from CSW Methods</i>	
average industrial earnings	95.75
national accounts average earnings	88.70
medical card	80.70
tax exemptions	75.00
minimum wage	83.41/95.33
average net household income for 2 adult/2 child household: 60per cent/65per cent	87.75/95.0
<i>Minimum Income Estimate for a Single Adult from Other Methods</i>	
stated minimum income, single person households depending on social welfare: elderly/non-elderly	82.6/90.95
stated minimum income, 2 adult/2 child households depending on social welfare	75.11
average net household income, all households:	
50per cent ^a	67.5/71.5
60 per cent ^a	80.75/85.75
CSW Priority Rate Upated in line with prices	60.99
CSW recommended range upated in line with prices	67.77/81.32
<i>Social Welfare basic weekly payment rate</i>	
Contributory Old Age Pension (Under 80)	75.00
Widow's/Widower's Contributory Pension	68.10
Non-Contributory Old Age Pension (Under 80)	64.50
Widow's/Deserted Wife's/Prisoner's Wife's Non-Contributory Pension	
Unemployment and Disability Benefits	
Long-term Unemployment Assistance	
Short-term Unemployment Assistance	62..40
Supplementary Welfare Allowance	

^a Equivalence scale 1/0.66/0.33.

It is also important to emphasise how far the social welfare rates being paid in 1985 fell below the bottom of the range the CSW then recommended. Only

contributory OAP reached the bottom of that range, non-contributory pension for a single adult was 88 per cent of the bottom, UB/DB were about 80 per cent, long-term UA was 70 per cent, and the lowest rates then payable, for short-term UA and SWA, were only 64 per cent. Considerable convergence in rates has taken place since then. Increases in social welfare since 1986 have given priority to bringing up what were then the lowest rates of payment. Single adults on contributory or non-contributory old age pension have seen their rates rise by about 7 per cent in real terms, UB and DB rates rose by 20 per cent, but the increases in UA and SWA have been between 35 per cent and 44 per cent. This has brought the lowest rates a good deal closer not only to adequacy benchmarks indexed to prices but, for the lowest paying schemes, also to those indexed to average net earnings. Average net industrial earnings rose by 23 per cent in real terms, but this quite rapid rise was substantially exceeded by the rate of increase implemented for the lowest-paying schemes. Support rates for the elderly, on the other hand, have lagged significantly behind real net earnings. Growth in average net equivalent household income has however been rather slower than growth in earnings.

In addition to giving priority to increasing what were the lowest payment rates in 1985, the most substantial increases in rates since then have been for the single adult case on which the CSW concentrated. Increases for child and more particularly for adult dependants have been lower, with the result that the equivalence scales implicit in social welfare schemes now look rather different to 1985. For UA and SWA, the extra payment for an adult dependant in 1985 came to about 72 per cent of the rate for a single adult, whereas by 1996 that figure was down to 60-62 per cent. The latter is in line with the relativity recommended by the CSW, but that recommendation was not based on an in-depth examination of the issue. A marginal decline in the payment for children (including Child Benefit) relative to the personal rate has also been seen.

In assessing the adequacy of the basic rate of cash transfers, other forms of assistance available to recipients either in the form of additional cash payments or non-cash benefits also have to be taken into account. Such additional cash and non-cash benefits have increased in importance since the CSW reported. The various benefits involved and the types of recipient entitled to receive them was set out, and an attempt was made to assign each a value. The most important were seen to be entitlement to medical card cover, assistance with heating and energy costs, and direct or indirect housing subsidies. These extra benefits are most important for the elderly and long-term social welfare recipients. Some illustrative examples showed that extra benefits could add up to 20 per cent to the value of basic cash support. This could clearly make a considerable

difference in the assessment of the overall value of support *vis-à-vis* adequacy benchmarks derived from, for example, average income. However, entitlements to these extra benefits vary a great deal by scheme and across households in different circumstances, assigning them a value is in some cases problematic particularly for housing, and simply adding an average estimated value for these benefits to the basic payment rate is not particularly meaningful. The extended role of these benefits clearly needs to be taken into account in assessing the evolution of income support rates since the CSW reported, and ways of taking them fully into account in the derivation of adequacy standards need to be developed.

9.6 Assessing the Direct Impact on Poverty

In order to assess the likely impact of implementing alternative adequacy standards, four different payment rates were chosen which spanned most of the range of standards identified in earlier chapters. The lowest rate considered was £68 in 1996 terms, with rates of £75, £82 and a rate of £90 (close to the top of the range) also being considered. Exploring the likely impact of implementing such payment rates is a difficult and complex task. Changes in welfare rates, particularly those involving very substantial changes in relative terms, can have far-reaching implications not only for those dependent on welfare, but for the wider labour market and the economy in general.

The policy packages examined included increases in FIS income limits, designed to maintain work incentives for families with low incomes relative to their needs. We found that the costs of payment rates at £68, £75, £82 and £90 per week were approximately £160m, £530m, £940m and £1,400m per annum (all in 1996 terms). These sums equate to tax cuts forgone or tax rate increases of about 1+ percentage points, 4 to 5 percentage points, 8 percentage points and 11 or 12 percentage points respectively in all tax rates (standard rate, top rate and marginal relief rate). These calculations are based on a technical assumption that there would be no change in behaviour associated with the package. Possible impacts on incentives and behaviour were considered at a later stage, but are central to an overall assessment of the alternative payment rates.

Within this framework of analysis, we found that for the £68 payment package, just under half of the additional social welfare expenditure would go towards reducing income shortfalls relative to that £68 target; and the package would close about one-quarter of the aggregate gap relative to that income standard. For the £75 per week package, about 55 per cent of the additional expenditure would go towards reducing the income shortfalls, and more than half of the initial income gap would be closed. At the highest standard considered (£90 per week), almost 60 per cent of the additional expenditure would be "on target" and about 70 per cent of the initial income shortfall would be reduced –

again, on the technical assumption of no change in labour market or other behaviour.

Overall, the results indicate that increases in social welfare payments could, on the technical assumption of no change in behaviour, have a substantial impact on rates of income poverty – whether measured by the numbers falling below income poverty lines, or income shortfalls relative to that line. But a substantial proportion of the additional expenditure does not go towards reduction of poverty at the relevant income standard; and some of the income shortfalls are not amenable to reduction through increases in welfare payments as some individuals on low incomes find themselves ineligible for any scheme. The factors underlying this deserve further investigation, but complete effectiveness and efficiency would require pound for pound withdrawal of benefit above the target income standard, with very serious implications for incentives.

9.7 Assessing the Impact on Work Incentives

Given the overall budgetary constraints, and in particular, the net revenue which the tax-transfer system must generate to finance other government expenditures, there is a trade-off between the level of income support and the effective tax rates on income from employment. This trade-off is brought into very sharp relief by simple tax-transfer systems, such as proposals for a basic income (see Callan, O'Donoghue and O'Neill, 1994); but it is also inherent in more conventional systems including the current Irish tax-transfer system.

It should come as no surprise, therefore, that an increase in social welfare payment rates, from a base of around £64 per week in 1996 terms, to a level of £90 per week (with corresponding increases in adult and child dependant rates) should involve sharp increases in taxes, and a substantial worsening of financial incentives to work. For example, the £90 per week payment package involves a tax increase (or tax cut forgone) of 12 percentage points in the standard and top tax rates, affecting upwards of 800,000 individuals; and would lead to a situation in which about 30 per cent of employees, and 64 per cent of the unemployed would face replacement rates of more than 70 per cent. In our view these dramatic changes in the financial incentives to work would lead to significant reductions in labour supply and employment, and increased unemployment.

A more modest increase in social welfare rates, to a level of around £68 per week, would have a much lesser impact on work incentives. It could be financed by an increase in tax rates (or a tax cut forgone) of about 1+ per cent. The impact on the distribution of replacement rates would be much less dramatic. The proportion of employees facing "high" replacement rates (over 70 per cent) would rise from just under 16 per cent to just over 18 per cent, while the proportion of unemployed persons facing high replacement rates would rise from

31 per cent to about 39 per cent – but with most of the increase occurring in the 70 to 80 per cent replacement rate bracket.

In the present context, we see the analysis of work incentives as a crucial part of the overall assessment of adequacy of payment rates. Any assessment of adequacy which fails to take account of the impact on incentives runs the risk of focusing on payment rates which could be unsustainable. We have seen that the £90 per week payment rate, in the present economic context, involves very substantial deterioration in financial incentives to work. This, in turn, could lead to reductions in employment and a diminution in the tax base which would create a requirement for further increases in taxes.

The direction, and to some extent, the magnitude of the impact on work incentives, is reasonably clear from our analysis. But estimates of the likely behavioural response to packages of the type analysed here are not currently available, and are of central importance in establishing the crucial trade-offs between income support rates, employment and poverty. A number of approaches can offer helpful insights into these central questions, including the estimation and simulation of labour supply responses at micro-level, macroeconomic modelling, and, in time, approaches combining information from micro- and macroeconomic models. Such research can assist not only in assessing the trade-offs between different levels of income support, but in improving the efficiency of the tax/transfer system at any given level of income support.

9.8 Uprating Social Welfare Rates

The way in which social welfare rates are uprated from one year to the next, and in particular how adequacy considerations enter into these decisions, was another important issue to be addressed. An examination of the approaches to uprating social welfare rates publicly articulated by different Irish governments over the past twenty-five years showed that, despite a good deal of variation in content and in the extent of explicit pre-commitment, there were a number of consistent themes. The first and most commonly-accepted aim was to protect the value of social welfare payments for pensioners against inflation, and where possible to extend the same protection to others relying on social welfare. The second consistent theme was concern about work incentive effects. A third theme is adequacy: rates should be increased to the point where recipients can afford the basic minimum standard of living. A fourth theme was the desirability of social welfare recipients sharing in improvements in the living standards of the community as a whole. Finally, throughout the period rates increases were set in the context of affordability in terms of the state of the economy and the public finances. The interaction of these objectives and constraints over the twenty years from 1976 was shown to have produced a significant increase in

basic support rates for the unemployed as a proportion of take-home pay in industry.

How should this crucial element in social welfare policy be approached in the future? In this study we have repeatedly emphasised that both the level of social welfare rates at any point in time and changes in these rates over time are matters of societal choice exercised through the political process, and that adequacy itself is only one element and cannot be set apart from considerations of efficiency and the desired degree of redistribution. The point of departure for the present study is however the CSW's concept of adequacy, so we have focused on how that notion of adequacy, if wholeheartedly embraced, might be taken more fully and explicitly into account in the uprating process. The first point made in this context is that the manner in which the rates recommended by the CSW have tended to be employed in uprating so far – as a target which moves upwards over time only in line with prices – is clearly inconsistent with the Commission's underlying approach to adequacy.

If adequacy is to be assessed against the standards of the society in question at a given point in time, as the CSW envisaged, the target will move up over time as general living standards in the community rise. However, many questions remain to be tackled as to the nature of that relationship and how it is best incorporated into the decision-making process. Most importantly, what indicators of "general" living standards are most appropriate, and how is the adequacy standard to be linked to those indicators? The information currently available for Ireland from which such indicators might be constructed is extremely limited, and we have highlighted priorities for development in that area. These include more regular and comprehensive data on earnings and household incomes and their distribution, and on other non-monetary indicators of general living standards.

However, progress can still be made towards a more explicit process of evaluating adequacy in uprating using the data currently available. Changes in consumer prices, in average take-home pay and in average income per head excluding social security transfers provide three indicators to which specific reference could be made in assessing how an adequacy standard was changing over time. Using these indicators in the way suggested in the European Union's Minimum Income Recommendation to regularly and publicly review changes in what constitutes an adequate income in the Irish setting would be a major step forward, and would in itself highlight the need for more comprehensive information. Implementing such an explicit assessment of the way in which an adequacy standard is changing over time does not imply either that the standard itself has to be derived as a fixed proportion of average earnings or income, or that adequacy will then be the only consideration in making decisions about the

way rates are actually updated. Indeed, a complementary exercise assessing the efficiency and incentives aspects of the evolution of social welfare rates and secondary benefits *vis-à-vis* income from work, again carried out on a regular basis and made publicly available, would also be a valuable input into the decision-making process. In such an environment, both public debate and political choices about social welfare rates, adequacy and economic efficiency would be better informed and necessarily more explicit about the hard choices involved.

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