Research Briefing

Social impact assessment of the main welfare and tax measures for 2014

February 2014

This is a social impact assessment of the main welfare and tax measures for 2014, undertaken by the Department of Social Protection. The assessment is intended to contribute to public understanding of the impact of budgetary policy.

Social impact assessment is an evidence-based methodology which estimates the likely distributive effects of welfare and tax policies on household income and social groups. It supports the implementation of the national social target for poverty reduction, which is to reduce consistent poverty to 4 per cent by 2016 and to 2 per cent or less by 2020.

The assessment is based on the tax/welfare microsimulation model (Switch) developed by the Economic and Social Research Institute. Responsibility for the results and their interpretation rests solely with the Department of Social Protection.

An Roinn Coimirce Sóisialaí
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Main findings

- The combined welfare and tax measures for 2014 result in a loss of 0.8 per cent in average household income (0.9% in 2013).
- The largest percentage loss is for the top and bottom quintiles at 1.1 per cent, followed by a 0.8 per cent loss for the second quintile. The remaining quintiles lose between 0.6 and 0.7 per cent.
- The combination of changes in DIRT and tax relief on health insurance and pensions is responsible for the biggest impact (0.4 per cent), largely centred on the top quintile.
- The property tax and welfare measures have smaller impacts (0.2 to 0.3 per cent each), and affect the bottom quintiles most.
- The family type most affected is unemployed single people. This impact does not allow for behavioural changes, such as jobseekers moving to training schemes or securing employment.
- There are also higher than average impacts for non-earning couples without children, and the retired.
- The family types least affected are employed families, including those with children.
- There is no significant change in the at-risk-of-poverty rate, as social transfers continue to perform strongly, substantially reducing the at-risk-of-poverty rate during the economic recession.
- The 2014 measures compared with the 2013 measures show a somewhat reduced average loss in household income, though they have a greater impact on the highest income group.

Introduction

This research briefing presents the social impact assessment of the main welfare and tax measures for 2014. It is prepared by the Department of Social Protection, which is responsible for the welfare component of Budget 2014.

Social impact assessment is an evidence-based methodology to estimate the likely distributive effects of policy proposals on income and social inequality. It is a widely used tool at the European level.[i] Though relative new in the Irish context, it builds on the experience of poverty impact assessment and is similar in concept to 'equality budgeting'.[ii] It is being developed to strengthen the implementation of the national social target for poverty reduction and to facilitate policy coordination.[iii]

The social impact of welfare and tax policies is of particular importance during the economic crisis. Recent research demonstrates the crucial role of social transfers in preventing poverty. It finds that social transfers reduced the at-risk-of-poverty rate from 55 per cent to 16 per cent in 2011, thereby lifting two-fifths of the population out of at-risk-of-poverty.[iv] Social impact assessment is also pertinent to the Medium-Term Economic Strategy, which seeks to build a fairer Ireland by reducing inequality and improving poverty outcomes.[v]

The social impact of a range of potential welfare and tax measures were assessed as part of the deliberative process for Budget 2014. This included some measures suggested at the department's Pre Budget Forum with community and voluntary groups. The publication of the final outcome is intended to inform public discourse about the impact of budgetary policy.

Methodology

The assessment uses a tax-welfare simulation model developed by the Economic and Social Research Institute (ESRI) known as Switch.[vi] The model simulates the impact of changes in welfare and income tax for a representative sample of 5,000 households, drawn from the CSO *Survey on Income and Living Conditions*. The tax and welfare data are updated to reflect trends in population, employment and incomes.[vii] Responsibility for the results and their interpretation rests solely with the Department of Social Protection.

Consideration of the social impact of the welfare measures alone is a limited exercise, given the targeted nature of income supports. Tax changes also impact across the whole population, including welfare recipients. To ensure a comprehensive analysis therefore, the assessment combines 2014 welfare and tax measures announced in Budget 2014 and previous budgets. The tax measures include the DIRT increase and restrictions on tax relief for health insurance and pensions.[viii] These items are included for the first time using alternative data sources. Also included is the full-year implementation of the Haddington Road Agreement on public sector pay.

The assessment does not include the non-welfare expenditure measures for 2014. The Department of Social Protection and the ESRI are working with line departments to improve the capacity of the Switch model to support this analysis in future. The comparator policy is the 2013 policy which freezes taxes and welfare payments in nominal terms. Finally, the distributive impact of the 2014 measures is compared with 2013.

Main components of the analysis

The main components of the analysis are presented in table 1, covering welfare and tax, along with official estimates of savings. There are six welfare measures included in the analysis, with savings of €153.5 million. The tax items include the full year implementation of the local property tax, with a total revenue of €642 million. The savings are calculated on a full-year basis, which in the case of the jobseeker's allowance measure will not be until 2017 (the savings for 2014 are estimated at €32m).

Certain welfare items are not included in the assessment due to constraints in the Switch model. Administrative measures, including additional expenditure on labour market programmes, are also excluded.[ix] Some other tax changes are also not included. Details of the excluded measures can be found in the Budget 2014 documentation.[x] The public sector pay measures include a reduction in pay for those earning more than €65,000 and a reduction in the pension levy.[xi]

The findings of the assessment are presented in four parts:

- the distributive impact of the main measures
- the composite impact
- the impact on family types and poverty
- the composite impact of Budgets 2013 and 2014.

Distributive impact is measured by income groups (five quintiles ranked by equivalised income), by 14 family types (differentiated by composition and employment status) and by at-risk-of-poverty, using the 60 per cent median income threshold, disaggregated by social group.[xii] In presenting the findings, no account is taken of statutory non-cash benefits such as the medical card.

Table 1: Savings from the main welfare and tax measures for 2014

Measures	Savings €m
Welfare total	**153.5**
• Reductions in jobseekers allowance for 22-25 year olds (full implementation)	72
• Standardisation of child benefit at €130 per month	7
• Removal of back-to-school clothing and footwear allowance from students over 18 years in third level education	2.5
• Abolition of the telephone allowance	47
• Reduction in the one parent family payment earning disregard	18
• Increase in the minimum contribution for couples for the Rent and Mortgage Interest Supplement	7
Tax total	**642**
• Full year implementation of local property tax	250
• Increase in DIRT to 41 per cent[xiii]	140
• Restrictions on tax relief for medical insurance over €1,000 per adult	127
• Restrictions on tax relief for pensions over €65,000 per annum	125

Distributive impact of the welfare and tax measures

The impact of each of the main welfare and tax measures for 2014 is set out in Table 2, with the tax measures divided between local property tax and all other taxes. The welfare component gives rise to an average loss of 0.2 per cent of average household income. Next largest is the local property tax component, which leads to an average loss of 0.3 per cent of average household income. The other tax measures have the greatest impact with a loss of 0.4 per cent in average household income.

Table 2: Impact of the welfare and tax measures for 2014[xiv]

Measure	% Loss	Savings
Welfare	-0.2%	€132m
Local property tax	-0.3%	€215m
Other tax	-0.4%	€305m (e)

Diagram 1 presents the diverse distributive impact of the three budgetary measures:

- Welfare measures (purple bar) have a disproportionate impact on the lower quintiles, with losses of up to 0.5 per cent. This reflects their high dependence on welfare payments. The smaller losses in middle income quintiles arise from reductions in non-means-tested benefits.
- The impact of the local property tax (green bar) is felt across all income groups, though a slighter greater loss in the bottom quintile (-0.4 per cent). This loss may be reduced where low income households avail of the deferral option, though take-up has been low.[xv]
- Other tax measures (blue bar) are strongly progressive, with by far the largest loss in the top quintile (-0.8 per cent). By contrast, the remaining quintiles lose 0.3 per cent or less.

Diagram 1: Distributive impact of the welfare and tax measures for 2014
(Percentage loss in household income by equivalised income quintile)[xvi]

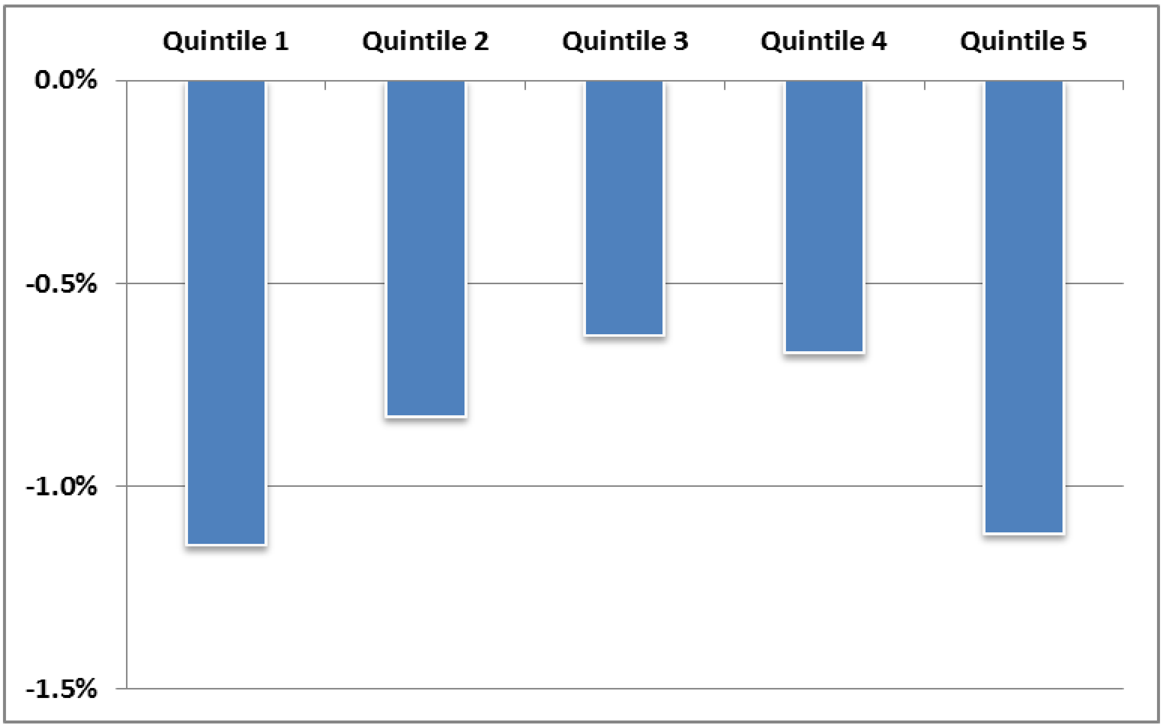
Source: Switch, the ESRI tax-benefit model

Distributive impact of the composite 2014 measures

The analysis of the distributive impact of the composite 2014 measures is now considered. The impact does not allow for behavioural changes, such as welfare recipients moving to training schemes or securing employment. The average loss is 0.8 per cent of average household income.

Diagram 2 shows the distributive impact by income quintile. The greatest losses are for the bottom and top quintiles at 1.1, followed by the second quintile at 0.8 per cent. There are smaller percentage losses in the remaining quintiles, at 0.7 and 0.6 per cent.

Diagram 2: Distributive impact of the composite 2014 measures
(Percentage loss in household income by equivalised income quintile)



Source: Switch, the ESRI tax-benefit model

Impact on at-risk-of-poverty

Under the combined welfare and local property tax measures, there is no significant change in the at-risk-of-poverty rate for the total population or for social groups.[xvii] In part, this is accounted for by a marginal fall in the at-risk-of-poverty threshold (-0.2 per cent). It also reflects the continuing strong performance of social transfers in alleviating income poverty during the economic crisis.

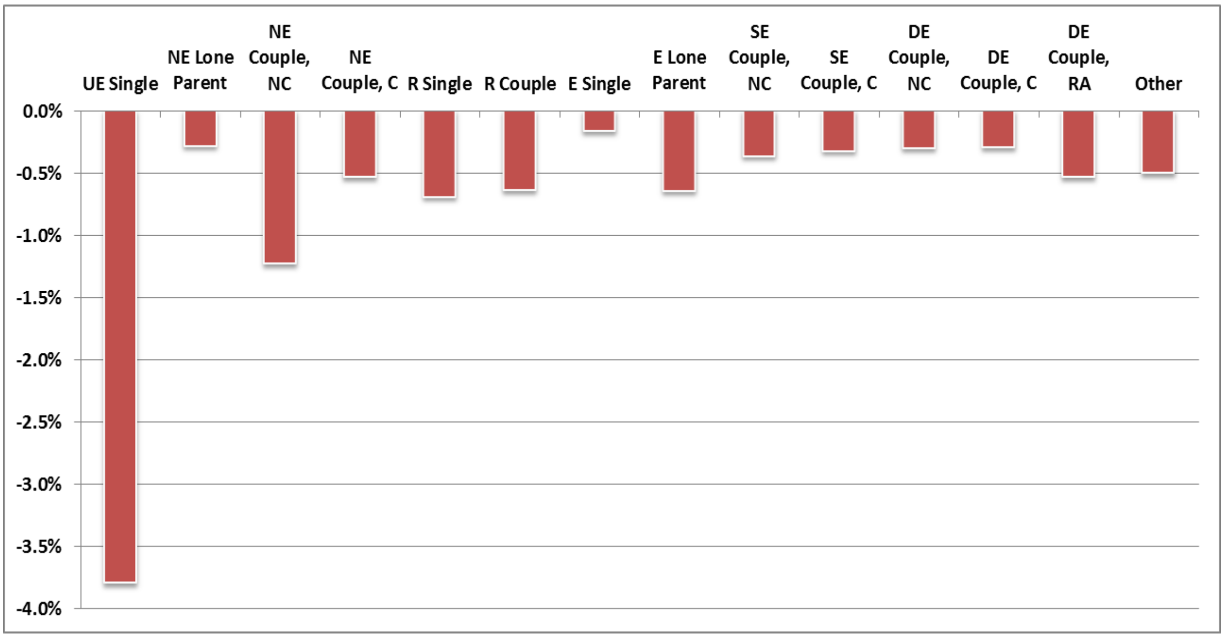
Distributive impact on families

Diagram 3 presents the distributive impact of the welfare and local property tax measures on families.

The average loss thus falls to 0.4 per cent. The main features of the distributive impact are:

- The model finds that unemployed single people are the most affected, losing 3.8 per cent of their average income. However, the Budget 2014 jobseekers' measure did not provide for a reduction to the existing rate of payment of any jobseeker recipient. Instead, it raised the age threshold at which a young jobseeker qualifies for a higher payment rate from 22 to 25. The Switch model captures the effect of this change by modelling it across the entire single unemployed cohort. In addition, the impact shown below reflects the full year [2017] impact. This impact can be avoided if a young jobseeker participates in a training or employment programme.
- Other families with higher than average losses are non-earning couples without children (loss of 1.2 per cent), and retired single people and couples (loss of 0.7 and 0.6 per cent).
- Generally, families with an employed adult are least affected and their losses are below average.
- The exception is employed lone parents, who lose 0.6 per cent.

Diagram 3: Distributive impact on families of the welfare and local property tax measures
(Percentage loss in household income by household family)*



Source: Switch, the ESRI tax-benefit model

* E=employed; UE=unemployed; NE=non-earning; R=retired; SE=single earner; DE=dual earner; C=children; NC=no children; RA=relative assisting

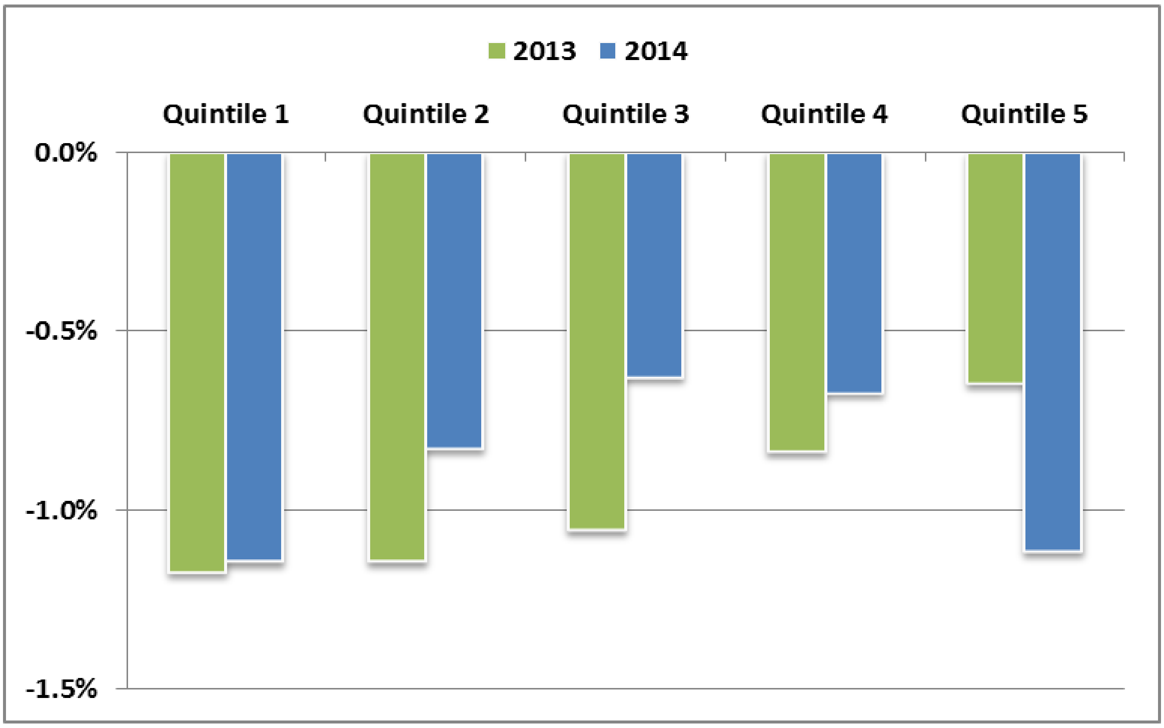
Distributive impact of the 2014 measures compared with 2013

The distributive impact of the composite package of Budget 2014 (blue bar) is now compared with Budget 2013 (green bar). The average household loss is similar across both budgets – 0.8 per cent in 2014 compared to 0.9 per cent in 2013.

Diagram 4 shows the percentage loss by quintile for 2013 and 2014. The main results are:

- The biggest difference is in the top quintile with the 2014 measures having almost twice the loss as compared with 2013.
- For the second to fourth quintiles the 2013 measures have a bigger impact.
- For the bottom quintile the impact in 2013 and 2014 is similar.

Diagram 4: Distributive impact of composite 2014 measures compared with Budget 2013
(Percentage loss in household income by equivalised income quintile)



Source: Switch, the ESRI tax-benefit model

Endnotes

[i] See http://ec.europa.eu/social/main.jsp?catId=89&langId=en&newsId=935&furtherNews=yes

[ii] See www.equalitybudgeting.ie

[iii] See http://www.socialinclusion.ie/NPT.html

[iv] Ibid. This equates to a poverty reduction effect for social transfers, excluding pensions, of 60 per cent. This is the best performance of all EU member states and is almost twice the EU average (see Eurostat website).

[v] Department of Finance (2013), *A Strategy for Growth. Medium-term Economic Strategy.* Dublin: Stationery Office. See http://mtes2020.finance.gov.ie/

[vi] Stimulating Welfare and Income Tax Changes

[vii] Information on the design, underlying data and model construction can be found at www.esri.ie/switch.

[viii] Information on the additional tax measures is available in *Distributional Impact of Tax, Welfare and Public Service Pay Policies: Budget 2014 and Budgets 2009-2014*.

[ix] These include Community Employment, Tús, JobBridge, and initiatives under the Youth Guarantee.

[x] http://www.welfare.ie/en/downloads/budfact14.pdf and http://budget.gov.ie/Budgets/2014/2014.aspx

[xi] http://per.gov.ie/wp-content/uploads/Haddington-Road-Agreement.pdf

[xii] This includes the impact for children, older people, and gender. Consideration of the impact on people with disabilities or ethnic minorities is not analytically possible, but it is hoped to rectify this in future social impact assessments.

[xiii] This figure includes the rate of retention tax that applies to DIRT, together with rates of exit tax that apply to life assurance policies and investment funds.

[xiv] Note the figures presented from the SWITCH model take into account tax and welfare expenditure offsets against the Budget measures. The other tax figure quoted is indicative; it was estimated from the composite figure for SWITCH savings. Percentage loss figures quoted are rounded.

[xv] In modelling the local property tax, the charge is attributed to the owner of the property and not the tenant / renter. Reductions in tax liability linked to disability or other factors are not included. Official estimate based on property tax for half year with deferral of 15%. The actual rate of deferral in 2013 is 3%. It is not possible to model the estimated rate of take-up as its distribution is unclear.

[xvi] The equivalisation scales used are 1 for a single person, 0.66 for an additional adult and 0.33 for a child (< 14 years).

[xvii] It is not possible to include other tax measures in the poverty impact as these are outside of the SWITCH model.