

ANALYSIS OF BUDGET 2007

1 Introduction

This analysis examines the tax/welfare measures introduced in Budget 2007 and assesses their impact on income distribution and poverty.¹ It complements the submission made by Combat Poverty in advance of the Budget. The analysis is intended to inform policymaking on poverty, in particular the assessment of the poverty impact of budgetary policy, which is an explicit requirement under the National Anti-Poverty Strategy.² This assessment has added significance as Budget 2007 marks the end of the revised five-year National Anti-Poverty Strategy (2002–2007).

This analysis begins with an overview of Budget 2007 and summarises the headline tax/welfare changes introduced in the Budget. It uses the ESRI micro-simulation model (SWITCH) to examine the distributive and poverty impact of welfare and tax changes for a national representative sample of households.³ The impact of Budget 2007 is also examined in the context of the last five and ten budgets, to see the cumulative policy impact under the National Anti-Poverty Strategy. The analysis then compares the Budget outcomes with the proposals made by Combat Poverty. Finally,

consideration is given to the specific tax/welfare policy changes made in Budget 2007.

2 Budget 2007: an overview

The fiscal context for Budget 2007 was very positive, with exchequer finances boosted by significant growth in tax revenues, while public expenditure was below forecast. The positive state of the public finances enabled an increased tax/welfare package of €2,748 million in Budget 2007, up €362 million (15 per cent) on 2006.⁴ Table 1 outlines the main elements of the tax/welfare package. Welfare improvements and tax reductions account for the majority of the allocation at €1,162 million (42 per cent) and €1,342 million (49 per cent), respectively. A modest €244 million or 9 per cent has been allocated to child income support. This is a major reduction in provision for child income support compared to Budget 2006 (down a half), marking a return to the approach in Budget 2005 when child income support accounted for 10 per cent of the total. The main beneficiary of these changes is income tax, which increases by €421 million (46 per cent) on 2006. The welfare component goes up by a lesser amount of €204 million (21 per cent).

Table 1: Tax/welfare expenditure in Budgets 2006, 2007

	Budget 2006 €m (%)	Budget 2007 €m (%)	Change €m (%)
Social welfare	958 (40%)	1,162 (42%)	+ 204 (+ 21%)
Child income support	507 (21%)	244 (9%)	- 263 (- 52%)
Income tax	921 (39%)	1,342 (49%)	+ 421 (+ 46%)
Total	2,386 (100%)	2,748 (100%)	+ 362 (+ 15%)

Table 2 summarises the main features of the tax/welfare package. The biggest welfare expenditure is on higher welfare rates (€972 million in total). This is broken down between €574 million on the minimum personal welfare rate, €325 million on other personal welfare rates and €73 million on qualified adult rates. Other expenditure items include €36 million on the fuel allowance and a collective €152 million for reforms in welfare provision for carers, older people, people of working age and people with disabilities. Child benefit is the major expenditure under child income support at €138 million. A further €104 million is provided for targeted schemes,

including €56 million on child dependent allowances and €32 million for family income supplement. On the tax side, the largest items are the increases in tax credits (employee and personal) at a combined cost of €625 million. A figure of €365 million is allocated to widening the tax bands, while the 1 per cent cut in the top rate of tax costs €186 million. A further €190 million is provided for targeted income tax measures, including increases in exemption limits, thresholds for PRSI and the health levy, and mortgage interest relief. Finally, there is a tax revenue gain of €34 million from a higher health levy rate.⁵

¹ This analysis was prepared by Jim Walsh, Head of Research and Policy, Combat Poverty.

² A partial poverty-impact assessment of the Budget's income-tax measures is carried out by the Department of Finance and included in Budget Day documentation.

³ Tax/welfare models provide a comprehensive assessment of the effects of tax/welfare changes, taking into account the wide diversity of individual and family circumstances relevant to tax liabilities and welfare entitlements. The SI of households. For further information on the model and its use as a tool for analysing tax/welfare policy, see T. Callan et al., 2001, *Reforming tax and welfare*, Dublin: Economic and Social Research Institute.

⁴ These figures are based on full year costs. They do not take account of the delay in introducing the child benefit increase.

⁵ Details of the Budget measures, including the financial statement of the Minister for Finance, can be found at www.finance.gov.ie and www.welfare.ie.

Table 2: Tax/welfare package in Budget 2007

Category	Measures	Cost (€m)
Minimum welfare rate	Increase of €20 per week	574
Pension and other rates	Increase of €16–18 per week	325
Qualified adult rates	Increases of €10.70 to €11.90 per week	73
Fuel allowance	Increase of €4 per week	36
Carers	Assessment of means, etc.	76
Pensioners	Assessment of means, etc.	38
Working age	Assessment of means, etc.	21
Disabilities	Assessment of means, etc.	17
Other		2
Total		1,162
Child benefit	Increase of €10 per month	138
Child dependent allowances	Increase of between €0.30 and €5.20 per week	56
Family income supplement	Increase in threshold of €15 to €185 per week	32
Clothing/footwear allowance	Increase of €60 and €90 per annum	13
School meals	Increased provision	3
Other		2
Total		244
Employee tax credit	Increase by €270 p.a.	264
Personal tax credit	Increase by €130/€260 p.a.	361
Standard rate bands	Increase by €2,000/€4,000 p.a.	365
Top rate of income tax	Reduce by 1%	186
Other income tax	Exemption limits and credits	44
PRSI threshold	Increase by €39 p.a.	32
Health levy threshold	Increase €40 p.a.	44
Health levy rate	Increase by 0.5% for high earners	(34)
Mortgage interest relief	Increase in ceiling, especially for first-time buyers	70
Other		10
Total		1,342

3 Distributive impact of Budget 2007

We now examine the distribution of the tax/welfare resources across the population using the ESRI SWITCH model. A key component in the analysis is the comparator budget. The standard approach is to examine budget changes against a backdrop of no policy change, i.e. welfare and tax rates are frozen in nominal terms, based on the previous year's budget. This is misleading in that it assumes a starting point of losses in real income for those depending on welfare payments, as inflation erodes the real value of fixed

nominal payments; at the same time income growth with fixed credits and bands means that taxes rise as a proportion of income ('fiscal drag').

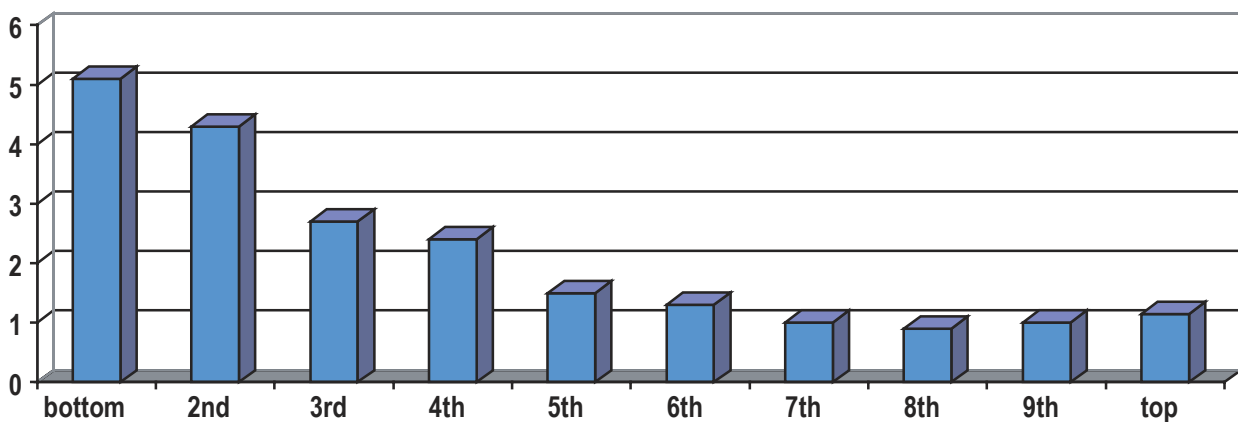
An alternative benchmark is to index tax and welfare rates in line with wage growth, which gives a similar increase in income for all population categories in line with growth in national income. Such a budget is both distributionally neutral and maintains the overall share of taxes and welfare expenditure as a percentage of GNP. For this analysis of Budget 2007, the benchmark used

is the 2006 tax and welfare rates increased by 5.5 per cent, which is the wage growth forecast for 2007 at the time of the budget.⁶ The distributive analysis focuses on the first-round impact of budgetary changes, based on the technical assumption of no change in behaviour.

In Budget 2007, the resources available after indexation of welfare and income tax in line with wage growth amounted to just under €1,100 million or 40 per cent of the total allocation. The distribution of the budget package compared to a wage-indexed 2006 policy

is presented in Diagram 1, based on a ranking of the population in ten equally sized income deciles from poorest to richest.⁷ The average percentage gain from Budget 2007 is 1.5 per cent. There is considerable variation in the percentage gain across income deciles. The greatest increase is for lower-income groups, with between 4 and 5 per cent for the bottom two deciles and an average of 2.5 per cent for the third and fourth deciles, both above the average gain. Thereafter, the gain tapers off for all other income categories to around 1 per cent, only slightly below the average gain.

Diagram 1: Distributive impact of Budget 2007 against wage-indexed budget 2006 policy
(percentage change in disposable income by decile)⁸



The average cash gain is €9.40 per household unit per week. The cash gain across the population varies between €7 and €17 per week. Low-income households get between €8 and €11 per week, as their higher percentage gains do not translate into larger cash amounts due to their low income base. There is greater variation among higher income groups, with the richest decile getting the largest cash gain at almost €17 per week. By contrast, the seventh and eighth deciles record the smallest cash improvement at €7 per week. In overall terms, Budget 2007 contributes to a progressive redistribution of income, which principally stems from the large increases (€20 per week) given to welfare recipients on relatively low incomes. The substantial cash gains arising for high-earning tax payers are much less in percentage terms.

4 Other measures of distributive impact

Another perspective on distributive impact is to examine

the share-out of total resources between income categories (Diagram 2). To put this in context, we compare this allocation with how all income is divided across the population (bearing in mind that the Budget package is of the order of 2 per cent of total income).⁹ For ease of comparison, the unit of analysis is now quintiles. In Budget 2007, compared to a wage-indexed 2006 policy, the share-out of resources was equally divided between the bottom and top halves of the population. At a micro-level, more variation is apparent, with the richest quintile getting the largest share at 28 per cent, while the fourth richest quintile gets 15 per cent and the third receives 17 per cent. Using the standard measure of income inequality, the richest quintile gets 1.5 times the budgetary resources of the poorest.¹⁰ The Budget outcome is quite unlike the distribution of all income in the population, which is more unequal across income categories. At its most extreme, the top fifth have almost five times the income of the poorest fifth.

⁶ This is an important difference to the approach adopted by the Department of Finance in its use of SWITCH to assess the poverty impact of the budget.

⁷ The unit of analysis is an income-sharing unit, defined as follows:

Disposable income is adjusted for household size using the following equivalence scale: 1 for the first adult, 0.66 for each subsequent adult and 0.33 for each child.

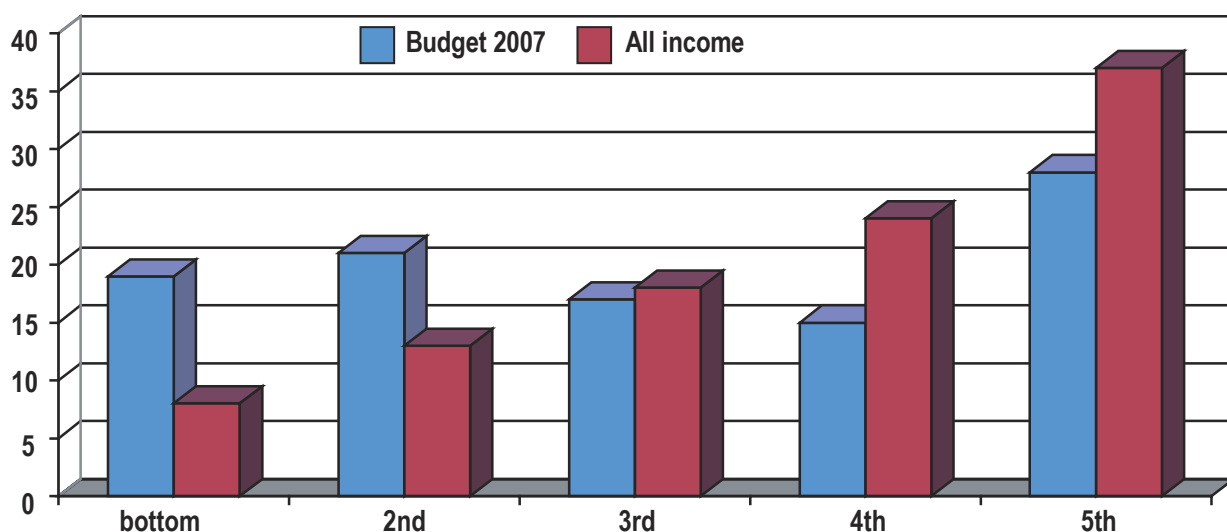
⁸ The range of disposable income per adult is > €738.

⁹ This is based on the results of the EU Survey on Income and Living Conditions 2005.

¹⁰ The S80/S20 quintile share ratio is one of the common

total equivalised income received by the highest income quintile to the lowest income quintile.

Diagram 2: Distribution of Budget 2007 resources (over a wage-indexed 2006 policy) and distribution of all income (2005)
(percentage share of disposable income by quintile)



The analysis now moves from income to families, classified by composition and income source. Table 3 shows how non-working families of diverse composition do better than their employed counterparts. Single and dual unemployed families get the highest percentage rise of between 3.9 and 5.5 per cent. Retired households also do well, with gains of between 2.6 and 2.9 per cent. All earner households do less well, regardless of composition. Dual earner couples gain the least in percentage terms. Across all family categories, those

containing children fare less well in percentage terms. This is in sharp contrast with Budget 2006 and reflects the smaller package of child income support in Budget 2007. Non-earning couples with children record the largest cash gains in Budget 2007 at €23 per week. Non-earning couples without children and retired couples also get a relatively large amount (€16). These patterns reflect the large welfare increases and targeted improvements in child income support.

Table 3: Distributive impact of Budget 2007, against wage-indexed 2006 policy
(percentage change in disposable income by family type)

Family type	Percentage	Cash (€)
Single unemployed NC	5.5	8.79
Non-earning couple NC	4.4	16.17
Non-earning couple C	4.3	23.35
Non-earning lone parent	3.9	12.69
Retired couple	2.9	16.30
Single retired tax unit	2.6	6.52
Single earner couple NC	1.5	11.08
Employed lone parent	1.4	7.99
Single employed NC	1.3	6.28
Dual earner NC	1.1	12.54
Single earner couple C	1.1	9.93
Dual earner couple C	1.0	12.84
Dual earner couple other	0.7	6.68
Other	5.2	7.98
All	1.5	9.05

NC = no children C = children

5 Poverty impact of Budget 2007

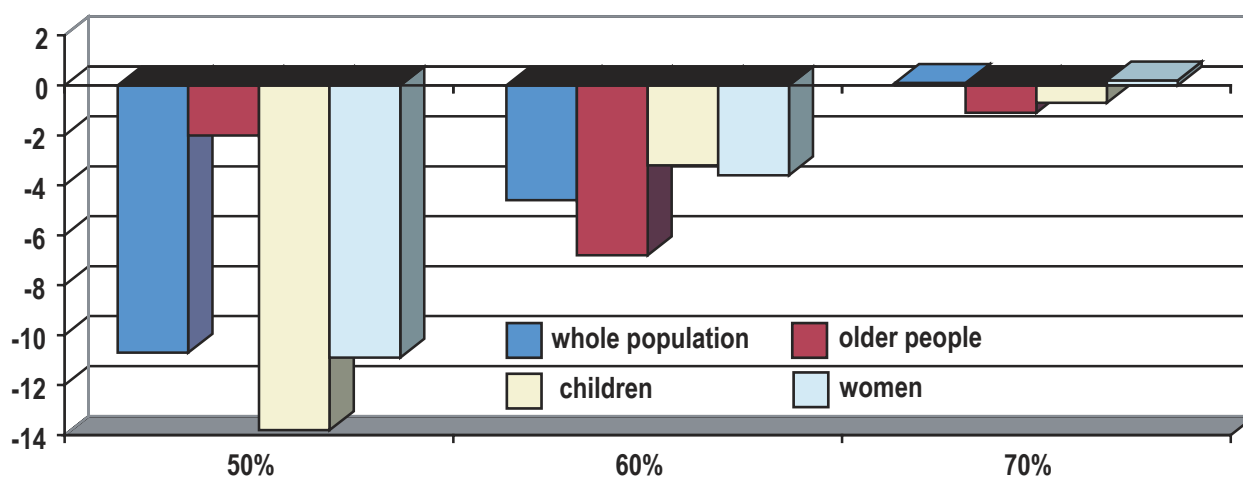
We turn now to consider the budgetary impact on relative income poverty, again using a wage-indexed 2006 policy as the comparator. Diagram 3 illustrates the positive effect of Budget 2007 on the percentage of the population below conventional income poverty thresholds (50–70 per cent of median income).¹¹ The ‘at risk of poverty’ rate falls by 11 per cent at the lowest threshold of 50 per cent of the median. The reduction is

a smaller 5 per cent at 60 per cent of the median, while there is no change in income poverty at the highest threshold, 70 per cent of median income.

Another poverty measure is the extent to which the population falls below the various income thresholds (called the poverty gap). This gap is reduced by between 6 and 12 per cent across all income thresholds.

Diagram 3: Effect on income poverty rate in Budget 2007 (against wage-indexed 2006 policy)

(change in poverty rate at various median income thresholds)



It is useful to look at the impact on poverty for vulnerable groups such as older people, children and women. At the lowest threshold, the risk of poverty among older people falls to a smaller extent than among the population as a whole. A bigger reduction is found at the 60 per cent threshold, where the decrease is 7 per cent. It is at these higher thresholds that most older people experience poverty. Child poverty also falls, with the reduction concentrated at the 50 per cent threshold, where the headcount declines by a substantial 14 per cent. The numbers of adult women in poverty decline in line with the situation for the general population. This reflects the absence of a specific gender focus in the welfare package of the Budget. For all vulnerable groups, the poverty gap also decreases by significant amounts, especially in the case of older people.

6 Unpacking the components of Budget impact

The analysis now looks in detail at the components of Budget 2007. The budgetary resources available after indexation of welfare and tax policy are divided equally between additional welfare and tax measures,

with further child income support only attracting 3.5 per cent.¹³ Diagram 4 details the contribution of tax and welfare (including the small child income support element¹⁴) across the income schedule. This shows that only at the fifth decile is their contribution of equal importance. Among the bottom 40 per cent of the population, social welfare contributes almost 100 per cent of the gain. From the sixth decile up, tax reductions are the main factor in income gain, ranging from 80 per cent for the sixth and seventh decile to over 90 per cent for the top three deciles. This polarised pattern reflects the targeted nature of the social welfare system, the limited expenditure on universal child income support and the concentrated burden of income tax on better-off households. Looking at the impact on poverty of these two policies, it is not surprising that the income-tax changes worsen income poverty through increasing the median income, thereby causing more households to fall below the various thresholds. Although the social welfare gain also raises the median income, this is compensated for by the targeted increases in lower incomes, which results in a significant fall in the percentage of the population in income poverty.

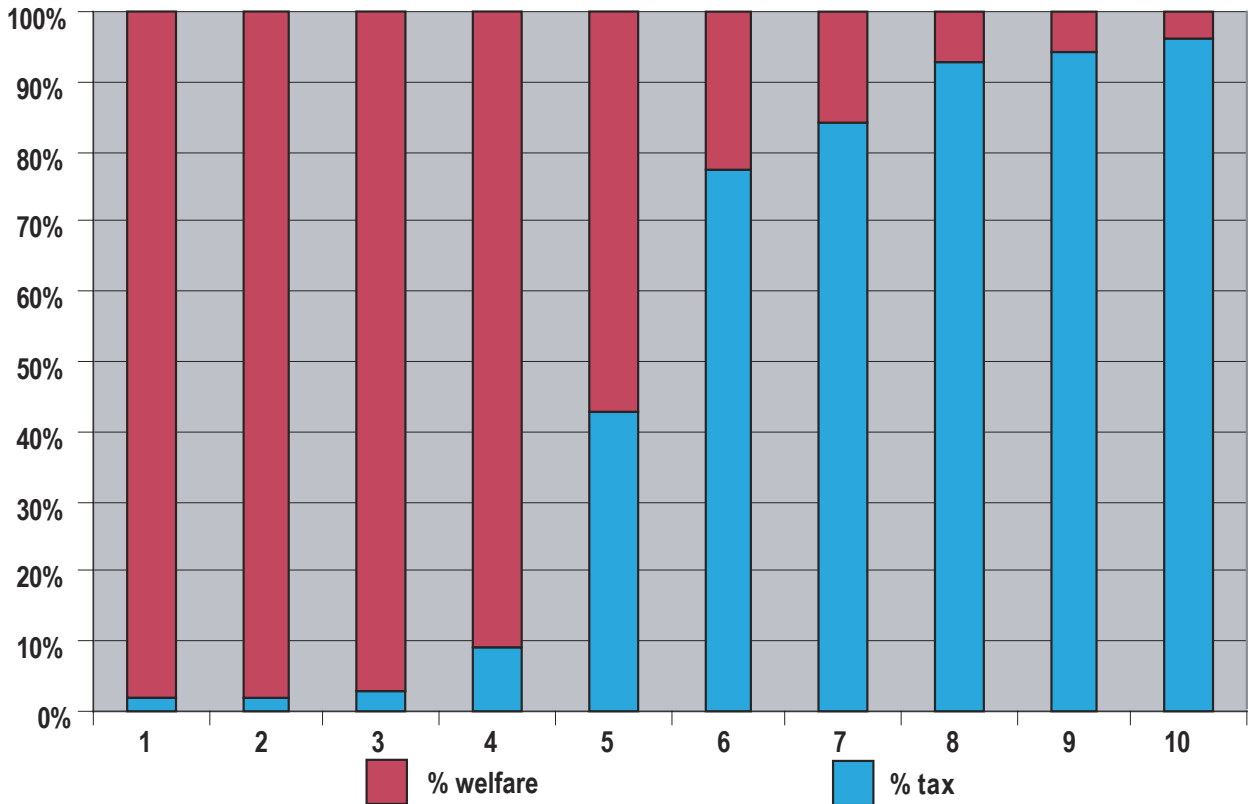
¹¹ The weekly equivalised disposable income of these thresholds is: 50 per cent = €213; 60 per cent = €256; 70 per cent = €298.

¹³ This low allocation for children reflects the failure to increase the early childcare supplement, resulting in a devaluation of this payment.

¹⁴ The small additional child

Diagram 4: Composition of distributive impact of Budget 2007 (social welfare and income tax)

percentage share of change in disposable income by income deciles

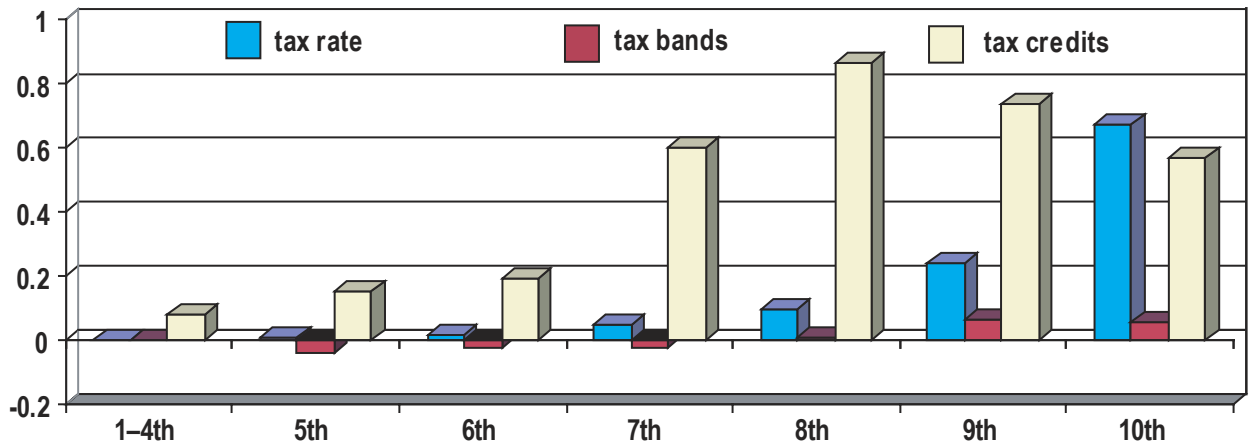


We extend this analysis to examine the distributive impact of the income tax measures in Budget 2007, where three different policy options are used to reduce income tax: tax credits (employee and personal), standard rate tax bands and a cut in the top rate of income tax. Two-thirds of the gain (over a wage-indexed policy) is derived from tax credits, one-third from the tax rate cut and nothing from the changes in the tax band.¹⁵ The distributive impact of each measure is presented in Diagram 5. The first point to note is how little gain there

is in the bottom four deciles (grouped in one category) under any of the tax measures, which reflects the pattern in the previous diagram. The cut in the top rate of tax is the most regressive of the three tax measures. Its benefits are concentrated in the top 10 per cent of households, who get three times the gain of the ninth decile and seven times that of the eighth decile. (Looked at in another way, the top 10 per cent receive 72 per cent of the total gain in disposable income from the tax cut.)

Diagram 5: Distributive impact of various income tax measures in Budget 2007 against wage-indexed policy

(percentage change in disposable income by decile)



¹⁵ The income-tax cut, though the smallest tax expenditure

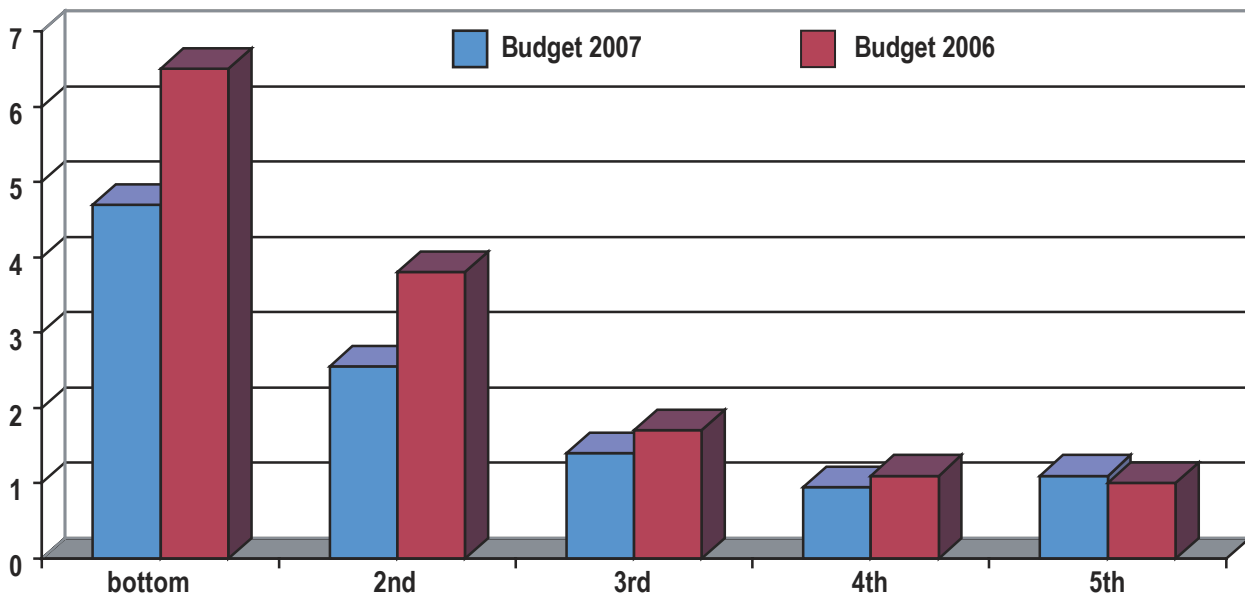
Tax credits, by contrast, are more equitable for the top 40 per cent, while the rest of the population get less than one-third of the percentage gain. This highlights the limited benefit to be derived from increased tax credits by low-earners who have no liability to income tax. The increases in the tax bands replicate the impact of a rate cut, but at a much smaller scale. Interestingly, middle-income groups record a small loss here, which arises from the limited transferability of bands in one-earner couples. Overall, the disproportionate tax gain among higher income groups reflects the concentrated burden of income tax on these households, as the richest 20 per cent of taxpayers pay over 70 per cent of all income tax. Nonetheless, it is apparent that the choice of measure to reduce income tax can significantly affect the distributive outcome.¹⁶ However, even the most progressive measure, tax credits, is constrained in reaching low earners.¹⁷

7 Budget 2007 in a comparative perspective

Now we examine the impact of Budget 2007 from a comparative perspective to identify budgetary policy trends over time. In the first instance, Budget 2007 is compared with its predecessor, Budget 2006, using five equally sized income groups (quintiles) for ease of analysis. Diagram 6 shows that the direction in the last two budgets is broadly similar, though Budget 2006 is slightly more generous for lower-income groups. The average gain in Budget 2007 is almost one-quarter less than that in Budget 2006. In addition, Budget 2007 is more favourable towards the richest quintile, which gains 10 per cent more in Budget 2007 than in its predecessor, despite the reduction in the average gain. This reflects the higher share of Budget resources allocated to tax reductions in 2007 (more favourable to the better-off), while the allocation to universal child income support was reduced (proportionately more beneficial to low- and middle-income families).

Diagram 6: Distributive impact of Budget 2007 and 2006, against wage-indexed policies

(percentage change in disposable income by quintile)



A longer-term perspective is provided by analysing the last five Budgets (2003–2007) and the last ten Budgets (1998–2007). These two periods coincide with the ten-year National Anti-Poverty Strategy (first introduced in 1997 and revised in 2002).¹⁸ Diagram 7 illustrates the poverty effect of Budgets 2006 and 2007. This shows that both Budgets have a positive effect on income poverty, especially at the lowest 50 per cent median

threshold. This pattern diverges at the higher thresholds, with Budget 2007 having twice the reduction at the 60 per cent threshold, while Budget 2006 had a far greater impact at the 70 per cent line. The differing approaches to child income support is likely to be the reason for this, with Budget 2007 concentrating on poorer children, while Budget 2006 improved the position of all children, especially those under six years.

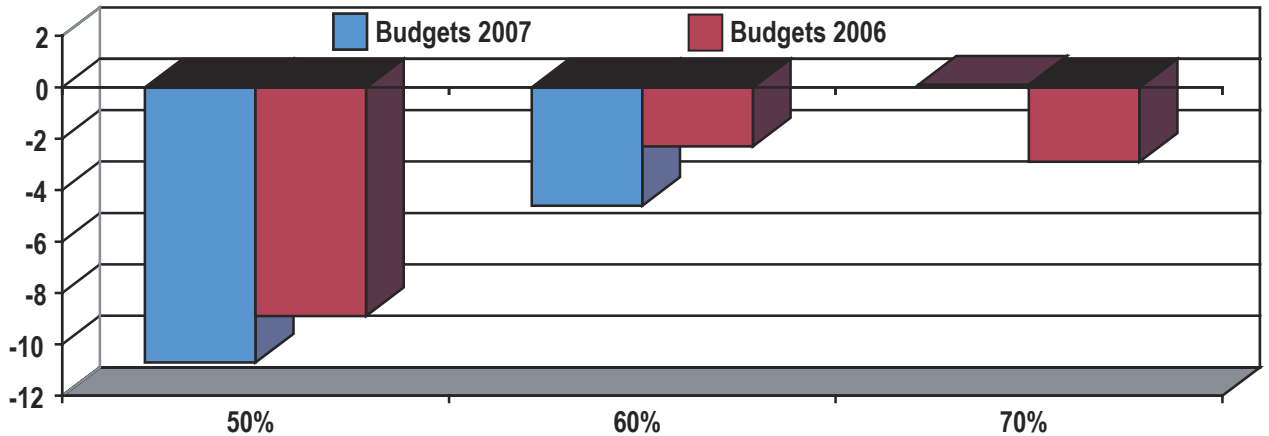
¹⁶ Another option is to reduce the standard rate of income tax. This is not modelled as it was not used in Budget 2007.

¹⁷ This finding is different to the assertion by I

¹⁸ They also coincide with the last two programmes for Government and overlap with a number of social partnership agreements. The periods coincide with generally strong exchequer finances, though Budgets 2003–2005 were smaller in scale.

Diagram 7: Effect on income poverty in Budgets 2006 and 2007 (against wage-indexed policies)

(change in poverty rate at various median income thresholds)

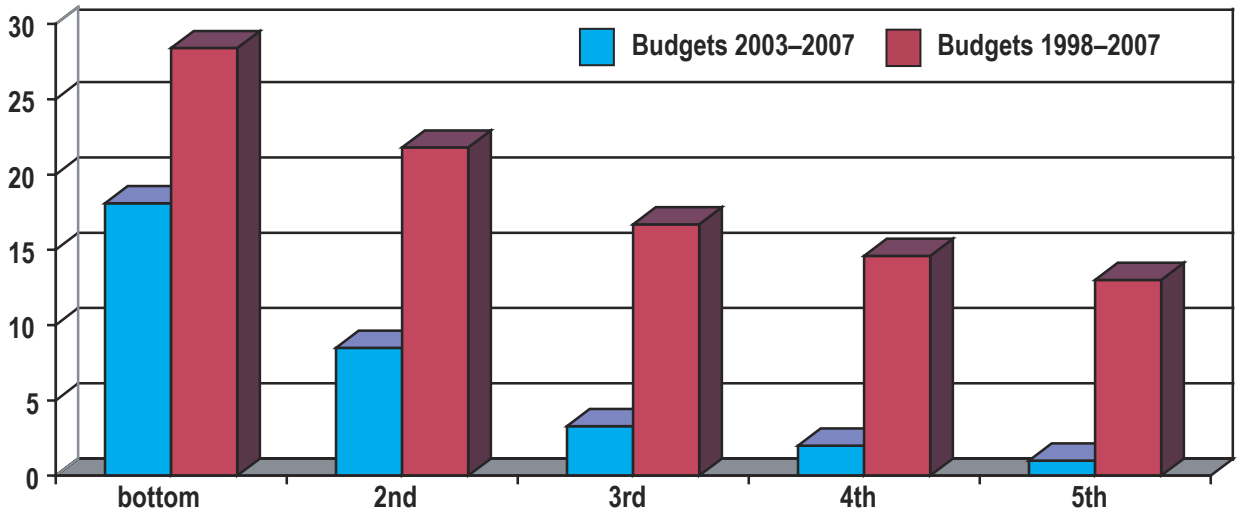


We turn now to the cumulative pattern over the last five and ten Budgets (Diagram 8). The average income gain over the last five years is 3.5 per cent. Low-income groups get far more than this, with the bottom fifth benefiting by over five times the average (18 per cent) and the second fifth by more than twice the average (8

per cent). Higher income groups do less well, recording cumulative gains of between 1 and 2 per cent, well below the average. Budget 2007 is broadly in step with recent policy direction, featuring welfare increases far ahead of wage indexation, with tax reductions only slightly more than wage growth.

Diagram 8: Distributive impact of Budgets 2003–2007 and Budgets 1998–2007, against wage-indexed policies

(percentage change in disposable income by quintile)



A ten-year perspective shows an average gain of 16 per cent. The period 1998–2002 is the dominant contributor to this gain, with three-quarters being delivered in the first five years compared to one-quarter in the last five years. The distributive pattern over the longer period still favours low-income groups, but to a far lesser extent than in recent years. Middle- and high-income quintiles

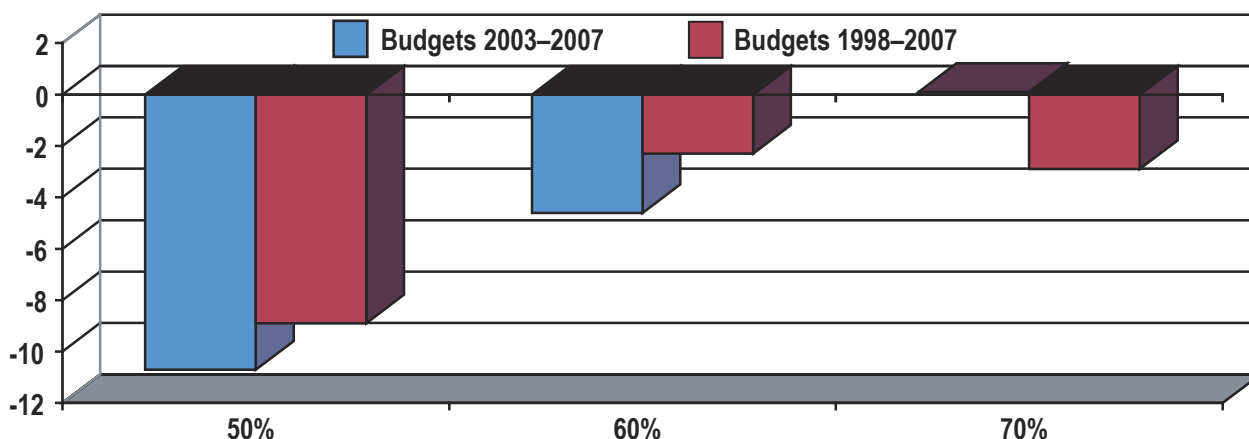
show significant gains of 13 to 17 per cent, in line with the average. Most of this gain is attributable to the large tax packages in Budgets 1998–2002. The poorest quintiles show total gains of between 22 and 28 per cent, with most of this accruing between 2003 and 2007. This indicates a substantial shift in budgetary policy under the revised NAPS, when a more modest scale

of resources was targeted at low-income households through the medium of large welfare increases.¹⁹ This policy change is slowly redressing the tax-oriented Budgets at the turn of the millennium.

Diagram 9 illustrates the contrasting poverty impact of budgetary policy over the longer-term. Taken together, the last five budgets have reduced the rate of income poverty by 37 per cent at the 50 per cent threshold, with smaller falls of 8 per cent and 4 per cent at the 60 and

70 per cent thresholds, respectively. The reduction in poverty was greater for older people over this period and smaller for children. Over the ten-year period, the impact on poverty is less positive at the lowest threshold, where the total fall is 25 per cent (indicating that the poverty headcount increased in the earlier 1998–2002 budgetary period). The pattern at the other thresholds is more consistent with the last five years, with total reductions of 11 and 6 per cent, respectively (poverty gap).

Diagram 9: Effect on income poverty in Budgets 2003–2007 and Budgets 1998–2007, against wage-indexed policies
(change in poverty rate at various median income thresholds)



8 Combat Poverty proposals

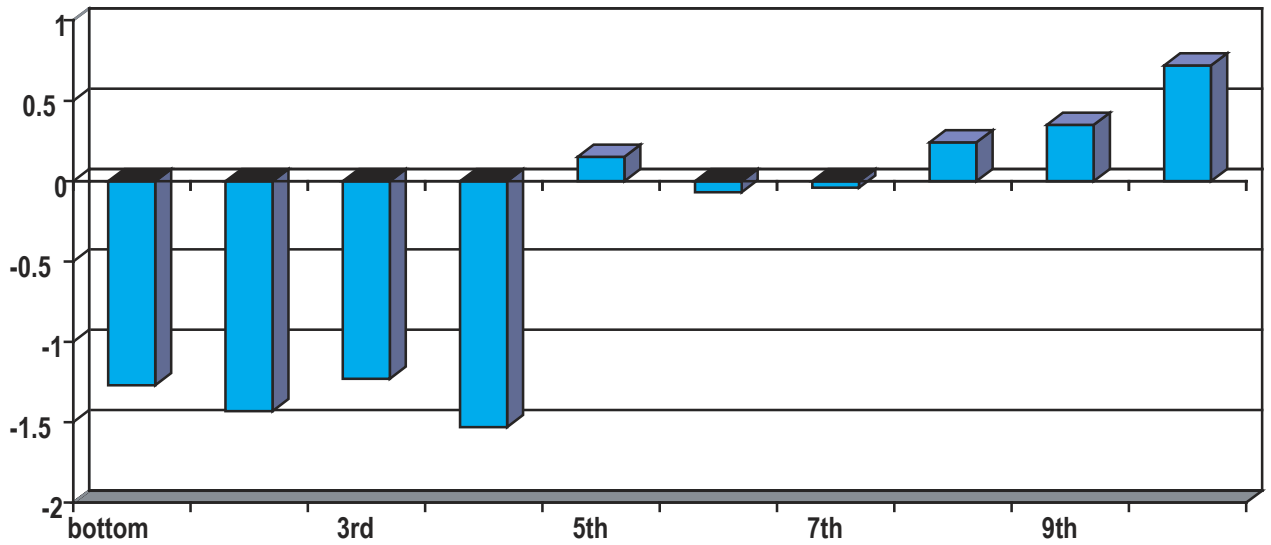
How does Budget 2007 compare with the proposals made by Combat Poverty in advance of the Budget? In its pre-Budget submission, Combat Poverty had proposed a budget costing €2,360 million, in line with Budget 2006. Half of this was allocated to welfare improvements, with a quarter each for child support and income tax. The outturn in the Budget is a tax/welfare package which was almost €400 million bigger (16 per cent) than recommended. The division of the package is also different, with 49 per cent provided for income tax, 42 per cent on social welfare and only 9 per cent on child income support. In terms of specific measures, most of the welfare proposals are replicated in Budget 2007. The main points of difference are in regard to child income support (especially the early childcare supplement) and tax reductions (the size of the increase in tax credits and the cut in the top rate of tax).²¹

Diagram 10 compares the outcomes of Budget 2007 with those that would have been achieved in the Combat Poverty package. For comparative purposes, the Combat Poverty proposals are increased by 15 per cent to equate with the actual expenditure in Budget 2007. Budget 2007 has a different distributive outcome, giving between 1 and 2 per cent less of a gain to lower-income groups than proposed by the Combat Poverty proposals. By contrast, the top 30 per cent of the population do slightly better than under the Combat Poverty package. Middle-income groups would benefit to a similar extent under both packages.

¹⁹ This policy change was first apparent in Budget increase of 1 per cent. The average gains in the next three Budgets were modest. It is only in Budgets 2006 and 2007 that significant gains have again been recorded by low-income groups.

²¹ *Making poverty the policy priority. Submission budget 2007*, Dublin: Combat Poverty (2006)

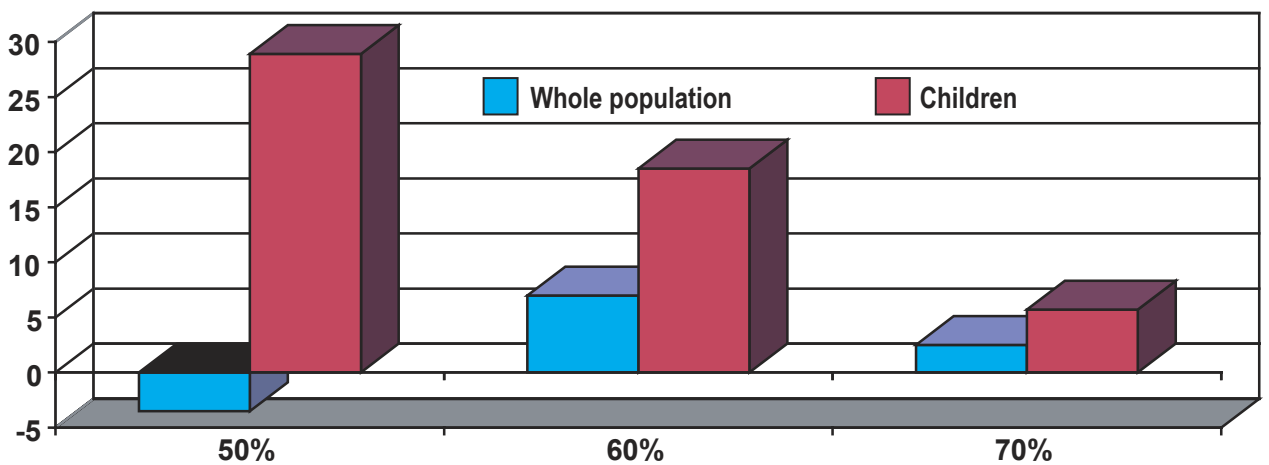
Diagram 10: Distributive impact of Budget 2007 compared with Combat Poverty package of equal cost
(percentage change in disposable income by quintile)



The differing impact on poverty of the Combat Poverty proposals and Budget 2007 is illustrated in Diagram 11. Generally, the Budget 2007 proposals have a lesser impact on poverty. Only at the 50 per cent threshold does Budget 2007 achieve a greater poverty impact (3.5 per cent less). At the 60 and 70 per cent thresholds, Budget 2007 increases poverty by between 2.5 and 7 per cent as compared to the Combat Poverty proposals. Similarly, Budget 2007 increases the poverty gap at

all thresholds by between 7 and 13 per cent. There is an even greater contrast in terms of poverty outcomes for children between the two budgets, reflecting the Combat Poverty priority to tackle child poverty. Budget 2007 leaves between 6 and 29 per cent more children in poverty than would have been the case with the Combat Poverty package. Similarly, the poverty gap for children is between 20 and 43 per cent higher under the Budget.

Diagram 11: Effect on income poverty in Budget 2007 compared with Combat Poverty proposals of equal cost
(change in poverty rate at various median income thresholds)



In aggregate terms, the difference between the Combat Poverty proposals and Budget 2007 is under €200 million (7 per cent) and is mainly accounted for by the substitution of the cut in the top rate of tax for increases in the early childcare supplement (double payment for pre-school children and 50 per cent payment for children aged 6–12 years). Thus, the redistribution of a relatively small proportion of the total tax/welfare package in the Budget would have achieved an enhanced poverty impact, especially for children. A greater awareness of the distributive outcome of tax/welfare policies in budgetary decision-making could have resulted in different policy choices.

9 Commentary on individual policies

We now conclude with a discussion on developments in social welfare, child income support and taxation policies in Budget 2007.

9.1 Social welfare

Welfare rates are central to poverty performance, as well as being intrinsic to achieving a minimal societal

level of existence. The revised NAPS specifies a target of a minimum welfare payment of €150 per week (2002 values) by 2007. In line with this target, Budget 2007 continues the recent policy of large increases in the lowest personal welfare rates, with an increase of €20 (12 per cent). Over the last five years, the minimum welfare payment has increased by a cumulative €67 (56 per cent), an average of €13 per annum.²² In its own right this is a major increase in a short time frame and is far in excess of price inflation or wage growth (17 per cent and 29.5 per cent, respectively).

To what extent has this major increase met the original target? To answer this question, we adjust the target amount to reflect 2007 values using a variety of methods in the absence of specific policy guidance. These are: price inflation, wage growth and 30 per cent of gross average industrial earnings (GAIE).²³ These figures and their relationship with the 2007 minimum welfare rate are set out in Table 3.

Table 3: Implementing the minimum welfare target of €150²⁴

Methodology	Inflation	Wage growth	30% GAIE
Estimate	€175.58–€180.32	€194.25	€185.80
Difference with actual rate	€10.22 to €5.48 more	€8.45 less	Identical

Adjusting for inflation up to 2007, the target figure is €175.58 per week. The 2007 welfare rate comfortably exceeds this range by €10 per week. Adjusting by wage growth, the target figure is €194.25. This leaves a shortfall of €8.45 on the 2007 welfare rate. Using the measure of 30 per cent of GAIE, the target rate is estimated as €185.50. This is almost exactly the same as the welfare rate post-Budget 2007. It can be concluded from this that the NAPS adequacy target has been met on two of three possible adjustment mechanisms. There remains a small shortfall, however, using a general wage-growth benchmark.

A separate welfare target set by Government was for a payment of €200 per week for the state pension (non-adjusted). In Budget 2007, the means-tested

state pension increased by €18 to reach the €200 target, while the contributory payment increase of €16 exceeds the target by €9.30. (Payments for carers also increased to €200.) There is no NAPS target for qualified adult allowances (QAA), which are generally set at 66 per cent of the adult rate (though in Budget 2000, a commitment was made by the then Minister for Finance to bring this up to 70 per cent). In Budget 2007, allowances increased pro rata with the personal rate (between €10.70 and €13.30). The QAA for the state contributory pension got a special increase of €23.70 to €173 per week, in line with a commitment to bring this payment up to the level of the non-contributory state pension over the next three years.

²² The actual increases are 2003 – €6, 2004 – €10, 2005 – €14, 2006 – €17 and 2007 – €20.

²³ This interpretation of the €150 target!

Economic Review. Developing a Fairer Ireland, Dublin: CORI Justice.

²⁴ The inflation figure for 2002 to 2007 is 17.1 per cent. This is based on the CSO inflation rate for 2002–2006 of 12.7 and the forecast rate for 2007 of 3.9 per cent (ESRI QEC, December 2006). The figure for wage growth is 29.5 per cent, which is drawn from the ESRI SWITCH model. The figure for growth in GAIE is 23.9 per cent, as calculated by CORI Justice. It should be noted that GAIE is a narrower measure of wages than that used in the SWITCH model.

Budget 2007 introduces further reforms which widen entitlement to welfare payments for older people, carers, people of working age and people with disabilities. This is achieved through more generous means tests, especially in regard to the treatment of income from employment (e.g. higher disregards for earnings and higher income thresholds for retention of benefits). An omission from the welfare reform package is the proposed parental allowance for carers of children under eight years, replacing the One Parent Family Payment and the qualified adult allowance.

9.2 Child income support

Reform of child income support is a feature of recent Budgets, with a major increase in child benefit since 2000 and the introduction of the early childcare supplement in Budget 2006. Budget 2007 maintains the emphasis on child benefit with a €10 per month (€2.30 per week) increase (7 per cent), though there is no increase in the childcare supplement. The innovative feature of Budget 2007 for children is the first increase in the child dependent allowance since 1993 of up to €5.20 per week (up to 31 per cent). Other means-tested payments for children are also increased, including

the Family Income Supplement (FIS) (between 3 and 30 per cent) and the clothing and footwear allowance (50 per cent). The maximum total gain for children in welfare-dependent families (standard rates) is a substantial €8.63 per week (between 12 and 16 per cent).

Table 4 summarises the structure of child supports featuring five different payment strands for low-income families with two broad age categorisations (other variations for size of family and age of child are left out for reasons of simplicity).²⁵ The key policy target for child income support is to ensure the combined package of support is the equivalent of 33–35 per cent of the minimum personal welfare rate. The combined child package for younger children is now €81.38 (per week), which is the equivalent of 44 per cent of the adult rate. For older children, the combined amount is €62.23 (per week), which is the equivalent of 34 per cent of the adult rate. For low-waged families on FIS, the package for younger children is €113.38 per week, falling to €94.23 for older children. These are the equivalent of 61 per cent and 51 per cent of the adult rate, respectively. A premium for older children, reflecting evidence of higher costs, is still lacking

Table 4: The structure of child income support (standard rates in weekly € equivalent)

Category	CB	ECS	CDA	CFA	FIS	Total (% of adult rate)	Means-tested share
Welfare							
< 6 years	36.78	19.15	22.00	3.45	–	81.38 (44%)	31%
6 years+	36.78	–	22.00	3.45	–	62.23 (34%)	41%
Low paid							
< 6 years	36.78	19.15	–	3.45	54.00	113.38 (61%)	51%
6 years+	36.78	–	–	3.45	54.00	94.23 (51%)	61%

The discontinuity between welfare-dependent families and low-paid (working) families remains a feature of child income support and has to some extent intensified, contrary to the proposals for an integrated second tier of child income support. A related issue is the balance between universal and means-tested supports and the accompanying withdrawal rate. Targeted payments represent between 30 and 40 per cent of the total package for welfare-dependent families. The proportion

is much higher for low-paid families, where it varies between 50 and 60 per cent. Both of these issues may exacerbate transitions from welfare to work. Another consideration is the diversity of mechanisms for delivering child income for a low-income family (up to four) and their varied frequency (from weekly to annual). This may dilute the overall impact of the child income support package.

²⁵ These are child benefit (standard rate of €160 per month); child dependent allowance (standard rate of €10 per month); Family Income Supplement (standard rate of €10 per week);

9.3 Taxation

Budget 2007 features an extensive package of income tax reductions, including employee tax credits (+ 18 per cent), personal tax credits (+ 8 per cent), standard rate tax bands (+ 6 per cent), a 1 per cent cut in the top tax rate and a doubling of mortgage interest relief for first-time buyers. The distributive implications of these reforms have already been discussed. The return to cuts in rates of tax for the first time in over five years is of concern, as these are less equitable and also harder to claw back if required in the future. The structure of the increases in tax credits and bands prioritises employees and dual working couples in line with recent policy. Another policy goal is to exempt employees on the minimum wage. Under Budget 2007, those on an hourly wage of €8.65 will not be liable for income tax (almost 40 per cent of the workforce). However, for those whose earnings fall short of the tax threshold, these changes will have no benefit.

One other income-tax change of note is the renewal and expansion of the Business Expansion Scheme at a tax foregone cost of €25 million. This measure seems to run counter to the reforms in tax relief schemes introduced in Budget 2007, in response to concerns about the high cost to the Exchequer, the regressive impact of tax relief schemes and their unclear value for money. Other tax changes in Budget 2007 relate to excise duty on tobacco and fuel, VAT for small businesses, farmer taxation, corporation tax and stamp duty. The poverty implications of these measures are minimal. In that context, the lack of fundamental reform in the structure of indirect taxes is disappointing. Indirect taxes now account for half of the tax take and 50 per cent more than income-tax returns. Their effect is far more regressive than other forms of taxation, accounting for one-fifth of the incomes of the poorest decile compared to 10 per cent of the richest.²⁶ In this context, a rebalancing of the tax burden from regressive to progressive taxes is required.

10 Conclusion

Tax/welfare policy has a key role to play in redistributing resources and reducing relative income poverty, under the framework of the National Anti-Poverty Strategy.

Budget 2007 significantly enhances the progressive outturn of recent budgets, delivering gains of up to three times the average for low-income groups. Budget 2007 has a positive effect on relative income poverty, especially at the lowest threshold. The engine of poverty reduction is the big increases in welfare rates, augmented by a targeted allocation on child income support. The substantial tax package delivers proportionately little to less well-off groups, with the richest deciles the main beneficiaries. Taken together with budgetary policy since the revised NAPS in 2002, there is a significant reduction in income poverty in line with European best practice.²⁷ This improvement should be built upon in the new National Action Plan for Social Inclusion 2007–2016.

The fly in the ointment is the outturn of the massive government subvention of SSIA's, which are maturing in late 2006 and early 2007. The value of the SSIA's subvention at €3 billion is almost three times the tax/welfare package of Budget 2007 (after indexation). This expenditure has a number of inequitable features: it is being shared among a minority (38 per cent) of the adult population; there is a high take-up among people in employment, in particular those in professional and administrative occupations, with only 16 per cent of unemployed people as beneficiaries; there is no cognisance of children in the structure of the scheme.²⁸ In addition, there is an income-tax subvention of almost €3 billion per annum for private pensions, which is mainly received by high-income taxpayers.²⁹ Greater transparency as to the distributive and poverty impact is required in these policy areas, as is the practice with general tax/welfare changes. This could lead to a refocusing of these massive public resources in favour of low-income groups and a significant development of their ability to combat poverty in the years ahead.

Finally, this analysis highlights the key role of the SWITCH model in understanding the distributive and poverty impact of budgetary policy, and thus in implementing official poverty impact assessment guidelines.

²⁶ A. Barrett and C. Wall (2006), *The distributive impact of Ireland's indirect tax system*, Dublin: Combat Poverty Agency

²⁷ This is borne out by the recent EU SILC findings on poverty (Central Statistics Office, 2006, *EU Survey of Income and Living Conditions 2005*, Dublin: CSO).

²⁸ Central Statistics Office (2006), *Quarterly National Household Survey. Special Savings Incentive Accounts*, Dublin: CSO

²⁹ G. Hughes (2005), 'Pension tax reliefs and equity', in J. Stewart (ed.) *For richer, for poorer; an investigation of the Irish pension system*, Dublin: Tasc



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