



# **Indexation of the Taxation and Social Protection System**

**Submission to the Select Committee on Budgetary Oversight**



## Contents

Introduction .....	3
<b>Benchmarking – policy context.....</b>	<b>3</b>
<b>Benchmarking Social Welfare Payments, 2001-2011.....</b>	<b>3</b>
<b>Social welfare benchmarking and indexation working group .....</b>	<b>3</b>
<b>Benchmarking Social Welfare Rates as starting point for indexation .....</b>	<b>5</b>
<b>Rationale for indexation .....</b>	<b>6</b>
<b>Social welfare and poverty reduction.....</b>	<b>6</b>
<b>Benchmarking, Indexation and estimated impact on poverty .....</b>	<b>7</b>
<b>Impacts of indexation.....</b>	<b>8</b>
<b>Creation of an indexation system.....</b>	<b>9</b>
<b>Operation of indexation.....</b>	<b>9</b>
<b>Budgetary sustainability .....</b>	<b>10</b>
<b>Conclusion .....</b>	<b>10</b>

## Introduction

*Social Justice Ireland* welcomes the opportunity to make a submission to the Select Committee on Budgetary Oversight on the Indexation of the Taxation and Social Protection System. Our submission reviews the process by which the basic social welfare payment became benchmarked to 30 per cent of Gross Average Industrial Earnings and makes proposals regarding current social welfare rates and indexation and how this might be progressed.

## Benchmarking – policy context

### Benchmarking Social Welfare Payments, 2001-2011

This section outlines the transition to benchmarked social welfare payments. That process centred on three elements: the 2001 *Social Welfare Benchmarking and Indexation Working Group* (SWBIG), the 2002 *National Anti-Poverty Strategy (NAPS) Review* and the *Budgets 2005-2007*.

### Social welfare benchmarking and indexation working group

In its final report the SWBIG agreed that the lowest social welfare rates should be benchmarked. A majority of the working group, which included a director of *Social Justice Ireland*, also agreed that this benchmark should be index-linked to society's standard of living as it grows and that the benchmark should be reached by a definite date. The working group chose Gross Average Industrial Earnings (GAIE) to be the index to which payments should be linked<sup>1</sup>. The group further urged that provision be made for regular and formal review and monitoring of the range of issues covered in its report. The group expressed the opinion that this could best be accommodated within the structures in place under the NAPS and the *National Action Plan for Social Inclusion* (now combined as *NAPinclusion*). The SWBIG report envisaged that such a mechanism could involve:

- the review of any benchmarks/targets and indexation methodologies adopted by government to ensure that the underlying objectives remain valid and were being met;
- the 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;
- the assessment of emerging trends in the key areas of concern, e.g. poverty levels, labour market performance, demographic changes, economic performance and competitiveness, and
- identification of gaps in the area of research and assessment of any additional research undertaken in the interim.

### National Anti-Poverty Strategy (NAPS) review 2002

In 2002, the NAPS review set the following as key targets:

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<sup>1</sup>The group recommended a benchmark of 27 per cent although *Social Justice Ireland* argued for 30 per cent.

*To achieve a rate of €150 per week in 2002 terms for the lowest rates of social welfare to be met by 2007 and the appropriate equivalence level of basic child income support (i.e. Child Benefit and Child Dependent Allowances combined) to be set at 33 per cent to 35 per cent of the minimum adult social welfare payment rate.*

*Social Justice Ireland* and others welcomed this target. It was a major breakthrough in social, economic and philosophical terms. We also welcomed the reaffirmation of this target in *Towards 2016*. That agreement contained a commitment to 'achieving the NAPS target of €150 per week in 2002 terms for lowest social welfare rates by 2007' (2006:52). The target of €150 a week was equivalent to 30 per cent of Gross Average Industrial Earnings (GAIE) in 2002<sup>2</sup>.

Table 1.1 outlines the expected growth rates in the value of €150 based on this commitment and indicates that the lowest social welfare rates for single people should have reached €185.80 by 2007.

**Table 1.1: Estimating Growth in €150 a Week (30% GAIE) for 2002-2007**

	2002	2003	2004	2005	2006	2007
% Growth of GAIE	-	+6.00	+3.00	+4.50	+3.60	+4.80
30% GAIE	150.00	159.00	163.77	171.14	177.30	185.80

**Source:** GAIE growth rates from CSO Industrial Earnings and Hours Worked (September 2004:2) and ESRI Medium Term Review (Bergin et al, 2003:49).

### ***Budgets 2005-2007***

The NAPS commitment was very welcome and was one of the few areas of the anti-poverty strategy that was adequate to tackle the scale of the poverty, inequality and social exclusion being experienced by so many people in Ireland today.

In 2002 *Social Justice Ireland* set out a pathway to reaching this target by calculating the projected growth of €150 between 2002 and 2007 when it is indexed to the estimated growth in GAIE. Progress towards achieving this target had been slow until Budget 2005. At its first opportunity to live up to the NAPS commitment the government granted a mere €6 a week increase in social welfare rates in Budget 2003. This increase was below that which we proposed and also below that recommended by the government's own tax strategy group. In Budget 2004 the increase in the minimum social welfare payment was €10. This increase was again below the €12 a week we sought and at this point we set out a three-year pathway (see table 1.2).

<sup>2</sup>GAIE is calculated by the CSO on the earnings of all individuals (male and female) working in all industries. The GAIE figure in 2002 was €501.51 and 30 per cent of this figure equals €150.45 (CSO, 2006: 2).

**Table 1.2: Proposed Approach to Addressing the Gap, 2005-2007**

	2005	2006	2007
Min. SW payment in €'s	148.80	165.80	185.80
€ amount increase each year	14.00	17.00	20.00
<b>Delivered</b>	✓	✓	✓

Following Budget 2004 we argued for an increase of €14 in Budget 2005. The Government's decision to deliver an increase equal to that amount in that Budget marked a significant step towards honouring this commitment. Budget 2006 followed suit, delivering an increase of €17 per week to those in receipt of the minimum social welfare rate. Finally, Budget 2007's decision to deliver an increase of €20 per week to the minimum social welfare rates brought the minimum social welfare payment up to the 30 per cent of the GAIE benchmark.

*Social Justice Ireland* believes that these increases, and the achievement of the benchmark in Budget 2007, marked a fundamental turning point in Irish public policy. Budget 2007 was the third budget in a row in which the government delivered on its NAPS commitment. In doing so, the government moved to meet the target so that in 2007 the minimum social welfare rate increased to €185.80 per week; a figure equivalent to the 30 per cent of GAIE.

*Social Justice Ireland* warmly welcomed this achievement. It marked major progress and underscored the delivery of a long overdue commitment to sharing the fruits of this country's economic growth since the mid-1990s. An important element of the NAPS commitment to increasing social welfare rates was the acknowledgement that the years from 2002-2007 marked a period of 'catch up' for those in receipt of welfare payments. Once this income gap had been bridged, the increases necessary to keep social welfare payments at a level equivalent to 30 per cent of GAIE became much smaller. In that context we welcomed the commitment by Government in *NAPinclusion* to 'maintain the relative value of the lowest social welfare rate at least at €185.80, in 2007 terms, over the course of this Plan (2007-2016), subject to available resources' (2007:42). Whether or not 30 per cent of GAIE (or equivalent values such as average weekly earnings) is adequate to eliminate the risk of poverty will need to be monitored through the *SILC* studies and addressed when data on persistent poverty emerges.

#### Benchmarking Social Welfare Rates as starting point for indexation

The benchmark of 27.5 per cent of average earnings is applied in Table 1.3 using CSO data for 2019 and 2020. Given uncertainties in 2021 and lack of wage projections; we conservatively assumed a 0 per cent change for 2021. Based on these calculations, in 2021 the updated value of 27.5 per cent of average weekly earnings equalled €222.08, implying a shortfall of €14 between the minimum social welfare rates being paid in 2022 (€208) and this threshold.

**Table 1.3: Benchmarking Social Welfare Payments for 2021 (€)**

Year	Average Weekly Earnings	27.5% of Average Weekly Earnings
2019*	774.68	213.04
2020**	807.57	222.08
2021**	807.57	222.08

**Notes** \* actual data from CSO average earnings.

\*\* simulated value based on CSO data/trends and an assumed 0% growth rate in 2021.

The current deficit highlights a need for the Government, to further increase minimum social welfare rates and commit to converging on a benchmark equivalent to 27.5 per cent of average weekly earnings. Government could choose to close this gap over two budgetary cycles, and then develop a pathway to index core social welfare rates to a set target, which *Social Justice Ireland* suggested should start at 30 per cent of average weekly earnings.

### Rationale for indexation

#### Social welfare and poverty reduction

*Social Justice Ireland* believes in the very important role that social welfare plays in addressing poverty. As part of the *SILC* results the CSO has provided an interesting insight into the role that social welfare payments play in tackling Ireland's poverty levels. It has calculated the levels of poverty before and after the payment of social welfare benefits.

Table 1.4 shows that without the social welfare system almost 4 in every 10 people in the Irish population (37.9 per cent) would have been living in poverty in 2020. Such an underlying poverty rate suggests a deeply unequal distribution of direct income. . In 2020, the actual poverty figure of 13.2 per cent reflects the fact that social welfare payments reduced poverty by 25 percentage points.

Looking at the impact of these payments on poverty over time, the increases in social welfare over the period 2005-2007 yielded noticeable reductions in poverty levels. The small increases in social welfare payments in 2001 are reflected in the smaller effects achieved in that year. Conversely, the larger increases, and therefore higher levels of social welfare payments, in subsequent years delivered greater reductions. This has occurred even as poverty levels before social welfare increased.

A report by Watson and Maitre (2013) examined these effects in greater detail and noted the effectiveness of social welfare payments, with child benefit and the growth in the value of social welfare payments, playing a key role in reducing poverty levels up until 2009. The CSO have also shown that in 2009 social welfare payments (including child benefit) reduced poverty among those under 18 years of age from 47.3 per cent to 18.6 per cent – a 60 per cent reduction in poverty risk (CSO, 2010:47)<sup>3</sup>.

These findings underscore the importance of social transfer payments in addressing poverty;

<sup>3</sup> This data has not been updated in subsequent SILC publications.

a point that needs to be borne in mind as Government develops policy priorities.

**Table 1.4: The Role of Social Welfare (SW) Payments in Addressing Poverty**

	2001	2004	2008	2012	2016	2020
Poverty pre-SW	35.6	39.8	43.0	50.2	44.9	37.9
Poverty post-SW	21.9	19.4	14.4	16.9	16.2	13.2
<b>The role of SW</b>	<b>-13.7</b>	<b>-20.4</b>	<b>-28.6</b>	<b>-33.3</b>	<b>-28.7</b>	<b>-24.7</b>

**Source:** CSO SILC Reports (various years) using national equivalence scale.

Table 1.5 presents the results of an analysis of five key welfare recipient groups performed by the ESRI using poverty data for five of the years between 1994 and 2001. These were the years that the Irish economy grew fastest and the core years of the ‘Celtic Tiger’ boom. Between 1994 and 2001 all categories experienced large growth in their poverty risk. For example, in 1994 only five out of every 100 old age pension recipients were in poverty. In 2001 this had increased ten-fold to almost 50 out of every 100. The experience of widow’s pension recipients is similar.

**Table 1.5: Percentage of Persons in Receipt of Welfare Benefits/Assistance Who Were Below the 60 Per Cent Median Income Poverty Line, 1994-2001**

	1994	1997	1998	2000	2001
Old age pension	5.3	19.2	30.7	42.9	49.0
Unemployment benefit/assistance	23.9	30.6	44.8	40.5	43.1
Illness/disability	10.4	25.4	38.5	48.4	49.4
Lone Parents allowance	25.8	38.4	36.9	42.7	39.7
Widow’s pension	5.5	38.0	49.4	42.4	42.1

**Source:** Whelan et al (2003: 31).

Table 1.5 highlights the importance of adequate social welfare payments to prevent people becoming at risk of poverty. Over the period covered by these studies, groups similar to *Social Justice Ireland* repeatedly pointed out that these payments had failed to rise in proportion to earnings and incomes elsewhere in society. The primary consequence of this was that recipients slipped further and further back and therefore more and more fell into poverty. In 2022, as policy makers and politicians examine the issue of indexation, the impact of adequate social welfare payments in addressing poverty must be borne in mind.

#### Benchmarking, Indexation and estimated impact on poverty

In general, fluctuations in the poverty rates of those largely dependent on the welfare system has correlated in the past with policy moves that allowed the value of welfare payments to fall behind wage growth before eventually increasing these payments to catch up. If those dependent on social welfare are not to fall behind the rest of society at times of economic growth, the benchmarking of welfare rates to wage rates is essential.

*Social Justice Ireland* estimates that more than 12,000 working age adults would have been raised out of poverty in 2016 had minimum social welfare payments been benchmarked at 27.5 per cent of average earnings. 28,000 would have been raised out of poverty had the benchmark been 28.5 per cent. By moving this benchmark gradually towards a target of 30 per cent of average earnings certainty would be given to households on fixed incomes, Government would have budgetary certainty, and issues regarding one off impacts of high

costs of utilities for example could be addressed in a more targeted manner. Poverty impacts hardest on those experiencing it in their day-to-day lives. It limits their options and opportunity and narrows their focus to week-to-week survival and the unavoidable trade-offs of living on inadequate incomes. The indexation of social welfare rates would provide certainty to households and people on fixed incomes and it would also begin to address the many challenges of making ends meet with limited resources on an ongoing basis.

*Social Justice Ireland* supports the indexation of minimum social welfare payments to ensure recipients do not fall behind the rest of society. We propose the benchmark should start at 27.5 per cent of average earnings as a minimum, and that Government should commit to reaching this benchmark over a two year period. We further propose that a pathway and process is then outlined for the indexation of social welfare payments to 30 per cent of average weekly earnings. This should be overseen by an independent body which would independently outline the indexation pathway, base any recommendations on independently verified data and calculations such as that developed by the Living Wage Technical Group for example, and outline the maximum annual changes in social welfare payments that this may entail.

#### Impacts of indexation

There is comprehensive research to show that the social welfare system is the key to reducing poverty in Ireland. Welfare payments target those most in need within Irish society. They also play a central role in alleviating poverty. When resources are focused on the welfare system they assist those who need most help. Conversely, when Government provides limited resources to the welfare system it undermines the living standards and needs of the weakest in our society.

Although the number of people in poverty is much the same as a decade ago, the period from 2016 -2019 has been one of notable decline in the level of poverty risk. This has seen the proportion of the population in poverty fall from 16.2 per cent in 2016 to a record low of 12.8 per cent in the 2019 SILC survey. The 2020 SILC survey, while not directly comparable to previous years due to a break in time series, shows that the proportion of the population in poverty is 13.2 per cent. While the period 2016-2019 incorporates social welfare increases from two budgets, the period 2019-2020 is a period where there was a failure to increase core social welfare rates in Budgetary cycles.

*Social Justice Ireland* welcomed the progress in reducing the risk of poverty between 2016 and 2019. It reflects a dividend from budget policy over the period which, for the most part, distributed resources more generously to welfare dependent households. Our consistent message in advance of these Budgets was to reverse the regressivity of previous policy choices and to prioritise those households with the least resources and the most needs.

Our post-Budget analysis of the income distribution effects of recent Budgets highlights these effects (*Social Justice Ireland*, 2016-2022). Looking at the entire period from 2017 to 2021 budgetary policy resulted in all household types recording an increase in their disposable income.

The larger gains experienced by welfare dependent households explain much of the reasons why the levels of poverty and income inequality have fallen in recent years. *Social Justice*



*Ireland* has consistently argued for the prioritisation of low income welfare dependent families in Budgetary policy and welcome these outcomes.

However, the analysis also reveals that the three most recent Budgets have shifted away from this approach. By implication, much of this recent progress will be reversed unless policy reasserts a focus on welfare increases and supports for those households on the lowest incomes.

### Creation of an indexation system

*Social Justice Ireland* is of the opinion that the best anchor for indexation is average weekly earnings, beginning with reaching the benchmark of 27.5 per cent of average weekly earnings and then setting out a pathway to move towards 30 per cent of average weekly earnings. We outline the case for setting a benchmark of 27.5 per cent earlier in this submission. A recent report from the Parliamentary Budget Office (2021) analysed changes in social welfare rates from 2011-2022.

This report looks at core social welfare rates over time, and rate changes compared to both inflation and wage changes. The analysis shows that flat increases in social welfare payments, such as the €5 increase to be applied to core benefits in 2022, result in disproportionate percentage changes and do not systematically account for price (or wage) inflation in a consistent manner.

Looking at core social welfare rates, specifically Jobseeker's Benefit the report finds that although Jobseeker's Benefit will have increased 10.6% in nominal terms between 2011 and 2022, but the real increase is substantially less over that period at 2.3% - accounting for inflation and the 2022 inflation forecast. Following no increases between 2011 and 2016, Jobseeker's Benefit increased from €188 to €203 between 2017 and 2019 and following two years of no increases to 2021, will increase to €208 in 2022.

One of the key findings of the report is that a failure to index core social welfare rates to either wages or inflation has resulted in a significant fall in the real value of these payments. Examining Jobseekers benefit over the period 2011-2022 the Parliamentary Budget Office found that in the absence of increases in many years over the period, the real rate in 2022 will be €192.36 (2011 base). For the rate to stay in line with wage growth over the period and maintain the 2011 rate, the rate in 2022 would need to be €233.10.

The analysis shows that over the period 2011-2022 social welfare rates have not kept pace with wage growth or recent inflation increases over the entire period. The report notes that the core Consumer Price Index used in the analysis may be underestimating the real cost of living increases faced by many households at present. Energy and fuel costs, which disproportionately impact those in the lower income deciles and rural areas, are driving inflation at present but housing costs are also a key driver.

### Operation of indexation

*Social Justice Ireland* has consistently argued the case for indexation against wages, and for core social welfare rates to be benchmarked at 27.5 per cent of average weekly earnings. This was the standard set in 2007 and is the most appropriate measure. The Parliamentary Budget

Office analysis points to an underestimation with regard to the Consumer Price Index and the real cost of living.

Indexation to average weekly earnings would also avoid the situation of large increases or decreases in inflation that have to be dealt with in a short period of time. As outlined above, a Social Welfare Commission, modelled on the Low Pay Commission for example, with an independent membership consisting of experts on welfare, poverty, unemployment and social exclusion, including a majority representing the Community, Voluntary and Social Inclusion sectors, should be established to set out the appropriate process and pathway for indexation and how any changes might be administered on an annual basis.

Such an approach would also allow Government the space to react to pressure in particular areas in a Budgetary context, utilising the appropriate mechanisms and tools available to it within the social protection and revenue systems to administer any increased payments or to identify a particular target group, such as those in energy poverty for example.

#### Budgetary sustainability

Indexation would provide certainty for Government in terms of resourcing and revenue generation, and it would also provide certainty for those on fixed incomes who have to make ends meet on limited resources on an ongoing basis. All social welfare payments should be included in the indexation process, with the baseline target being a commitment to benchmark core social welfare rates to 27.5 per cent of average weekly earnings as the starting point for the indexation process.

As outlined, when designing the process and pathway for indexation, appropriate targets should be set and a ceiling on the proportional increase in any one year. This would eliminate the problem of sudden shocks to the Exchequer. Indexation allows for certainty and for planning, and time to assess resourcing needs and plan for any additional revenue raising measures on a measured and considered basis. In terms of resourcing, all direct taxation should be included.

The estimated cost of going halfway towards bridging the gap between core social welfare rates and the benchmark of 27.5 per cent of average weekly earnings in 2021 (including restoring Jobseekers aged under 25 up to the higher rate) would have been €544m.

#### Conclusion

In general, fluctuations in the poverty rates of those largely dependent on the welfare system has correlated in the past with policy moves that allowed the value of welfare payments to fall behind wage growth before eventually increasing these payments to catch up. If those dependent on social welfare are not to fall behind the rest of society at times of economic growth, the benchmarking of welfare rates to wage rates is essential.

*Social Justice Ireland* has consistently made the case for indexation of core social welfare rates to average weekly earnings, starting with a benchmark of 27.5 per cent of average weekly earnings, and moving, over a specific time period to a target of 30 per cent of average weekly earnings.

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