FINAL REPORT OF THE SOCIAL WELFARE BENCHMARKING AND INDEXATION GROUP

(Established under the Programme for Prosperity and Fairness)

September 2001

This report includes the result of analyses conducted by the Working Group using SWITCH, the tax-benefit model developed at the ESRI. The model is described in *Simulating Welfare and Income Tax Changes,* by T. Callan *et al,* Dublin: ESRI, 1998. No responsibility for the analyses in the present document is accepted by the ESRI or by the authors of the model software.

CHAPTER 1 - Introduction

1.1 <u>Background</u>

1.1.1 Section 3.2.3 of the Programme for Prosperity and Fairness (PPF) provided for the establishment of a Working Group to examine the range of complex issues associated with the benchmarking and indexation of social welfare payments. The Social Welfare Benchmarking and Indexation Working Group was established in late 2000. The Group comprised representatives from the social partners and relevant Government Departments (see Appendix A) and was chaired by an independent Chairperson - Professor Kieran Kennedy, former director of the Economic and Social Research Institute (ESRI). The Secretariat to the Group was provided by the Department of Social, Community and Family Affairs.

1.1.2 The origins of the PPF commitment were contained in the 1999 NESC Report - "Opportunities, Challenges and Capacities for Choice". The report developed the debate around the establishment of a benchmark for adequacy for social welfare payments and set its commentary in the context of the achievement of the Commission on Social Welfare's recommended minimum rate for all social welfare payments in 1999. The Council recommended that social welfare payments be linked to improvements in the general standard of living and provided a number of options to progress this objective (see Chapter 4).

1.1.3 The PPF envisaged that the Group would report by April 2001. Given that the Group did not commence its deliberations until December 2000, and given also the complexity of the issues involved, this original deadline was acknowledged to be unrealistic. Instead, the Group fixed the end of July 2001 as the deadline for the conclusion of its deliberations, in order that its findings could feed into the 2002 Budgetary process. An Interim Report was published by the Group in April 2001.

1.2 <u>Terms of Reference</u>

1.2.1 The terms of reference of the Group were drawn from the PPF and required it to:

i) examine the issues involved in developing a benchmark for adequacy of adult and child social welfare payments, including the implications of adopting a specific approach to the ongoing uprating or indexation of payments, having regard to their long-term economic, budgetary, PRSI contribution, distributive and incentive implications, in light of trends in economic, demographic and labour market patterns; and

ii) examine the issue of relative income poverty.

1.3 Methodology

1.3.1 The Group interpreted its terms of reference to require it firstly to consider the concepts of benchmarking and indexation and, secondly, to test suggested benchmarks and/or indexation methods against each of the criteria mentioned above - i.e., to assess their economic, budgetary and social insurance impacts, and their effects on income distribution and on employment incentives. It interpreted the requirement to assess the impacts of any measures proposed on income distribution to mean that regard must be had to the question of the adequacy of the payment rates. The issue of non-cash benefits is of relevance here. The Group took the view that, notably in relation to indexation methods, account must be taken of the practicalities associated with any option being considered.

1.3.2 In examining those aspects of the terms of reference which required the Group to address distributional and incentive implications, the most effective tool available to the Group was the SWITCH tax-benefit model developed at the ESRI. The underlying database in SWITCH is based on a representative cross-section of the population from the Living in Ireland Survey. While the overall numbers of welfare claimants contained in the model correlates broadly with the overall actual numbers known to exist currently, this correlation does not extend in all cases to the numbers in receipt of specific welfare payments. In order to validate the results generated in relation to the distributional and incentive implications of the various illustrative benchmark and indexation options considered, the costings produced by the SWITCH model were cross-checked against DSCFA-generated estimates. The results from this exercise are described in detail in Chapter 4.

1.3.3 The Group operated in parallel with the wider review of the National Anti-Poverty Strategy (NAPS) which was progressing in accordance with the terms of the PPF. While the Group was not a formal element of this wider review, it was intended that its work would help to advance consideration of the theme of income adequacy and income poverty measurement.

1.4 Outline of Report Structure

1.4.1 The aim of this Final Report is to fulfil the terms of reference in the PPF and examine the issues involved in developing a benchmark for adequacy of social welfare payments and the implications of adopting an indexation methodology. Issues associated with the measurement of relative income poverty are also discussed.

1.4.2 *Chapter 2* examines the concept of income adequacy and explores the issues associated with determining an adequate income level. Examples of the types of approaches which have been taken in trying to establish an adequate income are described.

1.4.3 *Chapter 3* provides a context for the discussion on benchmarks and indexation methodologies. It sets out current Government and social partnership commitments of relevance to the Group's work. It looks at the trends in demographic, labour market and economic patterns and seeks to highlight the key areas of concern insofar as welfare rates policy development is concerned. The issue of social insurance is also considered.

1.4.4 *Chapter 4* examines four illustrative benchmark options which have been considered by the Group, representing a range of payment levels, and analyses these options against the various criteria set out in the terms of reference. Three of these options were drawn from the National Economic and Social Council's 1999 report - "Opportunities, Challenges and Capacities for Choice" - while the fourth is based on a recommendation from the Report of the Pensions Board - "Securing Retirement Income" (1998).

1.4.5 *Chapter 5* examines the issue of child-related payments - Child Benefit, Child Dependent Allowances, and Family Income Supplement. It discusses research undertaken in relation to establishing a level of income adequacy for children. The issues of equivalence scales and child poverty are addressed.

1.4.6 Indexation methodologies are discussed in *Chapter 6*, examining the various indices which may be used for the uprating of social welfare payments and the benefits and drawbacks of each approach.

1.4.7 *Chapter 7* looks at the issue of relative income poverty and discusses the factors which influence the trends in this poverty measure. A discussion on the relative merits of relative income poverty and consistent poverty is also included.

1.4.8 Finally, *Chapter 8* sums up the conclusions reached by the Group and sets out its recommendations.

1.5 Secretariat

1.5.1 The Working Group wishes to record its gratitude to the Secretariat of the Group, Mr Eoin O Seaghdha and Mr Ciaran Lawler. The Group's desire to submit a Final Report in time to feed into the budgetary process for Budget 2002 left a short time to cope with the complexities of the issues under consideration, and added to the already heavy burden borne by the Secretariat - a burden which they carried cheerfully and skillfully throughout. The Group deeply appreciates the dedication and expertise manifested by the Secretariat in the course of this work.

CHAPTER 2 - Adequacy

2.1 Background

2.1.1 The Group's terms of reference required it to examine the issues involved in developing a benchmark for adequacy of adult and child social welfare payments. It was acknowledged at the outset that it is not possible to derive, in an objective and scientific way, a definition of income adequacy which is universally acceptable, since any assessment is necessarily subjective. Indeed, the terms of reference did not require the Group to attempt to undertake such a task, but rather required it to have regard to a range of criteria in its deliberations on the issue of adequacy. It is possible, however, to agree a definition of adequacy expressed in conceptual terms. In this regard, it was noted that the PPF states that one of the objectives under the heading of income adequacy is *"to provide every person with sufficient income to live life with dignity"*[1]. This wording, in turn, echoes the income adequacy objective in the National Anti-Poverty Strategy adopted by Government[2] which states*:* *"Policies in relation to income support, whether these policies relate to employment, tax, social welfare, occupational pensions or otherwise should aim to provide sufficient income for all those concerned to move out of poverty and to live in a manner compatible with human dignity*."

2.1.2 In one sense, therefore, the task the Group faced was to seek to reconcile the broader PPF objective described above with the very specific criteria set out in the terms of reference.

2.1.3 As outlined, the objective of income adequacy is 'to provide every person with sufficient income to live life with dignity'. While social welfare payments play an important role in this regard, it is important to recall that the majority of people and families achieve income adequacy through income other than social welfare or through a combination of welfare and other income.

2.1.4 Income from employment, intra-family transfers, occupational and private pensions, and other sources plays a crucial role in achieving income adequacy and, in considering an adequacy benchmark, thought must be given to the relationship between social welfare and these other sources of income.

2.1.5 One of the objectives of the PPF is to 'create the condition where people can achieve economic independence' and the EU Lisbon Council established a number of targets to increase the employment rate in EU countries in the period to 2010. As OECD

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[1] Section 3.2 PPF
[2] NAPS, p.13

research has shown that the primary reason why people in OECD countries move out of poverty is due to taking up employment or an increase in income in employment[3], it is also critical from this perspective that consideration be given to the relationship between social welfare rates and employment opportunities.

2.1.6 It remains the case, however, that there are social welfare recipients who are not attached to the labour market and whose only recourse, even on a long-term basis, is to social welfare income, e.g. people who are too ill to work. In this regard, the Group noted that, while employment is the primary route out of poverty, taking up a job is not an option for some welfare claimants and the adequacy of the income of such people should be determined by reference to the level of their social welfare payment.

2.2 What do we mean by adequacy?

2.2.1 Typically, the debate on adequacy centres on three very basic questions: adequate for what?, for whom?, and for how long? The answers offered to these questions may vary widely depending on the perspectives of the respondent.

2.2.2 Adequate for What?

As noted earlier, the first objective cited in the PPF under the heading of Income Adequacy is "*to provide every person with sufficient income to live life with dignity*".

2.2.3 The Commission on Social Welfare (CSW) stated 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*".[4] The CSW concurred with Townsend's (1979) view of poverty as exclusion from the ordinary living patterns and customs. The range of methods explored by the CSW in its attempts to arrive at an acceptable minimum adequate income level for welfare claimants are described briefly in section 2.4 below.

2.2.4 The ESRI, in a report published in 1996[5], examined the methods used by the CSW in assessing adequacy . This study again produced a range of possible rates of payment. The ESRI argued that the core criterion against which adequacy of payments should be assessed is whether they are sufficient to allow recipients to cover their living costs and to avoid poverty. They emphasised, however, that neither the methods employed by the CSW nor those used by the ESRI itself "*allow one to derive in an unproblematic, objective and scientific way estimates of income adequacy which would be universally convincing".*

[3] It was acknowledged that a move from unemployment into employment may not, in every instance, equate to a shift out of poverty.
[4] CSW, 1986 p.123
[5] ESRI, A Review of the Commission on Social Welfare's Minimum Adequate Income (1996)

2.2.5 Adequate for Whom?

The welfare system is designed to provide income support to people who may be faced with one of a range of different contingencies: unemployment, illness, disability, caring, lone parenthood, widowhood, old age, dependent children, etc. It provides for both social insurance based payments and means-tested social assistance payments. Generally speaking, social insurance payment rates are pitched at a higher level, reflecting the contributory principle.

2.2.6 The question arises as to whether it is appropriate that the different nature of these contingencies should be reflected in the rates of welfare payable. In practical terms, successive Governments have taken the view that it is appropriate to do so and this is reflected in the variation in the current levels of weekly payments (ranging from £84 for short-term Unemployment Assistance (UA) to £106 for Old Age Contributory Pension).

2.2.7 Different views on this issue of relativities were held by members of the Group. While some saw little or no justification for the variation in payment rates, others contended that the variation in payment rates reasonably reflected the quite different contingencies catered for by the welfare system, and took the view that if the lowest rate is considered to be adequate, then it is open to the Government of the day to decide to allocate additional supports to particular categories of claimants to address policy objectives other than adequacy. Other issues that arise for consideration in this regard include, for instance, financial incentives to work (e.g. unemployed vs pensioners) and/or the depletion of resources over time (short-term vs long-term payments). In the circumstances, the Group agreed that the most appropriate approach lay in focusing, in particular, on the lowest current rates of payment (Supplementary Welfare Allowance (SWA) and short-term UA)[6] in considering the issue of a benchmark for adequacy of welfare payments.

2.2.8 Adequate for how long?

Townsend defined poverty as a situation arising for "*individuals and families whose resources, over time, fall seriously short of the resources commanded by the average individual or family in the community in which they live".* The position of those who are relying on social welfare on a long-term basis therefore merits particular attention. While, in the short-term, an individual may have capital both in the form of money and durable goods, this capital may diminish over time. Households may be able to supplement income for a time by using up savings or by borrowing. Thus, a level of social welfare payment sufficient to avoid poverty in the short-term may not suffice for those dependent on it over a longer period.

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[6] The Supplementary Welfare Allowance is a means-tested weekly payment, currently set at the level of short-term UA, which provides a standard basic minimum income for those in need who do not qualify for payment under other State schemes. Unemployment Assistance is a means-tested weekly payment made to people who are unemployed and who do not qualify for (the insurance-based) Unemployment Benefit (UB) or whose entitlement to UB has expired.

2.3 Non-Cash Benefits

2.3.1 As well as providing direct income support through the range of weekly welfare payments, the State also invests significantly in the provision of non-cash benefits, most notably the ‘Free schemes’ and the Medical card. For the purposes of this section, the social welfare fuel allowance is also included as a ‘non-cash benefit’ although this is a cash payment of £5 per week (£8 per week in smokeless fuel areas) payable for a 29 week period from early October to late April. In determining the level of income of a particular household, it is appropriate to acknowledge the value of these non-cash benefits since they represent a significant element (estimated at over 10% in 1997) of the State’s social welfare expenditure.[7] Caution must be exercised in doing so, however, since the impact of non-cash benefits is unevenly spread amongst welfare recipients. In considering the issue of a benchmark for adequacy of welfare payments, the Group agreed that the most appropriate approach lay in focussing, in particular, on the lowest current rates of payment (SWA and short-term UA). Recipients of these payments do not have the same entitlements to the range of State benefits as some other welfare recipients.

2.3.2 The ‘Free schemes’ (Travel, Electricity/Gas Allowance, TV License, Telephone Allowance), for instance, are predominantly made available to the elderly and, to a lesser extent, to people in receipt of disability or carer’s payments. They are not generally available to those in receipt of other welfare payments (including SWA and short-term UA).

2.3.3 The Fuel Allowance scheme is designed to assist householders who are on long-term welfare or health board payments and who are unable to provide for their own needs. It is paid subject to a household means-test. Short-term claimants (e.g. SWA and short-term UA claimants) are not entitled to avail of the scheme.

2.3.4 Medical cards are issued to those deemed by the Health Boards to be unable to afford health care for themselves and their dependants without undue hardship. Entitlement is based on a means test (although the Health Boards may, at their discretion, award a Medical Card to a person who does not satisfy the means test if it is considered that his/her particular circumstances warrant it). The income levels in the means-test are pitched above the basic welfare rates so that a household which is reliant on the welfare system for income support will qualify for coverage under the Medical Card scheme. The Medical Card entitles the holder (and his/her spouse and any dependant children) to free GP services, prescribed drugs/medicines, in-patient and out-patient hospital services, and dental, ophthalmic and aural services.

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[7] Goodbody - Disincentive Effects of Secondary Benefits (1998) p.15

2.3.5 A recently published report by the ESRI[8] examined the effect that non-cash benefits may have on the numbers below the various relative income lines. (This issue is considered in greater detail in Chapter 7.) The report noted that there are a number of methodological problems in devising values for secondary benefits and these include, for example:

- It is not known whether households would have bought the same amount of the goods or services in question if they were not provided free or at a subsidised rate;
- In general, recipients will place a value on non-cash benefits that is less than the market price of the good or service because the recipient has no choice in its allocation. (However, in a review of the Free schemes[9], it was noted that : "*The results of the surveys conducted as part of this research indicate that they* [the free schemes] *are highly valued by the recipients and are preferred to their cash equivalent*';
- According to a 1998 report[10], there is a widely held view that people place a contingent value on the Medical Card much in excess of the value imputed from estimates of average expenditure per cardholder. That is, the Medical Card is a form of insurance;
- With regard to the Medical Card, if the cost of the free or subsidised services is simply added to the household income of the people using those services, it would imply that sick people are richer than the healthy at any cash income level;
- A service which is, in principle, provided free to everyone may actually be readily available only in certain areas or to certain groups, and is in any case likely to be taken up to a varying degree by different people.

2.3.6 Notwithstanding these methodological difficulties, imputed values for non-cash benefits were drawn up by the ESRI and these are summarised below:

Table 2.1: Imputed Values for Non-Cash Benefits (per recipient)

	Yearly Value (1997) £	**Weekly Value (1997) £**
Free TV Licence	69.21	1.33
Free Telephone Rental	164.08	3.16
Free Electricity	137.63	2.65
Free Natural Gas	115.00	2.21
Free Bottled Gas	163.37	3.14
Fuel Allowance	130.00	2.50
Smokeless Fuel Supplement	78.00	1.50
Free Travel (per person)	64.23	1.24

8 ESRI, "Non-Cash Benefits and Poverty in Ireland", 2001
9 Quinn, 'A Review of the Free Schemes operated by the Dept. of Social, Community and Family Affairs' 2000
10 "The Disincentive Effects of Secondary Benefits", Goodbody Economic Consultants, 1998

2.3.7 The ESRI calculated the costs of the benefits on the basis of the cost to the State per recipient. In relation to the Medical Card, the ESRI derived its value by estimating age-specific average costs of providing the service. For GMS services, the age weights were based on the pattern of spending on pharmacy services across the age groups. For hospital services, the ESRI used the average number of nights spent in hospital by those with medical card cover from the 1987 ESRI household survey.

Table 2.2: Imputed Value for Medical Card by Age, 1997

	GMS value	Hospital value	Total yearly value	Weekly Value (1997)
Under 5	£53.35	£19.54	£72.89	£1.40
5-15 years	£44.01	£20.08	£64.09	£1.23
16-44 years	£145.01	£28.70	£173.71	£3.33
45-64 years	£329.93	£36.20	£366.13	£7.02
65 plus	£445.99	£64.80	£510.79	£9.80
All	£228.01	£34.42	£262.43	£5.03

2.3.8 In summary, there is an acceptance that it is valid to recognise the investment by the State in non-cash benefits since they provide supports which, by definition, alleviate the risk of poverty for beneficiaries. It is necessary to be cautious, however, in attributing the value of these benefits since they are not uniformly available.

2.3.9 The ESRI has noted that housing is an area which it regards as of the highest priority for in-depth research in the Irish context. However, it notes that it is particularly complex to analyse and was beyond the scope of its non-cash benefits study. "*Households paying below market rents in local authority housing are receiving an implicit subsidy from the state, improving their purchasing power on a given cash income. Valuing this subsidy is problematic, however, and a household owning its own house is also in a very different position to one with a very large mortgage.*" (Ibid: p.6). While not coming within the scope of non-cash benefits, the Group noted that there are other reliefs in respect of housing provided via the tax system.

2.3.10 While not directly related to the issue of non-cash benefits, the Supplementary Welfare Allowance (SWA) is relevant as it gives additional assistance to people on very low incomes. SWA provides a safety net against poverty in that it gives a statutory entitlement to a minimum weekly income, based on criteria set out in legislation. Apart from a number of excluded categories, anyone in the State whose means are insufficient to meet their needs is entitled to assistance under the SWA Scheme. Payment may be made in the form of a Basic

Payment, a once-off Exceptional Needs Payment (ENP) or a weekly supplement towards rent[11], dietary needs and so on.

2.3.11 The Back to School Clothing and Footwear (BSCF) Allowance Scheme is designed to assist certain recipients of social welfare and health board payments with the cost of children's school uniforms and footwear. The scheme operates from the beginning of June to the end of September. A person may qualify for a payment of the BSCF allowance if they are in receipt of a social welfare or health board payment or are participating in an approved employment scheme or attending a recognised education and training course and have household income at or below certain prescribed levels.

2.4 Approaches to Establishing a Level of Income Adequacy

2.4.1 There are numerous approaches which can contribute to the development of a view on what is an 'adequate' income and some of these methods are outlined below. The list is not exhaustive and other, equally valid, approaches could also be used. The first seven methods were those employed by the CSW in its 1986 report. The other methods listed are identified in the ESRI's 1996 report (ibid).

i) *The Food Ratio Approach*

This method examines the expenditure of food in relation to total expenditure for equivalent disposable income deciles. The CSW found that total expenditure for the fifth decile was 2.98 times food expenditure. This multiplier was then applied to the average amount spent on food by the bottom three deciles to arrive at a minimum adequate income per adult equivalent.

ii) *The Institutional Budget Method*

This method is based on the cost of maintaining an adult in prison - averaging cost per prisoner of food, heat, light, laundry, recreation, and medical supplies. The CSW added a figure from the Household Budget Survey to take into account housing and transport costs.

iii) *Average Industrial Earnings Method*

This method uses average earnings of employees in industry as the benchmark. After deducting tax and PRSI, the CSW took half of the average earnings figure as a minimum adequate income for one person using this measure.

iv) *National Accounts Personal Disposable Income Per Capita*

Total personal disposable income in the national accounts was divided by the number of persons in the labour force to give average disposable income per labour force member. This

[11] Expenditure on rent supplementation is significant, with costs of almost £120m. in 2000. The level of rent supplement payable varies, depending on the local conditions, with the maximum supplement amounting to £850 per month in the Eastern Health Board area in 2001.

figure was then halved, and an adjustment was made to allow for the non-labour force population. After using equivalence scales, a minimum adequate income figure for a single person was derived.

v) *Official Standards*

This method used official standards for qualifying for certain benefits. The CSW pointed 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" (p.472-3). The CSW took the weekly medical card threshold, calculated its annual equivalent, deducted PRSI and tax payable, and produced a net weekly amount to represent the minimum adequate income.

vi) *Low Pay JLC Method*

The CSW, under this method, took the legal minimum wage rates set by Joint Labour Committees (JLCs) for agricultural workers as an alternative "official" point of reference. The CSW calculated the net wage that would correspond to the gross weekly figure and then used 70% or 80% of this figure as a minimum adequate social welfare payment.

vii) *Average Household Incomes Method*

The final method adopted by the CSW was based on average household disposable income for different household types, as calculated in the 1980 Household Budget Survey. The average income for households comprising a couple with two children was taken, uprated to 1985 prices, and alternative "replacement ratios" of 60% and 65% were taken. The resulting figures were converted to the corresponding figure for a one-person household through the use of equivalence scales. The same calculations for couples with one child gave higher figures.

viii) *Survey-based Relative Income/Earnings Benchmarks*

Using this method, the ESRI took percentages of average disposable income per adult equivalent as an adequacy benchmark. It was found that the results were sensitive to the equivalence scale used and the implied age at which a child becomes an adult for analysis purposes. The ESRI also made the point that the choice of a percentage is entirely arbitrary.

ix) *Assessing the Adequacy of Social Welfare via Relative Income Poverty Lines*

Starting from the point that the avoidance of poverty is a central element in income adequacy, the ESRI also looked at the extent to which those relying on social welfare payments fell below relative income poverty lines. Variations in the poverty risk for those relying on different schemes were found. For example, in 1994, 69.5% of households relying on Unemployment Assistance were below the 50% line, while only 1.6% of households relying on Old Age Contributory Pension were below the same line. It was also found 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.

x) *Assessing Adequacy of Social Welfare via Non-monetary Indicators of Deprivation*
This approach examined the extent to which households relying on social welfare for their current income were experiencing basic forms of deprivation (using the same non-monetary indicators employed in the consistent poverty measure - see Chapter 7). The aim behind such an analysis is to examine the effectiveness of individual schemes at enabling households to avoid such deprivation. Again the risk varied between schemes, ranging from 9.6% for those relying on Old Age Contributory Pension to 61.1% for those relying on Unemployment Assistance (1994 figures).

xi) *The Views of Social Welfare Recipients about Income Adequacy*
In the 1987 and 1994 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?"* Results showed that, in 1994, average minimum income needs stated exceeds mean actual income for most households types (dependent on social welfare payments), with the elderly having the smallest gap and households comprising a single adult and a single adult with a child having particularly large gaps. It was found that the formulation of the question itself can affect how people respond to it. In addition, even within particular household types, responses to the minimum income question produced quite wide variations.

xii) *Budget Standard Method*
The budget standard method was used in Carney et al's study (1994), "Cost of a Child" (see Chapter 5). This method uses a "typical" basket of goods and services which may be required to have a normal or adequate standard of living and costs the items in the basket to arrive at a minimum income.

While the ESRI pointed to the simplicity and transparency of such an approach as advantages, it also stated that the subjectivity of the approach (e.g. what is included in the basket of goods; what standard of good is included?) presented problems. Similarly, there is difficulty involved in deciding whether a particular basket of goods would be considered adequate by most people. The report added that budget standards, while presenting valuable illustrations of what finance is required for a particular standard of living, should not be seen as an attempt to define an adequate standard of living. They are also time-consuming and resource-consuming to establish and maintain.

xiii) *Case Studies from Money Advice Centres*

The ESRI warned against drawing any inferences about the adequacy of incomes, based on case studies of those receiving assistance from Money Advice Centres, particularly because the people concerned are not representative of low-income households but are referred to the Centres on the basis that the scale of debt is so large and unmanageable. The point has also been made that such case studies can be used to support arguments from opposite viewpoints. For example, the fact that people have to attend money advice centres in the first place can be used to argue that welfare payments are inadequate. On the other hand, it can be argued that, as the centres can assist people in easing and/or resolving their financial difficulties, it is budgeting within the household that is the problem rather than the level of payments.

xiv) An International Perspective

Finally, the ESRI looked at comparative rates of social welfare between Ireland and other EU states (with a particular focus on the UK). It found that, in 1994, Irish social assistance rates relative to earnings were not far below the EU average, but social insurance rates were very far below the average. In addition, it found that Ireland had replacement rates higher than the UK, Italy and Greece but similar to or lower than many other EU member states.

While the figures used are obviously now out of date, as a method in itself, the ESRI stated that comparisons with other states have to be qualified for a number of reasons. For example, income support levels for the unemployed are set everywhere with an eye to incentives as well as adequacy, and institutional structures and traditions differ across countries. The authors conclude (p.63) that is therefore not 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*."

2.5 Other sources of information

2.5.1 In the course of its work, the Group was presented with the summary results of a small-scale study, which had recently been undertaken by the Vincentian Partnership for Social Justice. While this 'Family Income Study' was not (and did not purport to be) a statistically robust exercise, its stated aim was "*to investigate in some depth the reality faced by households struggling to exist on low incomes by undertaking a study of living standards and budget choices*."

2.5.2 The study pointed to significant levels of indebtedness amongst those who participated in the study, highlighted the particular problems faced by one-parent families both in terms of incomes and access to employment/childcare, and drew attention to the nutritionally inadequate diets of many of the participants.

2.5.3 A review of the Money Advice and Budgeting Service[12] identified a number of factors contributing to indebtedness amongst clients of the service and these included: low or insufficient income; lack of budgeting skills/poor management or mismanagement of money; impact of difficult life events (death, marital breakdown, separation etc.); poor health; and addiction.

2.5.4 While the results of such studies, viewed in isolation, must be treated with caution (see, for example, Section 2.4.1 (xiii) above), they can provide valuable insights into the difficulties which may be faced by those depending on the welfare system for income support and represent a useful addition to more robust research efforts.

2.6 National Pensions Policy Initiative and adequacy considerations

2.6.1 The recommendations made by the Pensions Board in their 1998 report[13] were developed in the context of the Board's desire to form a judgement as to the reasonable level of income for older people which would meet social justice criteria and reflect society's concern to protect this group who, in the main, are not in a position to compete for income or to take advantage of labour market opportunities. The Board stated that "*the search for an objectively agreed income to avoid poverty is an unattainable goal. This does not, however, prevent a political/societal judgement being made about what is a reasonable level of income for older people ...*".

2.6.2 In that respect, the Board recommended that it would be desirable, over time, to increase social welfare pensions to 34% of the previous year's average industrial earnings. This figure was at the upper-end of the ESRI's recommendations in its 1996 report (ibid). It should be noted that it was not, in itself, a specifically constructed estimate of what would be adequate for an older person to live on but was chosen because it lay at the upper end of the revised CSW minimum estimates and was, in the view of the Board, the "*best strategy in order to, firstly, minimise the risk of poverty and, secondly, provide coverage to lower income people in the most efficient way*". In considering a benchmark for social welfare pensions, the Board stated (page 114) that "*to the extent that adoption of higher rates for old age pensions could create a political climate in which equivalent increases in other social welfare rates become inevitable, there could be several undesired side-effects, including additional fiscal cost and possible disincentive effects for employment and economic expansion. ... the Board considers that ... it would be inappropriate to link increases in retirement and related pensions directly with other social welfare payments*".

2.6.3 The benchmark recommended by the Pensions Board is discussed in some greater detail in Chapter 4. It should be noted at this point, however, that the Department of Finance

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[12] Eustace & Clarke, National Evaluation of the Money Advice and Budgeting Service (August, 2000)
[13] Pensions Board, 'National Pensions Policy Initiative', 1998

dissented from the Pension Board's recommendation, being unable to support any rate explicitly linked to earnings.[14] Furthermore, the employers' representatives on the Board, "*while recognising the aspiration of the Board contained in the recommendation, pointed out that defining a precise target for First Pillar pensions for the purposes of achieving such objectives as the avoidance of poverty in old age and assisting with ensuring adequacy of pension provision, is a complex and difficult issue*." Accordingly, they did *"not give unconditional support to the Board's recommendation.*" (p.88, Ibid.)

2.7 Comparative Approaches

2.7.1 In its submission to the Group, the Combat Poverty Agency[15] referred to the approach in a number of other countries to the establishment of a Minimum Income Standard (MIS).

2.7.2 A clear distinction must be drawn between a MIS and a minimum income guarantee (i.e. the basic rate of payment available through the welfare system). A MIS is defined as "*a political criterion of the adequacy of income levels for some given minimum real level of living, for a given period of time, of some section or all of the population, embodied in or symbolised by a formal administrative instrument or other construct."*[16] It is, in effect, a policy tool which can be used to assess the adequacy of all aspects of the income maintenance system, including welfare payments, minimum wage rates, tax thresholds, etc.

2.7.3 The approach adopted to the use of MIS in various EU and OECD countries varies considerably. In such countries as France, Belgium, Netherlands and Sweden, the income standard is related to levels of pay or minimum wages. In Australia, Finland and Norway, the standard relates to social security benefits/pensions. Amongst the countries where the income standard is related to basic welfare rates are Germany, the United States and New Zealand. The following includes an example from each of these approaches:

- France: The MIS is the statutory minimum hourly pay rate (SMIC). It was originally based on subsistence budgets and represents a 'family wage'. The SMIC is updated by changes in prices and wages and can be differentiated from the RMI, France's minimum welfare payment.
- Finland: The minimum pension for an individual serves as the MIS. It asserts a basic decency threshold for pensioners, independent of social assistance payments. The minimum pension informs welfare rates, tax thresholds and maintenance orders. Welfare payments were increased from 44 per cent to 80 per cent of the minimum pension reflecting a shift from a subsistence focus to an emphasis on reasonable living standards.

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[14] 'National Pensions Policy Initiative', 1998 - Section 5.2.5 (pps 116 - 118)

[15] CPA, "How much is enough? - setting an inclusive minimum income standard" - April, 2001

[16] Veit-Wilson "Setting adequacy standards: How Governments define minimum incomes" 1998.

- USA: three measures based in different ways on household or food budgets designed for very low levels of living were variously used as federal government MIS: the 'Orshansky' poverty measure; the Bureau of Labor Statistics 'Lower Living Standard Income Level'; and the Department of Agriculture 'Thrifty Food Plan'. In addition, two statistical measures based on Median Family Incomes in local areas were used to determine entitlement to some low income housing benefits.

2.7.4 In determining what equates to an adequate income, Veit-Wilson (ibid) notes that Governments usually arrive at a standard that is based on a broadly political - rather than academic - approach. It is necessary, however, to have a sustained and wide-ranging programme of research in order to inform this political process. A lack of comprehensive and up-to-date data in such areas as earnings, household incomes, general living standards, etc., represents a significant barrier to a comprehensive understanding of adequacy (and to progressing the MIS concept, if such an approach were to be considered appropriate).

2.7.5 The Group considers that there is scope for additional investment in the areas of data-collection and research. In this regard, the following areas may be considered:

- *Macro-economic analysis* of the impacts of increased welfare expenditure.
- *Scientific budget studies* using the evidence of actual standards of living, for both adults and children, and public opinion about necessities to construct 'modest but adequate' or 'low cost but acceptable' (or other) budgets for households of a variety of sizes and compositions;
- *Nutritional surveys* in order to study the levels of income at which household members fail on average to achieve the levels of nutrient intake which government scientific advisers recommend;
- *Educational surveys* to determine the correlation between poor educational experience and low incomes;
- *Focus group research* to discover what people see as the minimally decent levels of living and the disposable income levels at which they can be achieved.

CHAPTER 3 - Context

3.1 CSW Benchmark for Social Welfare payments

3.1.1 Policy in relation to the adequacy of social welfare payments has been influenced in large part by the recommendations made in the 1986 report by the Commission on Social Welfare (CSW). Since 1986, successive Governments have progressed towards the target of moving all social welfare rates above the minimum rate (£50 in 1986 terms), uprated by inflation, recommended by the Commission. This benchmark was finally attained for the lowest welfare rates in 1999.

3.2 Programme for Prosperity and Fairness (PPF)

3.2.1 It was against that background that the PPF provided for a fresh examination of the issues associated with setting a new benchmark for adequacy of welfare rates. The underlying aims of the PPF are to:

- keep our economy competitive in a rapidly changing world;
- provide a strong basis for further economic prosperity;
- improve the quality of life and living standards for all; and
- to being about a fairer and more inclusive Ireland.

3.2.2 The PPF contains a number of specific commitments in relation to social welfare rates. The most significant of these commitments are outlined below:

- In the context of the increased living standards provided for in the PPF, substantial progress will be made over the period of the Programme towards a target of £100 per week for the lowest rates of social welfare;
- All rates of social welfare will be increased in real terms over the life of the PPF. The rate of increase will reflect the availability of resources and increasing rates will have a high priority in the event that economic growth in excess of the expected rate on which the PPF is based generates additional resources;
- Child Benefit, as a key mechanism to reduce levels of child poverty and to provide child income support, will be substantially increased over the period of the PPF, with a priority focus towards £100 per month for the third and subsequent children;

3.2.3 Further notable commitments have been made by Government which were of relevance to the Group's work. Specifically, these are that:

- Investment in Child Benefit, including Budget 2001 increases, will be increased over three years (i.e. 2001-2003) by £1 billion;
- Over the period to 2002, all old age pensions will increase in line with average industrial earnings;

- All old age pensions will be increased to £100 per week by 2002;
- Qualified Adult Allowances (QAAs) will be brought up to 70% of the appropriate personal rates over the period up to 2002.

3.3 Demographic, economic and labour market trends

3.3.1 The Group's terms of reference required it to have regard to demographic, economic, and labour market trends in considering the issue of a benchmark for adequacy of welfare payments.

3.3.2 Demographic trends

The Central Statistics Office regularly publishes demographic projections – the most recent being its 1999 publication, 'Population and Labour Force Projections, 2001-2031'. Population projections are subject to a number of variables – notably fertility rates and migration levels.

3.3.3 The CSO report suggests that:

- the population of the State will exceed 4 million by 2006 if current migration and fertility patterns continue;
- In the long-term, births will experience a decline due to the expected fall in the number of females in the prime childbearing age group, 20-39;
- The 'old' population (i.e. persons aged 65 years and over) is projected to double between 1996 and 2031 under all combinations of assumptions chosen. The relevant population will be around 850,000 in 2031 compared with the 1996 level of 414,000;
- The 'very old' population (i.e. those aged 80 years and over) is projected to increase from its 1996 level of 90,000 to over 200,000 in 2031;
- The labour force is projected to increase from its 1998 level of 1.62 million to just under 2 million by 2011 assuming continuing net-inward migration. This would represent an average annual gain of 28,000 persons;
- Over two-thirds of the projected change in the labour force will result from demographic rather than labour force participation factors;
- The female share of the labour force, which stood at 40%, is projected to increase to 43%.

3.3.4 The major demographic trend over the medium to long-term is population ageing. This process is already underway but is not expected to gather pace until the period beyond 2006.

3.3.5 Table 3.1 below sets out demographic projections for the period 1999 to 2056 - these essentially comprise a rolling forward to 2056 of the projections contained in the CSO report (ibid).

3.3.6 The obvious consequence of population ageing is that it will have a negative impact on the dependency ratio – i.e. the population of dependent age expressed as a percentage of the population of working age. In this context, it should be noted that there is obviously a higher degree of certainty associated with estimates of the elderly population than any other population category (because all those aged 65 years or over during 2056 will have been born before 1 January 1992).

Table 3.1: Total Population and Dependency Ratio 1999 - 2056

Total Population (000s)	1999	2001	2006	2011	2016	2026	2036	2046	2056
0-19 years	1170	1150	1130	1130	1150	1070	960	920	860
20-64 years	2150	2230	2420	2530	2560	2580	2530	2320	2130
65+ years	420	430	460	510	590	760	930	1090	1120
TOTAL	3740	3810	4010	4170	4300	4410	4420	4330	4110
Total over 80s	90	100	110	120	130	170	240	290	340
Old Age Dependency Ratio	20	19	19	20	23	29	37	47	53
80+ years Dependency Ratio	4	4	5	5	5	7	9	13	16
Total Dependency Ratio	74	71	66	65	68	71	75	87	93

3.3.7 The demographic projections incorporate net migration figures as follows. As with all projections, it is recognised that these may err in either direction.

Table 3.2: Assumed Migration

	2001-2006	***2006-2011***	***2011-2016***	***2017-2056***
Net Inward Migration (annual average)	15,000	10,000	5,000	zero net

3.3.8 It will be seen from Table 3.1 that it is projected that the number of persons aged 65 and over will rise from 430,000 in 2001 to some 1.1 million in 2056. The share of the total population aged over 65 rises from 11% in 2001 to 27% in 2056.

3.3.9 A number of points emerge in relation to the issue of dependency.

- In the period to 2011, the old-age dependency ratio (the numbers aged over 65 relative to the numbers of working age) will remain stable. Thereafter, it begins to increase quite sharply, almost doubling by 2036;
- The dependency ratio for those aged over 80 begins to increase from 4:100 to 5:100 in 2006, and again starts to increase sharply after 2016. While this category is a subset of

the numbers aged over 65, the costs associated with it will be higher in terms of healthcare, etc;

- ❖ In terms of overall dependency (the combined total of persons aged under 20 and over 65 years for every 100 persons of working age), the ratio actually decreases in the short to medium term, and only matches the 2001 level (71:100) by 2026. Thereafter it rises very sharply, as the retired population more than offsets the projected decline experienced in relation to the young population. The total dependency is predicted to rise by a projected 30 per cent from 71:100 in 2026 to 93:100 in 2056;
- ❖ The key point that must be borne in mind in relation to the overall dependency ratio is that it is the components of the ratio which are of greatest relevance - i.e. the extra cost of the increase in old age dependency will outweigh any decrease in child dependency.

3.3.10 The implications of this change in the demographic structure will include a significant increase in the proportion of welfare expenditure relating to pensions. The significance of this phenomenon is reflected in the Government's decision to establish a Pension's Reserve Fund to partly offset the increased costs involved from 2026 onwards. The ageing of the population will also carry implications in relation to long term care and healthcare costs. These expenditure pressures will come at a time when there are proportionately less taxpayers to fund that expenditure. In the short term, there are high priority expenditure pressures on, for example, the infrastructure, health and pay fronts. Regard must also be had to the requirement of the Stability and Growth Pact that a broad budget balance be maintained over the economic cycle.

3.3.11 Quantitative economic analysis

It would have been helpful to the Group if a quantitative economic analysis of the impacts of the various benchmark options and indexation methodologies could have been undertaken. This would include, amongst other things, an assessment of the behavioral consequences arising from the implementation of any particular benchmark (e.g. in terms of impact on labour force participation and labour supply), an assessment of labour demand effects, potential wage impacts, potential impact on investment, competitiveness and public finances. In the event, it was not possible to commission such an analysis within the timeframe adopted for the Group's work. We do not, therefore, have quantitative estimates of the potential scale of the (indirect) effect of increased welfare rates on the wider economy.

3.3.12 PPF & economic issues

It was noted that the PPF provides for wider commitments in relation to economic issues which are of relevance - these include:

- "Sustaining economic advance will accordingly require continued observance of the following key principles, in order to maintain the competitiveness of the economy and both domestic and external confidence in its potential for growth:

- Full adherence to the spirit of this programme throughout its term;
- Conduct of fiscal policy over the programme period in a fashion which is consistent with economic stability, in particular low inflation, and which will fully adhere to the spirit of the Stability and Growth Pact;
- Conduct of tax and expenditure policies in a fashion which insures that initiatives undertaken in the course of the Programme will be sustainable to the longer term;
- Prioritisation of Public Capital Investment in order to overcome emerging infrastructure deficiencies and bottlenecks which otherwise have the potential to undermine the economic growth envisaged; and
- Continuance of the partial pensions pre-funding now in train.

- In conditions of strong growth and against a background of particularly favourable demographic trends, fiscal policy will be conducted with a goal of maintaining significant budgetary surpluses in each year of the programme. This fiscal parameter will lead to a further reduction in the burden of national indebtedness, freeing up further resources to underpin the sustainability of public policies. It therefore constitutes an overriding principle in the implementation of the Programme."

3.3.13 Labour market & economic trends

Figures provided by the Department of Finance suggest that employment growth will be sustained over the period to 2011, although the rate of growth will diminish considerably, from 3.5% in 2001 to less than 1% by 2011. At that stage, it is estimated that some 2 million people will be employed in the State.

3.3.14 The exceptional reductions in the unemployment rate experienced in recent years are not predicted to continue, with the unemployment rate remaining just above 3% for the next decade. Given the predicted growth in the labour force - an average yearly growth rate of 1.5% - the figure of 3% unemployment in 2011 represents an increase in the actual number of people unemployed. Overall, this represents an increase of 16.1% (or 292,000 people) on the current size of the Labour Force.

3.3.15 Gross Average Industrial Earnings (GAIE) will continue to increase, with substantial increases in the years to 2003 (8.5%, 8.5%, 7.5% respectively). The figures provided by the Department of Finance suggest that this will level off to slightly under 5% for most of the remaining years up to 2011. The Department of Finance also envisage that inflation will fall over the next three years, leveling off at 2% from 2004 onwards.

3.3.16 The above assessment is in line with the most widely anticipated economic scenario over the coming years - a relatively benign outlook of continuing growth, albeit at a considerably slower rate than recent years, slower expansion of the labour force, unemployment remaining at around the current low levels and inflation gradually converging down towards continental European levels. While this scenario is not without risks and will inevitably be subject to some peaks and troughs, the medium term outlook is generally favourable.

3.3.17 Labour market impacts

There are a variety of ways, both positive and negative, in which welfare expenditure can impact on the labour market and on the wider economy.

3.3.18 Employment disincentives/supply of labour

The level at which welfare payments are set and the conditions under which benefits are paid will influence the incentive to take up or remain in employment. Obviously, there are other important factors affecting employment incentives. The financial incentive is generally measured by examining replacement ratios - the net income available to a person in receipt of unemployment payments expressed as a proportion of the net income of that same person were s/he to take up employment at a particular rate of pay. In general, it is considered that replacement ratios in excess of 70% are undesirable (although there are differing views on this point). (In Chapter 4, the impact on replacement ratios of various benchmark options are considered in order to gain a perspective on the likely effects on employment incentives.)

3.3.19 It is recognised that the financial return from employment, as measured by replacement ratios, will not, however, capture the full range of factors which influence the take-up of employment opportunities. Such other factors may include, for instance, duration of unemployment, skill levels, the nature and quality of the job on offer, the potential for advancement and promotion, the scope for overtime, the local community ethos, the extent of occupational benefits, and personal fulfillment. A considerable amount of analysis of the broader issues relating to incentives has been undertaken elsewhere - see, for example, 'Integrating Tax and Social Welfare' (June 1996) and 'Tax and Welfare Changes, Poverty and Work Incentives in Ireland, 1987-1994' (Callan and Nolan, ESRI).

3.3.20 A further concern in relation to the supply of labour is that short-term disincentive issues may have more serious longer-term effects. This issue stems from the impact of high replacement ratios, which reduce the incentive to seek and take up work, and lead to an increase in the duration of unemployment. In turn, skills are lost or eroded and work habits decline as the duration of unemployment increases, and it becomes increasingly difficult to secure employment at an acceptable wage. Those affected may become discouraged and effectively opt out of the labour force, and thus become increasingly dependent on the welfare system for income support.

3.3.21 A particular point of interest relates to the eligibility criteria associated with unemployment payments. The OECD Employment Outlook, for instance, makes the point that eligibility criteria which make the payment of benefits conditional upon jobsearch and related behaviour "can offset, or even reverse, the disincentive effects which arise when benefits are paid without such conditions". The study highlights the fact that the manner of implementation of eligibility criteria is probably more important than 'enacting strict legislation'. The key point which can be drawn from this study is that "net replacement rates and durations of benefits alone are not decisive for the incentive impact of a benefit system, which can be properly assessed only by analysing them together with eligibility criteria".

3.3.22 It is necessary to apply caution, therefore, when the effects of welfare increases on replacement ratios are being considered. Where welfare increases contribute to an increase in replacement ratios, and a consequent worsening of the incentive to take up employment, this does not, of itself, represent a justification for lower welfare rates. There is a need most obviously to take full account of the requirement to ensure that everyone has an adequate income, as well as the effectiveness of active labour market programmes and in-work benefits, and the means by which the transitions from unemployment into employment are facilitated by the welfare system. In this regard, it should be noted also that the effects of welfare increases depend not only on the amount of welfare support provided, but also on the manner in which it is paid. One obvious example of this is the manner in which child income support is delivered. For some years past, increases in child income support have been delivered through the Child Benefit scheme, which carries no disincentive effects, as opposed to increasing the child dependant allowances associated with welfare payments.

3.3.23 Labour demand

Welfare rates also have the potential to impact on the demand for labour. Income support provided through the welfare system can set a floor to the level of wages that will be accepted: in other words, acceptable wages will generally be a mark-up on the alternative social welfare rate available. Jobs which offer wages which are at or near that wage floor will be at risk. It was noted that tax policy also has an influence on this issue. In this regard, the potential for difficulties in this area to be eased through the introduction of refundable tax credits was raised; but the Group was aware that the pros and cons of this much wider issue were being pursued separately under the terms of the PPF.

3.3.24 Social welfare increases may also affect wages in another way. As with all State expenditure, welfare increases have to be funded - whether through an expansion of the tax yield via economic growth, a widening of the tax base, through tax and/or PRSI increases, or through re-allocation of resources. If it is necessary to increase taxes, whether direct or indirect, there is inevitable pressure for compensatory wage increases. Even if the welfare increases can be funded without recourse to tax increases, wages may still rise more than otherwise, since the welfare increases will be using up public monies that could have been used, under partnership arrangements, to bargain for lower wage increases.

3.3.25 Higher wages can affect the competitiveness of the economy and the number of jobs on offer. In taking account of this issue, the possible link between the National Minimum

Wage, introduced in 2000, and welfare rates may also be of relevance. The level of the Minimum Wage may need to have regard to the level of welfare rates and vice versa.

3.3.26 Positive economic impacts

It is critically important to recognise that higher welfare rates are not purely negative in their economic impact; on the contrary, they can have significant productivity-enhancing effects. It would generally be accepted that a just and fair society is one that adequately protects its most vulnerable members.

3.3.27 Social exclusion, with its associated social ills such as unemployment, educational disadvantage, drug addiction, homelessness, and crime, is now widely understood to act as a constraint on economic development as well as being a waste of human potential. Indeed, it has been said that there is a reciprocal relationship between competitiveness and social inclusion. As NESC (1999:22) noted: "Competitiveness helps to generate the resources to enhance social inclusion and increased social inclusion facilitates enhanced competitiveness." The argument follows that providing people with the resources necessary by providing adequate income and supports through the social welfare system can assist people to participate fully in society. This can help overcome some of the barriers that exist to social inclusion by, for example, enhancing quality of life and increasing social participation.

3.3.28 Better welfare rates, allied to re-investment in education, will make for improved human capital – particularly as regards the health and education of children in disadvantaged homes. Such measures will have a positive impact on overall State expenditure by reducing the demands on health services, and by enhancing employability. The welfare state was not developed purely out of social concern; there was also a recognition that it would enhance the economic capability of the nation.

3.4.1 Social Insurance

The Social Insurance Fund (SIF) represents a tri-partite arrangement between employers, employees (including the self-employed) and the State, with the demands on the fund being met by way of employer and employee social insurance contributions and by Exchequer subvention. Social Insurance combines features of State income maintenance schemes, based on the principle of solidarity, and of commercial insurance in which benefit entitlements earned are related to contributions paid. The Social Insurance system is not insurance in the fully commercial or actuarial sense. The principle of solidarity means, in effect, that there is not a proportional link between contributions paid by individual insured persons to finance Social Insurance and the vulnerability of the persons covered related to knowledge of differences among them in the likely incidence of unemployment, sickness, occupational accidents and diseases, permanent incapacity for work and longevity.

3.4.2 Exceptionally, the very positive performance of the Irish economy in recent years has led to a situation where there has been no recourse to Exchequer subvention and the level of social insurance contributions has exceeded the demands arising by way of claims for insurance-based benefits. In considering the PRSI implications of adopting a new welfare benchmark, it is useful in the first instance to take account of the significant developments in the social insurance system over recent years.

3.4.3 In the period since 1994, there have been reductions in the main rates of Employer and Employee PRSI, the introduction of a Lower Rate of Employer PRSI, the introduction of a PRSI Free Allowance for employees, the introduction of a PRSI exemption threshold of £226 per week for all employees, and the abolition of the earnings ceiling for Employer's contributions. The net effect of the measures introduced in recent years, therefore, has been to reduce the potential 'take' from social insurance contributions. The very significant growth in the numbers in employment over recent years has, of course, had the effect of increasing the numbers making social insurance contributions.

3.4.4 On the other side of the equation, measures have been introduced which give rise to greater demands on the SIF. The most significant impact on the SIF, of course, arises from the costs associated with the annual increases in the rates of insurance-based welfare payments. Other measures include:

- the introduction of a Carer’s Benefit with effect from October 2000. This new Benefit expands social insurance cover to include a new contingency and complements the existing Carer’s Allowance scheme;
- enhancement of the pension entitlements of pre-1953 contributors who failed to qualify for Retirement and Old Age Contributory Pension and improvements in the rates payable for persons who have a reduced contribution yearly average;
- the transfer of the cost of expenditure relating to the Free Schemes payable to certain social insurance recipients from the Exchequer to the SIF;
- the extension of the duration of payment of Maternity Benefit.

3.4.5 These developments require that caution be exercised in considering the impact of significantly higher demands on the SIF arising from sharp increases in rates of welfare benefits, notwithstanding the current short-term buoyancy being experienced. Moreover, the possibility of the introduction of new benefit schemes, the extension of existing benefits or further reductions in PRSI contributions would also impact on the SIF. In this context, the scope for the extension of individualisation of welfare payments through the social insurance system is also an issue.

3.4.6 The recently updated (October 2000) actuarial review of social welfare pensions (which represent a very substantial element of the benefits paid from the SIF) indicates that, as early as 2006, expenditure on contributory pensions will exceed Social Insurance contributions for pensions - giving rise to a requirement for Exchequer subvention of the costs involved. The review aimed to assess the cost of pensions over a long-term period to 2056, having regard in particular to the impact on costs of an ageing population. The review indicates that the gap between contribution income and insurance-based pension payments will continue to expand significantly from 2006 onwards, most notably if payment rates are increased in line with projected increases in average earnings. The actuarial assessment of pension costs clearly demonstrated that projected revenue from social insurance contributions will greatly undershoot the payment levels required over the medium to long term. Thus, the current healthy position of the SIF does not reflect the “balance” between income and costs in the medium and long term. A broader actuarial review of the full SIF is currently underway. It might also be noted that, aside from expenditures on pensions, increased take-up of short-term benefits - for instance, increased take-up of Unemployment Benefit in the event of an economic downturn - would also impact on SIF expenditure.

3.4.7 The Group's consideration of the linkages between social welfare expenditure and macro-economic issues has been less specific than it would, perhaps, have wished. The Group found it difficult, in the absence of a full quantitative economic analysis (as described in 3.3.11 above) to estimate the impacts of varying levels of welfare expenditure. It believes that future consideration of social welfare budgetary policy can only be enhanced if such macro-economic analyses are undertaken from time to time and recommends accordingly.

CHAPTER 4 - BENCHMARKS

4.1 Why set a benchmark?

4.1.1 A benchmark for social welfare payments would represent an income standard against which the adequacy of cash income support delivered by the State through the welfare system may be judged.

4.1.2 As will have have seen in Chapter 2, there is no universally accepted definition of an adequate income. Essentially therefore, any benchmark figure is necessarily an arbitrary selection, albeit that it may be the product of negotiation and/or political judgement informed by research and analysis. Against that backdrop, some fundamental questions arise for consideration. What is the purpose of setting a benchmark for welfare payments? Is it necessary or even desirable that a benchmark is set? The remainder of this section sets out a flavour of the contending arguments in this debate.

Arguments in favour of setting a benchmark for Social Welfare payments

4.1.3 *In effect, the previous benchmark for welfare payments was the minimum rate recommended by the CSW in 1986 which, uprated in line with inflation, was finally attained for all welfare payments in 1999. While it may have taken thirteen years to achieve that benchmark, its very existence represented a yardstick against which the evolution of social welfare rates could be measured. The NESC suggested that it is necessary now that a new benchmark should be established, reflecting the changes in our economic circumstances and in society generally which have occurred since 1986. The selection of a new benchmark would set a clear direction for social welfare rates policy for the next few years, avoiding an ad-hoc approach from year to year. It is also argued that a benchmark, particularly if explicitly linked to earnings or to average household incomes, would provide 'parity of esteem' between those dependent on the welfare system for income support and the wider society. Those who would favour a continuation of an ad-hoc approach to welfare increases on the grounds that the Government must have flexibility in the allocation of resources from year to year must acknowledge that the specific commitments in relation to tax and pay contained in the partnership agreements also constrain the Government's flexibility. Welfare recipients should be afforded the same degree of certainty in relation to their incomes as is provided to employees by way of the pay increases and tax changes provided for in the partnership agreements.*

4.1.4 *It can be argued that a benchmark for pensions is in existence since the report of the Pensions Board (ibid) issued in 1998, albeit that this recommendation - that Old Age Pensions should, over time, be increased to 34% of the previous year's Gross Average Industrial Earnings - has not been adopted by Government. The current*

Government target, as set out in the Action Programme for the Millenium, is that all social welfare old age pensions will reach £100 per week by 2002. (The Government also committed to increasing pension payments in line with average industrial earnings in the period to 2002.) Progress towards this target rate has been made in the last number of Budgets. There is a need to establish a benchmark also for other welfare payments so that these payments keep pace with pension payments and thus with the incomes of the wider society.

4.1.5 *It can be contended that the effect of budgetary policy in recent years has been to increase the gap between the rich and the poor. The introduction of a benchmark for adequacy of welfare payments is necessary if the incomes of the poorest people in society are not to fall further behind those of the wider society, with all of the undesirable social consequences this entails.*

Arguments against setting a benchmark for Social Welfare payments

4.1.6 *On the other hand, there is also a case to be made against the setting of a benchmark for welfare payments. It could be said that a benchmark, particularly if it were to be explicitly linked to average earnings or household incomes, would introduce an undesirable level of inflexibility to the welfare system. Governments must have a reasonable amount of flexibility in determining budgetary policy from year to year, if they are to be in a position to respond quickly and effectively to changing circumstances. As a small open economy, we are vulnerable to shifts in a volatile external economy as well as to more localised events, such as the recent Foot and Mouth crisis. It is argued that there can therefore be no certainty that our current economic well-being can be sustained indefinitely and this uncertainty cautions against adopting an inflexible approach to a very significant element of Exchequer resources.*

4.1.7 *Welfare spending is but one of a range of high priority demands on Exchequer resources (health, education, infrastructure, etc.) and Government must have flexibility in setting priorities when allocating available resources. Benchmarking social welfare rates in isolation from these other competing needs could give rise to an undue prioritisation of social welfare expenditure over other social expenditure.*

4.1.8 *Our current economic prosperity and the consequent healthy Exchequer position derives from a prudent fiscal approach and a tax regime which seeks to reward employment and encourage job creation. Inappropriate expenditure policy, whether in the area of social welfare or otherwise must ultimately be financed through taxation or borrowing, with consequent implications for competitiveness and growth.*

4.1.9 *The introduction of a benchmark is not required in order to protect and enhance the incomes of welfare claimants. In the absence of such a benchmark, increases in social welfare rates over the last ten years or so have consistently exceeded inflation and have broadly matched increases in gross earnings. Indeed, during the 1980s, social welfare rates increased in real terms during periods when wider incomes actually fell. The current arrangement under the PPF is a sensible and reasonable approach, whereby a short-term cash target for the lowest welfare payment is set. This target can then be reviewed every few years in light of the prevailing wider economic circumstances.*

4.1.10 *By focusing on cash incomes, there is a danger that a benchmarking policy may divert attention from other policy initiatives which may be equally beneficial for social welfare dependent households (e.g. action on health, labour market programmes, secondary benefits, etc.) Also, benchmarking to an index other than inflation may, in certain circumstances, result in a fall in the real (or even nominal) value of social welfare payments.*

4.2 Illustrative benchmark options

4.2.1 While different views were held amongst the Group on the necessity or otherwise of setting a benchmark for welfare payments, it was necessary in the first instance, and in line with the terms of reference, to examine a number of illustrative benchmark options in order to assess their likely impacts.

4.2.2 In selecting these illustrative options the Group had regard in the first instance to the findings contained in the 1999 NESC report[17] which suggested a number of potential benchmark options as follows (although it was accepted that this is not an exhaustive list):

4.2.3

(i) *the upper bound of the CSW recommended rate, (£60 in 1985), uprated by prices*. The CSW estimated the minimally adequate basic rate to be in the range of £50-£60. [18] It was the lower bound of this range which became the effective benchmark against which welfare rates were measured in the period to 1999. The CSW envisaged that the adequacy standard would move up over time in line with general living standards and it was suggested therefore by the NESC that the upper bound of the range might now be a more appropriate option.

(ii) *a percentage of Average Industrial Earnings*. The NESC noted that while welfare increases had exceeded (in percentage terms) growth in gross average industrial earnings (GAIE) since 1987, they had increased less in percentage terms than net average industrial earnings (NAIE) - reflecting the tax reductions introduced in the

[17] NESC 'Opportunities, Challenges and Capacities for Choice' (December 1999)

period. They suggested that if a steady relationship is to be maintained with the disposable income of the general population, a linkage with NAIE rather than GAIE would be appropriate. (Some of the practical difficulties associated with deriving a net average earnings figure are discussed in Chapter 6.)

(iii) *50% of Average Weekly Household Income*. The NESC also included 50% of AWHI, which is often used as a threshold for relative income poverty, as another benchmark option. AWHI is derived from the ESRI's analysis of the annual Living in Ireland Survey and represents the average weekly disposable income of an adult equivalent.

4.2.4 We were conscious of the fact that the National Pensions Policy Initiative published by the Pensions Board had recommended that social welfare old-age pensions should, over time, be increased to 34% of the previous year's Gross Average Industrial Earnings (GAIE). While this recommendation has not been adopted by Government, it was appropriate that the Group should take it into account, most obviously since it related to payments covered by its terms of reference.

4.2.5 The Pensions Board recommendation was that the target rate for pensions be set at the upper bound of the range produced by the ESRI in its review of the CSW's work.[19] This review had presented an updated range of £68-£96 (in 1996 terms) for minimum welfare payments.

4.2.6 For reasons of practicality, the Pensions Board then decided to express this figure (£96 in 1996 terms) as a percentage of GAIE - which amounted to 34%. The Board proposed that the target be achieved over a 5-10 year period.[20]

4.2.7 The Board acknowledged that, in practice, the target SW rate for a particular year would have to be set by reference to the earnings in the previous year, reflecting the fact that welfare rates are set some months in advance (in the Budgetary process) and that up-to-date earnings figures would not be available. In effect, therefore, the benchmark rate is subject to a one-year time lag - e.g. the post-Budget 2001 Old-Age Contributory Pension personal rate of £106.00 represents some 31% of the gross average earnings figure for 2000 (estimated to be £345.53), with the Pensions Board target of 34% equating to some £117.50.

4.2.8 It was noted (without prejudice to the views held by some members of the Group on the issue), that if the current post-Budget 2001 relativities between welfare payments were maintained, the 34% GAIE target for pensions of £117.50 would equate to an SWA/STUA rate of c. 27% of GAIE or £93.10. It was also noted that if the pensions target were

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[18] See Chapter 2 for a discussion of the approach adopted by the CSW.
[19] ESRI - Review of the Commission on Social Welfare's Minimum Adequate Income (1986)
[20] Note also the views of the Pensions Board on the issue of knock-on effects on other welfare rates.- section 2.6.2.

expressed in (estimated) 2001 (i.e. current year) GAIE terms, then the pensions target and the basic welfare rate targets would equate to some £127.50 and £101.00 respectively.

4.2.9 Ultimately, four illustrative options[21] were selected which were considered to provide a broad range of payment levels for further assessment and these were as follows:

- ***The upper bound of the CSW recommended rate, uprated by prices (£93.25 for the lowest rate in 2001).*** This was one of the options suggested by the NESC (ibid).

- ***27% of GAIE (estimated to be £101.00 for the lowest rate in 2001).*** When existing relativities are preserved, the Pension Board's target rate for old age pensions of 34% of previous year's GAIE produces a basic welfare rate of £93.10. This is equivalent to 27% of previous year's GAIE. This is practically the same as the first of our illustrative options. Instead, and in order to give a range of options, 27% of the current-year estimate of GAIE is illustrated.

- ***30% of GAIE (estimated to be £112.50 in 2001 terms)[22].*** The selection of this option was essentially arbitrary, and again designed to provide a balanced range of options for consideration.

- ***50% of Average Weekly Household Income (estimated[23] to be £128.15 in 2001).*** This was one of the options suggested by the NESC (ibid).[24]

4.2.10 The Group took the view that it should focus primarily on the lowest current welfare rates (Supplementary Welfare Allowance and short-term Unemployment Assistance). Table 4.1 shows the current weekly rates of payment for this and for selected other welfare payments together with the equivalent figures for each of the benchmark options expressed in 2001 terms. (For convenience, relativities are assumed to remain unchanged.) Table 4.2 shows the current rates of (monthly) Child Benefit and, again, the effects of the benchmark options considered, on the basis that the existing child equivalence rate is maintained (see para 4.3.1 below). Table 4.3 sets out the full-year costs of the social welfare improvements introduced over the past three years.

[21] These are cash welfare payments - no account is taken here of the value of secondary benefits

[22] We considered using 30% of net Average industrial earnings as an illustrative benchmark. Since this was practically identical to the uprated upper bound of the CSW recommended rate (£93.11 as against £93.25), we opted instead for a gross earnings figure for the reason stated.

[23] Based on the latest Living in Ireland Survey (LIIS) data, the average weekly household equivalent income for 1998 was established to be some £187.23. 50% of this figure amounted to £93.62 in 1998 terms. As this is a net measure, we have decided to uprate this in terms of indicative increases for Net Average Industrial Earnings, providing a 2001 figure of £128.15.

[24] It was also the preferred benchmark option of the Community and Voluntary Pillar

Table 4.1: Examples of current weekly rates of payment and equivalents under the benchmark options

SW PAYMENT	Current rate	CSW (u)	27% GAIE	30% GAIE	50% AWHI
Short-term UA & SWA	£84.00	£93.25	£101.00	£112.50	£128.15
Carer's Allnce	£88.50	£98.30	£106.50	£118.50	£135.00
OAP (Non-Con)	£95.50	£106.00	£114.90	£127.90	£145.70
UB	£85.50	£94.90	£102.80	£114.50	£130.40
OAP	£106.00	£117.70	£127.50	£142.00	£161.70

Table 4.2: Current monthly Child Benefit rates and equivalents under the benchmark options

Child Benefit	Current rate	CSW (u)	27% GAIE	30% GAIE	50% AWHI
Lower Rate	£67.50	£80.20	91.50	£108.50	£131.50
Higher Rate	£86.00	£98.70	110.00	£127.00	£150.00

Table 4.3 Cost of Social Welfare Budget Improvements - 1999-2001 (£m)

	Rates	Child Benefit	FIS	Total
1999	200.83	40.76	4.24	245.83
2000	248.96	105.80	6.90	361.66
2001	439.44	328.82	13.00	781.26

4.3 Budgetary implications

4.3.1 In order to arrive at a cost for each benchmark option, it was necessary to adopt a number of working assumptions, without prejudice to the positions the Group members might reach on such issues as relativities, the time period over which any benchmark might be reached, the appropriate level of child income support, etc.

- For simplicity, the costs for each benchmark option are shown as if the rates were to apply with immediate effect from a base year of 2001 - i.e. account was taken of the range of tax, PRSI and welfare changes provided for in Budget 2001.

- The benchmark figures were applied to the lowest welfare rates (STUA and SWA) and all other welfare rates were increased by the same percentage amount, effectively maintaining the existing relativities.

- Qualified Adult Allowance (QAA) rates were assumed to be set at 70% of the relevant personal rate, in line with a Government commitment to apply from 2002. (In the case of those few payments where this target has already been exceeded (e.g. Old-Age Contributory Pension where the QAA rate is equivalent to some 75% of the personal rate, that higher percentage rate was used.)

- An assumed equivalence rate for child-related payments of 34% was derived for the lowest existing welfare rate by noting the weekly entitlements currently received via a combination of CDAs and Child Benefit. Such additional resources as were required to maintain this equivalence rate under each benchmark figure were channeled via Child Benefit - again in line with current Government policy.

- The income thresholds governing entitlement to Family Income Supplement (FIS) were increased (in line with the combined increases in the UA personal rate and UA QAA rate) to maintain the existing incentive to remain in employment provided by the scheme.

4.3.2 Table 4.4 sets out the full-year costs of each option assuming, for simplicity, that the benchmark rate is achieved with immediate effect (i.e. all values are expressed in 2001 terms).

Table 4.4: Expenditure Implications of the Benchmark Options (Change £m p.a.)

	Uprated CSW	**27% GAIE**	**30% GAIE**	**50% AWHI**
Total Social Welfare	**678**	**1235**	**2073**	**3217**
Insurance Payments	265	476	789	1212
Assistance Payments	233	417	692	1059
Child Benefit	159	301	513	801
FIS *	22	41	79	145

4.3.3 * These costings assume a 66% take-up of FIS. It is recognised that there are difficulties in determining the actual rate of take-up of FIS. Research undertaken by the Economic and Social Research Institute in 1997, which was based on the results of the Living in Ireland Survey 1994, suggested that fewer than one in three of potentially eligible claimants were actually in receipt of the payment. Since those with a higher entitlement are more likely to avail of the scheme, the take-up in expenditure terms was estimated to be somewhat higher at between 35% and 38% of potential expenditure. It should be noted, however, that the number of claimants had continued to rise in the interim - from some 10,600 claimants at the end of 1994 to 14,399 at end-March, 2000. By the same token, however, the numbers of people in employment had of course also risen significantly in recent years. More recently, the numbers qualifying for FIS have fallen back again - to some 13,200 at end-2000. This reduction is attributed largely to the impact of the introduction of the National Minimum Wage in April, 2000 allied to an appreciable growth in wage levels generally. The Group noted that, given the overall scale of expenditure envisaged under each of the benchmark options, the estimated spend on FIS is not hugely significant. It noted also that the potential for paying FIS via the tax system - with a view to overcoming take-up problems - was being explored separately under the terms of the PPF.

4.3.4 The Group thought it useful, however, to note the effects of each benchmark option on the net earnings thresholds which govern entitlement to FIS. Currently, where a person with one dependent child satisfies the qualifying conditions for FIS, and has a net income (gross earnings less tax, PRSI and superannuation contributions) of less than £278 per week, s/he will have an entitlement to a payment amounting to 60% of the difference between the net income figure and the income threshold. The thresholds increase in line with the number of dependent children in the family, up to the highest net threshold of £397, which applies where there are seven or more dependent children. (Gross average earnings industrial earnings in 2001 are estimated at some £375.00.)

Table 4.5 : Impact on FIS thresholds of each benchmark option (2001 terms)

	Current (2001)	**CSW (u)**	**27% GAIE**	**30% GAIE**	**50% AWHI**
Lowest FIS Threshold	£258	£292	£314	£347	£391
Maximum FIS threshold	£397	£431	£453	£486	£530

4.4 Income Distribution Effects

4.4.1 The income distribution effects reflect only the additional welfare expenditure arising from each of the benchmark options. No account is take of changes to income tax and social insurance which would normally be introduced in parallel with welfare increases. Thus, if income taxes had to be increased to finance increased public expenditure, this would further reinforce the distributive effect depicted below while, on the other hand, tax reductions would tend to result in a more even distribution across deciles. The following tables are based on the DSCFA estimates of the costs arising from the introduction of each benchmark option, using the profile of distributional effects generated by the SWITCH model. This provides us with a more reliable picture of expenditure and weekly gains per decile.

4.4.2 While there are some people in certain deciles who do not gain from the uprating, (e.g. students, high-earners without children etc.) the average gain per adult equivalent relates to all people in the decile, i.e. both those who gain and those who do not.

Table 4.6: Average Change in Disposable Income per adult equivalent

Income range (£ p.w.)	CSW(U) £	27% GAIE £	30% GAIE £	50% AWHI £
<=86	9.00	14.90	26.20	39.76
>86 <=102	13.41	22.49	40.51	62.16
>102 <=117	13.35	22.21	39.90	61.09
>117 <=151	11.96	20.16	36.75	56.88
>151 <=191	5.39	9.16	17.54	29.27
>191 <=227	3.69	6.36	11.65	18.40
>227 <=268	3.09	5.41	9.82	15.34
>268 <=322	2.87	4.96	9.10	14.22
>322 <=394	1.90	3.28	6.06	9.44
>394	1.52	2.63	4.86	7.56

Table 4.7 Average percentage gain in disposable income per adult equivalent

Income range (£ p.w.)	CSW(U) %	27% GAIE %	30% GAIE %	50% AWHI %
<=86	10.2	18.3	29.6	45.0
>86 <=102	9.9	18.0	30.0	46.0
>102 <=117	8.6	15.5	25.7	39.4
>117 <=151	5.4	9.8	16.6	25.7
>151 <=191	1.8	3.4	6.1	10.1
>191 <=227	1.1	2.0	3.4	5.4
>227 <=268	0.8	1.5	2.5	3.9
>268 <=322	0.6	1.1	1.9	3.0
>322 <=394	0.3	0.6	1.1	1.7
>394	0.2	0.3	0.5	0.8

4.4.3 It will be seen that the greatest gains are concentrated in the bottom four income deciles. This is borne out in Tables 4.8 and 4.9 below which show the level of additional spending applied to each decile in monetary terms and in proportionate terms respectively. Table 4.9, for instance, indicates that c. 70% of the additional expenditure is allocated to the bottom four deciles under each of the options.

Table 4.8 : Amount of additional spending per decile (£m p.a.)

Income per adult equivalent (£ p.w.)	CSW (u) £m.	27% GAIE £m.	30% GAIE £m.	50% AWHI £m.
<=86	94.5	169.1	275.1	417.3
>86 <=102	148.2	268.8	447.7	687.2
>102 <=117	125.4	225.4	374.8	573.6
>117 <= 151	120.4	219.4	370.1	572.7
>151 <=191	55.3	101.7	180.0	300.3
>191 <=227	37.9	70.4	119.5	188.5
>227 <=268	31.7	59.9	100.7	157.3
>268 <=322	29.5	55.0	93.3	145.8
>322 <=394	19.5	36.4	62.2	96.9
>394	15.5	29.2	49.9	77.6
Totals	677.9	1235.2	2073.1	3217.2

Table 4.9 : Cumulative % of additional spending per decile

Income per adult equivalent (£ p.w.)	CSW(u) (%)	27% GAIE (%)	30% GAIE (%)	50% AWHI (%)
<=86	13.94	13.69	13.27	12.97
>86 <=102	35.80	35.45	34.87	34.33
>102 <=117	54.30	53.70	52.95	52.16
>117 <= 151	72.06	71.46	70.8	69.96
>151 <=191	80.22	79.69	79.48	79.29
>191 <=227	85.80	85.39	85.24	85.15
>227 <=268	90.47	90.24	90.10	90.04
>268 <=322	94.82	94.69	94.60	94.57
>322 <=394	97.70	97.64	97.60	97.58
>394	100	100	100	100

4.5 Relative Income Poverty

4.5.1 The impact on relative income poverty of each benchmark option in relation to the base year is shown in Table 4.10. (Data on relative income poverty rates are produced by the ESRI and derived from analysis of results from the Living in Ireland Survey (LIIS) and the most up-to-date data relates to 1998. The issue of relative income poverty is discussed in some depth in Chapter 7. The figures in Table 4.10 are generated by the SWITCH model. These will not always accord exactly with those shown by the Living in Ireland Survey, because SWITCH, in effect, models the social welfare and tax elements of income whereas the LIIS-based results will use actual reported amounts from respondents. Because of this, both the disposable income of a given household, and mean disposable income across households and thus the relative income lines, may differ. Therefore, the fact the relative income poverty rates for 2001 shown below are lower than LIIS-based rates for 1998 (see table 7.1) cannot be taken to mean that poverty rates have fallen or that the impact of policy has been in that direction - like is not being compared with like. For the purposes of this exercise, it is more relevant, therefore, to concentrate on the proportionate reduction in relative income poverty from the base year to the levels produced by the benchmark options.)

Table 4.10: Proportion of Households Below Mean Relative Income Lines (%)

	Base year (2001)	Uprated CSW	27% GAIE	30% GAIE	50% AWHI
40% line	8.64	6.68	3.33	2.45	1.62
50% line	20.12	16.33	13.66	11.12	7.46
60% line	27.27	26.53	25.13	22.22	17.61

4.5.2 In the far-right column, it can be seen that, despite the fact that the lowest social welfare payment would be increased to 50% of Average Weekly Household (Equivalent) Income in 2001 terms, this does not have the effect of eliminating relative income poverty at the 50% line as, by raising aggregate income, an increase in social welfare rates also results in an increase in average income. It would equally be the case that if the additional spending on welfare increases was applied elsewhere within the income distribution (e.g. income tax reductions), it would also have the effect of increasing the 50% income threshold by driving up average incomes although the impact on numbers below the various income lines would be different.

4.5.3 The actual cash amounts in terms of average weekly household equivalent income under the various options are shown below: (Note that these cash amounts apply to single adult equivalents only.)

Table 4.11: Equivalent Cash Figures (2001 terms)[25]

	Base	CSW (u)	27% GAIE	30% GAIE	50% AWHI
40% line	£97.90	£99.67	£101.13	£103.31	£106.32
50% line	£122.37	£124.59	£126.42	£129.14	£132.91
60% line	£146.84	£149.50	£151.70	£154.97	£159.49

4.6 Incentive issues

4.6.1 It was noted in Chapter 3 that the financial incentive (as measured by replacement ratios - RRs) is not the only factor which will influence unemployed people to take up employment opportunities. It remains, however, a valid and objective means of examining the relative impacts of the measures under consideration. Briefly, a replacement ratio

[25] The Base figures used here are estimates generated by the SWITCH model and may not accord exactly with reported income levels for 2001 when they become available.

represents the net income available to a person in receipt of unemployment payments expressed as a proportion of the net income of that same person were s/he to take up employment at a particular rate of pay. A RR of 100 would therefore mean that there would be no financial gain (or loss) from taking up employment. [26]As the RR decreases, the financial gains increase and the incentive to take up employment is higher. While there are different viewpoints on the issue, it is generally accepted that solely from the perspective of financial incentives, RRs in excess of 70% are undesirable.

4.6.2 The RRs are based on a minimum wage rate of £4.70, which is the statutory rate in effect from 1 July, 2001[27]. The SWITCH model generates tables which show the distribution of RRs faced by those in receipt of unemployment payments. Table 4.12 beneath shows the proportion of those in receipt of unemployment payments facing RR levels of 50% to 80%.

Table 4.12 - % of UA/UB claimants at specified RR thresholds

Replacement Rate	Base (2001)	CSW(u)	27% GAIE	30% GAIE	50% AWHI
<50	75.6%	58.5%	52.3%	41.4%	31.9%
<60	82.8%	80.1%	76.0%	60.7%	48.8%
<70	**89.8%**	**86.2%**	**84.5%**	**80.9%**	**66.3%**
<80	94.6%	93.4%	92.3%	90.3%	87.2%

4.6.3 Currently, almost 90% of recipients of unemployment payments face RRs of less than 70%. Under the various benchmark options, this number drops gradually to some 81% under the 30% GAIE option and down to 66% under the most expensive option. It is necessary to recognise however that the disincentive effects will vary depending on household composition.

4.6.4 For illustrative purposes, it is useful to observe the impacts of each option on the actual numbers in receipt of unemployment payments at end-December 2000 (122,200) at the 70% RR level. This figure is further disaggregated by reference to family type in order to indicate where the disincentive effects are most pronounced.

Singles:	73,687
Couples - no children	8,603
Couples with children	39,910
Total	122,000

[26] The RRs being examined here are based on cash figures and do not take into account the value of secondary benefits. It is possible therefore that a RR of less than 100% could mean that there is no financial gain from taking up employment.
[27] The national Minimum Wage will increase further to £5.00 (6.30 Euros) per hour from 1 October 2002 .

4.6.5 The tables below show the number of claimants estimated to be facing RRs greater than 70% under the base case (2001) and under each of the benchmark options in turn.[28] The impact is shown for each option below.

Table 4.13 - Indicative Effects on nos. facing RRs > 70% - UA/UB recipients

Family Type	A 2001	B CSW (u)	B - A Nos. affected	C 27% GAIE	C - A Nos. affected	D 30% GAIE	D - A Nos. affected	E 50% AWHI	E - A Nos. affected
Single	0	0	0	0	0	147	147	13485	13485
Couple w/o children	1035	1488	453	1831	796	2156	1121	3533	2498
Couple with children	13746	18701	4955	21099	7353	25774	12028	28171	14425
Total	14781	20189	5408	22929	8148	28077	13296	45189	30408

4.6.6 It is important to recall that this analysis is based on a wage rate from employment of £4.70 per hour – the level of the national minimum wage. Where a wage in excess of that amount was on offer, the RR would be affected accordingly. Bearing that point in mind, the key points emerging from this exercise can be summarised as follows:

- The first three options have no impact or a negligible impact on singles, a category which represents some 60% of all those in receipt of unemployment payments. A more significant impact is observed where the benchmark is set at 50% AWHI.

- It is clearly demonstrated that the issue of financial incentives are of greatest relevance to families with dependent children. Even at the lowest benchmark figure, the shift in the numbers facing RRs of more than 70% is substantial, while the impact naturally increases as the benchmark figures rise. Under the 30% GAIE benchmark, almost two-thirds of this household category would face RRs in excess of 70% as against approximately one-third under the base case. Where the benchmark is set at 50% AWHI, over three quarters of families with children would face RRs of more than 70%.

Table 4.14 - % of persons on home duties at specified RR thresholds

Replacement Rate	Base (2001)	CSW(u)	27% GAIE	30% GAIE	50% AWHI
<50	32.2%	25.5%	23.6%	18.5%	16.1%
<60	48.1%	44.0%	41.9%	37.3%	32.8%
<70	**68.3%**	**65.9%**	**63.6%**	**61.3%**	**55.6%**
<80	87.1%	86.5%	84.6%	83.0%	79.4%

[28] It should be noted that the figure of 122,000 used here represents the 'stock' LR figure and that there are significant levels of flows onto and off the LR. Roughly speaking, in the course of a year, twice the numbers shown in these tables could be expected to be affected by the changes in the RRs arising from increases in the SW rates.

4.6.7 The Group's concern in relation to persons on home duties relates to those in receipt of a welfare payment, primarily recipients of One-Parent Family Payment. In this case, while the proportionate impact of each of the benchmark options on the numbers facing RRs of less than 70% is in line with that observed earlier in relation to claimants of unemployment payments, it can be seen that over 60% continue to face RRs of less than 70% under each of the first three options. It must be noted, however, that the table shows the RRs for all persons on home duties, but it is not possible to disaggregate the proportion of those who are in receipt of welfare payments.

4.6.8 The table below shows the effect on replacement rates for employees under each of the four options. Replacement rates for employees are calculated as the percentage of current income (from employment) that would be available to the individual if s/he were instead to avail of social welfare payments. From a financial incentives point of view, it would again be desirable that replacement rates were kept below 70%.

Table 4.15: % of Employees at specified RR thresholds

Replacement Rate	Base (2001)	CSW(u)	27% GAIE	30% GAIE	50% AWHI
<50	65.7%	60.3%	55.6%	48.8%	39.5%
<60	78.4%	75.4%	72.9%	67.9%	59.2%
<70	**88.3%**	**86.8%**	**85.4%**	**83.0%**	**77.2%**
<80	94.6%	93.9%	92.9%	91.9%	89.6%

Table 4.16: Indicative effects on nos. facing RRs > 70% - Employees

Family Type	A 2001	B CSW (u)	B - A Nos. affected	C 27% GAIE	C - A Nos. affected	D 30% GAIE	D - A Nos. affected	E 50% AWHI	E - A Nos. affected
Single	16185	20038	3854	21580	5395	28156	12331	77482	61657
Single with children	9523	10237	714	12570	3047	13760	4238	16141	6618
Couple w/o children	49853	54901	5048	60896	11043	68153	18300	78250	28397
Couple with children	117254	132721	15486	144197	26943	169145	51891	201078	83824
Total	192814	217898	25084	239243	46429	279575	86760	373311	180496

4.7 PRSI & economic implications

4.7.1 In the case of the costs relating to social assistance schemes, Child Benefit and FIS, these must be met from Exchequer resources. As noted earlier (see Chapter 3), there are a variety of ways in which the costs of the increased social insurance liabilities can be met. Four different payment routes were identified:- from buoyancy in social insurance contributions (where relevant); by way of Exchequer subvention; by way of adjustments to the social insurance rates/thresholds[29]; or by way of a combination of Exchequer subvention and adjustments to the social insurance regime. (Buoyancy (both in relation to PRSI receipts and tax receipts) refers to receipts over and above those projected at Budget time. In this regard, it is worth noting that while the exceptional economic conditions of recent years resulted in taxation revenue generally being underestimated at Budget time, the slowing of economic growth which is evident this year means that a shortfall over Budget estimates for tax receipts is now envisaged for 2001). It was noted in turn that, where questions of Exchequer subvention arise, the potential for meeting such costs through an expansion of the tax yield via economic growth, a widening of the tax base, through tax and/or PRSI increases, or through re-allocation of resources would need to be considered.

4.7.2 In the ordinary course, the costs of social welfare Budget packages and other publicly funded expenditures will be met from Exchequer resources, generated by way of taxes and levies, and, if necessary, by borrowings. In recent years, the sustained growth in output, in employment and in earnings has ensured that the Government has been in a position to generate an exchequer surplus. Budget 2001 projections indicate that a positive Exchequer surplus will be generated in the period to 2003, at least, although it needs to be noted that these estimates are predicated on an average GNP growth rate of 6.6% in the period 2001 to 2003, and do not take account of the costs to the Exchequer of measures relating to BSE and pre-dated the slowdown in the US economy and the outbreak of Foot and Mouth disease. They also include technical provisions for all Budget initiatives in 2002 and 2003 for all tax relief and expenditure increases (including changes in social welfare payment rates) with full year costs, respectively, of £1.3 billion and £1.2 billion for tax and expenditure changes combined.

4.7.3 In the medium term, current forecasts predict a path of continued economic and employment growth but are, almost by definition, fraught with uncertainty. Clearly, a sustained positive Exchequer position in the medium and longer term is subject to many factors. These include, for instance, the level of economic performance and employment, the impact of demographic pressures on health and welfare services, and pressures to improve the levels of services across all aspects of Government activity.

4.7.4 While the path of increasing growth and employment is seen as the most likely scenario over the medium term, there is also the possibility of a shock to the economy which could upset the forecast considerably. As a relatively open economy, relying heavily on foreign direct investment, Ireland is especially exposed to sudden changes in the international economic situation, particularly from the United States. The recent concern expressed at an

[29] The Trade Union pillar were of the view that, without a radical review of the SIF, there should be no direct linkage between the amount of resources available within the SIF and (i) the level at which benefits are paid, and (ii) the extension of the range of benefits.

apparent slowdown in the US economy illustrates this. There are other concerns too. For example, a rising exchange rate for the Euro could put pressure on exporters and consequently on employment and growth. Concern has also been expressed that the current tight labour market could lead to a situation whereby the equilibrium rate between growth and wage rates could be overshot, resulting in a loss of competitiveness.

4.7.5 In order to illustrate the scale of the expenditure envisaged under each of the benchmark options considered, the cost of each option is expressed as a percentage of the post-Budget 2001 estimate for, in turn, income tax, corporation tax, and value added tax. The figures do not take into account the latest official projection of a short-fall of £500m in the overall estimate of tax revenue. It must be emphasised that this is purely a hypothetical exercise. It assumes for instance that the full cost of each benchmark option is incurred immediately, i.e. that the benchmarks are introduced with immediate effect.

Table 4.17: Illustrative scale of benchmark expenditures

	% of Income Tax Revenue (2001 est.)	% of Corporation Tax Revenue (2001 est.)	% of VAT revenue (2001 est.)
CSW Uprated	8.7	20	9.8
27% GAIE	15.9	36.5	17.8
30% GAIE	26.6	61.2	29.9
50% AWHI	41.3	95	46.5

4.8 Percentage v. fixed amount increases

4.8.1 The approach adopted of applying the same percentage increase to each welfare personal payment rate has the effect of maintaining the existing relativities between these payments. Consequently, it means also that those on the higher rates of payments (e.g. pensioners) enjoy a higher cash increase than those on the lowest payments. (For example, an increase of 11% gives rise to an increase in the weekly rate of Short-term UA of £9.25 while the personal rate of Old-Age Contributory Pension rises by £11.70.) The Group were interested therefore to observe whether there would be a significant difference in cost if, rather than providing for a fixed percentage increase in each personal rate, a fixed cash increase was instead applied across the board.

4.8.2 It could be argued that neither approach mirrors precisely the approach taken in the social welfare Budget packages of recent years. There has, for instance, been a notable emphasis on providing for more substantial increases in pension payments, in particular, in recent years, which have served to increase the gap between the highest and lowest welfare rates.

4.8.3 The costs associated with the 'fixed cash amount increase' approach are set out below.

Table 4.16: Comparison between costs of percentage and fixed cash amount increases in welfare rates (additional cost to Exchequer £m) - excluding CB and FIS

	% increase	fixed £ increase	Difference (£m.)	Difference (%)
CSW Uprated	497	454	43	8.7
27% GAIE	893	813	80	9.0
30% GAIE	1481	1343	138	9.3
50% AWHI	2271	2066	205	9.0

4.8.4 There would be no difference in the cost of Child Benefit increases under the two approaches, since this is related solely to the equivalence rate derived from the level of child income support payable to the claimants of the lowest existing welfare rates via a combination of Child Dependent Allowance and Child Benefit. The increase in the rate of the lowest welfare rate is precisely the same, of course, whichever approach is adopted. FIS costs would also remain virtually identical under the two approaches, since they are linked directly to long-term Unemployment Assistance, which is at the lower end of the range of payment rates.

4.8.5 While applying a fixed cash increase to all rates would cost some 8% - 9% less than maintaining existing relativities, the orders of magnitude in costing terms remain largely the same. This is because appreciable differences in costs only arise in relation to the highest rates of welfare payments - it is only at those levels that the gap between a percentage increase and a fixed cash amount increase becomes significant. This is best demonstrated by looking at the impact on welfare rates on the most expensive of the benchmark options under consideration - 50% of AWHI.

Table 4.17 - Effect on selected SW personal rates

Welfare payment	Current personal rate	53% increase	Cash inc. of £44.15
Short-term UA	£84.00	£128.15	£128.15
Disability Allowance	£85.50	£130.40	£129.65
Invalidity Pension	£89.10	£135.90	£133.25
OAP (Non-Con)	£95.50	£145.60	£139.65
OAP	£106.00	£161.70	£150.15

Chapter 5 - Child-related Payments

5.1 Child income support in Ireland

5.1.1 The Group's terms of reference required it to give specific consideration to the issue of a benchmark for adequacy of child-related welfare payments. Child income support is primarily provided via three welfare payments - Child Benefit, Child Dependant Allowances, and Family Income Supplement[30] payments. (Under the Supplementary Welfare Allowance Scheme, provision is made for the payment of Back-to-School Footwear and Clothing Allowances. The welfare system also makes provision for Contributory and Non-Contributory Orphans' Pensions.) The Group concentrate, however, on the three key payments mentioned above.

5.2 Child Benefit

5.2.1 Child Benefit (CB) is a universal monthly payment payable, generally to the mother, in respect of children who are under 16 years of age; or who are between 16 and 19 years of age and are disabled or in full-time education.

5.2.2 CB is not subject to a means test and is paid regardless of household income or employment status. It is neither taxed nor withdrawn if employment is taken up. Consequently, it does not contribute to poverty or unemployment traps or contribute to employment disincentives.

5.2.3 The current monthly rate of CB (from June 2001) is £67.50 in respect of each of the first two qualified children and £86.00 for each subsequent qualified child. Double the monthly rate of CB is payable in respect of multiple births of triplets or more, for as long as at least three of the children remain qualified. CB is payable at 150% of the normal rate in the case of twins. Grants are also available in the case of multiple births of two or more children - £500 at birth, and further grants of £500 when the children reach the ages of 4 and 12 years.

5.2.4 The PPF contains a commitment in relation to Child Benefit which states that "Child Benefit, as a key mechanism to reduce levels of child poverty and to provide child income support, will be substantially increased over the period of this Programme, with a priority focus towards £100 per month for the third and subsequent children". (It will be noted that the Budget 2001 commitment, as described below in para 5.5.8, means that this target will be exceeded.)

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[30] It should be noted that FIS is not a child income support payment per se but is designed to provide income support for low-wage employees with children and thereby preserve the incentive to remain in employment in circumstances where the employee might only be marginally better off than if s/he were claiming other social welfare payments.

5.2.5 The 2001 Budget provided for increases of £25 and £30 in the lower and higher rates of Child Benefit respectively, at a full-year cost of some £330m, bringing total expenditure on the scheme to approximately £900 million in a full year.

5.3 Child Dependant Allowances (CDAs)

5.3.1 Child Dependant Allowances are paid as an increase on a welfare claimant's personal payment. They are payable in respect of all children up to the age of 18 years. Currently, where a claimant is in receipt of a long-term social welfare payment, CDAs are payable where children are in full-time education up to the age of 22 years, or up to the end of the academic year after the 22nd birthday. The PPF contains a commitment that, "over the course of the Programme, Child Dependent Allowances will be payable to all social welfare recipients where the child is under 22 and in full-time education."

5.3.2 There are at present three different rates of CDAs in payment, ranging from £13.20 per week to £17 per week (see Appendix B for details). The reasons for the existence of different rates are largely historical. The Commission on Social Welfare (1986) recommended rationalisation of the extensive range of CDAs then in payment. In line with this recommendation, the number of different rates has been reduced from thirty-six to the current three rates. The cost of paying a uniform rate of CDA at the highest rate has been estimated to be in the region of £48m. While such an approach would run counter to the thrust of current policy in this area - see 5.5.6 and 5.5.7 below - it is noted that it would directly benefit those on the lowest social welfare payments.

5.4 Family Income Supplement

5.4.1 Family Income Supplement (FIS), which was first introduced in 1984, is designed to provide income support for low-wage employees with children and thereby preserve the incentive to remain in employment in circumstances where the employee might only be marginally better off if s/he were claiming other social welfare payments. FIS is payable at a rate of 60% of the difference between the weekly net income and the income limit for that family size. There is not therefore a set amount payable per child; rather the level of supplement payable is contingent on the level of net income and on the number of qualified children. The basis of the FIS scheme is not to provide a minimum income to families but rather to maintain financial incentives to take up employment and, accordingly, the FIS thresholds are adjusted upwards annually to take account of Budget increases in social welfare rates.

5.5 Objectives of Child Income Support

5.5.1 As stated in the Report of the Commission on the Family (1998), the State, at a general level, has taken a role in sharing the costs of raising children across the community: in part, this can be seen as involving an element of redistribution of income over the life-cycle, and in part an element of redistribution as between those with and without children. There is also redistribution towards families who have insufficient resources, through child-related additions to social welfare payments. In recent years, there has been increased emphasis on providing child income support in a way which is most "employment friendly": it is the concern with financial work incentives for lower income workers which led to the setting up of the Family Income Supplement scheme and the child additions to tax exemption limits.

5.5.2 More recently, the National Children's Strategy[31] identifies as one of its objectives that "children will be provided with the financial supports necessary to eliminate child poverty" and proposed that targets for the elimination of child poverty be set under the National Anti-Poverty Strategy.

5.5.3 The Child Benefit Review Committee (1995) remarked that "Child Benefit represents a contribution towards the costs of children. It does not meet the full costs of children - households with limited resources receive considerably higher levels of payment for children via CDAs, FIS, etc., in order to help them meet more of the costs of child rearing."

5.5.4 In addition, the Committee examined the different roles of CB and considered it appropriate to assess options for improvement against a number of different criteria, viz: assistance towards the costs of children; child poverty; cost to Exchequer; impact on incentives; redistributive impact; intra-family income distribution; impact on labour force participation; horizontal equity; payment recipient; impact on administration; and participation in education.

5.5.5 The structure of the CB scheme ensures that additional resources are targeted at the larger families, who are at greater risk of poverty, through the existence of a higher rate of payment in respect of the third and subsequent qualified children.

5.5.6 In recent years, policy in relation to child income support has placed an emphasis on significantly raising the levels of CB. This policy direction was driven primarily by the widespread recognition of the employment disincentive effects of CDAs, an issue highlighted by the Expert Group on the Integration of the Tax and Social Welfare Systems in their report published in 1996.

5.5.7 The level of CDAs has been frozen since 1994 while resources are now channeled through the universal, and more costly, CB payment. Since 1994, the combined CB/CDA payment has increased by more than double the rate of inflation. In terms of tackling work disincentives, the shift towards CB has been significant. In 1994, CB represented 29% of the total CB/CDA payment for a four-child family; after Budget 2001, it represents 57%.

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[31] National Children's Strategy, 'Our Children - Their Lives', (2000) pps. 63-64

5.5.8 In presenting the 2001 Budget, the Minister for Finance indicated that the increases provided for in 2001 represented the first step in a three-year programme of investment in the CB scheme. In his Budget speech, he stated : " The House will be well aware of the great diversity of views that are held in relation to addressing the childcare issue. The Government's core objective is to provide support which will offer real choice to parents and will benefit all our children. This we can do through Child Benefit. …. [The 2001] increase of over 50% in current payment rates marks the first step in a three year programme. At the end of this process, an additional £1bn. will have been invested directly in our children's well-being. Child Benefit monthly payments will stand at £117.50 and £146 …. This unprecedented increase will help all parents with the costs of caring for their children and will represent a major move towards achieving the goal of ending child poverty in this country".

5.6 Adequacy of Payments

5.6.1 Any determination of the adequacy, or otherwise, of current child income support payments, needs to consider the same issues we have already set out in relation to adults in Chapter 2. For what should the payments be adequate? Should consideration be given to different payment levels for different groups (in this case, for example, should different payment levels be given to children of different ages)? In relation to research available on the adequacy of payment rates, the Group noted that there was less research in relation to children than adults. The main research available was a budget standard study - "Cost of a Child" by Carney et al (1994) - and also studies of equivalence scales.

5.6.2 "The Cost of a Child" was produced to compare actual costs of rearing a child with the level of direct state support for children at that time. The researchers used the budget standard approach to determine the average cost of a child. This approach arrives at a cash amount through the estimation of the cost of a particular basket of goods and services. The report (p.5) states:

> "*This approach attempts to combine both absolute and relative concepts of need. It uses expenditure surveys to inform its choice of which areas of expenditure to include. This method combines both an assessment of physical needs and of social norms.*"

5.6.3 Thus, in devising their basket of goods and services, the researchers did not look only at the minimum amount necessary for survival but also the costs associated with normal participation in society. It should be noted, however, that the study does not include any childcare costs. It should also be noted that the study was carried out in 1992 and is now in need of review.

5.6.4 Two estimates were presented by the authors:

i) *A Basic Minimum Budget Standard* which provided for a basic diet, a modest wardrobe, essential schooling costs and limited spending on recreation, outings, holidays and presents; and

ii) *A Modest-but-Adequate Budget Standard* which provided for a more varied diet, for additional spending on toys and presents, and for extra educational expenditure such as pre-school participation and a visit to the Gaeltacht.

5.6.5 The Basic Minimum Budget excludes medical costs (primarily because it is assumed that a medical card would be possessed at this income level) and baby-sitting costs. While costs differ considerably depending on the age of the child, the average under this budget amounts to about £30 per week (in 1992 prices). Uprated to 2001 using CPI, this would amount to about £37 per week. Breaking the costs down on an age-related basis (i.e. in three equal intervals of six years each), the costs averaged at £20, £30 and £40 respectively. This gives figures, in 2001 terms, of £24.76, £37.13, and £49.51 per week. As a working assumption, the Group confined itself to the current Child Benefit payment structure. It did not, therefore, discuss the issue of age-differentiated child income support.

5.6.6 The Modest-but-Adequate Budget (which includes a more varied diet, longer holiday, more pocket money, allowance for pre-school costs (age 3-4 years), and £2.50 in baby-sitting costs) results in a cost range of £24.90-£49.15 per week (in 1992 terms) which amounts to £30.82-£60.84 at 2001 prices. On average, the additional costs to afford this standard amount to nearly £10 (1992 prices) per week.

5.6.7 The post-Budget 2001 level of child income for a STUA claimant amounts to some £28.78, comprising the CDA of £13.20 and a weekly (lower rate) CB payment of £15.58. If one takes the higher rate of CB payment (£19.85) and a CDA of £13.20, the weekly child income support for the child is £33.05.

5.7 Equivalence Scales

5.7.1 An alternative approach to setting an adequacy rate for children might be to draw on research in relation to equivalence scales. Equivalence scales are used to adjust household income for the differences in needs associated with differing size and composition. For instance, one such scale which is frequently employed would ascribe a value of 1 to the first adult in the household, 0.66 to each additional adult, and 0.33 to each child (1.0/0.66/0.33). There are other equivalence scales in common usage also - e.g. 1.0/0.6/0.4 is frequently employed in UK research and a scale often called the 'OECD scale' attributes values of 1.0/0.7/0.5.

5.7.2 The matter of what constitutes a reasonable equivalence scale either for children (or adults) is a matter of judgement and would have recourse to consideration of economies of scale. While there has been some commentary on this issue in an Irish context (Conniffe and Keogh (1988); Nolan and Farrell (1990); Carney (1994)), "*it remains the case that there is no consensus internationally about the best way to estimate the 'needs' of one type of household vis-a-vis another, and that equivalence scales covering a wide range are in common use*" (Callan, Nolan and Whelan, 1996).

5.7.3 It may be useful at this point to observe the current levels of child income support as a proportion of selected welfare payments (maximum, post-Budget 2001). For simplicity, the calculations are based on the basic level of payment for the adult and a household with one child. Consequently, no account is taken of the higher rate of Child Benefit in these calculations. The child income support is the combined level of CDAs and a weekly Child Benefit (lower rate) payment.

Table 5.1: Child Income Support as Percentages of Selected Welfare Payments

SW Payment	SW Payment Level	Child Income Support Level (per week)	Implied Equivalence Scale
Unemployment Benefit	£85.50	£28.78	33.7%
Unemployment Assistance (short-term) & SWA	£84.00	£28.78	34.3%
Disability Benefit	£85.50	£28.78	33.7%
Pre-Retirement Allowance	£85.50	£28.78	33.7%
One-Parent Family Payment	£85.50	£30.78	36%
Invalidity Pension (under 65)	£89.10	£30.78	34.5%
Widow's/Widower's (Con) Pension (under 66)	£89.10	£32.58	36.6%

5.7.4 It will be noted that the table excludes some of the higher rates of welfare payments - e.g. Old-Age Pensions, which would have a lower equivalence rate. However, the extent of child dependency associated with such payments is obviously less prevalent. In 1999, for example, CDAs were paid in respect of some 429,000 children, and less than 5,000 of these were associated with Old-Age and Retirement pensions.

5.7.5 It will be seen that the implied equivalence rate falls into a fairly narrow range of 33% - 37%. Given that the particular focus of the Group in terms of benchmarks is on the lowest personal welfare rates, it might be noted that the implied equivalence applying to Short-term Unemployment Assistance and Supplementary Welfare Allowance is currently (2001) 34.3%.

5.7.6 Conniffe, Nolan and Whelan (1998) suggested that a single child, on average, may add about 35% to the income needed to attain a particular living standard and that a second child may add, on average, about 30% to the income required to reach the living standard of a single adult. The implications of this finding - that later children add less rather than more to household costs than the first child - could perhaps be viewed as conflicting with the current policy of providing higher rate CB payments in respect of the third and subsequent children. It should be noted, however, that the study did not examine the impact of third and subsequent children, and it cannot therefore be automatically assumed that their impact on income needs would be the same as those of the second child. In any event, the point can be made that current CB policy is driven by a recognition that the larger households face a higher risk of poverty and that it is appropriate therefore to target greater levels of support to such households.

5.8 Impact of Child Benefit increases

5.8.1 As noted earlier, the Government is committed to increasing CB rates to £117.50 and £146 per month respectively by 2003. At that stage, weekly child income support for the lowest welfare payment will have risen to a minimum of some £40.32 per week, assuming that CDAs continue to remain at existing levels. It is estimated that the average cost of a child, as estimated by Carney et al, uprated by CPI, will amount to £39.25 in 2003.

5.8.2 The issue of caring for children is a highly complex one which has acquired greater relevance in recent years as employment levels have grown rapidly. Caring for children may be viewed in the conventional context of the needs of parents engaged in employment, training or education, or it can be seen to embrace a wider range of activities - e.g. baby-sitting costs, extra-curricular school activities such as home work clubs and after-school care, and child development activities such as summer projects, etc.

5.8.3 While childcare is an issue which fell outside the Group's terms of reference, it was raised in the context of divergent views on the role which CB is expected to play in the future, in light of the Budget 2001 statement made by the Minister for Finance when announcing the planned substantial investment in the scheme - see 5.5.8 above.

5.8.4 While clearly welcoming the recent and planned increases in CB, the Community and Voluntary Pillar, in light of the Minister for Finance's Budget statement, believe that there is a need for Government to be clear that there are adequacy/poverty and costs of caring functions within CB. The Pillar believes that there will remain a gap between the estimated costs of rearing children and the level of child income support to be reached by 2003, especially given that the function of equitable care for children is being more fully incorporated into CB. If CB is seen to be of assistance towards the costs of caring, then assessment of that cost needs to be built into the process of determining benchmarks for adequacy on minimum income standards for children.

5.8.5 The trade union and employer pillars view CB as a child income support payment designed to assist all parents with the basic costs of rearing children, such as food, clothing and shelter. It is not accepted that CB should also serve to assist working parents with the additional costs of paid childcare. The trade unions and employers wish to see early implementation of the PPF commitment (in Sec. 3.2.4) to increase CB to £100 per month as well as early agreement (as per PPF Sec. 4.3.11) on an equitable manner of assisting working parents with the costs of paid childcare for both pre-school and school-age children.

5.8.6 Noting the Minister for Finance's Budget statement (see 5.5.8 above), other members of the Group were of the view that CB is a holistic payment, which offers parents a choice in the manner in which it is used - some families might use it to supplement household expenditure generally, while others might use it specifically to assist with the costs of formal childcare. They were further of the view that it is neither appropriate nor possible to disaggregate the CB payment according to particular functions.

5.8.7 The various benchmark options for adult payments considered in Chapter 4 would provide that the lowest welfare rate would have risen by 2003 to levels shown beneath and would imply a child equivalence rate as shown:

Table 5.2: Implied child equivalence rates in 2003

Benchmark Option	Estimated level of STUA in 2003	Implied child equivalence rate
CSW - uprated	£98.90	40.7%
27% GAIE	£117.80	34.2%
30% GAIE	£131.20	30.7%
50% AWHI	£149.50	27%

5.9 Child Poverty

5.9.1 The level of child poverty, while subject to a number of causal factors, is integral to the discussion on child income support. The latest comprehensive data available on the issue of relative income poverty among children as a group relates to 1997 and is based on results of that year's Living in Ireland Survey. However, some data has been published in relation to 1998 and shows that the risk of relative income poverty for households with three or four (or more) children had significantly reduced in 1998.

5.9.2 The primary factor behind the rapid fall in relative income poverty for households comprising two adults and three children between the 1997 and 1998 Living in Ireland surveys was falling unemployment, with a significant number of these households seeing their reference person moving from unemployment into work.

5.9.3 As far as children overall are concerned, it is worth noting that the gap in relative income poverty rates between working-age households with and without children narrowed very substantially between 1994 and 1998, and by 1998 had come close to converging. There remain however specific types of households with children which have relatively high poverty risks - notably lone parent families and dual-parent families with 4 or more children. According to Nolan (1998), some two-thirds of all poor children live in households where no-one is in paid work, due to either unemployment, illness/disability, or working full-time in the home.

Table 5.3: Percentage of Households Below 40% Relative Income Poverty Line by Household Composition Type, Living in Ireland Surveys, 1994, 1997 and 1998

	1994	1997	1998
1 adult	2.2	3.4	18.8
2 adults	3.4	5.4	4.7
3 or more adults	5.7	5.1	3.8
2 adults, 1 child	3.0	3.0	12.8
2 adults, 2 children	1.2	6.1	8.5
2 adults, 3 children	3.7	21.1	7.1
2 adults, 4 or more children	5.4	31.2	14.6
Others with children	11.2	8.7	18.5
All	4.9	6.3	10.7

Source: ESRI, 2001

Table 5.4: Percentage of Households Below 50% Relative Income Poverty Line by Household Composition Type, Living in Ireland Surveys, 1994, 1997 and 1998

	1994	1997	1998
1 adult	22.5	40.1	50.8
2 adults	9.3	14.1	17.3
3 or more adults	10.0	12.1	12.0
2 adults, 1 child	14.0	17.0	14.8
2 adults, 2 children	12.7	12.8	13.1
2 adults, 3 children	22.5	28.2	9.8
2 adults, 4 or more children	36.7	39.5	24.9
Others with children	32.7	26.2	28.6
All	18.6	22.4	24.6

Source: ESRI, 2001

Table 5.5: Percentage of Households Below 60% Relative Income Poverty Line by Household Composition Type, Living in Ireland Surveys, 1994, 1997 and 1998

	1994	1997	1998
1 adult	50.4	51.7	56.3
2 adults	26.1	31.6	30.6
3 or more adults	18.3	23.6	20.3
2 adults, 1 child	23.5	20.9	16.6
2 adults, 2 children	17.6	15.7	18.8
2 adults, 3 children	33.2	32.4	18.5
2 adults, 4 or more children	47.8	45.7	43.9
Others with children	46.7	40.8	39.4
All	34.2	34.3	33.4

Source: ESRI, 2001

5.9.4 Consistent poverty has also reduced for children in recent times. Consistent poverty for children fell from 24.8% in 1987 to 16.9% in 1997 and further to 12% in 1998.

While the likelihood of children experiencing consistent poverty is still higher than for adults, the difference is narrowing.

5.9.5 Nolan (2000) also offered a picture of trends in child poverty up to 1997. The following table shows that, between 1973 and 1994, the risk of relative income poverty for children increased at all three lines. Between 1994 and 1997, however, the risk for children rose at the 40% line but fell at the other two cut-off points.

Table 5.6: Risks of Relative Income Poverty for Children and Adults, 1973-97

	1973 HBS	**1980 HBS**	**1987 ESRI**	**1994 LIIS**	**1997 LIIS**
	*% of children below relative income line**				
40% line	8.1	10.1	7.6	8.0	13.2
50% line	16.2	18.5	25.5	29.5	26.0
60% line	27.5	29.5	37.8	40.2	37.2
	*% of adults below relative income line**				
40% line	7.4	7.7	6.5	6.6	9.1
50% line	15.1	15.2	16.1	18.2	20.5
60% line	24.4	25.4	26.5	31.8	34.4

Source: Nolan (2000)

* Equivalence scale 1.0/0.66/0.33

5.9.6 Nolan attributes the general decline in relative income poverty among children between 1994 and 1997 at the 50% and 60% lines to the fall in unemployment that occurred during this period. He remarks also that "*this [rapidly-increasing average incomes] contributed to the divergent pattern with the lowest relative income line, where the poverty risk for children actually rose, reflecting the fact that this line had in effect caught up with social welfare support rates*."

5.9.7 He also states that children living in larger families continued to be at high risk of relative income poverty (although this should be seen in the context of above tables showing decline in risk for these families in 1998) and a very high risk for children in households relying on social welfare payments.

CHAPTER 6 - Indexation and Uprating of Social Welfare Payments

6.1 Introduction

6.1.1 The Group's terms of reference required it to examine the implications of adopting a specific approach to the ongoing uprating or indexation of payments. This chapter examines some of the indices that might be used in this context and seeks to set out the issues and implications associated with their use. Firstly, however, it is useful to consider the purpose behind adopting any specific approach to indexation and to question whether it is necessary or desirable to do so. (The Group recognise that adoption of a benchmark denominated in terms of a particular index, whether earnings, incomes or otherwise, would contain an in-built indexation mechanism.)

6.1.2 The adoption of any specific indexation methodology will be driven by an underlying policy objective. The Group focused on three indexation methods - involving a direct linkage with prices, with earnings, or with household incomes. (Within each, there is, of course, scope for almost unlimited variation - for instance, provision could be made for prices plus a given percentage.) In relation to earnings, there is also the question of whether a gross or net measure should be used.

6.1.3 If the policy objective is to maintain the real value of welfare payments - i.e. to ensure that the purchasing power of the recipient remains constant from year to year - then a direct linkage with prices would be the appropriate approach. A linkage with gross earnings will ensure that welfare rates keep pace with the growth in average earnings and the consequent increases in the before-tax income of the average worker. Linking welfare rates to average household incomes which, inter alia, also takes account of changes in the number of people in employment, would aim to maintain the relative value of welfare payments by reference to the wider prevailing standard of living.

6.1.4 Some of the arguments rehearsed in relation to setting a benchmark rate (see Chapter 4) apply also in the case of indexation policy. Advocates of a formal specific indexation approach would contend that it is necessary to have an explicit linkage with, for example, earnings or household incomes in order to guarantee that the incomes of a vulnerable sector of society are maintained relative to the wider population and to ensure that the negative societal consequences of growing income inequalities are avoided.

6.1.5 On the other hand, it can be argued that such objectives are capable of being met without recourse to a specific indexation methodology. This is illustrated by the fact that over the past ten years, welfare increases have outstripped those in gross average earnings. The current ad-hoc system provides Government with the necessary flexibility to respond to the demands across the range of public expenditure, but without the constraints associated with a rigid system of indexation. (It was argued, however, that constraints on expenditure already exist, e.g., in relation to tax reduction commitments.)

6.2 Broad issues

6.2.1

Practicality

A critical issue in relation to indexation is that of practicality. Any indexation process requires, by definition, that a suitable index exists (or can be devised) and that it is accurate, timely and reasonably well understood. It would also be desirable that an index should not be volatile, i.e. that it would not be liable to fluctuate severely from year to year.

6.2.2

Linking to actual or projected increases?

Any projection of increases in earnings, inflation or other measures is necessarily tentative, and all the more so in a small, open economy such as Ireland's. It could be argued, therefore, that certainty would be provided by uprating welfare increases in retrospective terms - e.g. by reference to the known increase (or decrease) in the selected index in the previous year. Even in the very short-term, it can be difficult to accurately predict the likely level of increases in prices or earnings. Where estimates are used as the basis for welfare increases, and that estimate is either too high or too low, the question arises as to the extent to which there should be a balancing adjustment in the following year (This type of scenario may have different effects on long-term and short-term welfare claimants. While compensatory increases/decreases in the uprating of payments would balance out over time in the case of long-term claimants such as pensioners, short-term claimants could be relatively better off or worse off depending on where in the cycle they had recourse to welfare supports.)

6.2.3 On the other hand, uprating welfare payments by reference to the previous year's increase in the selected index, while introducing greater certainty as to the ‘right’ level of increase, would mean that increases for welfare claimants would not be contemporaneous with that of the wider population. This issue was one which the Pensions Board faced when making their recommendation in relation to pension payments – see Section 4.2.7. Having said that, the time-lag in data production for annual increases in GAIE means that there would still be an element of estimation required.

6.2.4

The Ratchet Effect

With a view to enhancing the relative living standards of welfare claimants, the option of selecting the higher of two separate indexation methods (e.g. inflation and earnings) on a year-on-year basis can seem attractive. Such an approach can create difficulties, however, by way of what is known as the ratchet effect. When welfare rates are increased in line with the growth in either earnings or inflation – whichever is the higher - in any given year, the cumulative effect is to increase payment rates at a higher rate than either prices or earnings (assuming that the relationship between the two fluctuates).

6.2.5 For example, if earnings rose one year by 10% and CPI by 5%, and the following year earnings increased by 5% and CPI by 7%, social welfare payments would see a cumulative increase over the two years of 17.7%. This would compare to a cumulative increase in earnings of 15.5% and CPI by 12.35%. Over time, the position of social welfare recipients would improve significantly relative to the working population, and there would be a negative impact on the financial incentive to work. Thus, while the intention in the formula may be to maintain a relationship between social welfare payments and earnings (with a compensatory adjustment for higher inflation), the outcome may be very different.

6.3 Indexation options

6.3.1 To the extent that it is possible, illustrative cost implications over a five-year period of adopting specific indexation methods are shown. These are derived from the indexation of the social welfare rates in place after changes announced in Budget 2001 and on a 'no-change' basis - i.e. the number of recipients in each scheme remains static (which clearly will not be the case). It should be emphasised that cost estimates only apply to existing (2001) levels of social welfare payments and do not assume any up-front benchmark-related increase which would mean, of course, that subsequent costs of indexation would be more expensive.

6.3.2 All personal social welfare rates are uprated by reference to the projected annual increase in each index. QAA rates are assumed to be 70% of the personal rates in all cases and a child equivalence rate of 34% is maintained by leaving CDA rates unchanged and channeling the additional expenditure required through the Child Benefit scheme, in line with current policy.

6.3.3

(i) Consumer Price Index

The Consumer Price Index (CPI) - which measures the rate of inflation - is published on a monthly basis by the Central Statistics Office. Figures published refer to the CPI level for the year leading up to the previous month. The CSO also publishes an annual CPI average which becomes available early in the following year.

6.3.4 *Trends to date and future projections*

Since 1991, increases in weekly social welfare rates have generally outstripped inflation, in some cases by a substantial margin, as resources were targeted towards the CSW minimum rate.

6.3.5 The following table shows the annual percentage increase in the CPI over the past decade compared with increases in the rates of sample social welfare payments for a single person.

Table 6.1: Annual percentage and cumulative increases in CPI compared to Social Welfare increases (1991-2001)

Year	STUA	OACP	LTUA	UB\DB	CPI
1991	11.1	4.1	5.8	4.2	3.1
1992	6.0	4.0	4.0	6.0	3.2
1993	4.9	3.4	3.5	4.9	1.4
1994	5.9	3.0	3.1	9.8	2.3
1995	2.5	2.6	2.5	2.4	2.5
1996	3.3	3.0	3.2	3.2	1.7
1997	4.8	3.9	4.7	4.6	1.5
1998	4.6	6.5	4.5	4.5	2.4
1999	5.3	7.2	4.2	4.2	1.7
2000	5.6	7.9	5.4	5.5	5.6
2001	10.5	10.4	10.3	10.3	4.5
1991-2001	86.6	72.2	64.6	78.2	34.2

6.3.6 Department of Finance projections suggest that inflation will fall to 3.5% in 2002, to 2.5% in 2003, levelling off at around 2% for the rest of the decade.

6.3.7 The table below shows the estimated additional costs (excluding FIS), without taking into account any existing PPF or Government commitments, if social welfare rates were to be increased in line with projected CPI increases[32] over the next five years.

Table 6.2: Estimated Annual costs (£m) of uprating social welfare rates by CPI (Base: Post-Budget 2001)

Year	Additional cost (rates)	Additional cost (CB)	Total additional cost
2002	159	41	200
2003	118	41	159
2004	96	33	129
2005	98	34	132
2006	100	35	135

[32] CPI projections provided by the Department of Finance.

6.3.8 The level of inflation in the economy is a figure which is readily available and which is easily understood. CPI figures are published on a regular basis (monthly) by the CSO. Simply linking rates to the projected inflation figure would serve to protect the real value of social welfare payments.

6.3.9 One of the objectives contained in the PPF is "*to ensure that the real value of Social Welfare payments is maintained and where possible enhanced to ensure that all share in the fruits of economic growth" (p.80).*

6.3.10 Obviously, a direct link to inflation would simply ensure that the real value of social welfare payments would be maintained at current levels and would not meet the PPF objective for the enhancement of the real value of payment. At a time when incomes are increasing at a rate significantly ahead of inflation, linking social welfare rates to the CPI would leave social welfare recipients progressively further behind the living standards of the majority of the population. One option which could be considered would be to seek to overcome this problem by providing for increases of inflation "plus".

6.3.11 Looking to the longer term, it must be acknowledged that the reverse position also holds, i.e. when incomes are falling (or increasing at a rate lower than inflation), a direct link to inflation would be relatively beneficial to social welfare recipients.

6.3.12

(ii) Gross Average Industrial Earnings

Figures for GAIE are published by the Central Statistics Office on a quarterly basis and are subject to an approximate six-month time-lag although forecasts are widely available. The CSO also publishes an annualised GAIE average which is based on the results from the previous year's four quarters.

6.3.13 *Trends to date and future projections*

Increases in GAIE over the last decade have, in aggregate terms, been outstripped by increases in social welfare rates (see Table 6.3 below). In some individual years, however, some or all of the social welfare rates were increased by less than GAIE. Over the period, Short-term Unemployment Assistance has risen, in monetary terms, by approximately 87% while GAIE has increased by 66%. In comparison, Unemployment Benefit has increased by 78% over the period with a corresponding increase in Old Age (Contributory) Pension of 72%.

Table 6.3: Annual and cumulative percentage increases in GAIE compared to Social Welfare increases (1991-2001)

Year	STUA	OACP	LTUA	UB\DB	GAIE[33]
1991	11.1	4.1	5.8	4.2	4.5
1992	6.0	4.0	4.0	6.0	3.8
1993	4.9	3.4	3.5	4.9	5.6
1994	5.9	3.0	3.1	9.8	2.8
1995	2.5	2.6	2.5	2.4	2.0
1996	3.3	3.0	3.2	3.2	4.8
1997	4.8	3.9	4.7	4.6	3.1
1998	4.6	6.5	4.5	4.5	4.4
1999	5.3	7.2	4.2	4.2	5.6
2000	5.6	7.9	5.4	5.5	7.2
2001	10.5	10.4	10.3	10.3	8.5
1991-2001	86.6	72.2	64.6	78.2	66.4

6.3.14 It should be noted that because GAIE represents only a relatively small proportion of workers, and because it reflects structural shifts peculiar to the manufacturing sector, it may not be fully indicative of wage trends in rest of the economy. Nonetheless, GAIE is likely to prove a more stable measure than AWHI (see 6.3.22 below).

6.3.15 Providing a direct link between social welfare payments and increases in gross average industrial earnings, while seeking to maintain a link between workers and social welfare recipients, would not, however, reflect the improvements in net earnings in a period where tax reductions have been introduced, as has been the case in recent years.

6.3.16 The following table shows the projected annual increases (provided by the Department of Finance) in GAIE for the next decade.

Table 6.4: Projected annual increases in GAIE (2001-2011)

Year	GAIE increase	GAIE (£ p.w.)
2001	8.5%	375.00
2002	8.5%	407.00
2003	7.5%	437.00
2004	4.9%	459.00
2005	4.2%	478.00
2006	5.3%	503.00
2007	4.6%	527.00
2008	4.6%	551.00
2009	4.6%	576.00
2010	4.7%	603.00
2011	4.7%	632.00

[33] *Average Industrial Earnings have been rebased by the Central Statistics Office from September 1995. Averages given after this period are not directly comparable with earlier figures. Average Industrial Earnings for 2000 and 2001 are estimated by the Department of Finance.*

6.3.17 The projected cost of linking social welfare rates to increases in GAIE are presented below.

Table 6.5: Annual cost (£m) of uprating social welfare rates by GAIE (Base: Post-Budget 2001)

Year	Additional cost (rates)	Additional cost (CB)	Total additional cost
2002	386	119	505
2003	370	125	495
2004	260	89	349
2005	234	79	313
2006	307	105	412

6.3.18
(iii) Net Average Industrial Earnings (NAIE)

There is no official measure of NAIE available. It is possible, however, to construct an index based on the GAIE figures in respect of a specific family type (e.g. by calculating the net income of a single person in receipt of the GAIE, taking account only of basic allowances). Such an index will not reflect the different circumstances of the various family types that exist or the range of other reliefs available. This method is used to construct the index used in Table 6.6.

6.3.19 *Trends to date and future projections*
Increases in NAIE have outstripped increases in social welfare rates (see Table 6.6 below) significantly over the last decade, mainly due to the significant tax changes that have been made over the period.

Table 6.6: Annual and cumulative percentage increases in NAIE compared to Social Welfare increases (1991-2001)

Year	STUA	OACP	LTUA	UB\DB	NAIE increase
1991	11.1	4.1	5.8	4.2	4.7
1992	6.0	4.0	4.0	6.0	6.2
1993	4.9	3.4	3.5	4.9	3.0
1994	5.9	3.0	3.1	9.8	5.6
1995	2.5	2.6	2.5	2.4	5.2
1996	3.3	3.0	3.2	3.2	5.7
1997	4.8	3.9	4.7	4.6	6.1
1998	4.6	6.5	4.5	4.5	7.0
1999	5.3	7.2	4.2	4.2	11.4
2000	5.6	7.9	5.4	5.5	9.2
2001	10.5	10.4	10.3	10.3	12.6
1991-2001	86.6	72.2	64.6	78.2	109.1

6.3.20 Future changes in net average earnings are critically dependent on changes in the taxation and social insurance regimes. In the absence of forecasts in relation to these factors, it is not possible to construct a reliable projected index of NAIE. This presents an obvious problem in attempting to determine the likely cost and other effects of indexing social welfare rates to NAIE in the future.

6.3.21 Nonetheless, by taking account of tax changes, the NAIE measure can be seen as a closer approximation of disposable incomes than GAIE. Once more, however, it is important to bear in mind that net earnings growth will not always exceed gross earnings growth. While net earnings have outstripped gross earnings in recent years, this was not the case during the 1980s when only modest increases in tax allowances allied to the introduction of income levies saw increases in gross earnings substantially exceed net earnings growth.

6.3.22

(iv) Average Weekly Household Income (AWHI)

The available figures for Average Weekly Household Income are based on the ESRI's analysis of the annual Living in Ireland Survey. The figure is derived by analysing the household data and applying an equivalence scale to reduce the figure to an average single person's income.

6.3.23 *Trends to date and future projections*

Increases in welfare payments, and all other measures/indices, have lagged significantly behind increases in AWHI (due largely to employment growth) in recent years, and this explains, in large part, the recorded increase in relative income poverty (see Chapter 7) which has been observed over the period. As data on household incomes from the Survey have been published on an intermittent basis only, we do not have a year-on-year retrospective index for AWHI. The available figures for AWHI relate to the years 1994, 1997 and 1998 - when the ESRI analysed the Living in Ireland Survey data from a poverty perspective. Table 6.7 (below) shows the increases in AWHI and rates of selected social welfare payment during the time periods in question.

Table 6.7: Percentage increases in AWHI compared to Social Welfare increases (1994-1998)

Period	STUA	OACP	LTUA	UB/DB	AWHI
1994-1997	11.0	9.9	10.7	10.6	27.3
1997-1998	4.6	6.5	4.5	4.5	13.6
1994-1998	16.1	17.0	15.7	15.6	44.6

6.3.24 From a practical perspective, there is a significant time-lag (to date, two years) in the publication of AWHI data. For example, the latest available data on AWHI relate to 1998.

This causes particular problems in trying to link social welfare rates - which are adjusted annually - with this measure.

6.3.25 Given that the composition of AWHI is a function of a number of factors - notably, changes in the tax and social insurance regimes, in household composition, in earnings levels, and in the number in employment - it is not possible to construct a meaningful projection of changes in AWHI. Indeed, changes in household composition and the number in employment can lead to fluctuations in AWHI at a time when wage levels remain stable.

6.3.26 The key merit of linking welfare rates to average household incomes, however, is that it would act to maintain the relative value of welfare payments by reference to the wider prevailing standard of living (requiring that AWHI can adequately capture this concept). If this is the desired objective, it might equally be met by linking welfare rates to a different measure - e.g. gross earnings - and adjusting the level of increases as AWHI data becomes available if it is demonstrated that the objective is not being met. This approach, however, may be rather unwieldy and fails to meet the objectives of practicality as stated earlier in this chapter.

CHAPTER 7 - Relative Income Poverty

7.1 Background

7.1.1 The National Anti-Poverty Strategy (NAPS) set a global target of reducing the number of people in consistent poverty over the lifetime of the Strategy. This measure, developed by the ESRI and described below, combines elements of both low income and deprivation.

7.1.2 The Group's terms of reference required it to examine the issue of relative income poverty which is an alternative poverty measure based on income alone. The potential effect on relative income poverty of increasing social welfare rates to particular levels has already been shown. This chapter provides a more in-depth analysis of relative income poverty, examining the concepts behind the measure, recent trends in Ireland, and the various causal factors that lead to fluctuations in its level. While the Group identified some of these causal factors, it was not in a position to fully examine their relative impacts on the measure.

7.2 Definitions and concepts

7.2.1 The concept of 'relative poverty' is based on the view that poverty cannot be viewed in an absolutist manner - i.e. that all citizens must have an absolute minimum necessary for survival - but rather that the poverty standard must reflect wider prevailing social standards. Townsend (1979) suggests that people experience relative poverty when "*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*". The NAPS definition is similarly framed in terms of exclusion from *"activities which are considered the norm for other people in society*". Thus, a fundamental requirement in attempting to quantify the extent of relative poverty is that the particular measure used can adequately capture what are widely regarded as "normal" or "average" living standards. There are a number of ways of measuring relative poverty (see Chapter 2.4.1 for an overview of some methods). Two commonly cited measures in Ireland are 'consistent poverty', as used in the NAPS overall target, and 'relative income poverty'.

7.2.2 Relative income poverty is defined by reference to an income threshold set at a particular percentage of average (either mean or median) income, adjusted for family size and composition using equivalence scales. In Ireland, data on the levels of relative income poverty have been derived from analysis of the results of the Living in Ireland Survey and Household Budget Surveys and is typically expressed in terms of percentages of mean household disposable income.

7.2.3 The issue of relative income poverty forms part of a wider debate on the nature and extent of poverty generally; the manner in which poverty is measured; the manner in which poverty reduction targets set by Government in the National Anti-Poverty Strategy are framed;

and the effectiveness or otherwise of the policy measures devised to tackle and eradicate poverty.

7.2.4 This first point of focus in the debate relates to the methodology employed to measure poverty, and specifically on the relative merits of the two measures most commonly used here in Ireland - relative income poverty and consistent poverty.

7.2.5 It was have noted earlier how relative income poverty is defined. While it is a valid instrument, it is limited and cannot, in isolation, reliably capture the full extent of poverty and the types of household most seriously affected. Some of the issues associated with the relative income poverty instrument are explored later in this chapter.

7.2.6 The consistent poverty measure was developed by researchers at the Economic and Social Research Institute in seeking to overcome some of the difficulties associated with a purely income-related poverty measure (see Section 7.6.2). The ESRI have stated that the value "*in using both income and indicators of deprivation, rather than income alone, is that one can identify more accurately those excluded from the ordinary life of society due of lack of resources*". It seeks to quantify the numbers falling below percentages of average weekly household equivalent income (AWHI) and also experiencing enforced basic deprivation. The deprivation index used is also a relative measure as items are included on the basis of a survey of households where people are asked whether they consider items to be basic necessities, whether they have them, and whether an absence of an item is enforced due to lack of money. Therefore, the threshold of deprivation should rise over time to reflect general improvements in living standards. To date, the basic deprivation indicators have not changed since they were first applied in 1987.

7.2.7 Relative income poverty includes all those falling below a specified percentage of AWHI. It is inevitably the case that deprivation (as defined by the index used by the ESRI) is not experienced by all those falling below the income lines. Therefore, the numbers falling below the relative income lines are invariably larger than those that experience consistent poverty. Each measure provides relevant insights into different aspects of poverty and income distribution although, depending on the particular policy focus, their value as targets or indicators may be quite different.

7.2.8 It can be seen therefore that, while households in consistent poverty are a subset of households in relative income poverty, the two instruments are aimed at capturing different life situations[34]. While subject to certain limitations, each is an intrinsically valid instrument

[34] It should be noted that it is possible for households above arbitrary income lines to experience "generalised deprivation", as measured by the basic deprivation index. However, the ESRI combine the relative income poverty lines with the basic deprivation index to construct the consistent poverty measure in which households have both a limited income and are experiencing basic deprivation.

but, as will be seen below, each has followed quite different trends in Ireland in recent years. Rather than being seen as conflicting, however, it is suggested that the two measures can better be viewed as complementary, providing a more rounded and clearer picture of the evolution of poverty over time and a better understanding of the policy steps required to tackle poverty.

7.3 Measurement

7.3.1 The measurement of income in the Living in Ireland Survey (the Irish element of the European Community Household Panel) is based on the results of a questionnaire which is answered by the household reference person. The study is a longitudinal one, i.e. the same households are questioned annually, although some attrition has occurred in the sample (see 7.3.3 below). Following Eurostat guidelines, the household reference person is defined as the owner or tenant of the accommodation or, in cases of joint ownership or tenancy, the older of the two or more persons who are equally responsible for the accommodation.

7.3.2 For most sources of income, details are recorded in respect of the amount received in the current pay period although a longer reference period was used for certain other income sources (e.g. self employment, farming, investment income). The income data relates to disposable income (which includes social welfare payments) which is defined as gross income minus compulsory deductions of income tax, health and social insurance payments. It is important to note that "*all other deductions, including superannuation contributions, Trade Union subscriptions, life insurance premia, VHI subscriptions, regular savings or mortgage repayments deducted by the employer at source from gross pay, etc., were added back to the net take-home pay to provide our measure of disposable income*." (Callan et al, 1996:52). As is explained later in this chapter, the Survey does not attribute value to either non-cash benefits provided by the State or those provided to employees by their employers.

7.3.3 It should be noted that there has been a sizeable amount of attrition in the Survey sample between 1994 and 1998. While this has occurred, the ESRI has applied a set of weights to the sample to compensate for any known biases in the distribution of characteristics in the completed survey sample. Accordingly, the ESRI states that "*the evidence at this point does not suggest that households with specific characteristics related to the measurement of poverty and income distribution are being selectively lost from the sample*" (ESRI, 2000, p.9). This is qualified, however, by the statement that "*given the scale of attrition and the shrinking size of the sample, the results presented have to be seen in the light of the possibility that an unmeasured bias has been produced*" (ESRI, 2000, p.9). For this reason, the Survey was supplemented during the 2000 wave of interviewing with the support of the Department of Social, Community and Family Affairs.

7.4 Survey evidence

7.4.1 The data produced by the ESRI clearly demonstrates the different functions of the two poverty measurement instruments. It shows that, since 1987, the number of households falling below the relative income lines has generally increased while the level of deprivation has fallen. This has resulted in a drop in consistent poverty in recent years but an increase in relative income poverty (except at the 60% line).

7.4.2 The trends in the numbers falling below the relative income lines (drawn at 40%, 50% and 60% of AWHI) over the course of the period from 1987 to 1998 are shown in Table 7.1 below.

Table 7.1: Percentage of Households falling below relative income lines

	1987	1994	1997	1998
40% AWHI	6.2	4.8	6.3	10.5
50% AWHI	16.3	18.6	22.4	24.6
60% AWHI	28.5	34.1	34.3	33.4

Source: ESRI, 2000

7.4.3 One can see that, with the exception of the 60% line (where relative income poverty has begun to fall), there has been a general increase in those falling below the relative income lines since 1987. One of the obvious reasons for these increases is that, in a period of exceptional and sustained economic growth, increases in average incomes (driven in large part by increased numbers of people in employment) outstripped the increases applied to social welfare rates, notwithstanding the fact that these latter increases were, in turn, substantially ahead of prices.

7.4.4 This rise in the incidence of relative income poverty, while illustrating that more people are living on incomes well below the average, also masks a rise in the real incomes of the poor. For instance, the ESRI data shows that, at an income standard set at 50% of mean equivalised income in 1987 and adjusted in line with prices only, the number of households falling below that line declined from 16.3% in 1987 to 5% in 1994 and to 1.7% in 1998. More pertinently, consistent poverty (measuring households below the 60% relative income line and experiencing enforced basic deprivation) declined from 16% in 1987 to 15.1% in 1994 and to 8.2% in 1998.

7.4.5 The above figures show that there are a number of different trends occurring in each of the measures analysed. Consistent poverty and the real income standard measures show that living standards have been rising over a number of years with the result that people in general have more resources at their disposal than in previous years. However, the relative income poverty measure shows that, compared to the population in general, there are a greater number of people on low incomes in comparison to the average. Neither outcome can be ignored if a rounded perspective on the evolution of poverty over time is to be gained.

7.5 Issues associated with relative income poverty

7.5.1 It will be recalled that the measurement of relative income poverty seeks to quantify the level of poverty defined as having a level of income "seriously below" that generally enjoyed by society (Townsend, 1979). As such, it is a useful tool for illustrating the level of low income in society at a point in time and the trends in low income over the longer term. As a widely used instrument, it also facilitates cross-country comparisons.

7.5.2 Used in isolation, however, the relative income poverty measure gives rise to a number of issues. Briefly, these include:

- As 'income' under this definition is essentially limited to cash income only, no account is taken of factors such as access to non-cash benefits or, perhaps even more importantly, housing costs, which can have a significant effect in determining command over resources. Thus, AWHI, as currently measured, may not adequately capture the concept of "normal" or "average" living standards which is fundamental to the measurement of relative poverty;
- A focus on the numbers below a particular line does not take account of the depth of poverty (see below) of these households;
- Any marked increase in living standards of those under the income line, which is also shared by the rest of the population, is not reflected in the numbers living in relative income poverty;
- Conversely, during a recessionary period, a general decline in living standards of the population as a whole may leave unchanged, or even reduce, the number of people experiencing relative income poverty and will tend to overlook the fact that the incomes of people relying on welfare payments may actually have declined in real terms. For example, in Hungary, the relative income poverty rate would have decreased between 1991 and 1997 from 15.3% to 13.9% using the relative threshold of 60% of the median of each year, but it would have increased from 15.3% to 37.3% when holding the 1991 threshold constant in real terms;
- Since it focuses on current income only, no account is taken of the way resources have been accumulated or eroded over time, factors which play a key role in influencing the likelihood of current deprivation and exclusion;
- Another issue relates to the cut-off point for the definition of relative income poverty. Do we use mean or median household income? Do we use a 40%, 50% or 60% line? The choice of a particular percentage is necessarily arbitrary, although the use of a median line removes the sensitivity of the measure to a small number of very high or very low incomes, which may not be representative of social 'norms';
- Even accepting an arbitrary income threshold, simply measuring the stock of people below that threshold at a point in time tells us nothing about the persistence or mobility of

such households at that income level - a key factor in determining their relative living standards.

7.6 Issues associated with the consistent poverty measure

7.6.1 Consistent poverty, as noted earlier, is defined as falling below 50%-60% of average weekly household equivalent income (AWHI) combined with the experience of enforced basic deprivation. The inclusion of the deprivation indicators effectively captures the notion of resources being eroded over time from persistence on low incomes.

7.6.2 Critics of the consistent poverty approach suggest that the deprivation index does not capture the reality of living in poverty and places too much emphasis on very basic living conditions, thus understating the true level of poverty. In particular, commentators have pointed to the list of basic deprivation indicators which has remained unchanged since 1987, arguing that this does not capture the rise in living standards we have seen since then.

7.6.3 The basic deprivation indicators are:

- Not having new, but second-hand clothes;
- Not having a meal with meat, fish or chicken every second day;
- Not having a warm waterproof overcoat,
- Not having two pairs of strong shoes;
- Not having a roast or its equivalent once a week;
- Had day in the last two weeks without a substantial meal;
- Had to go without heating during the last year through lack of money;
- Experienced debt problems arising from ordinary living expenses or availed of charity.

7.6.4 The ESRI emphasises that the basic deprivation items used in the consistent poverty measure are not intended to define the standard of living of the household in either a descriptive or a normative fashion. Instead, the aim is to identify a group of households that are distinguishable from the remaining ones in terms of a set of characteristics that conform with a theoretical understanding of the phenomena of poverty.

7.7 Relative Merits of the Two Measures

7.7.1 Sections 7.5 and 7.6 identified many of the issues associated with the use of the relative income poverty and consistent poverty methodologies as poverty measurement tools. According to the ESRI, who devised the measure, consistent poverty identifies households and people who are experiencing generalised deprivation due to lack of resources. As noted earlier, the 'consistently poor' is a subset of all those that fall below the 50% and 60% relative income lines (i.e. those that experience relative income poverty). In that respect, while there is debate about the appropriateness of either approach, the starting point in each case is the identification of those below a percentage of Average Weekly Household Income. The question is whether this cohort of the population needs to be further disaggregated.

7.7.2 A discussion on the relative merits of each of these measures needs to address, inter alia, the following questions:

What situation does each of the measures aim to capture and do they do this successfully?

7.7.3 As stated above, the ESRI's consistent poverty measure aims to identify a group of households/people who are experiencing generalised deprivation due to lack of resources. In the first instance, the households identified are only those who fall below a particular percentage of AWHI. Based on the assumption that a 'point in time' income measure cannot tell the whole story about people's standard of living (e.g. a household's income could fluctuate throughout the year and the AWHI measure, for the most part, only asks about income from the previous week), the use of a deprivation index attempts to identify those who are both on low incomes and experiencing generalised deprivation. If a household scores on one or more items in the deprivation index, it is then assumed to be living in consistent poverty. In this respect, one could say that the consistent poverty measure successfully identifies a cohort who are not only experiencing generalised deprivation, but who are experiencing this due to a lack of both money and resources. The opposing argument here hinges on what generalised deprivation actually means and how it is measured.

7.7.4 In this regard, the validity of the consistent poverty measure was disputed by some members of the Group. In their view:

- the consistent poverty measure is based on an unrealistic and out-of-date set of indicators (which have been unchanged for fourteen years) and, thus, does not take account of rising living standards as provided for in the NAPS definition of poverty, i.e. those who are "excluded and marginalised from participating in activities which are considered the norm for other people in society";
- the measure, while identifying a specific group of people with a particular experience of poverty, does not identify all those who are poor;
- it simply distinguishes between the very poor and the poor, a distinction that tends to lead in practice to a situation where the poor receive far less priority than is required if their situation is to be tackled;
- the results produced through this measure should be examined in conjunction with other research undertaken by international bodies[35].

[35] E.g. Annual UN Human Development Reports; Reports of the Institute for Public Health

7.7.5 The majority of the Group did not accept these views and tended towards the position stated regularly by the ESRI to the effect that the aim of the measure is to identify a group of households that are distinguishable from the remaining ones in terms of a set of characteristics that conform with a theoretical understanding of the phenomena of poverty. (See also 7.7.13 et seq below.)

7.7.6 The aim of a relative income poverty measure is to identify a group of households/people on incomes well below the average in society. In that respect, it aims to reconcile the measure with definitions of poverty (which have become generally accepted) which categorise as poor those people whose income and resources are not adequate to enable them to participate in activities which are considered the norm for other people in society. While the relative income poverty measure seeks to identify people well below average incomes, reservations about the ability of AWHI, which underpins the relative income poverty measure, to fully capture "normal" or average living standards have previously been noted. Notwithstanding this point, it is also open to question whether it follows that all people living on these incomes are necessarily excluded from participating in activities which are the norm. There are two main reasons for this. Firstly, as we noted above, the income measurement is done on a preceding week basis and does not take account of accumulated savings or other resources. Secondly, in a period of rapidly increasing incomes, it may take some time before the expectations of what is considered the 'norm' in society catch up with these increasing incomes.

7.7.7 A problem common to both measures is that each uses arbitrarily chosen cut-off points for income. For example, is a household on 59% of AWHI and experiencing deprivation in consistent poverty while a household on 61% of AWHI and experiencing deprivation is not? The same applies to those just above and below the lines used for identifying those in relative income poverty.

Do each of the measures perform consistently over time while other (e.g. macro-economic) circumstances change?

7.7.8 Both consistent poverty and relative income poverty have been measured on a regular basis over the past number of years. Since 1994, we have seen a general decline in consistent poverty and an increase in relative income poverty (except at the 60% AWHI line, where this measurement of poverty has begun to fall).

7.7.9 In the case of consistent poverty, it is claimed that the reduction in its level reflects the increases in living standards experienced by those in poverty over the last number of years. This is borne out by data which shows increases in the real incomes of the poorest in society over recent years (see Section 7.4.4). It should be noted, however, that the basic deprivation index has remained static during this period and has not been supplemented on the basis of increasing living standards since 1987.

7.7.10 With regard to the relative income poverty measure, again it is seen that this performs largely as would be expected. As social welfare payments have lagged increases in household incomes in the last number of years, it would be expected that more households would fall below the respective relative income lines and this has generally been the case. This must be set against the backdrop of unprecedented and rapid increases in household incomes, however.

7.7.11 In view of the rapid increases in incomes over recent years, one may question whether the relative income poverty measure, focusing on a 'point in time' analysis on a year-on-year basis, is capable of fully reflecting the reality of poverty over time. This may be overcome somewhat by further study into the persistence of relative income poverty over a number of years. The ESRI (Layte et al, 2001) found that, through recording the number of people below the relative income lines on a persistent basis over a period of five years, the consistently poor have a distinctive persistent poverty profile. The authors conclusion was that "*this finding complements the evidence ... that the present consistent poverty measure is quite successful in identifying a group who have experienced what would be seen as serious deprivation as a consequence of a persistent shortage of income*" (p.64-65).

Are the methodologies used statistically robust?

7.7.12 The methodologies used in calculating both relative income poverty and consistent poverty have already been covered in Sections 7.2 and 7.3. While there was some concern in recent years with regard to the attrition of the sample of households in the Living in Ireland Survey, this has been relieved somewhat by supplementation in the 2000 wave.

7.7.13 The main point of concern that has been raised in relation to the measures has been the validity of the basic deprivation index as the indicators used in assessing basic deprivation (used to calculate the level of consistent poverty) have not changed since it was first formulated in 1987. Several members of the Group have argued that the index does not reflect the actual experience of living in poverty.

7.7.14 The ESRI has undertaken analysis in recent years to assess whether the basic deprivation index should be broadened at this point in time. If relying solely on responses to the survey questionnaires, an additional five items from the secondary deprivation index would have been included in a revised basic deprivation index as they were now available to a substantial majority of households and came to be perceived as necessities by comparable numbers. Using factor analysis, however, which assesses variables according to their correlative status, the ESRI (2001) found that:

7.7.15 "... *results for the late 1990s turn out to be remarkably similar to 1987. In particular, the additional five items on which we are focusing continue to cluster with the secondary rather than basic deprivation. Since these results suggest that these dimensions continue to* *be determined by rather different factors ... we should restrict ourselves to the original basic deprivation items*."

7.7.16 Further analysis found that households that would be regarded as consistently poor on the basis of the addition of the five items to the basic deprivation index were little different from the non-poor, and quite different to the current consistently poor, in terms of the level of (self-assessed) economic strain, psychological distress and fatalism.

7.7.17 The majority of the Group recognised that the ESRI has undertaken a rigorous statistical analysis of the index and has found that, at this point, it remains relevant in identifying a set of households that is experiencing generalised deprivation as a result of prolonged constraints in terms of command over resources.

7.8 Depth of Poverty

7.8.1 While a simple headcount of numbers below the income lines offers part of the picture of the prevalence of poverty, it does not take account of the depth of poverty of those below the lines. The ESRI uses two measures to determine the depth of poverty, i.e. the per capita income gap and the distribution-sensitive weighted poverty gap. The per capita income gap, in effect, combines information on the proportion of the sample falling below a particular income line and the size of the gap between their incomes and that income line. The second measure is also sensitive to the distribution as well as the depth, i.e. it has the effect of giving most weight to those whose income gaps are greatest (those with the lowest incomes).

7.8.2 While the period between 1987 and 1994 saw a fall in the depth of poverty, the years between 1994 and 1998 saw the poverty gap rise again for both measures (and for all equivalence scales although only the 1.0/0.66/0.33 scale is used here) as the tables below show. (The higher the figure in the table, the greater the depth of poverty for that year.)

Table 7.2: Per Person Income Gaps Using Relative Income Poverty Lines, 1994, 1997 and 1998

Relative Poverty Line								
40%			*50%*			*60%*		
1994	1997	1998	1994	1997	1998	1994	1997	1998
.0103	.0137	.0161	.0338	.0390	.0427	.0736	.0775	.0775

Table 7.3: Distribution-sensitive Weighted Poverty Gap Measure Using Relative Income Poverty Lines and Different Equivalence Scales, 1994, 1997 and 1998

Relative Poverty Line								
40%			*50%*			*60%*		
1994	1997	1998	1994	1997	1998	1994	1997	1998
.0030	.0046	.0056	.0094	.0121	.0139	.0228	.0263	.0281

7.9 Composition of households experiencing Relative Income Poverty and Consistent Poverty

7.9.1 While the trends in numbers experiencing consistent poverty and those experiencing relative income poverty seem to be moving in opposite directions, it is useful to examine the breakdown (i.e. the percentage of poor taken up by specific groups) of households experiencing these forms of poverty to determine whether the composition of the groups differ to any notable extent. (It should also be recognised that farmers' income is calculated through the completion of a dedicated farm questionnaire which uses income from the previous year as its reference. In this respect, it should be borne in mind that farmers are subject to income fluctuations which may overstate or understate poverty levels, depending on the year being analysed.)

Table 7.4: Breakdown of Households experiencing relative income poverty and those experiencing consistent poverty (at 60% line) by Labour Force Status

Head of Household	60% Relative Income Poverty Line (1998)	60% Relative Income Line Combined with Deprivation (1998)
Employee	8.4	7.4
Self-employed	5.7	2.6
Farmer	7.2	4.7
Unemployed	14.5	25.6
Ill/disabled	7.1	10.8
Retired	23.1	17.4
Home Duties	34.1	31.5

Source: ESRI, 2001

7.9.2 In the case of the unemployed, one can see here that the proportion of those experiencing consistent poverty is much higher than the proportion of those below the relative income poverty line. This suggests that, while retirees and those on home duties dominate those that are experiencing relative income poverty at the 60% line, the unemployed become more prominent when one considers the impact of consistent poverty. People on home duties (at least some of whom have a potential labour force attachment) remain as the largest group when deprivation is taken into account.

7.9.3 It may also be useful to compare the respective risks (i.e. the percentage of a particular group who experience poverty) of households in relation to these two concepts of poverty.

Table 7.5: Risk of households experiencing relative income poverty and those experiencing consistent poverty (at 60% line) by Labour Force Status

Head of Household	60% Relative Income Poverty Line (1998)	60% Relative Income Line combined with deprivation (1998)
Employee	6.7	1.4
Self-employed	23.3	2.5
Farmer	35.1	5.3
Unemployed	72.1	29.7
Ill/Disabled	80.4	28.1
Retired	42.7	7.5
Home Duties	69.3	15.3

Source: ESRI, 2001

7.9.4 We can see some stark contrasts between the risk levels for groups in relation to these two poverty measures. For instance, while 69.3% of households headed by someone on home duties fall below the 60% line, 15.3% - or just over one fifth of those falling under the line - experience consistent poverty.

7.9.5 On the other hand, 72.1% of households with an unemployed person as head fall below the 60% relative income line. 29.7% of the unemployed are at risk of consistent poverty. This implies that over 40% of households with an unemployed head below the 60% line are experiencing deprivation. Similarly, 35% of households headed by a person who is ill or disabled and who are below the 60% line also experience basic deprivation.

7.9.6 These figures underline the fact that while the concepts of consistent poverty and relative income poverty are intertwined, they effectively measure two very different things and are affected by different influences. Indeed, this is emphasised by the opposite trends both concepts have been displaying over the past decade.

7.10 Targeting Poverty

7.10.1 When the National Anti-Poverty Strategy (NAPS) was launched in 1997, the Government announced a target to reduce consistent poverty to below 5-10% by the year 2007. The target was set by reference to the latest available data (1994) at that time which showed consistent poverty at a level of 9-15%. Upon publication of more up-to-date data (1997) from the ESRI, which showed consistent poverty at a level of 7-10%, the Government revised its target in 1999 and now aims to reduce consistent poverty below 5% by 2004. The latest figures, relating to the 1998 Living in Ireland Survey, show that movement towards this target continued as consistent poverty was then at a level of 6-8%.

7.10.2 The ESRI has promoted the consistent poverty measure as a better method of identifying those who are excluded due to a lack of resources rather than relying on an income measure alone. This is based on the understanding that it captures a group of households that are on low income and also do not have the back-up resources to avoid deprivation. The ESRI has also suggested, however, that solely relying on a consistent poverty measure as a poverty target may not be the most appropriate route to take:

7.10.3 "*Very rapid economic growth has produced very welcome improvements in living standards not only in absolute terms but relative to general notions of adequacy in the society, and this has been captured by the consistent poverty measure. However, in the future, when growth rates have stabilised at more normal levels for some time, expectations and views about adequacy are likely to catch up and new, higher standards will be set in the society as to what constitutes acceptable living standards and capacity to fully participate in ordinary life. In thinking about poverty targets as opposed to measuring poverty at a point in time, this has to be taken into account."*[4]

7.10.4 For this reason, the ESRI (ibid.) has suggested the adoption of a tiered poverty target, along the following lines:

"a) Priority is given to ensuring that those on low incomes see their real incomes rise, and their deprivation levels using a fixed set of indicators decline.

b) Next, relative incomes and deprivation levels using a set of deprivation indicators which changes as far as possible in line with expectations should produce a decline in the combined income/deprivation measure.

c) Finally, the proportion of the population falling below relative income poverty lines, particularly for a sustained period, should be declining".

7.10.5 The stated rationale behind this set of tiered targets is that each of these tiers can be regarded as encapsulating a necessary but not sufficient condition for a sustainable reduction in poverty. In the case of (a), the rationale is that it reflects the assumption that if real incomes of the poor are falling and their deprivation levels rising, then, even if their relative positions were improving, most people would see poverty as increasing. In the second tier (b), this reflects the assumption that the combined effect of changes in relative incomes and deprivation should be to reduce the extent of what is regarded as exclusion at a point in time. Finally, (c) reflects the assumption that, in the long term, poverty can only be eradicated if no section of the community falls too far, for too long, below the level of command over resources generally available in society.

[4] "Monitoring Poverty Trends and Exploring Poverty Dynamics in Ireland", ESRI, 2001

7.11 Children and Relative Income Poverty

7.11.1 The latest data available for relative income poverty among children relates to 1997 and is based on results of that year's Living in Ireland Survey. "Child Poverty in Ireland" (Nolan, 2000) analyses this data in more detail. The report shows that one in four Irish children live in households with incomes below 50% of AWHI. Two in five children live in households with incomes below 60% of AWHI.

7.11.2 Other findings were as follows:

- From 1994 to 1997, the poverty rates for children declined at the 50% and 60% relative income lines but increased at the 40% line.
- Children in out-of-work families are at greatest risk of poverty (i.e. where the head of household is unemployed, ill or disabled or engaged in home duties). Such families account for two-thirds of all poor children.

7.11.3 As far as children overall are concerned, it is worth noting that the gap in relative income poverty rates between working-age households with and without children narrowed very substantially between 1994 and 1998, and by 1998 had come close to converging. There remain, however, specific types of households with children which have relatively high poverty risks - notably lone parent families and dual-parent families with 4 or more children - and a significant proportion of children still live in households where no-one is in paid work, due to either unemployment, illness/disability, or working full-time in the home.

7.11.4 Consistent poverty has reduced for children in recent times. Consistent poverty for children fell from 24.8% in 1987 to 16.9% in 1997. Figures are available for 1998 in respect of children's consistent poverty and show a further drop to 12%. It should be noted, however, that, as with relative income poverty, the likelihood of children experiencing consistent poverty is still higher than for adults reflecting the fact that children outnumber adults in poor households, although, again, the risks for both adults and children have been converging over recent years.

7.12 Non-Cash Benefits and Relative Income Poverty

7.12.1 When mean disposable incomes are calculated as part of the Living in Ireland Survey, they do not take into account either the non-cash benefits distributed by the State nor those given to employees by some employers (e.g. creche, sports facilities). It has been claimed that the absence of such an analysis may distort the overall level of relative income poverty.

7.12.2 The ESRI has recently published a report on the effect that these non-cash benefits may have on the numbers below the various relative income lines. The paper, while recognising limitations in the methodology, used imputed values for the various non-cash benefits and calculated revised figures for the extent of relative income poverty.

7.12.3 In the first instance, the ESRI assessed the impact, in 1994, of including State non-cash benefits (including the medical card) in the analysis. This showed a reduction in relative income poverty at all three lines.

Table 7.6: Percentage of Households Below Relative Income Poverty Lines Excluding and Including State Non-cash Benefits, 1994

% of mean equivalised income	Income excluding non-cash benefits[36]	Income & non-cash except medical card	Income & all non-cash benefits
40% line	5.0	4.9	3.9
50% line	19.1	16.8	14.5
60% line	34.6	31.2	27.0

7.12.4 The 1994 Survey also contained a series of questions "on the receipt of a limited range of fringe benefits from employment" for those that worked more than 15 hours per week. These included pension contributions, childcare, health/medical insurance, sports/leisure facilities, and subsidised housing/mortgage.[37] The ESRI then estimated approximate valuations for each of the benefits. As is shown below, when these benefits are added into the equation, they offset some of the effect of State non-cash benefits. It should be noted that, while the ESRI included the impact of employer pension contributions, this was not deemed appropriate by some members of the Group who considered that, as these contributions provide an income stream on retirement (some of the currently retired population are in receipt of such pension payments), it is not appropriate to also include the current value for these contributions. On the other hand, the view was expressed that one of the issues faced by poor people is the lack of provision for their own and their family's future. That issue is being addressed, in part at least, for the better off by the provision of pension contributions that, in effect, increase their assets.

Table 7.7: Percentage of Households Below Relative Income Poverty Lines Adjusting Income for State & Employer Non-cash Benefits

	Cash Income	+ State Non-Cash Benefits	+ Employer non-cash (except pension)
40% line	5.0	3.9	4.1
50% line	19.1	14.5	15.2
60% line	34.6	27.0	27.8

[36] Note that these figures may be slightly different from figures for the same year elsewhere in this report as figures are published at different times and ongoing analysis of the LIIS leads to slight changes in reported poverty levels.
[37] Very few employees said they benefited from housing/mortgage subsidies. About 3% had employer funded childcare, 12% had employer-provided sport or leisure facilities, 41% had pension entitlements, and 14% benefited from healthcare/insurance.

7.12.5 The authors of the report emphasise that the computation of values both for State and employer non-cash benefits is not without its difficulties and judgements and that results should be viewed as a supplement to existing data rather than a replacement for figures based on cash income.

CHAPTER 8 -Summary & Conclusions

8.1 Introduction

8.1.1 In the earlier Chapters of this report, the Group examined the concept of adequacy, set out the context in which the Group's work was set, and examined the issues associated with the development of benchmarks for adequacy of adult and child welfare payments and the issue of indexation. The issue of relative income poverty was also examined. Having done so, we set out here the views of the Group as to how the complex issues involved may be advanced.

8.2 Adequacy

8.2.1 Due to the wide variety of perspectives which can be brought to bear on the question of adequacy, it is acknowledged that it is not possible to derive an adequacy rate which is indisputable and universally accepted. Chapter 2 outlined some of the approaches that have been taken in attempting to derive an adequate income level. The work undertaken by the Commission on Social Welfare and by the ESRI, for example, produced a range of income levels rather than a single figure, underlining the difficulties involved. Some of the issues associated with deriving a value for non-cash benefits provided by the State to certain social welfare claimants were also noted.

8.2.2 The Group's aim in dealing with the issue of adequacy was to seek to reconcile the PPF objective (i.e. "to provide every person with sufficient income to live life with dignity") with the various criteria set out in our terms of reference (i.e. economic, budgetary, PRSI contribution, distributive and incentive implications, and trends in economic, demographic and labour market patterns), with a particular focus on the lowest current welfare rates payable.

8.2.3 Set against that background of conflicting views on the nature of adequacy, the effective outcome is that the definition of an adequacy standard is as much, at least, a reflection of political and economic judgement as it is the outcome of efforts to arrive at an objective view of 'how much is enough'. In that context, the Group believes that there is scope for enhancements in the area of research into income adequacy in order that the policy-making process is increasingly better informed in the future**.** The Group recommends that priority should be given to updated research on the costs of rearing children. In addition, the need for quantitative economic analysis of the impact of social welfare changes was identified as an area which particularly merits further detailed research.

8.3 Context

8.3.1 Chapter 3 explored the context in which the Group's deliberations were set, noting the relevant commitments in the Programme for Prosperity and Fairness as well as other significant Government commitments, notably in relation to Child Benefit.

8.3.2 As well as noting the short term spending pressures on areas such as infrastructure, health and pay, the Group also noted the significant long term expenditure demands associated with the changing demographic profile, particularly on old age pensions, long term care and health care for the increasing elderly population. In looking at labour market and economic issues, the Group sought to identify the various strands of the relationship between welfare expenditure and the wider economy. The issues associated with the development of the social insurance system were also noted.

8.4 Benchmark for adult payments

8.4.1 Chapter 4 explored firstly the issue of the appropriateness or otherwise of setting a benchmark for welfare payments, citing a range of views on either side of this debate and then proceeded to examine the implications of introducing a number of illustrative benchmark options.

8.4.2 The Group's terms of reference did not require it to make a recommendation on the issue of what particular benchmark, if any, might be adopted by Government. Nonetheless, the Group sought to explore the potential for achieving consensus on this difficult issue. In the event, given the very diverse range of views held by the members of the Group, such a consensus was not achieved. The debate on this matter focused on two separate, though inter-related, points.

8.4.3 Firstly, the Group examined the potential for recommending to Government an adjustment to the existing PPF commitment in relation to social welfare rates - i.e. that "substantial progress will be made over the period of the Programme towards a target of £100 per week for the lowest rates of social welfare". While there was an acceptance by most members of the Group that there was scope to adjust this target upwards, it did not prove possible to agree on a revised figure.

8.4.4 Secondly, the issue of setting a benchmark for the medium term was considered. The Group noted that the current arrangements, under the PPF, involve setting a cash target - not linked to any specific index (e.g. earnings) - which can be reviewed in the context of the partnership arrangements. Such an approach is necessarily short-term in nature and may be said to derive from the view that the uncertainty associated with the medium to long-term well-being of the economy requires that the Government should not be tied into a fixed position in a critical area of public expenditure.

8.4.5 Clear differences of approach amongst Group members emerged as to the future direction of policy in terms of setting social welfare rates. Briefly, and reflecting the arguments presented in Chapter 4, the preferred positions expressed fall into a range between the following two contrasting positions.

- A view that it was inappropriate to establish a formal benchmark and that the existing arrangements, which have seen real increases (i.e. in excess of inflation) in welfare rates should continue to apply. Essentially, it would be left to the discretion of the Government to determine the level of welfare increases from year to year, having regard to the range of high priority demands on the Exchequer and to issues of affordability, sustainability and compatibility with the social, economic and employment needs of the economy on a continuing basis. This position was held by the representatives of the Departments of Finance and Enterprise, Trade and Employment, and by the Employer's Pillar.

- A view that it was fundamentally necessary, as of right, to establish a formal linkage between welfare rates and average earnings in order to ensure that the income of welfare recipients keep pace with those of the wider population. The preferred position of those advocating this approach (the Community and Voluntary and Trade Union Pillars) was that the lowest welfare rates should be increased to reach 27% of GAIE in the short-term (i.e. by 2003) and to 30% of GAIE in the medium term.

8.4.6 It was acknowledged that these contrasting positions could not be reconciled within the context of the Working Group. Recognising that the exact rate was a matter for Government, and having balanced the various factors set out in the terms of reference, the majority of the Group considered that the target of 27% of GAIE (on a current-year basis) for the lowest social welfare payments was not an unreasonable policy objective. Given current uncertainties in relation to the short term economic position, it was difficult to be prescriptive about the precise time frame, although it would not be unreasonable to expect that the target would be met in full by 2007 (i.e. in the Budget announced late in 2006). This does not of course rule out setting a higher target, e.g. 30% of GAIE, in the context of the review process set out below in section 8.8.

8.4.7 For the reasoning set out in 8.4.5 (first bullet point) above, the representatives of the Departments of Finance and Enterprise, Trade and Employment, together with the Employer Pillar did not agree with this recommendation.

8.4.8 A rough estimate of the total costs arising over the period to 2007, assuming a steady incremental progress towards the target rate in the period 2002 - 2007 and assuming that existing relativities between welfare rates were maintained in full would indicate that additional expenditure of the order of £2.9bn would be required in respect of weekly welfare rates and FIS payments if the target of 27% GAIE were reached at that stage (i.e. excluding child-related payments - see section 8.5.5). It should be noted that annual increases will, in any event, be provided for in the rates of weekly welfare payments. Accordingly, the net additional cost associated with the proposal would therefore be lower.

8.4.9 The Group believes that, in conjunction with the majority proposal for a social welfare benchmark, an essential part of a strategy for income adequacy should be a proactive policy of engagement with people of working age on social welfare to ensure that, where possible, they have the opportunity to avail of employment, education and training opportunities[38].

8.5 Benchmark for child payments

8.5.1 Chapter 5 examined the available evidence on the costs of rearing a child and the issue of equivalence scales. The Group noted in particular the Government's commitment to invest heavily in the Child Benefit scheme over the next two years (following on the very significant increases introduced in 2001) and that this investment implies that the basic weekly level of child income support for social welfare recipients will have reached some £40.30 by 2003.

8.5.2 The Group noted also that the available research on the costs of rearing a child (based on a budget-standards approach and excluding the cost of childcare) suggests that this cost will have risen to some £39.25 by 2003. In that context, the future role of Child Benefit, in light of the Budget 2001 statement by the Minister for Finance was discussed.

8.5.3 As regards equivalence scales, the Group noted that such research as is available in an Irish context suggests that social welfare dependent households with children require an income per child of some one-third of the single adult rate to maintain the same standard of living. Accordingly, it was the view of all Group members that the appropriate equivalence level of basic child income support (i.e. Child Benefit and Child Dependant Allowances combined) should be set at 33% - 35% of the minimum adult social welfare payment rate.

8.5.4 The Voluntary and Community Pillar offered qualified support to this position, citing concerns that the minimum adult rate must be set at an adequate level if the proposal is to be meaningful, and pointing to the need for renewed research on the costs of rearing children in order to inform the development of policy in this area.

8.5.5 Having regard to the majority recommendation that the lowest adult rate should reach 27% of GAIE by 2007, this would mean that basic child income support would be in the range of £47 to £50 per week. Aggregate additional expenditure of some £363m. to £526m. on Child Benefit payments would be needed, over and above the existing £1 bn. Government commitments for the period to 2003, over the period to 2007 in order to achieve that level,

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[38] The Trade Union Pillar believed that this should be complemented with a range of in-work benefits.

assuming that the current policy of channeling all additional child income supports through the Child Benefit scheme remains in place

8.6 Indexation

8.6.1 Chapter 6 examined the question of whether it was appropriate to adopt a specific approach to the indexation or uprating of welfare payments. The Group noted the importance of having a practicable and widely understood indexation methodology. It was recognised that it is possible to overcome some of the difficulties associated with indexation where a benchmark is denominated in term of a specific index, since it would have an automatic in-built indexation mechanism.

8.6.2 The issues associated with the range of available indices were set out, and the particular difficulties associated with trying to devise a reliable index of net income measures were noted. The Group also drew attention to the difficulties associated with indexing on a current year basis - effectively indexing on a forecast figure.

8.6.3 Notwithstanding the reservations outlined in this regard, it will have been noted that the majority recommendation made earlier in relation to benchmarking is that the lowest welfare rates should be brought up to a given percentage of Gross Average Industrial Earnings on a current year basis. It is recognised that there are potential difficulties with this approach, particularly if there are serious under-estimations or over-estimations in the forecasts involved since it would give rise to issues of re-balancing from year to year. The Group considers this to be an issue which would clearly require careful monitoring.

8.7 Relative Income Poverty

8.7.1 In Chapter 7, the issue of relative income poverty was explored. Relative income poverty, defined by reference to the number of people/households below certain percentages of Average Weekly Household Income, has increased in Ireland in recent years at the 40% and 50% income lines while it has stabilised and begun to fall at the 60% line. Consistent poverty (the poverty measure used by the National Anti-Poverty Strategy in its global target), on the other hand, has been decreasing. This underlines the fact that, while income inequalities - i.e. the gap between the poor and the better off, have been increasing, the real incomes of the poor have also increased.

8.7.2 While the relative income poverty measure is clearly a valid instrument, it has limitations as a measure of exclusion from the norm and a number of qualifications have to be made if one is to use it in isolation and categorise as poor all those below an arbitrary percentage of average household income. It is valuable as an indicator of trends in income inequalities and potential future trends in exclusion. The consistent poverty measure is also subject to some limitations since it may be anticipated that, in the future, when growth rates have stabilised at more normal levels for some time, expectations and views about adequacy are likely to catch up and new, higher standards will be set in the society as to what constitutes acceptable living standards and capacity to fully participate in ordinary life.

8.7.3 The Group agreed that both consistent poverty and relative income poverty have merits in relation to our understanding of poverty generally and that trends in both measures should be monitored to gain a more rounded perspective of the evolution of poverty over time. It was not within the Group's remit to consider which measure should be accorded priority when targets for the eradication of poverty are being set in the context of the National Anti-Poverty Strategy.

8.8 Review and Monitoring mechanisms.

8.8.1 Regardless of how the Government chooses to develop social welfare budgetary policy in the coming years, the majority of the Group is strongly of the view that regular and formal review and monitoring of the range of issues covered by this report should be provided for. The Group believes that this can best be accommodated within the structures in place under the National Anti-Poverty Strategy and the National Action Plan for Social Inclusion.

8.8.2 Such a mechanism could involve:

- review of any benchmarks/targets and indexation methodologies adopted by Government to ensure that the underlying objectives remain valid and are being met;
- assessment of such benchmarks/targets and indexation methodologies against the various criteria set out in the Group's terms of reference to ensure their continued relevance;
- assessment of emerging trends in the key areas of concern - e.g. poverty levels, labour market performance, demographic changes, economic performance, competitiveness, etc.;
- identification of gaps in the area of research and assessment of any additional research undertaken in the interim.

Appendix A

Membership of the PPF Benchmarking and Indexation Group

Professor Kieran Kennedy (Chairperson)

Mr Cathal Buckley (Irish Creamery Milk Suppliers Association)

Ms Rosheen Callender (Irish Congress of Trade Unions)

Ms Deirdre Carroll (Department of Social, Community and Family Affairs)

Mr Mel Cousins (Adviser to the Minister of Social, Community and Family Affairs)

Mr Eugene Forde (Department of Enterprise, Trade and Employment)

Mr Brian Geoghegan (Irish Business & Employers Confederation)

Fr Sean Healy (Conference of Religious of Ireland)

Ms Camille Loftus [subsequently replaced by Mr Tony Monks] (Irish National Organisation of the Unemployed)

Mr Con Lucey (Irish Farmers Association)

Ms Esther Lynch (Irish Congress of Trade Unions)

Mr Aebhric McGibney (Irish Business & Employers Confederation)

Ms Anne McManus (Department of Social, Community and Family Affairs)

Mr Joe Mooney (Department of Finance)

Ms Mary Murphy (St Vincent de Paul)

Mr Tom Murphy (Department of Finance)

Mr Eoin O Seaghdha (Secretariat)

Mr Ciaran Lawler (Secretariat)

Appendix B

Maximum rates of Child Dependant Allowances

A.	Unemployment Benefit	}	£13.20
	Unemployment Assistance	}	
	Health and Safety Benefit	}	
	Supplementary Welfare Allowance	}	
	Farm Assist	}	
	Carers Allowance	}	
	Disability Benefit	}	
	Disability Allowance	}	
	Blind Person's Pension	}	
	Occupational Injuries Benefits	}	
	Pre-Retirement Allowance	}	
	Old Age (Non-Contributory) Pension	}	
B.	One-Parent Family Payment	}	£15.20
	Invalidity/Disability Pension	}	
	Retirement Pension	}	
	Old Age (Contributory) Pension	}	
C.	Widow's/Widower's (Contributory)	}	£17.00
	Death Benefits (Survivor's Benefits)	}	