

A Generation of Change, A Lifetime of Difference?

Model Lifetime analysis of changes in the British Welfare State since 1979

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Abstract

This paper introduces research that will be published in a book, 'A Generation of Change, A Lifetime of Difference? British social policy since 1979', in September 2009. The research employs a series of lifetime simulations to examine the changes in taxation and social security provision since 1979 in Britain, using the Lifetime Opportunities and Incentives Simulation (LOIS) to profile hypothetical individuals who live their whole lives under the rules in place at three points in time: 1979, 1997 and 2008. These three years are taken to represent the cumulative changes in policy that have been taken by three differing political approaches to social policy. 1979 represents the culmination of 'Old Labour' – a left social democratic approach; 1997 represents the culmination of 18 years of right-wing Conservative governments under the Prime Ministers, Margaret Thatcher and John Major and 2008 represents the culmination of 11 years of 'New Labour' under Tony Blair and Gordon Brown. Three hypothetical families are used to produce lifetime profiles and each is based on contemporary levels of earnings for each year: the Meades are median earners, The Moores are twice median earners and the Lowes earn 50 percent of median earnings. The paper outlines the methodology of 'model lifetime' and demonstrates the differences in inputs and outputs from taxes and benefits for each model family over their hypothetical lifetime for both comparison years and shows outcomes for poverty.

Introduction

2009 marks the 30th anniversary of the 1979 general election that brought Margaret Thatcher to power and began a sustained period of overhaul of the British welfare state: a withdrawal from universalism and concerns for equality that marked the high-tide of 1970s social policy under the Wilson and Callaghan governments. The historical changes and the underlying political and ideological differences that characterise the past 30 years have dominated social policy discussion in Britain. This paper focuses on examining the *design* rather than the rhetoric of British social policy and how this had changed using consistent measures of outcomes. An analysis that covered the whole of social policy is a huge and daunting and we focus primarily on the tax and benefit system

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and the changing impact on incomes. We return to Beveridge's concept of provision from 'the cradle to the grave' and employ a lifetime profile to capture a large range of programmes of social security and other cash transfers as well as income tax and other forms of direct taxation.

The majority of this paper discusses the methodology and results of a fairly complex analysis and it is worth beginning the paper for a non-British readership with an overview of what changed and when.

The political change that occurred in 1979 was a dramatic one. While the earlier economic crisis in the mid 1970s had led the Old Labour government to abandon a Keynesian commitment to full employment, the monetarist and free-market approach of the Thatcher governments and the consequent willingness to have major restructuring of the economy accompanied by large levels of unemployment were unprecedented since the War. Widespread privatisation, large scale retrenchment of Union negotiating rights and power and deregulation of banking, housing and other aspects of the economy changed the underlying economic assumptions of the British welfare state. Only the headlines of changes to social policy can be outlined in the limited space available in this paper but the period leading up to Thatcher in the 1970s can be seen as a high point in the development of the British Welfare State in terms of universal entitlement and redistribution. The Old Labour governments of Wilson and Callaghan (1974-1979) moved away from the 'flat rate' assumptions of Beveridge's design and introduced earnings-related state pensions, including invalidity pensions, and universal programmes of child benefit and disability benefits in order to make social assistance provision shrink to a minimal safety net. Old Labour was openly redistributive and income tax rates were high at the margins for those with high incomes – an 85 percent rate at the highest point, subsidies to social housing ensured low rents, and at a time of high inflation long-term benefits such as pensions were committed to be up-rated in line with earnings to keep relative values intact.

The 18 years of Conservative rule saw such a 'tax and spend' approach as anathema. Low taxation and a smaller role for government went hand in hand and reducing levels of income taxation were a high priority. The higher rates of income tax were slashed immediately in the 1979 budget. Over the subsequent 18 year period tax income tax rates reduced significantly but other forms of more regressive taxation grew: social insurance contributions were raised, local government based property taxes grew and there was a deliberate move to indirect taxation through a large increase in VAT. At the same time the generosity of transfers was seen as a problem of individual level work incentives as well as a macro-economic spending problem. All earnings-related elements of sickness and unemployment benefits were ended in the early 1980s along with any commitment to up-rate any form of benefit with earnings. Means-tested social assistance was prioritised as the best targeted and most efficient form of transfer but cut back to low levels of generosity, particularly for the unemployed while means-tested help with rental costs was made less generous even as rents were encouraged to move towards market levels. On the other hand, means-tested benefits to support low paid employment to families with children were made more generous to promote job entry and universal disability benefits were broadened in scope to help those with lower level needs from disability. Privatisation, of sickness and maternity benefits, paid by employers, and of second tier pensions was pursued and private pensions were miss-sold to many who would be better off remaining in state or employer superannuation schemes. The high point of Thatcherism was 1990 but the most radical elements of policy proved to be unsustainable and the introduction of the 'poll

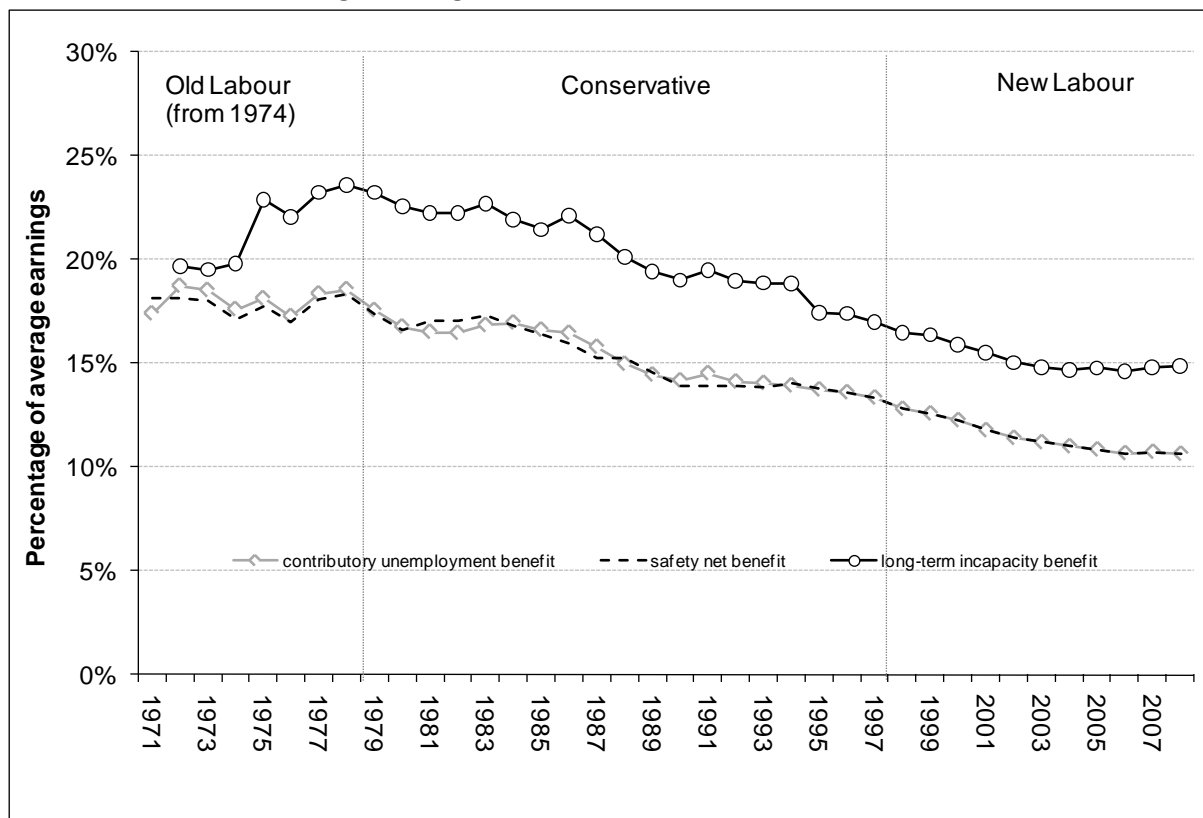
tax' in 1989 led to Thatcher's resignation and replacement with Major, who pursued a slightly softer agenda – universal child benefits were raised to recover some of their lost purchasing power.

The arrival of the New Labour government of Tony Blair in 1997 heralded a change of approach from *both* Old Labour and Thatcherism. 'No return to tax and spend' is Brown's phrase that epitomised the approach that not only maintained the low tax approach of Thatcherism but developed it further to take headline income tax rates further down to 20 percent in the 2007 Budget. However, the displacement of the tax burden into more regressive forms continued and both national insurance and local government taxes grew. The difference between New Labour and the Conservatives can be seen in the introduction of a national minimum wage and in a greater investment in transfer programmes that compensate in part for higher taxation but also took forward historic promises made in 1999 to end both child and pensioner poverty. Transfers for children were significantly increased for both out of work and in-work families and refundable tax credits were the mechanism chosen to do so. Childcare provision was expanded and funded by a mixture of supply subsidies targeted on the poorest areas of the country and tax-credits to help parents pay user-fees. Social assistance levels for pensioners was dramatically increased and pension system revised twice to improve performance of state and private pensions for lower income workers. Out of work transfers for unemployed and economically inactive people were made increasingly conditional on employment and left to fall further and further behind wages and relative income standards.

This brief summary of policy change can be further supplemented for interested readers by more detailed histories (Glennerster 2000, Timmins 2001, Evans and Williams 2009). However the effects of such changes on the overall progressivity of taxes and benefits were considerable and this retreat from progressive fiscal policy contributed significantly to increasing income inequality alongside higher earnings dispersion and changes in household structures and ageing. First, benefit levels were mostly left to fall in relative terms as shown in Figure 1. This was both a continuation of policy from 1979, of up-rating benefits with prices only when referring to unemployment, sickness and most social assistance, and of an overturn of policy for long-term benefits such as basic state pension and incapacity benefits.

It is also worthwhile outlining the aggregate effects of changes in the incidence of taxes and benefits across the whole populations for the three years that will form our comparisons. Official British Government analysis of the incidence of taxes and benefits are only available up to 2006 at the time of writing but Figure 1 gives the overall changes in the incidence of taxes and transfers across the income distribution for 1979, 1997 and 2006. Figure 2 gives three profiles, of transfers in a), of taxation in b) and of the combined effects of both tax and transfers in c) across income deciles. Clearly, transfers have become less generous to the poorest deciles and this is partly a reflection of population composition change: pensioners were the majority of the poorest decile in 1979 but over time as new cohorts of pensioners with better pension entitlements have retired they have become less concentrated in the poorest deciles and replaced by families with children and other working age adults. The reduction in progressivity of transfers for the poorest is also a reflection of the

Figure 1
Values of Benefits to Average Earnings 1971-2008



Source DWP 2008

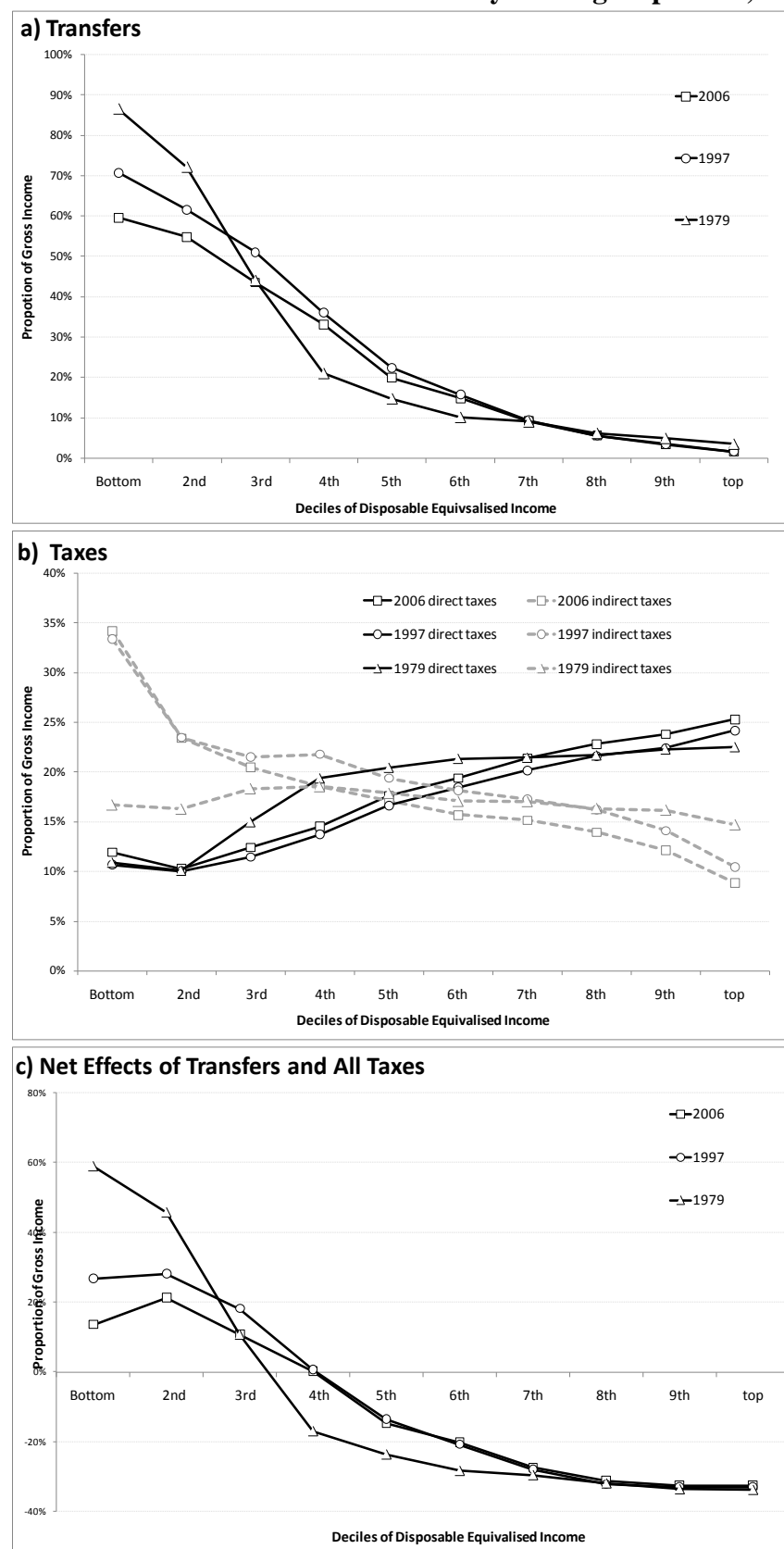
falling relative value of transfers that have maintained value only in purchasing power and thus fallen against real earnings and relative measures of poverty. Transfers have also moved to represent higher proportions of income in the 3rd to 5th decile groups – reflecting both compositional change as pensioners have increasingly moved into this sector of the income distribution and also changes in targeting towards families with children.

The changing incidence of taxes shown in Figure 1(b) is even more dramatic but mainly so through the incidence of indirect taxes. Direct taxes appear to be lower in the middle of the distribution in 1997 and 2006 than they were in 1979 but indirect taxation (shown in the grey lines) has shifted significantly in a regressive way with far higher incidence in 1997 and 2008 in the bottom two deciles and less in the upper deciles. Putting taxation and transfers together to show the fiscal ‘net effect’ on gross income across the income distribution, Figure 1(c) clearly shows that there is little difference in the higher deciles, the 7th to top decile, between all three years’ systems but that the middle of the distribution have been gainers since 1979 and the bottom deciles have been big losers.

These outcomes are dramatic illustration of the overall changes that have arisen from the combination of both fiscal policy change and population and income changes over time. Unpicking and isolating the effects of changes in policy design is a difficult task and the approach we take in this paper is to hold policy still in 1979, 1997 and 2008 and simulate whole lifetimes lived under the policy rules for a set of hypothetical individuals and their families. How do the changes shown in Figure 2 play out in such simulations?

Figure 2

Tax and benefit incidence in Britain by decile groups 1979, 1997 and 2006



Source: ONS 1981, Stuttard (1998) and Jones (2008) adapted by the author to ensure consistency.

Model Lifetime Simulation

Figure 2 showed the changing incidence of taxes and benefits across the whole population. Our approach is different in that we want only to isolate issue of changes in the design of programmes rather than in underlying population composition and economic circumstances. Lifetime hypothetical tax-benefit models to produce profiles for *illustrative* individuals in 1979, 1997 and 2008 to calculate their entitlement to benefits and liabilities for tax on the rules for benefits and taxation in those three years. Our simulations are based on a purpose built model, the Lifetime Opportunities and Incentives Simulation (LOIS) developed specifically for this research.

Lifetime hypothetical models have been a small but growing part of social policy analysis since the early 1990s. Their beginnings lie in profiling pension provision (Evans and Falkingham, 1997; Evans et al, 1999; Johnson, 1999, Rake et al, 2000) before they were expanded to incorporate wider elements of lifetime incomes in profiling women's experience of earnings and pension penalties (Joshi et al, 1996, and Rake, 2000). Evans and Eyre (2004) widened the approach to look at all aspects of the 2003/04 tax benefit system in the form of 'model lifetimes' and Evans and Scarborough (2006) then moved on to analyse specific periods of the lifetime to assess the prospects for child poverty under 'model childhoods'.

Hypothetical models suffer from not being able to be representative of the population – we can show how individuals and families fare but not how many there are who face such circumstances. Using only individuals (and hypothetical ones at that) we are not able to show the aggregate costs and consequences of policy in a way that micro-simulation approaches can. This means that we cannot set out the total costs of the 1979 policy system if it operated in 1997 or 2008 and vice versa, nor change such cost profiles to match the underlying changes in life-expectancy, in female participation in employment, in the widening inequality of earnings or other significant macro-changes that have occurred since 1979. However, there are real strengths to our approach. First, we can show a range of provision that is beyond cross-sectional micro-simulation that focuses most on taxation and categorical and income-related transfers. Our approach allows us to look at contributory benefits – pensions in particular- alongside these. Second, we are able to put in a set of assumptions into our lifetime profiles that can most clearly identify and illustrate policy differences over time. Third, we can iterate our simulated lifetimes to take account of a range of assumptions that can help interpretation of policy change, for instance on the issues of inflation, behavioural differences over time and in mature versions of policy as well as the contemporary rules in place at points of time.

Our illustrative hypothetical individuals are based on earnings at different points in the overall earnings distribution and we give each simulation a name to clearly identify the earnings level assumed.

- The **Lowes**, earn 50 percent of median earnings and are low earners
- The **Meades** are median earners
- The **Moores** earn 200 percent of median earnings and are high earners

The main underlying assumption when using a hypothetical lifetime is that time stands still and people live their whole lives in a single year's rules and thus such simulations are primarily a

heuristic device to illustrate and compare sets of policy rules rather than an true empirical illustration

What is a model lifetime when compressed into a single year of policy? The advantage of hindsight allows us to look back at 1979 and see that the rules in place in that year affected different age cohorts, some born listening to news of the First World War and others to The Clash. In policy terms, some had paid into the Graduated Pension scheme in the 1960s while others were just beginning to pay into State Earnings Related Pension (SERPS), in 1979 for instance. In these terms the rules that exist on 1979 are not a coherent policy system at all but a conglomeration of a variety of policy legacies and commitments. How can one year's policy entitlement be separated from the inherent legacy of previous entitlements that coexist? Our approach is to capture what is in policy makers' minds, the overall design of the range of entitlements that, if time were collapsed, would best illustrate their design of social policy. This approach first means that we ignore transitional rules that allow old policy entitlements to be protected as new ones are implemented. The rules for 1979 and 2008 thus assume full implementation of most programmes. This is our first assumption: *'full implementation'*. This approach also means that the underlying cohorts in the population are flattened into a cross-sectional view when it comes to their behaviour. The retirement behaviour in 1979 is not that of the 30 year old who would retire in 35 years time in the 'real time' of 2014, but is that observed in 1979 as contemporary for a 65 year old. We can call this second assumption *'cross-section not cohorts'*.

However, these two assumptions together, full implementation across a flattened cross-sectional view of lifetime behaviour, mean that we introduce some problems of interpretation of an potential bias in capturing policy design and thus that some iteration is needed to make comparisons more complete and useful.

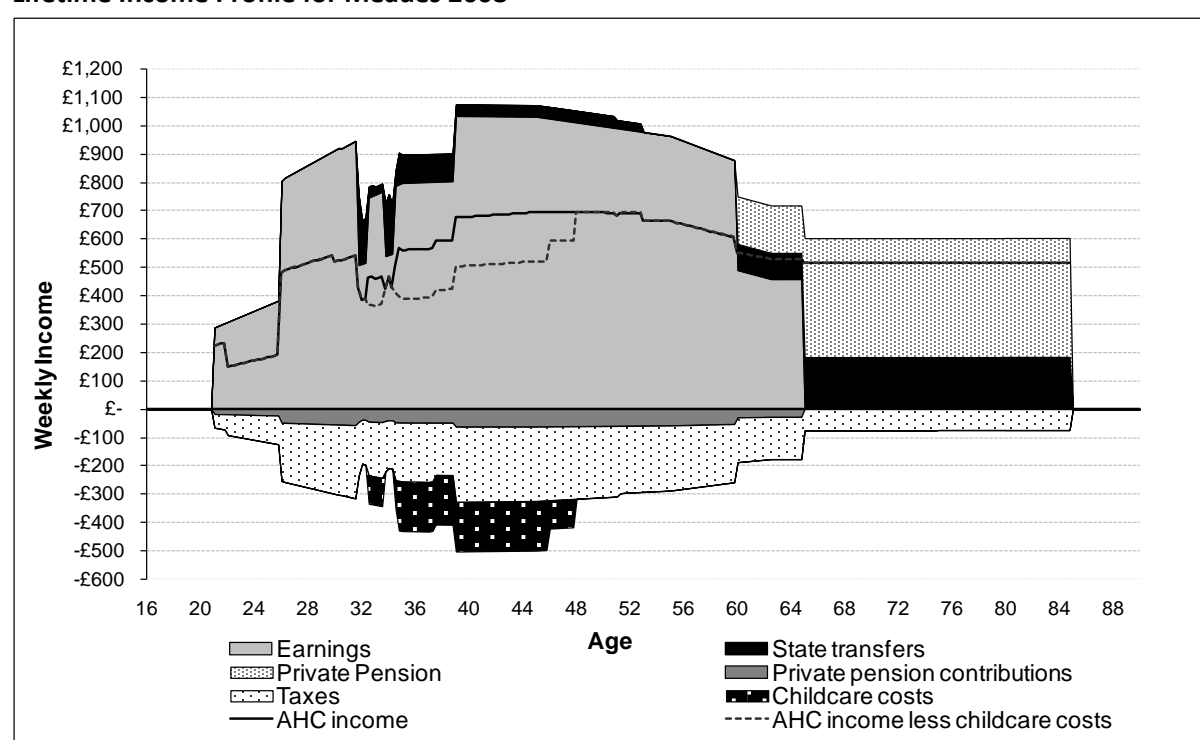
First, if we compare people's lives in 1979 and 2008 we see very different sets of behaviour. This is a problem because different behaviour can lead to different outcomes from social policy. For instance, women's participation in the labour market has grown hugely and in parallel the use of childcare and part-time work has increased. We adopt a two-stage approach by first assuming no behavioural change to establish a 'gross policy difference' and then secondly assuming behavioural change to establish a policy difference net of behavioural differences.

Second, assumptions for *'policy maturation'* have to be made to change contemporary rules to reflect those anticipated and planned for and this is especially true for pensions where changes to pension age to equalise this between men and women were planned in 1997 and where extending pension age to 68 are in place in 2008. 2008 policy maturity also introduces new pension provision in the form of subsidised savings into third tier private pensions, or 'Personal Accounts'. Policy maturity in 1979 only has to adapt taxation assumptions to pay for more generous state earnings-related secondary pensions.

Third, there is the problem of inflation. Under our basic frozen time assumption we also freeze inflation. But to assess the full extent of the differences between 1979 and 2008 systems we must additionally assess the differences in assumptions that policy makers make about up-rating taxes and benefits (see Sutherland et al 2008). We therefore produce one further set of versions of our policy systems that include the effects of inflation and up-rating policies of taxes and benefits.

This methodology means that there are a large range of different iterations of lifetime profiles for each of the three years and for each of our three model lifetime profile. Reporting on all of these is beyond this paper and we provide an overview of headline results and encourage readers to refer to the book (Evans and Williams 2009) for greater detail and context. In this paper we employ a reduced and simplified set of iterations that firstly illustrate the methodology and provide results on the simplest and most straightforward of the simulations using constant behaviour and no inflation on immature policy systems. We then show illustrative poverty models that additionally take inflation and up-rating into account. In truth, behaviour and maturation make smaller differences in lifetime results than inflation and thus we are able to focus on the sets of results that are of most interest.

Figure 3
Lifetime Income Profile for Meades 2008



Source: author's calculations from LOIS

Before we turn to the results for each of the model lifetime profiles it is worth giving an illustration of what a model lifetime simulation provides as an income profile. Figure 3 shows the results for the Meades (median earners) in 2008 with no inflation. The shape of the earnings area gives an indication of the underlying life events: the profile starts at 21 after university has finished and at age 26 they become a couple and at 32 have their first and at 34 their second child. Ms Meade retires earlier at age 60 and Mr Meade continues to work until 65. Their pensions are based on contributing to an employer run defined benefits pension scheme that provides a proportion of final earnings as pension. Additionally Figure 3 shows a curve to earnings that arises from using a lifetime earnings weighting to profile returns to skills and experience over the working life. We use British conventions in income definitions by adopting a summary measure of income 'after housing costs' that is gross income minus taxes and pension contributions and rent or interest on loans to purchase a house, and the latter is presumed for the Meades, based on contemporary average property

purchase prices. We employ a number of assumptions that purely keep profiles simple – Mr and Ms Meade die simultaneously and are of exactly the same age, for instance.

We now turn to the lifetime simulations and the comparison of 1979, 1997 to 2008 for our hypothetical median, half median and twice median earners. Detail of the underlying British systems of taxes and benefits are kept to a minimum in order to concentrate on illustrating the results of the comparison of systems to a non-British readership. However, there is one crucial point to emphasise at this point, the calculations used in simulations are based on income and direct taxation only and can make no estimation of consumption levels and thus of indirect taxation, which we know from Figure 2 was a crucial difference in overall tax incidence between 1979 and latter years.

The Meades

In common with the other results presented in later sections of this paper, the series of events and earnings profile that form the Meades' lifetime are a simple but consensual set of parameters against which to measure policy performance. Appendix 1 outlines the parameters of the Meades' lifetime for consistent use across all three years on a 2008 set of behaviours. One important consideration to make and to clarify at this point is that the *lifetime is a joint one* – there are periods when the lifetime only contains a single person, Ms M, but our results reflect the whole lifetime based on Ms M.

Table 1 shows a set of cumulative lifetime totals for taxes and benefits. Holding lifetime events and behaviour constant there is little difference in overall impact of taxation between 1979 and 2008 at 2% either side of 30% of gross lifetime earnings across all years. However, taxation here refers to income tax, national insurance contributions (NICs) and local authority levied property taxes (rates in 1979 and council tax in 2008). No account is made of the rise in VAT or other consumption taxes such as excise duties over the period but we do estimate the effect of student loans and treat these as analogous as a tax.

Table 1

The Meades lifetime in 1979, 1997 and 2008

Using constant 2008 behaviour and median earnings at contemporary levels.

(% of lifetime earnings)	1979 System	1997 System	2008 System
Direct taxation			
All direct taxes (incl. student loan repayments)	31.9	28.0	29.8
(excl. student loan repayments)	31.9	27.4	28.5
State transfers			
All	17.5	13.8	15.5
maternity/dependent children	2.2	1.9	3.8
retirement	15.3	12.0	11.8
Net effects of direct taxes and transfers			
	-14.4	-14.2	-14.3

Source: Authors' calculations using LOIS

Notes: No lifetime inflation

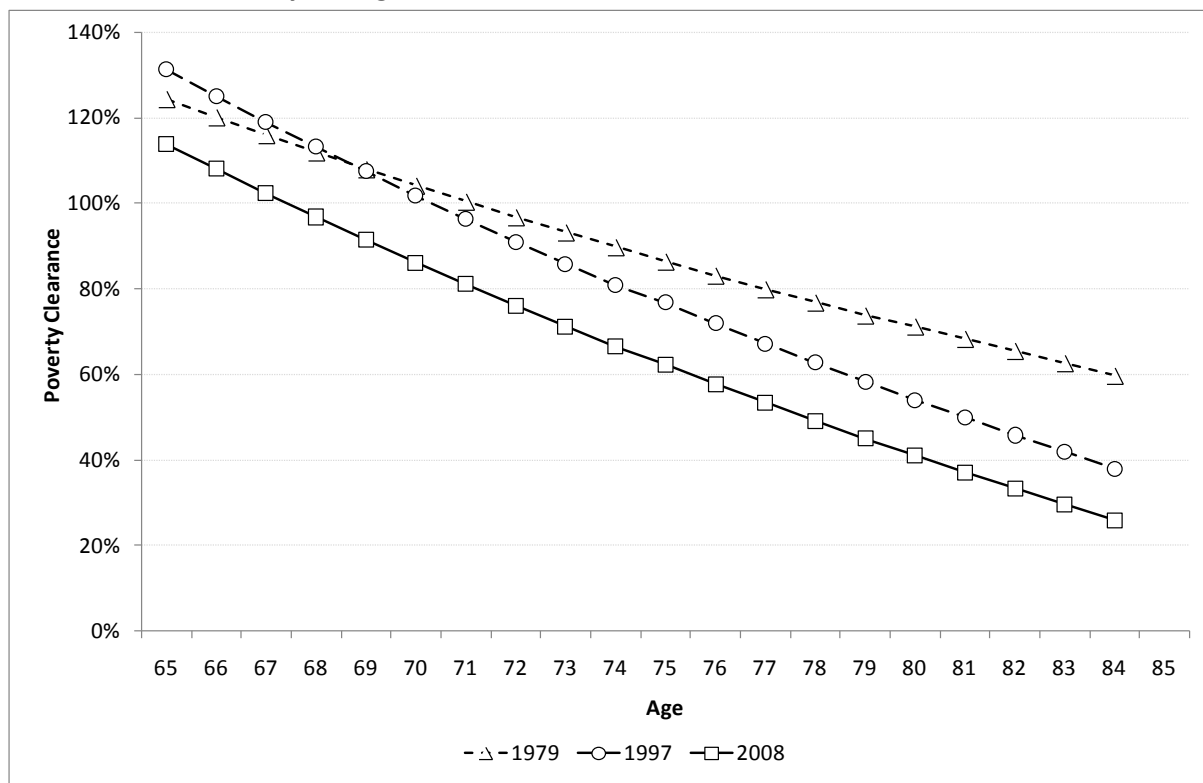
In terms of transfers, the 1979 system is most generous, 17.5% of lifetime earnings, compared with 13.8% in 1997 and 15.5% in 2008. However, the lifetime distribution of these transfers have changed with state pensions falling from 15% in 1979 to roughly 12% in 1997 and 2008 but with transfers for maternity and childhood highest in 2008 – a direct reflection of New Labour's approach.

The overall net effect is thus almost identical over all three systems. Huge ideological changes and much political bluster and hype on lower taxation and lower spending have had little effect on the median earner on these assumptions. However, if we put in the presumed effects of changes in consumption taxes we can presume that 1997 and 2008 will actually have worse outcomes than 1979 as we know from Figure 2 that median income households were small net losers in indirect taxation in 1997 compared to 1979. But the main conclusion is that underlying direct tax and transfer burdens remain fairly constant.

How do changing assumptions about behaviour and policy maturity change the results? For the median earners the main change comes from 1979 assumptions about Ms M's employment history after children, which if we adopt a more 'traditional' approach and have longer periods out of work and looking after children reduce both earnings and pension income. Mature policy assumptions raise taxes in 1979 and make the 'tax-cutting' agenda more clear, although the higher taxes were to pay for better pension provision, which in 1997 and 2008 are done through mature assumptions prolonging working lives and make pension ages equal between Mr and Ms M. We will not report these results here due to lack of space but the clear and larger differences between the systems arises from the treatment of inflation and this is most apparent in state pension entitlement, that keeps pace with earnings in 1979 rules but only prices in 1997 and 2008 rules. The clearest way to illustrate this is to show the differences between the systems in preventing pensioner poverty (defined as income below 60% of median income (before housing costs as most pensioners are full-owner occupiers and have no housing costs in Britain). Figure 4 shows the Meades in retirement from the age of 65 (ignoring Ms Meade's earlier retirement at 60) and shows how their incomes from state and private occupational pensions protect them against poverty with inflations assumptions included. The poverty line is assumed to rise with earnings at a real rate of 2% per annum (an average real earnings rate over past 20 or more years in UK). Incomes from pensions are fixed at a proportion of previous earnings and on underlying state pension, which is flat rate. In 1979 state pension rises with earnings but the private pension only keeps pace with prices and that means that the Meades' income falls towards the poverty line slowly (the majority of their income comes from private occupational pension). In 1997 compared to median income their income starts at a slightly higher relative position but falls faster. In 2008, median income growth has pushed the relative poverty line higher against original income and underlying state pension has fallen further in relative terms over the intervening years.

The cost of an earnings related state pension is however very significant and raises the 1979 transfer totals from 15% to over 30% of lifetime earnings and the compensating tax increase under the mature assumptions for the Meades is only 5% (although funding would in practice be by the working generation during the Meades' retirement under 'pay as you go' principles).

Figure 4
Meades' Risk of Poverty During Retirement



Source: Author's calculations using LOIS

The Moores

How do the Moores, who earn twice as much in each comparison year as the Meades, fare in the three systems? The Moores have similar lifetime profiles to the Meades but with less interruption to Ms Moore's earnings after children – we assume they she returns to work full-time and can afford the necessary childcare and nanny services. Table 2 shows the summary fiscal incidence of lifetime for the Moores and clearly shows that reduced direct taxation since 1979, roughly a 6% of lifetime earnings difference, has been offset to some extent by lower transfers but mostly drives the net fiscal effect falling from minus 30% of lifetime earnings to 25% to 26% in 1997 and 2008 respectively. Given the much higher marginal rates of income tax under the 1979 system for the very highest earners we also show a summary second set of results for exactly the same lifetime profile with double the earnings of the Moores, a lifetime profile we call the 'Evan-Moores'. The results from this profile reinforce understanding of the impact of changing direct taxation and the particular impact of reduced rates of income tax at the higher ends of the earnings distribution. In 1979 their direct tax over the lifetime was 49% and this fell to around 40% in 1997 and 2008. Of course, when we consider the effects of the change to greater consumption taxation in 1997 and 2008 compared to 1979 the evidence of their particular regressivity in Figure 2 clearly reinforces the lower tax incidence for these higher income profiles.

Table 2**The Moores and Evan-Moores Lifetime Tax and Benefit Incidence**

Using constant 2008 behaviour and earnings at contemporary levels

Percentage of lifetime earnings	1979 System	1997 System	2008 System
The Moores on 2x median earnings			
Direct taxation			
All taxes (incl. student loan repayments)	38.9	32.3	33.4
(excl. student loan repayments)	38.9	32.1	33.0
State transfers			
All	9.2	7.3	7.5
maternity/dependent children	1.1	1.0	1.3
retirement	8.1	6.3	6.2
Net effects of direct taxes and transfers			
	-29.7	-25.0	-25.9
The Evan-Moores on 4x median earnings			
All direct taxes	48.6	38.9	40.3
All state transfers	4.6	3.7	3.9
Net effects of direct taxes and transfers	-44	-35.2	-36.4

Source: Author's calculations from LOIS

Notes: No inflation.

The other model iterations of the Moores' lifetime assess the impact of policy maturity and inflation only as there is little evidence that higher income households have changed behaviour, particularly in terms of female participation around childbirth and rearing due to household budget constraints (Evans and Williams 2009) and these iterations add little to demonstrate policy change and we do not report these in this paper.

The Lowes

Instead, we focus on the low earning lifetime of the Lowes and the assumptions for this lifetime are given in Appendix 1 on the same assumptions as for the Meades (i.e. that this is a consistent set of behaviour relevant to 2008 that is used to consistently profile all three years' systems) . Table 3 shows the cumulative lifetime tax and benefit incidence for the Lowes on these basic set of assumptions, without allowing for inflation, policy maturity or relevant changes in behaviour over time.

Direct tax incidence is consistent at around 21% of lifetime earnings in 1979 and 1997 but rises to around 25% in 2008 due to higher levels of national insurance contributions and local government taxation in the main, the latter has risen ahead of earnings under New Labour.

Table 3**The Lowes' Lifetime Tax and Benefit Incidence**

Using constant 2008 behaviour and 50% median earnings at contemporary levels

(% of lifetime earnings)	1979 System	1997 System	2008 System
Direct taxation			
All direct taxes	20.9	20.9	24.6
State transfers			
All	43.4	34.4	47.4
maternity/dependent children	5.7	4.9	12.1
retirement	36.9	29.2	35.3
other periods	0.8	0.3	0.0
Net effects of direct taxes and transfers			
	+22.5	+13.4	+22.9

Source: Author's calculations from LOIS

Notes: No inflation

However, when it comes to transfers it is clear that the targeted approach of New Labour – targeting both in terms of means-testing and through a categorical prioritisation on childhood and old age to combat child and pensioner poverty- has both compensated for rising direct taxes and restored transfer levels to above their 1979 levels. It is 1997 that stands out as parsimonious. The high level of transfers for children, over 12% of lifetime earnings, in 2008 reverses the trend of lower transfers that had seen their value fall from 5.7% in 1979 to 4.9% of lifetime earnings in 1997. In retirement there has also been a reversal but levels in 2008 at just over 35% have overtaken the 1997 level of 29% but not returned to the 1979 levels of almost 37% of lifetime earnings. One noticeable trend is that transfers for periods of the working age lifetime where there are no children have disappeared, from just under one percent in 1979. These transfers were mostly to assist in rent affordability and it is another aspect of policy change that these have become less generous at the same time as rents for low income households have hugely increased and moved nearer to (but not up to) market levels in social housing while social housing has reduced to push more low income households into the pure market rented sector that was deregulated. Overall, the net fiscal effect shows that the combined lifetime incidence of tax and transfers is 9% higher in 1979 and 2008 compared to 1997. However, it is for the Lowes that the move to increased levels of indirect taxation potentially has the largest effect as low income households pay disproportionately more in consumption taxes in 1997 and 2008 compared to 1979. This would worsen 1997 and 2008 results significantly compared to 1979 but would mean little overall difference between 1997 and 2008. We could clearly say that the improved net fiscal position of 2008 compared to 1979 would disappear and it is likely from other results in micro-simulation evidence (Redmond et al 1998) that 1979 would be considerably more favourable to families such as the Lowes.

When we change the behavioural assumptions to allow for longer periods out of the labour market for Ms Lowe in 1979 this raises the amount of transfers for childhood because of more means-tested provision and lowers pensions and direct taxation in 1979 leaving overall lifetime net incidence at a lower rate but substitutes Mrs Lowe's lost earnings for childcare expenditure – with smaller net

effect on overall lifetime disposable incomes. Policy maturity in 1979 increased tax incidence alone but in 1997 and 2008 also changes the balance between working and pension ages. Discussion of these effects is beyond what can be covered in this overview paper but the outcomes of these changes are illustrated in the pensioner poverty profiles for the Lowes below.

Allowing for inflation is assumed to be neutral in direct taxation on an assumption of consistent absence of fiscal drag (which is verified by comparing the relative value of tax allowances over the 30 year period) but makes large differences between the systems in transfer spending, increasing in 1979 due to earnings up-rating of state pensions as seen earlier for the Meades. The effect on 1997 is to reduce state transfer spending as a proportion of lifetime earnings as all transfers are only price up-rated. The effect in 2008 is more neutral as only parts of the transfer system are up-rated by earnings. The effects are most clearly seen when we come to look at child and pensioner poverty for the Lowes.

How do the Lowes profile against poverty for the period of their lifetimes when there are children present? Figure 5 shows the overall 20 year period during which children are present from birth to the age of 18 and should be put alongside the lifetime events outlined in Appendix 1. At the birth of the first child, maternity benefits provide the highest income in 2008 and again at the birth of the second child, the 2008 system provides best income coverage. But under all three systems the Lowes are in poverty while they rely solely on 50% of median male earnings while Ms Lowe is at home with the young children. When Mrs L returns to work part time, the family are lifted out of poverty in 2008 and 1979 but only to the margins of poverty in 1997. However, the 1997 and 1979 systems keep their relative value over time better than the 2008 system. When Mrs L changes to full-time work then poverty clearance rates in the immediate term are best in 2008 but once again these erode. When children age past 14 their poverty needs rise according to OECD equivalisation and thus the poverty coverage of the combination of earnings and transfer package diminish and when the 2nd child passes 14th birthday the family are once again poor. Finally, when the oldest child 'ages out' of consideration poverty clearance levels rise again. Figure 5 shows that the 2008 system does best at the points of marginal change, maternity, birth and entering or changing hours of work, but tends to do worse over time as the transfer package erodes in relative value against the poverty line that is rising with median income and thus with overall earnings growth.

Figure 5 shows the results for pensioner poverty for all three systems but additionally for a mature version of the 2008 system after full implementation of pension reform and thus the combination of later retirement at 68 and subsidised third tier 'personal accounts' pensions. The impact of inflation and up-rating are clearly apparent in the same way as in Figure 3 for the Meades. In 1979, the combination of basic state pension, earnings protected and the additional state second tier pension not only starts with the highest level of anti-poverty protection but this erodes slowly over time and the poverty line is not crossed. The 1997 system provides outcomes at 65 that are at the margins over poverty and the Lowes fall further into poverty during their retirement. In the 2008 system a higher level of pensions (from improved 2nd tier pension compared to 1997) at 65 gives poverty clearance but then erodes quickly so that the Lowes fall into poverty. The mature 2008 system gives an illustration of what the combination of later retirement and additional third tier pension would provide for the Lowes – both a far higher income at later retirement and sustained clearance from poverty – that springs in part from a return to earnings up-rating of the low level basic state pension of the first tier provision.

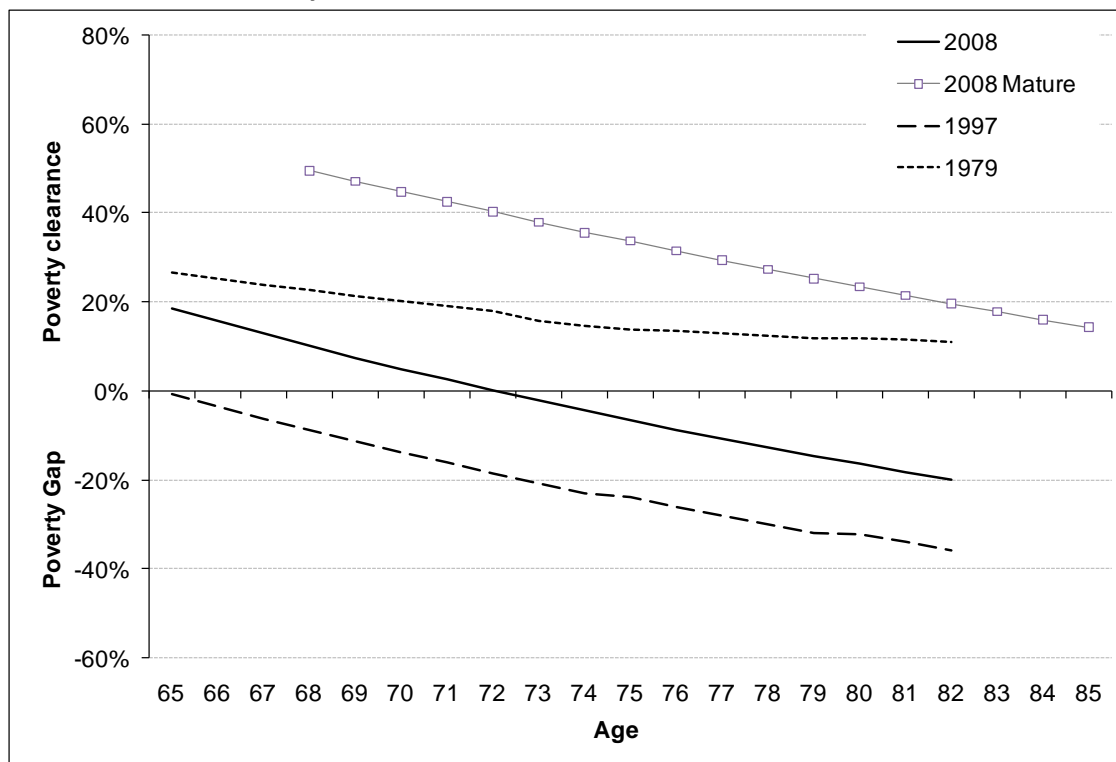
Figure 5
Lowes' Child Poverty Profile



Source: Author's calculations from LOIS

Notes: poverty line 60% of median income 'After Housing Costs'

Figure 6
Lowes' Pensioner Poverty Profile



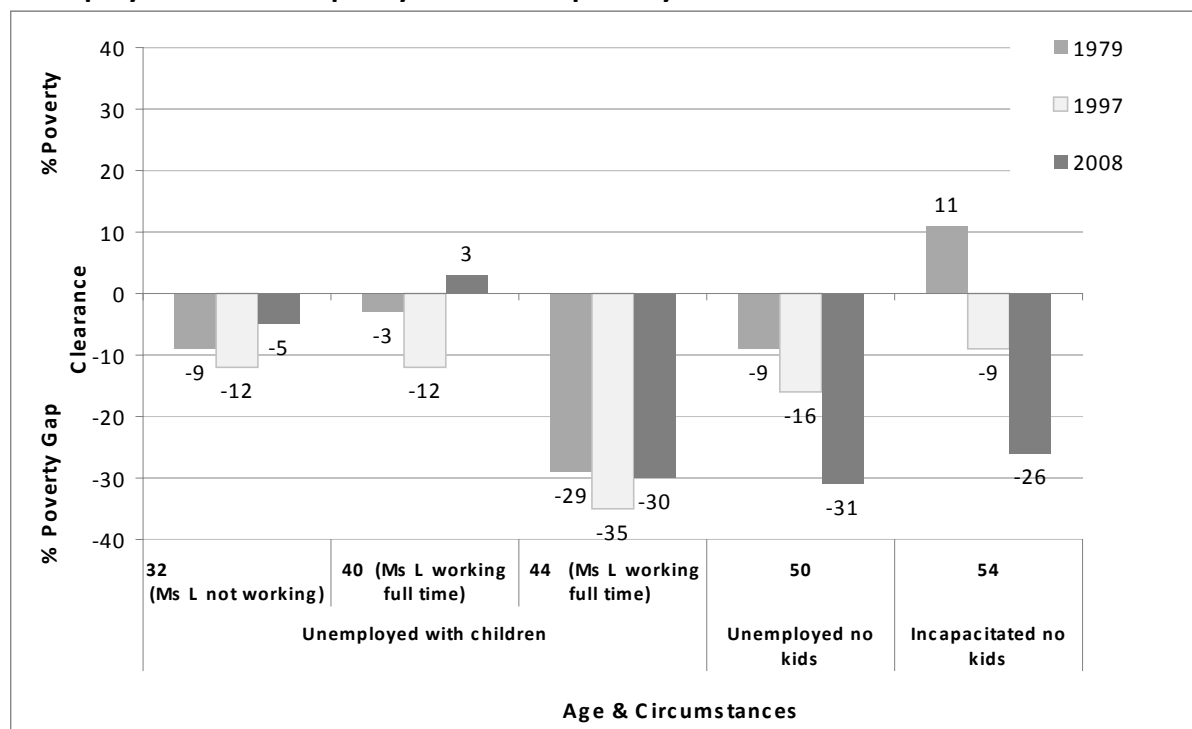
Source: Author's calculations from LOIS

Notes: poverty line 60% of median income 'Before Housing Costs'

However, it is worth pointing out how unrealistic it is to profile a low paid lifetime with no interruptions from unemployment, ill-health or other reasons. The interconnected risk of 'low pay, no pay cycles' is very high in the UK labour market (Stewart 1999). Figure 7 shows how the risk of poverty from unemployment and incapacity of Mr Lowe change over specific time points in the lifetime under the different systems. Unemployment interrupting Mr Lowes income when children are young and Mrs L is not working always results in poverty, but the more generous 2008 system reduces the depth of poverty to 5%, compared to 12% in 1997 and 9% in 1979. When children are slightly older and Mrs L is working part-time then poverty is avoided in 2008 because in-work tax credits are most generous to part-time workers with children when compared to 1979 and 1997. However, when Mrs Lowe is working full-time and children are older (14 or more) then poverty risk is very high under all three systems. When we consider a period when children are no longer present then poverty is worst in 2008 and reflects the fact that unemployment benefits and social assistance have continuously fallen in relative value since 1979, so that poverty gaps grow over time accordingly. Finally, when we consider the position where Mr Lowe is incapable of work due to ill-health then in 1979, replacement rates of contributory benefits are high and poverty is avoided. In 1997, these benefits have been reformed but are still more generous than unemployment benefits but poverty occurs. In 2008, then replacement rates are near to those with unemployment benefits the poverty gap is considerable.

Figure 7

Unemployment and incapacity events and poverty outcomes



Source: Author's calculations from LOIS.

Conclusions

The aim of this paper is to give a 'taster' of the approach of and some results from a comparison of three historically important versions of British social policy, and specifically of taxes and transfers. The political rhetoric and upheaval over the past 30 years have been huge – unemployment surged in the 1980s as Britain de-industrialised and as market driven policy took hold to change Britain from a 1970s 'left of centre' welfare state to one based on a more minimalist right-wing approach of low tax, low benefits and a greater reliance on incentives and returns from the market. New Labour under Tony Blair and Gordon Brown have tried to distance themselves from both the 'old left' and the 'new right' and have kept to the low tax approach but have tried to change the welfare state to minimise risk of poverty in old age and childhood and to maximise employment in-between.

Our approach has been to take a large tranche of social policy, one that returns to Beveridge's vision of provision from the cradle to the grave, and to see how lifetime design of policy has changed and with what outcomes. To do this we have employed an innovative approach – simulating whole lifetimes that are lived under rules at important turning points in the policy history, 1979, 1997 and 2008. The hypothetical lifetime simulations use assumptions that mean that time is frozen and that all policies present at a point of time operate over the whole lifetime. This enables us to capture all aspects of provision from maternity to death benefits alongside taxation but the assumptions about time and events mean that we have to use quite a few iterations to ensure that interpretation of policy change is optimised. This leads to considerable complexity and this paper has glossed over much of the detail of different simulations to present a succinct overview that captures the main findings that inform the larger report of the research published in the associated book (Evans and Williams 2009).

Our results match expectations from overall descriptions of policy change and from cross-sectional analysis of the incidence of taxes and benefits. We find that our low paid lifetimes, the Lowes, who earn 50% of median earnings, fare worse in 1997 than in either 1979 or 2008, even if they worked continuously. Indeed, 2008 system returns childhood income protection to levels well above those in 1979 and this is partly because New Labour is committed to end child poverty measured in relative terms. One problem is that consumption tax rises have taken much of any gains away in 2008 and have eroded further the poor position in 1997. The further problem for 2008 is that this new generosity erodes quickly over time against rising median incomes and relative poverty lines. But the underlying structural problem for the low paid is that out of work transfers have been allowed to fall in relative value continuously for 30 years as well as being made more conditional on employment – making poverty a certainty when children are not present and highly likely when they are. The lifetime approach emphasises how risks such as this should be seen as both a characteristics of low pay and a likely event in any low paid lifetime, thus undermining shorter-term objectives based on being in or out of work.

Much of the political rhetoric that characterises the changes of the past 30 years have been aimed at 'middle England' – the median voter – the middle class. Our analysis suggests that all the rhetoric has actually added up to very little change in fact – but tax composition has changed but direct tax rates have changed little. Any gains from lower taxes have tended to be lost through lower transfers. Much of the gains from the policy changes since 1979 have been concentrated in the

higher earning and higher income groups and our analysis confirms this, gains from lower taxation have far outstripped any losses from erosion of small scale entitlements to transfers.

These results thus confirm widespread assumptions, that the rich have got richer, but also show that the poor, while poorer under the purer right-wing Governments of Thatcher and Major, have gained some ground back – as long as they are in employment and that employment is continuous. This means they are clawing back ground climbing a loose scree slope and the current recession will bring out further the inherent contradictions in focusing so much on low paid employment as ‘opportunity’ rather than a more structural commitment to equality. Our results challenge most the assumptions of the middle ground. The low tax rhetoric is more clearly shown as potentially fiscal sleight of hand and a political conceit rather than substantive underlying reality.

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Appendix

Lifetime Profile Parameters for Meades

The life history that we employ for the Meades runs as follows.

- The profile starts at age 16. Ms Meade continues her secondary education and then takes a degree. She thus remains in full-time education until 21
- At age 21 she begins work. She works in the public sector and joins her employer's occupational pension scheme, contracting out from SERPS.
- She lives at home with her parents until at age 22 she moves into rented accommodation.
- At 26 she cohabits with Mr Meade (who has exactly the same age and has a very similar life history – he too works in the public sector beginning work and joining his employer's occupational pension scheme at age 21.)
- At age 28 they marry.
- At 30 they have sufficient savings for a 10% deposit on a house valued at the average contemporary purchase price for first time buyers, which they buy taking out a twenty five year mortgage.
- At age 32 they have their first child. Ms Meade takes a total of nine months maternity leave, returning to work part-time thereafter.
- At age 34 they have their second child, and again Ms Meade takes nine months maternity leave.
- At age 39 when her youngest child is five, Ms Meade returns to full-time work. Whilst Ms Meade is in work and her children are under 14, the Meades pay for childcare. Throughout their working lifetimes the Meades respectively work for the prevailing female and male median wages.
- Ms Meade retires at age 60. Mr Meade retires at age 65.
- They both die at age 85.

Lifetime Profile Parameters for Lowes

The simplified life history that we use to construct a lifetime profile for the Lowes in 2008 is as follows:

- At age 18 Ms Lowe begins work.
- At 22 she leaves the parental home and moves into rented accommodation.
- At 26 she sets up home with Mr Lowe (who as her male doppelganger is the same age as her and has a similar background).
- At age 28 they marry and have their first child. Ms Lowe leaves work to undertake full-time childcare.
- At age 30 they have a second child.
- At 33 she returns to part-time work.
- At 37 she returns to work full-time and until their youngest child reaches the age of 13; the Lowes pay for some childcare.
- Both children remain in full-time secondary education until they are 18.

- Throughout, Ms Lowe works for 50% of the female full-time median weekly wage weighted according to her age². Part-time is pro-rata half of her full-time wage.
- Mr Lowe works for 50% of the male full-time median weekly wage weighted according to his age
- Mr Lowe has an uninterrupted history of full-time employment up until his retirement.
- Neither of the Lowes make any private pension provision and so will rely entirely on state pensions in retirement.
- The Lowes live in social housing rented accommodation throughout their lives and pay contemporary average local authority rent.
- Ms Lowe retires at age 60.
- Mr Lowe retires at age 65.
- They both die at age 83.

² For Mr and Ms Lowe, under the 2008 system the age weighting calculation cannot lead to an hourly wage that is less than the applicable national minimum wage (NMW) and the NMW is used as a wage floor.