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social security and the changing labour market

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Introduction

Social protection was largely a social construction of the 20th century. In the 21st century global competition will intensify, traditional manufacturing and service occupations will be transformed in an e-world, conventional working patterns and working lives will change unimaginably. It will be an increasingly individualised world in which people will depend on their own human capital but will have to be flexible, adaptable and live with insecurity. For most this will bring increasing prosperity but those who cannot compete will be left far behind, afforded meagre, means-tested protection by the contented majority. It will be a modern version of “the quick and the dead”.

But this is only one view. There is an alternative.

Social protection has developed because it contributes to two central goals. It contributes to the efficiency of the economy and it contributes to the equity of the society. It facilitates and eases change and promotes fairness, which legitimates the state. As the economy and society change, what causes insecurity and what people can and do provide for themselves alters. But while the functions will change, there will be a continuing, perhaps growing, role for government in providing social protection.

The first view, associated with economic liberalism and a Thatcherite disdain for the importance of social provision, is now espoused in much of the Anglo-Saxon world. The growth of the US economy while welfare (primarily for lone-parent families) has been savagely cut back is used as evidence by writers such as Charles Murray that social protection is part of the problem, not part of the solution.

The second view, associated with democratic socialism and solidaristic thinking on the continent of Europe is defended by those who see untrammelled market forces as being neither socially efficient nor desirable. In contrast to the Anglo-Saxon priority for the economic, in much of the European Union a concern for justice in the ‘social space’ promotes integrative social institutions, which include social protection.

There is, therefore, a deep divide on social protection even if there are many gradations between the polarised alternatives set out here.

The purpose of this paper is to analyse some of the issues concerning the future of social protection based on the available evidence. In particular, Britain's level of social protection is of central concern. The approach is largely comparative examining whether countries with more or less social protection do better in terms of growth, employment or poverty; to do this the paper draws on evidence collected by the EU, the OECD and other researchers. The purpose is not to consider the future of all the social services nor to describe different systems of social protection in detail. In discussing social protection the focus is on social security in the British sense, concentrating on public provision, excluding the finance of health care and including where relevant tax credits.

In the next section the function of social protection is considered and how this affects its future role. The differences in the levels of social protection are considered and how these are related to economic performance. Aspects of social protection are then disaggregated to assess how protection for particular groups or through particular means of financing or delivery may be linked to performance. Then future developments that affect social protection are discussed. Finally, the challenge to Britain of improving its social protection is considered, setting out the costs and the benefits.

Social Protection and the Economy – Issues and Evidence

The growth of social protection has been motivated above all by a concern to prevent poverty – or tackle the evil giant of 'want' as Beveridge put it. This primary role will be considered later. Increasingly the economic function of social protection has also been recognised. The OECD (1999) summarised these positive economic aspects:

"Social protection … helps bind economies and societies together in the following ways:

- *Social policies are vital determinants of the rate of employment*. Social benefits are often conditional on job search activity; social benefits can support families in their balancing of caring and paid work; … by insuring against events which lead to loss of earnings, social insurance makes work in general more attractive.
- *There are costs to exclusion*. If people are excluded from society, they cannot fully contribute either in the labour market or in systems of family and social support.

- *Change is resisted*. Taking advantage of new opportunities requires risk-taking. But most people are risk-averse. Some form of income security can, for example, help in making the risk attached to long-term investments in lifelong learning attractive, as well as reduce protectionist sentiments. Social protection helps limit the potential downside risks of change, thereby promoting development.
- *Inequality can have costs.* Few would seriously dispute the proposition that wide disparities in income and high rates of poverty impose costs on society in terms of threats to property and the measures taken to contain these threats. Furthermore, trust in personal and economic relationships, dense networks of community organisations and wide participation by citizens have been identified as factors potentially contributing to economic growth. Growth in disparities in incomes can threaten this consensus." (p. 138).

Despite these positive aspects there are vocal and powerful advocates of reductions in social protection who want to "roll back the state" who see all forms of state intervention as threats to the health of the "free economy". But their arguments need to be clarified and considered carefully and the evidence assessed. Four concerns will be considered in turn.

1. *The cost of social protection, which now constitutes a large proportion of public expenditure. This contributes to the level of taxation, which may damage work incentives.*

   Considered as a part of total public expenditure and a cause of taxation, there is no reason to distinguish social protection from any other expenditure whether the cost of missiles, museums or the monarchy (which is itself a form of hereditary social protection). In general there is no convincing evidence that economies with lower public spending and taxation fare better. One obvious reason is that except in the most corrupt or incompetent states, taxation purchases services, which have also to be considered in assessing the net effects of the government sector. Even where taxation is lower there may be extensive compulsory private levies; Esping-Andersen (1999) compares US and Swedish health expenditures and shows that while the public-private balance differs, the overall extent of payment is quite similar.

2. *The burden of social security contributions is a tax on labour. This concern led the OECD job study to recommend reducing non-wage labour costs, especially in Europe, by reducing taxes on labour (OECD, 1994, p.46).*

High social security contributions, especially those paid by employers, may seem an obvious cause of unemployment. But the "obvious" is often illusory. Denmark and Ireland finance most of their social protection out of general taxation whereas in Belgium, France, Italy, Spain and Netherlands over two-thirds comes from social security taxes. Yet as Nickell and Bell (1996) point out, there is no significant relationship between social security taxes and unemployment. Their analysis concludes that: "The reason is that in the long run, payroll taxes tend to be shifted on to employees" (p.59). Thus, whether taxation is direct or indirect appears to have little link with employment levels.

3. *Pressures of competition with countries with lower social protection will lead to social dumping and a "race to the bottom" in which social protection is cut competitively.*

It is helpful, first, to clarify terms. As Alber and Standing (2000) write: "The term 'social dumping has a pejorative ring about it. … We can distinguish between dumping practices that occur in *markets* without state action, and forms of dumping induced by *government*. The first include such tendencies as the displacement of high-cost producers by low-cost producers, the relocation of firms to low-cost countries, and 'capital flight'…. *Social security dumping* refers to the extent to which transfers and services in social protection schemes are reduced or restructured by shifting the burden of financing" (pp 99-100).

There has not, as yet, been a 'race to the bottom' in social protection. While it is not helpful to adopt the perspective of the economist who, whenever he saw something working in practice, asked whether it could work in principle, why should this be? One reason is that in trade what matters is unit labour costs, which depend far more on pay levels and productivity than on non-wage labour costs. Even if one country alone cut or increased social security taxes and these were reflected in lower or higher prices the effect on trade would depend on whether there was adjustment in the exchange rate. A quite different, non-economic explanation is that each country has groups of workers and beneficiaries who rely on social protection who would restrain any competitive devaluation of social protection.

4. *The behavioural effects of social security benefits in creating labour market rigidities and encouraging unproductive behaviour that is "rewarded" with benefits.*

   There now exists a voluminous literature on the behavioural effects of social security encompassing effects or unemployment, retirement, family formation and fission, childbearing and saving. One thing that is clear is that a "simple dependence hypothesis" - that numbers dependent on a benefit are straightforwardly related to the level of benefit - is not borne out by the evidence (see Piachaud 1997).

   In relation to unemployment, Nickell (1997) argues that passive benefit systems influence unemployment via two mechanisms: "First, they reduce the fear of unemployment and hence directly increase upward pressure on wages from employees (via unions, for example). Second, they reduce the 'effectiveness' of unemployed individuals as potential fillers of vacancies, by allowing them to be more choosy. … The other important feature of the benefit system is the duration of entitlement. Long-term benefits generate long-term unemployment" (p 67). If, however, generous unemployment benefits are accompanied by pressure on the unemployed to take jobs by limiting the duration of benefit or increasing the ability or willingness of the unemployed to take jobs then this does not have serious implications for the level of unemployment (p 72).

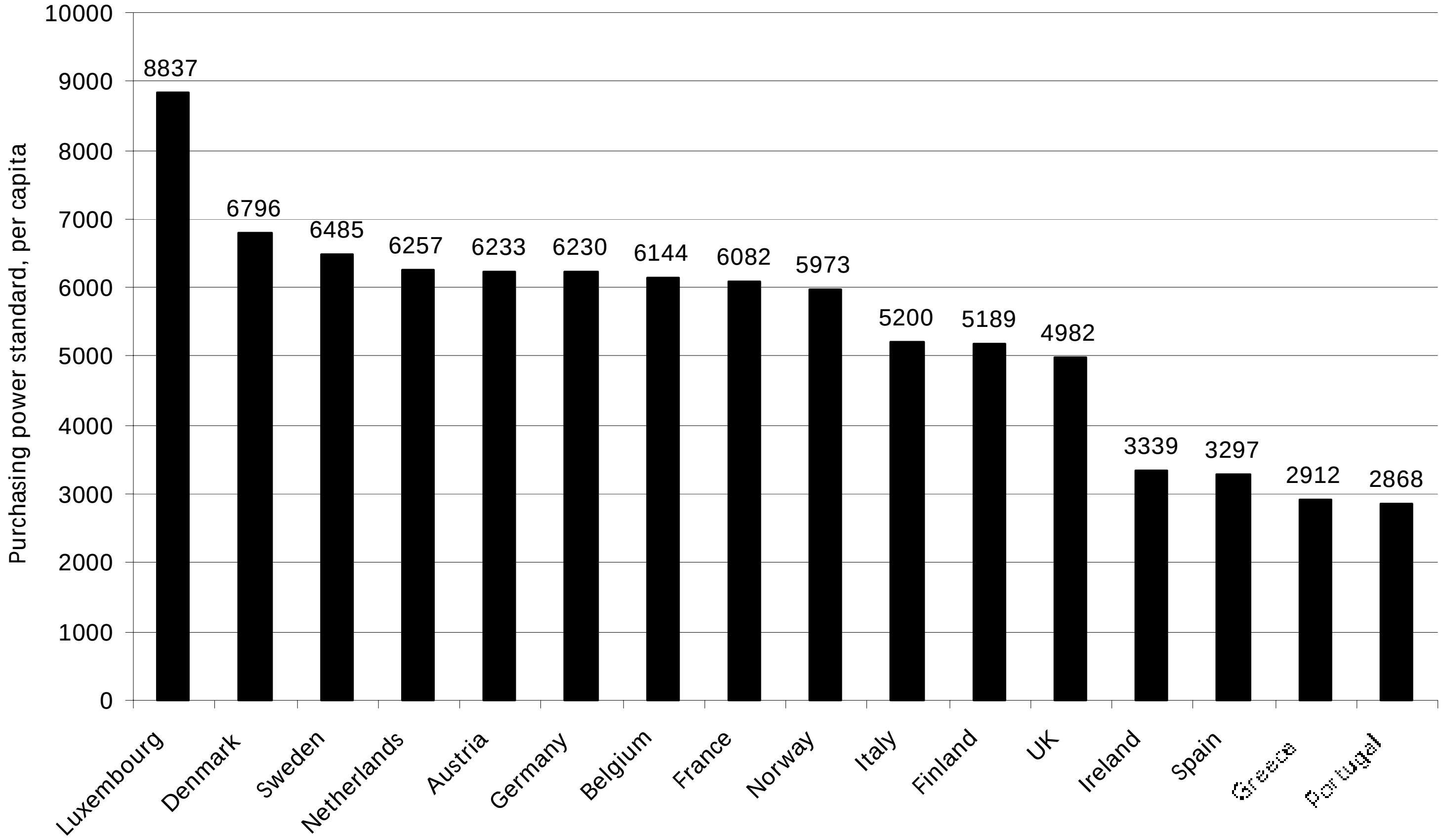
   Reviewing a set of empirical papers comparing the USA with European and Japanese labour markets, Blank (1994) concluded: " these papers give little evidence that labor market flexibility is substantially affected by the presence of social protection programs, nor is there evidence that the speed of labor market adjustment can be enhanced by limiting these programs. … The consistency of this conclusion is particularly striking because it occurs across papers that use very different data sets to investigate the effects of different programs in different countries" (p 15). One reason for this finding is that "countries with more extensive social protection systems find other ways by which adjustment can occur" (p 16); examples are changes in hours, in mobility, and in early retirement. Another reason is that, while many studies focus on individual labour supply, it is hard to conclude from these anything about the net effect on employment of social protection programs. More positively, Blank concludes that virtually all the papers that study specific social protection programs "point to changes in worker well-being provided by these programs…. they do serve as a reminder that these programs have substantial positive social benefits associated with them, benefits too rarely discussed in the economics literature" (p 17).

Social protection in Europe

Within the European Union there is a wide variation in spending on social protection. This is shown in Chart 1, based on a purchasing power standard. Expenditure in 1997 varied from 2868 per head in Portugal to 8837 per head in Luxembourg.

Chart 1: Expenditure on social protection, 1997

Source: Eurostat 'Statistics in focus', Population and Social Conditions, issue 6/2000

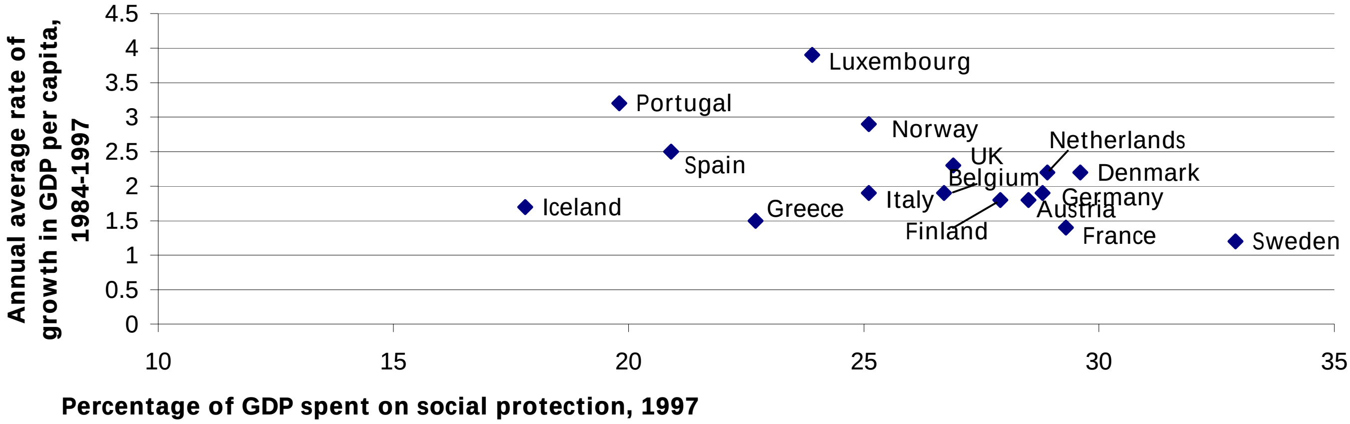


How is social protection related to economic growth?

In order to take account of differences in national prosperity, it is useful to express social protection spending as a proportion of gross domestic product. This is done in Chart 2, which compares levels of social protection and growth rates in 16 European countries; the social protection figures are for 1997 while the growth rates are for GDP per capita and cover the period 1984-1997. The chart shows most countries clustering in the centre, with average growth rates of around 2% a year and social protection spending tending to range between 25-30% of GDP. A linear regression showed that there was no significant correlation between the two; the level of social protection spending was not significantly associated with the growth rate.

Chart 2: Growth and social protection in 16 European countries

Sources: Eurostat 'Statistics in focus', Population and Social Conditions, issue 6/2000 and OECD Historical Statistics 1960-1997, table 3.2.

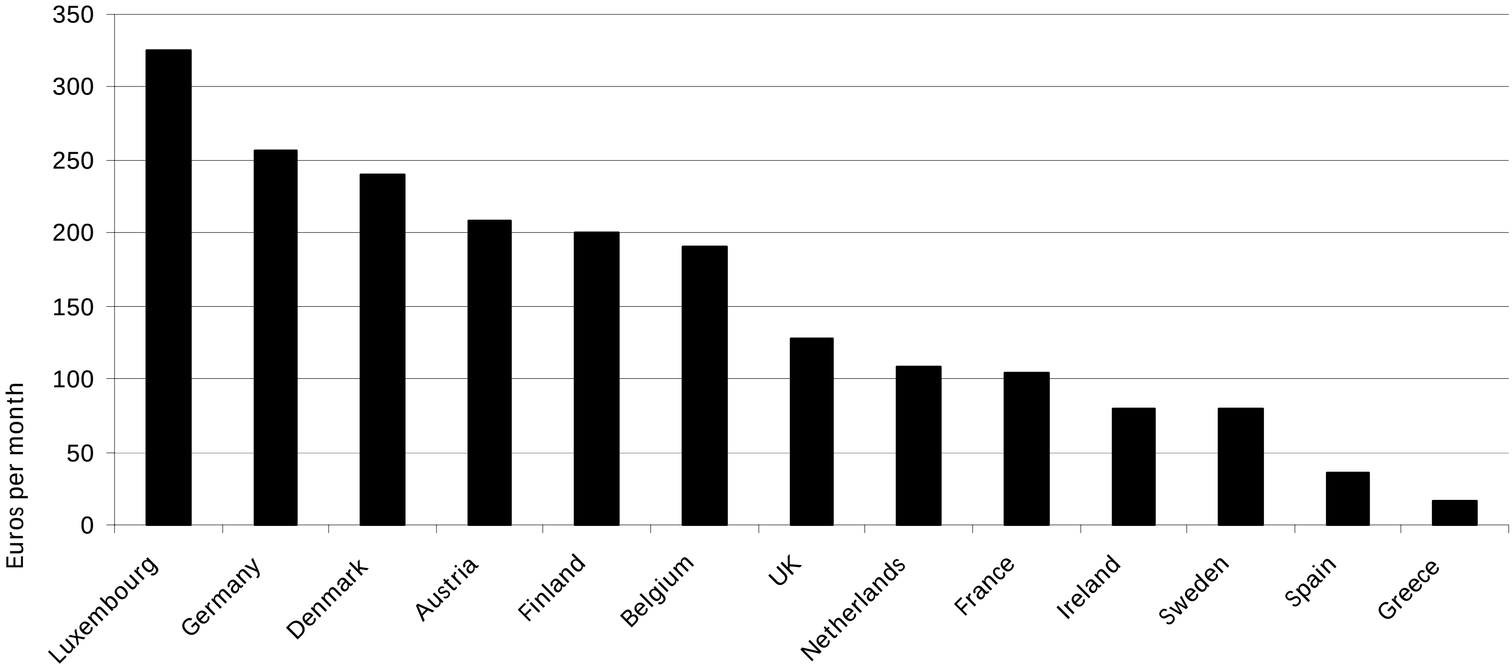


How do benefit rates differ in the EU?

(a) Children

Chart 3 shows the different rates of child benefits in 13 European countries in 1998. The rates shown are for a family with a child aged 4 and one aged 6, in euros per month, and relate to 1998. Although this is only one family type, it gives a general idea of the generosity of the different countries. The most generous countries are Luxembourg, Germany and Denmark, while the least are Greece, Spain and Sweden. The UK is in the middle.

Chart 3: Rate of child benefit, 13 EU countries, 1998
Source: MISSOC (1999) Social Protection in the Member States of the European Union

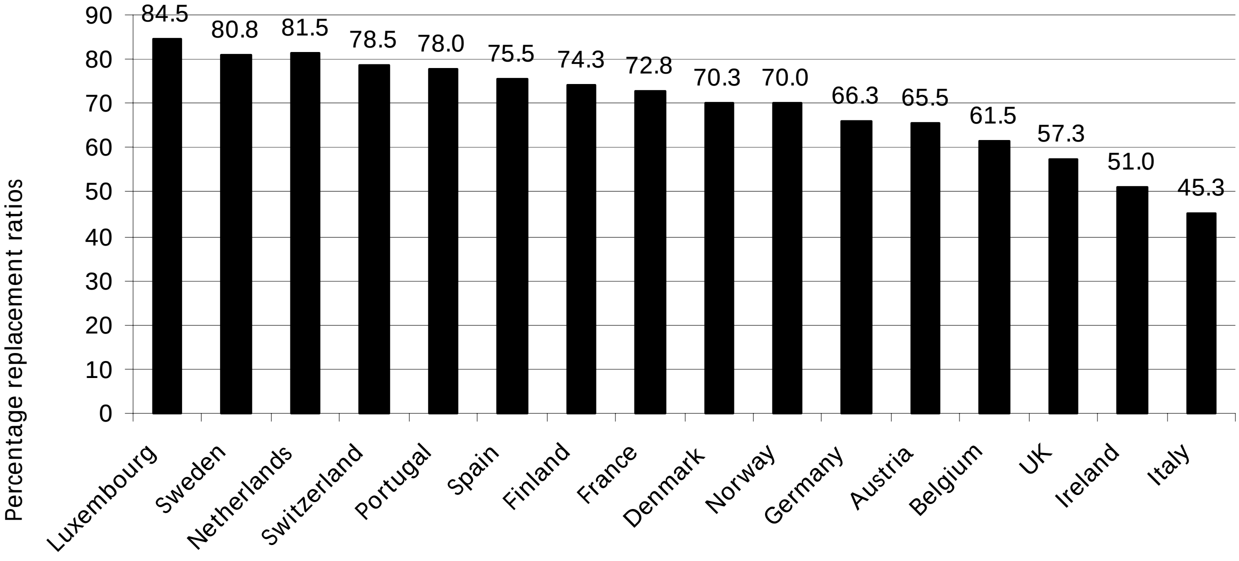


(b) Unemployment Insurance

Chart 4 (overleaf) shows the net replacement ratios for families on unemployment insurance in different European countries. This is the relationship between the net income which families receive when in work and that which they receive when on unemployment insurance benefit (in the UK, contribution-based Jobseeker's Allowance). A figure of 100 would indicate that families received exactly the same amount when out of work as when in work.

The figures in the chart are the average of OECD calculations for four different family types (a single person, a married couple without children, a married couple with 2 children, and a lone parent with 2 children). The chart shows that the Scandinavian countries tend to have the highest replacement ratios, around 80%, while the UK is near the bottom with an average replacement ratio of 57.3%.

Chart 4: Average net replacement ratios for the unemployed receiving unemployment insurance benefits
Source: calculated from OECD (1999) Benefit systems and work incentives

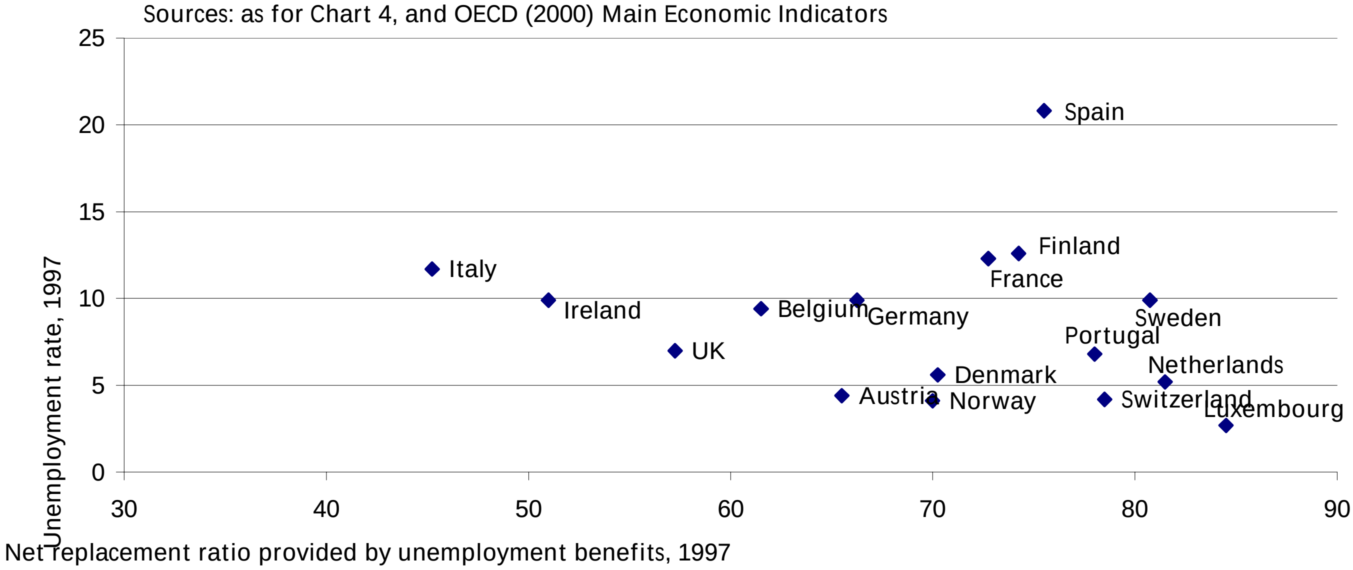


One debate about social protection has received much attention: do generous benefits to the unemployed encourage people to stay unemployed? In Chart 5 we compare the average replacement ratios from Chart 4 with unemployment rates, to see if there is any evidence for this concern. The chart shows no sign that high replacement rates are associated with high levels of unemployment, and this was confirmed by a linear regression.

(c) Social assistance

The incomes received by families on unemployment insurance benefits only tell

Chart 5: Unemployment rates compared with unemployment insurance benefits, 16 European countries
Sources: as for Chart 4, and OECD (2000) Main Economic Indicators

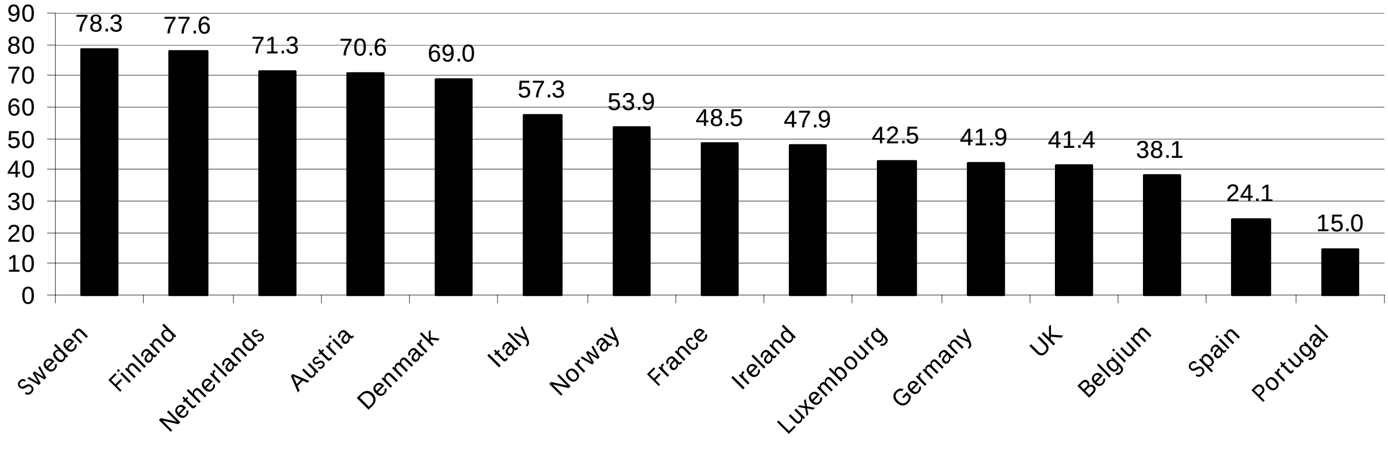


half of the story. In most countries, such benefits are time-limited and once they have been exhausted the claimants must either rely on other resources or, if their income is sufficiently low, will qualify for means-tested social assistance benefit. In the UK contribution-based Jobseeker's Allowance runs out after 6 months and then it may be possible to move on to claim income-related Jobseeker's Allowance instead.

Chart 6 shows the average net replacement ratio provided by social assistance for a number of European countries in 1992, after housing costs. In other words, it shows what proportion social assistance provides of a family's income when it is in work. For example, in the UK the average was 41.4%, so a family on relying Income Support would typically receive roughly 40% of what they would have received had someone in the family been working.

Chart 6: Average net replacement ratios for social assistance

Source: calculated from Eardley T. et al. (1996) Social Assistance in OECD Countries: Synthesis Report, tables 6.8b and 7.6b.



These rates are taken from the study of social assistance schemes by Eardley et al (1996) They took eight different family types and for each country and calculated what such 'model families' would receive in social assistance benefits, taking into account child benefits, taxes and other contributions, housing costs, health costs, and education costs. They then compared this with what the families would earn if the head of the family were in full-time employment and receiving the average male earnings for that country. Clearly some of these assumptions are not altogether realistic - for example it is likely that many families that become dependent on social assistance would not have had a member previously earning the average wage. Yet the figures provide a rough guide to the generosity of the social assistance system of each country. (The OECD used a different method to construct its estimates for unemployment insurance benefits presented above, so the two sets of replacement ratios should not be directly compared.)

Chart 6 shows that the replacement ratios provided by social assistance in the UK are low by comparison with most other European countries. Only Belgium, Spain, and Portugal have lower replacement rates, whereas the 12 other European countries in the comparison have more generous systems. The average of the countries compared is almost 52%, so the UK lags well behind.

Social protection and poverty

Chart 7 compares levels of social spending and poverty rates in 13 European Union countries. It shows a clear correlation between the two: the less a country spends on social protection, the higher its rate of poverty is likely to be. This was confirmed by a linear regression ($R^2 = 0.37$, significant at the 0.05% probability level). Those countries with the lowest rates of poverty (such as Denmark, the Netherlands and Luxembourg) have relatively high spending while those with the highest rates of poverty (such as Greece, Portugal, and Spain) tend to have lower spending.

Chart 7: Social protection and poverty in 13 EU countries

Sources: Eurostat 'Statistics in focus', Population and Social Conditions, issue 6/2000, page 2 and information supplied by Eurostat

The UK ranks about average in terms of spending, at just under 27% of GDP, but has a high poverty rate, 19%, which suggests that spending is not having as favourable an impact on poverty as it does in other countries. Total social security spending can be viewed as the product of the numbers receiving benefits and the levels at which benefits are paid. We have already seen that benefit rates in the UK are low by European standards, which suggests that the problem lies with the high numbers receiving benefits, particularly means-tested benefits. Although the proportion of the population dependent on such benefits has fallen since the peak of the recession in the early 1990s, it is still high by historical standards. If more people could be shifted off benefit, then actual benefit rates could be raised to a more civilised level, the poverty rate would fall, and overall spending would not need to rise. So far the government has been concentrating its efforts on the former task, getting people back to work. This is a laudable policy, but benefit rates are now so far below the poverty line that they need to be improved if groups such as pensioners, many of whom are forced to rely on benefits for their income, are to avoid poverty.

The table below shows how far benefit rates are below the poverty line for four different family types. For a couple with two children, for example, they make up 72% of the poverty line level. People receiving means-tested benefits only qualify because they do not have any major other sources of income. This implies that most people on such benefits by definition have incomes below the poverty line.

Income Support and Poverty Levels 2001-2[1]

Family type (all working-age)	Income Support	Poverty level	Income Support as % of poverty level
Couple with one child aged 6	£129.95	£192.06	67.7%
Couple with two children aged 4, 8	£162.15	£223.81	72.4%
Couple with three children aged 3, 8 11	£194.35	£265.08	73.3%
Lone parent with one child aged 6	£101.15	£120.63	83.9%

Source: D Piachaud and H Sutherland, 'Child Poverty', *New Economy*, 8.2, June 2001.

European reforms

The purpose here is not to describe all recent reforms of social protection. Rather three areas are selected for mention because of contrasting and interesting aspects.

a. Britain

The New Labour Government has, since 1997, given priority in social protection to tackling child poverty. Child Benefit has been increased for all families and Family Credit has been replaced by the greatly extended Working Families Tax Credit. At the same time the Welfare to Work Programme is providing training and work opportunity to bring down unemployment. Overall these changes will reduce child poverty by about one-third (Piachaud and Sutherland, 2000)

The rest of social protection remains largely unchanged although the Conservative plan to cut One Parent Benefit was carried through. National Insurance benefits are being uprated in line with prices whereas means-tested Income Support is, for pensioners, intended to rise in line with earnings. Even with the new State Second Pension and Stakeholder Pension schemes the numbers dependent on the means-tested state minimum will in the long run rise. Resources are being concentrated on the poorest but total social protection spending is a falling proportion of GDP.

In part this results from falling unemployment but in part it reflects the relative decline in the value of National Insurance benefits.

b. Scandinavia

Social protection in Scandinavia is a citizen's right, benefits are high by international standards and coverage is universal. Social spending as a proportion of GDP is well above the EU average and poverty is much lower.

In the 1990s reforms were made to contain costs and cuts were made; incentives to stay in or find employment were increased. But, despite the changes, Scandinavian social protection is still much more extensive and generous than in Britain. As Kuhnle (2000) wrote: "the Nordic welfare states stood the test" and showed that "an advanced universalistic welfare state is not a handicap when a sudden, unexpected economic crisis occurs." With faster growth and falling unemployment in the second half of the 1990s, the principles of universalism and high replacement ratios are not seriously questioned (Ferrera et al., 1999).

c. The Netherlands

Social protection in the Netherlands was, for most of the post-war period, a collectivist, solidaristic, social insurance system with high rates of benefit and spending. Since the 1980s cuts in coverage, benefits levels and duration and partial privatisation have marked a shift from collective to individual responsibility (van Oorschot, 1998).

The Dutch pioneered 'flexicurity' with rights for temporary workers strengthened and pension and social security benefits extended to all part-time and temporary employees (Visser and Hemerijck, 1997). Thus for some social protection has been cut back but for others, notably marginal workers, it has been extended.

The future of social protection

Many economists separate issues of efficiency and equity. Efficiency is, they argue, served by limiting social provisions and equity can be achieved by some, very limited, income redistribution. Yet, as explained earlier, social protection may assist the working of a dynamic economy. The evidence in the previous sections showed that the notion that "too much" equity damaged economic efficiency was, on recent European experience, simply not borne out. This is a negative finding but an important one in that it shows that British social protection could be enhanced up to the better European levels, thereby reducing poverty and inequality without any jeopardy to economic performance.

For the future, the case for improving social protection is not merely that it can be done. There are important changes that affect the need for, and form of, social protection.

Family

The family was and probably still remains the major source of social protection in all societies. But the stable family structure assumed by Beveridge is increasingly eroded. There is much greater variation in family patterns. For some this is welcome in that there is more choice of "life-style"; others see increasing breakdown of relationships as threatening the security and development of children. Whatever the ethical issues, the changes are a fact.

For social protection in Britain the family remains the basic unit of account. Indeed with the extension of means testing with the Working Families Tax Credit and the pensioners' Minimum Income Guarantee the family unit on which benefit entitlement in assessed is becoming increasingly important.

The promotion and subsidy of low-paid work through the Working Families Tax Credit is a key component of the strategy to eliminate child poverty within a generation. This involves a recognition that many parents cannot rely solely on universal benefits nor are they able to take full-time employment or obtain a job that pays above the poverty level. This family-focused subsidy in Britain is in contrast to the measures in many countries to ensure that all individuals have adequate social protection in their own right. As described above, in many European countries this depends on extending social insurance to those who are part-time or very low paid and to those with interrupted working lives due to care of children or of disabled relatives. Britain has tended to move in the opposite direction leaving those with little or no social insurance to depend on the means-tested Income Support Scheme. For those who do or will depend on Income Support there is a little incentive to earn or save. More fundamentally the family-based means test undermines individual entitlements and serves to encourage family break-up. To prevent this another adjustment to changes in the family has been the quest of government to reinforce the responsibility of absent parents through the Child Support Agency so that lone-parent mothers should not lose so much, nor fathers gain so much because of separation.

Changing employment patterns

Where employment is changing towards short-term contracts, individually negotiated pay and conditions, portfolio working and reduced occupational welfare the result is increased insecurity and more dependence on social protection. If employment is no longer life-long, then relying on occupational welfare for protection when sick or old is less and less possible.

Social protection in many countries is adapting to changing work patterns. In Britain only minor adaptations have been made and then largely as a result of adverse rulings of the European Court.

Atkinson (2000) sees a key role for social protection as encouraging risk-taking of desirable forms such as people investing in skills, setting up their own business or moving to a new job:

"Suppose that an individual is considering the choice between a certain, and known, situation, such as continuing with his or her current job, and an uncertain prospect, such as a new job where there is both a risk about whether or not it will work out …. It is clear that the existence of unemployment benefit, payable in the event of failure, reduces the downside risk, and hence increases the probability that the person takes the risk." (p14)

State-run social protection may allow the labour market to operate more smoothly and have a positive impact on restructuring.

What is clear in relation to unemployment is that social protection in most countries is increasingly conditional on meeting training and job-seeking requirements. In many countries this has accompanied the retention of high levels of benefit. In Britain nothing has been done to redress the Conservative Government's repeated assaults on the unemployed so that benefits for the unemployed remain far below the government's own poverty level.

Globalisation

Globalisation may present challenges to social protection because of its impact on production and employment and because of pressure to cut standards to compete with competitors with lower standards of social protection. There may be a further challenge if globalisation is perceived, rightly or wrongly, to undermine the ability of national governments independently to improve social protection. If globalisation persuades governments that efficiency must take priority then equity may get little attention, however important it may be for efficiency in the long run. It is therefore important to consider how globalisation may affect social protection.

First, globalisation may result in intensified competition in which differences in production costs are exposed. What matters are unit labour costs, not social protection costs although these are part of total labour costs. If a government reduced publicly provided social protection but responsibility and cost were shifted onto employers then overall labour costs would not fall. Or if responsibility were shifted onto workers and they obtained compensation in the form of higher wages then, again, overall labour costs would not fall. Thus reduced social protection does not necessarily improve competitiveness. Further, if, as discussed above, reduced social protection increased resistance to change this could in the long run reduce competitiveness.

Second, low-skilled labour may be particularly affected by competition with countries with low labour costs; this is almost certainly one reason for the growth in inequality of earnings. While there is controversy about the extent of this effect, if it occurs it presents a new challenge for social protection to subsidise low paid jobs to prevent "working poverty".

Third, globalisation may result in global relocation of production leading to job losses in some industries and gains in others. As the OECD (1999) state; "If job losses led to destitution, it would be unsurprising if global competition was resisted ……Thus, one effect of globalisation would be to increase the demand for social protection" (p137). In effect governments may face a choice between maintaining and improving social protection or facing growing pressure to introduce trade protection.

As well as affecting the need for social protection, globalisation may affect the ability of governments to raise the taxation necessary to finance it. Trans-national corporations arrange their tax affairs to minimise taxation of income and profits. This has led many governments to increase the burden of taxes on labour since labour is less "mobile" than profits. As mentioned above, the level of social security contributions has no clear relationship with economic performance. But if governments believe their taxes on labour are significantly above those of other countries, they may try to reduce them – thereby affecting the possible level of social protection.

Overall, then, the effects of globalisation on social protection are uncertain and hard to predict. What is clear is that the effects are not straightforwardly to cause reductions in social protection. Indeed, considering the increased insecurity that globalisation seems likely to engender, the balance of political pressure will most probably shift towards improving social protection.

The cost of catching up

British social protection is not the worst in Europe but it is a long way behind the best. What the evidence presented above shows is that Britain could catch up, perhaps not in one sudden lurch forward but certainly over a period of years, without jeopardising prudence in the management of its economic affairs or threatening economic growth. Improved social protection would serve to reduce the poverty that afflicts children, the unemployed, and many pensioners.

What would be the cost of catching up? Here we concentrate on two groups – children and people depending on social assistance. The extent of the deficit and the gross cost of making it up are shown in the table below.

	Britain's spending as a proportion of the EU mean	Cost of catching up with the EU mean
Child benefits[2]	84%	£1.34 bn
Social assistance[3]	79%	£5.70 bn

These are large figures and the cost of state pensions catching up would be higher still. But they must be kept in perspective. To catch up with the EU average with respect to both children and the unemployed would cost £7 bn or less than one percent of gross domestic product; we would still spend less than many other countries on social protection. But we would have taken a substantial step towards a fairer society.

Conclusion

Globalisation presents many challenges to welfare states. Yet we have seen that it requires us to sustain our levels of social protection, not reduce them. There is no evidence that increasing social provision would harm economic efficiency, and much to suggest that it would have beneficial effects on poverty and social harmony. The experience of some of our European neighbours suggests that the twin objectives of high economic growth and low poverty rates can be achieved simultaneously. Britain would do well to follow their example.

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Notes

1 Income Support level is mean of rates applying April – September 2001 and October 2001 – March 2002. Poverty level for 2001 – 2002 is based on 50% mean AHC income for 1998- 99 (Department of Social Security 2000b) adjusted for actual and forecast rise in Real Household Disposable Income and Retail Price Index set out in Pre-Budget Report, 2000 and Budget Report, 2001 (HM Treasury, 2000 and 2001).

2 The sum required to bring the UK up to the EU average for child benefit was calculated as follows. EU average monthly child benefit for a family with 2 children aged 4 and 6 was calculated, using data from MISSOC (1999). The European average excludes Italy and Portugal, for which child benefit could not be calculated from the data provided. UK child benefit for this family type was compared with EU average child benefit. The deficit was divided by 2, to arrive at an approximate average deficit per child. The deficit per child was multiplied by the number of children receiving child benefit (source: DSS Social Security Statistics 1999) and by 12, to arrive at the annual cost of increasing child benefit rates to the EU average. Finally this was converted from Euros into sterling. This calculation assumes that families on means-tested benefits gain the increase in child benefit rather than having it means-tested away.

3 The amount needed to bring the UK up to the EU average in social assistance rates was calculated as follows. Social assistance replacement ratios for 8 family types for OECD countries were taken from the study of social assistance by Eardley et al. (1996). Of these countries, just the EU ones were selected (excluding Greece, which barely has a social assistance system). The EU average replacement ratio for each family type was calculated. Then these ratios were applied to the figures for net in-work incomes in order to calculate in pounds what each family type would need to reach this EU social assistance level. These amounts were then compared with the amount each family type would actually receive in UK Income Support to see how large the deficit was, and the average deficit was taken across all the family types. Since the figures in the Eardley study relate to 1992, this average deficit was uprated according to the Rossi price index (which excludes housing) to arrive at the figure as it would be in today's prices. Finally, the average deficit was multiplied by the number of people receiving Income Support and income-related Jobseeker's Allowance (from Social Security Statistics) and by 12 to reach an annual figure for the sum necessary to bring the UK up to the EU average.

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