

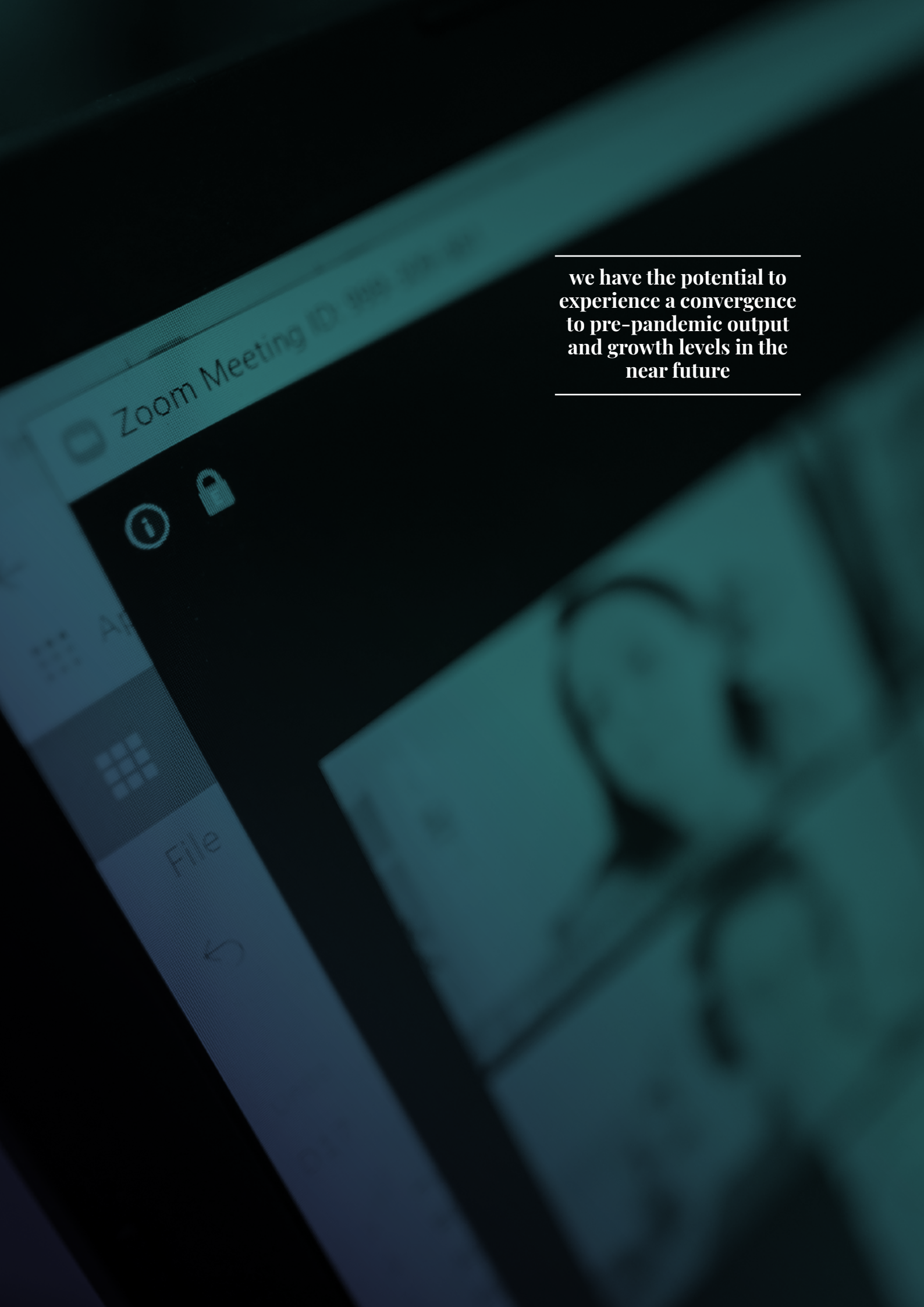
Social Security and the Pandemic –

An Extraordinary
Response?

NERI Report Series, No.8

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**we have the potential to
experience a convergence
to pre-pandemic output
and growth levels in the
near future**

Introduction

The covid-19 pandemic has been one of the most disruptive economic events to hit the developed world for many decades. In terms of its impacts on the labour market, to date it has caused more turmoil than the great financial crisis of 2008. However, the nature of this disruption is quite different to that of the great financial crisis. If the recovery from the pandemic builds on the policy response to the pandemic itself, our long-term assessment of this episode could be quite different.

Unlike the financial crash of 2008, governments could prepare for the economic disruption of the pandemic. In most cases businesses did not close through lack of economic activity, they were closed by the government. Financial support was provided to many of these businesses to give them the chance of re-opening once the crisis receded. The workers from these businesses did not simply join the ranks of those that were already unemployed. Instead, many governments decided to create a new labour market status and provide income support to maintain living standards throughout the disruption.

The actions taken by governments during this pandemic have meant that rather than experiencing an economic crash to rival the great depression of the 1930s, we have the potential to experience a convergence to pre-pandemic output and growth levels in the near future. When we think of the long shadow cast by the financial crisis of 2008, such an outcome seems truly remarkable.

What the pandemic has shown is that when government steps in to provide ultimate economic security, it can prevent the long legacy of economic misery that has followed so many previous economic crises.

One of the most significant lessons of this crisis has been that, rather than being a drag on growth or competitiveness, having a proper, well-funded social security net is one of the key components of a resilient economy. Providing income security in times of economic disruption not only alleviates distress for individuals and families, it is also a key investment in ultimate economic recovery.

This lesson is particularly pertinent for both the UK and Ireland. Prior to the current crisis, both economies have operated among the most threadbare of social security systems in Europe. The pandemic led to the creation of new systems of support for the unemployed that have shown that the capacity for such a system is possible.

This report seeks to scope out how the response to the pandemic has changed our system of social security and what it could mean for the future. It will look at the performance of Ireland and the UK in comparison to other developed economies. Importantly, that comparison will also be extended to how other countries seek to fund social security systems and the implications for how future reforms to social security could be realised.

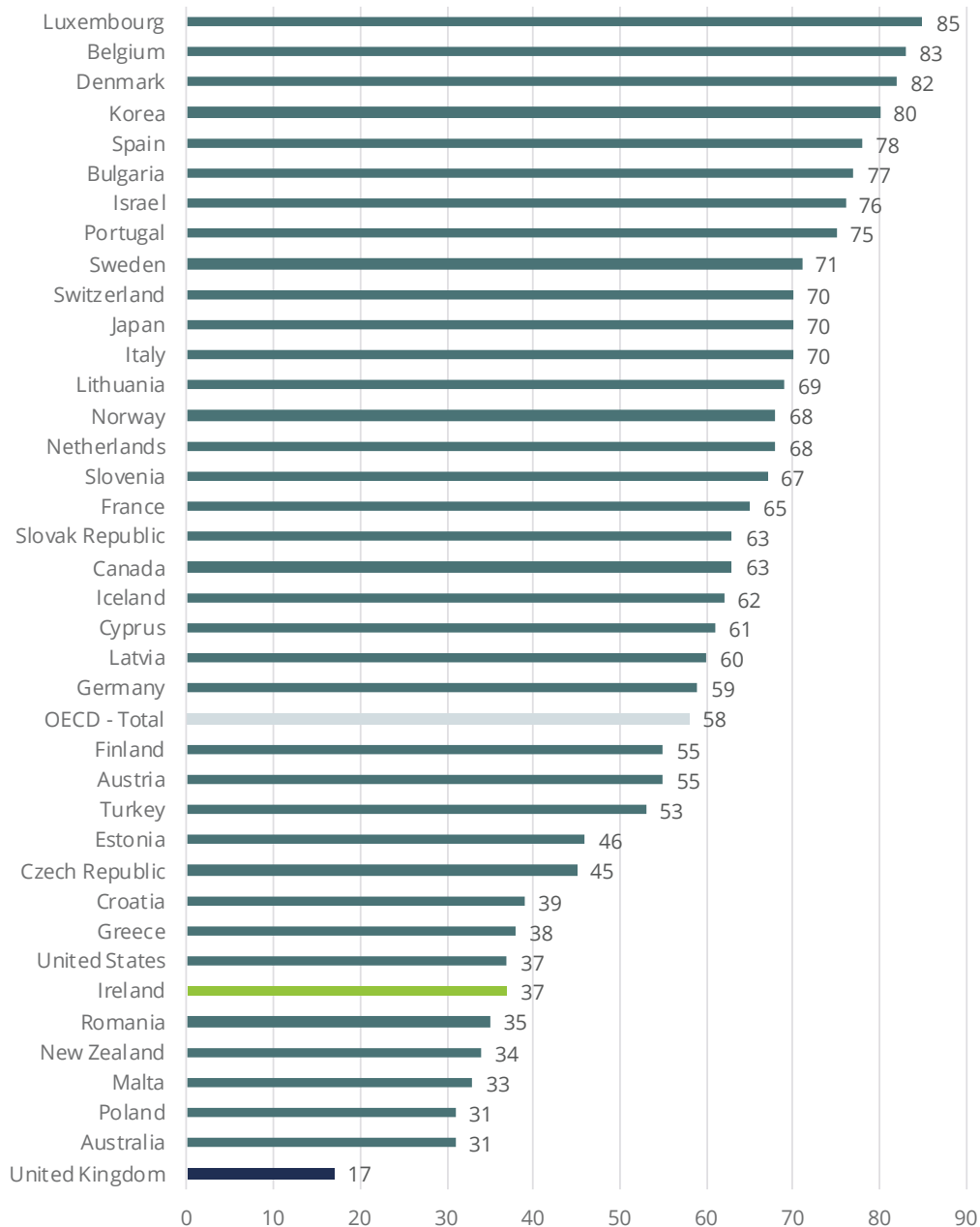
Social Security before the Pandemic

To begin with, this section looks at how support for the unemployed in the UK and Ireland compares with that in other developed economies. Obviously, the range and nature of supports to the unemployed is varied and unique to each economy, and so this analysis will focus purely on wage replacement. The net income replacement rate is calculated by dividing the total net welfare payment received by the total net earnings received in the month prior to unemployment. In addition to wage replacement, there are a number of other financial measures that may be available to persons who become unemployed, but these vary significantly and can often be dependent on household structure and other non-employment related factors. The example used here to compare across countries is wage replacement payments for a single person with no dependent children who has been unemployed for 5 months.

The following analysis will show the data for net earnings replacement rates in 2019. This provides the most efficient comparison as both average earnings and standard welfare rates have been temporarily and unevenly impacted in 2020. Before the onset of the pandemic, unemployment benefits in both the UK and Ireland were flat rate payments. This is in contrast to most other European countries where payments tend to be made as a percentage of previous earnings. In Ireland the highest rate of Job Seekers Benefit was €203 per week. This applied to all those who previously earned more than €300 per week. Anyone earning under €300 is either under 20 years of age or not working full-time as the Irish minimum wage is €10.20 per hour. For part-time workers then there are 3 graduated rates of payments between €203 and €91 per week. In the United Kingdom the standard rate of Job Seeker's Allowance is £73.10 (€83) per week with a lower rate of £57.90 (€65) applying to those aged 18-24.

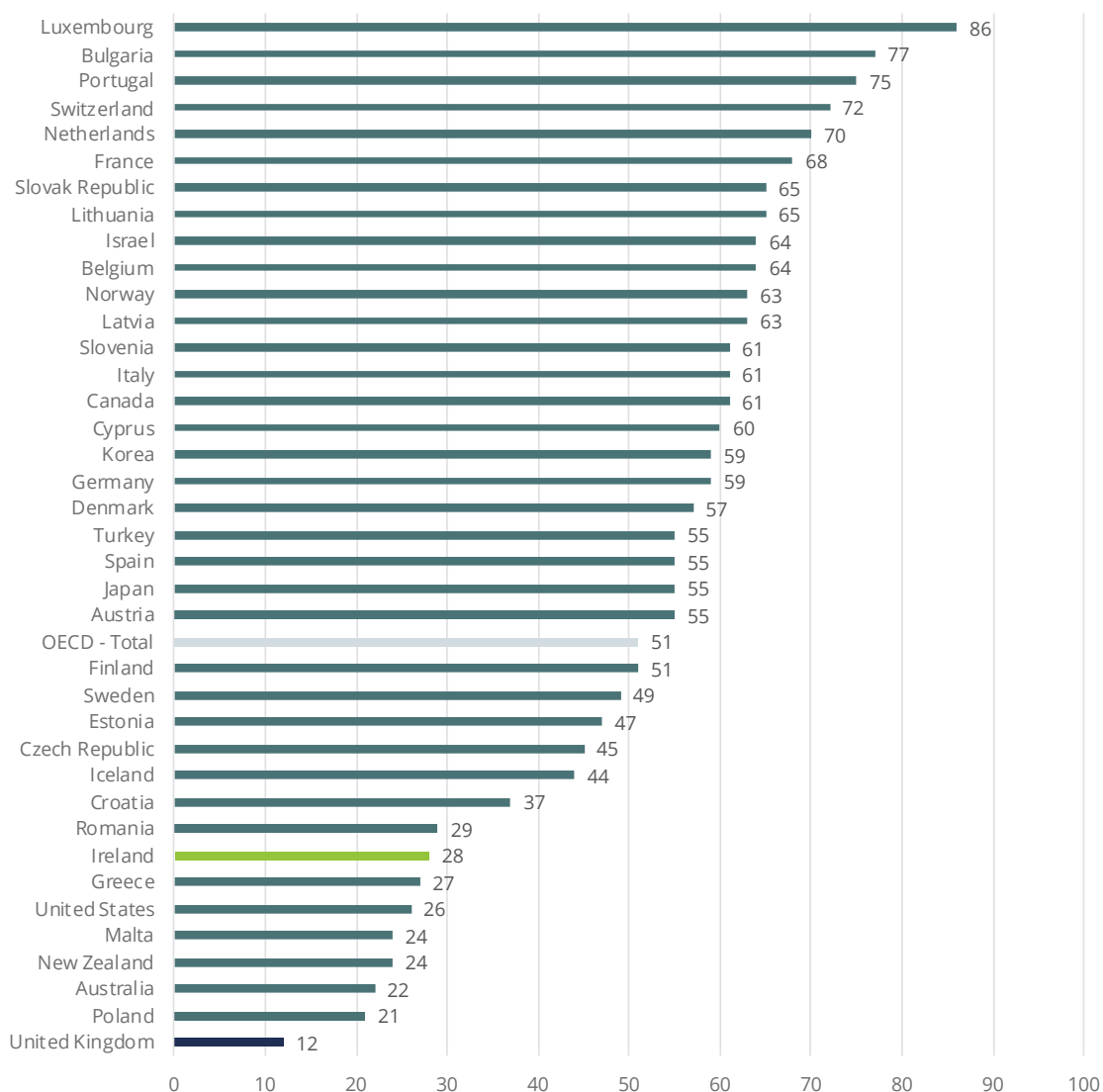
Chart 1.1 shows the net replacement rate for persons who earn two thirds of the average (mean) wage in their respective country. The United Kingdom has the lowest replacement rate of any OECD country, with just 17% net income replacement. The replacement rate in Ireland at 37%, whilst considerably more generous than the UK, is very much in the lower half of OECD countries. The OECD average replacement rate is 58%, significantly above both the UK and Ireland.

The United Kingdom has the lowest replacement rate of any OECD country, with just 17% net income replacement.

Chart 1.1 Net replacement rate in unemployment for 67% of Average Wage 2019

OECD (2020) Benefits, Taxes and Wages

Looking at the replacement rate for the average wage, Chart 1.2 shows that across the board, replacement rates are lower at upper levels of the earnings distribution. This reflects the fact that most unemployment insurance schemes which operate a percentage of income payment have caps on total payments. This means that as those on upper incomes hit that ceiling, the replacement rate is automatically reduced. Chart 1.2 still shows that the UK has the lowest replacement rate with Ireland still very much in the lower half of the table. The OECD average replacement rate for average incomes is 51%, down from the 58% replacement rate for earnings that are two thirds of the average.

Chart1.2 Net replacement rate in unemployment for Average Wage 2019

OECD (2020) Benefits, Taxes and Wages



The Pandemic

As the Covid-19 pandemic swept across the developed world, governments were faced with the prospect of having to order the closure of vast swathes of the economy. This left governments in the peculiar position of being able to plan for and sequence large scale unemployment. In the UK and Ireland, both governments decided that new payments would be introduced for people who would lose their jobs. It was quite clear from these decisions that neither government felt the existing unemployment payments were adequate.

As the pandemic took hold, in the UK, the government introduced the Coronavirus Job Retention Scheme (CJRS) in April 2020. It provided for a government funded payment to the value of 80% of previous wages. Under the CJRS, workers were furloughed, meaning they remained employed by their employer, but were not 'at work'. In Ireland, the process of supporting workers was more evolutionary and in the first instance focused on providing out of work support. The immediate response was to introduce a single flat rate Pandemic Unemployment Payment (PUP). It was initially set at the same level as the existing Job Seeker's Benefit of €203 per week, but it was quickly uprated to €350. The PUP was then moved to a 4 tier payment linked to previous earnings with €350 payment for those with previous average weekly earnings of €400 or more. The lowest earners received €203 per week, the same as JSB.

The Irish government did introduce an employment wage subsidy scheme but it eventually came to mirror the PUP rates of payments. The Employment Wage Subsidy Scheme (EWSS) therefore is intended to provide support for employees working in firms that experience an interruption to business rather than firms who are closed or forced to close. If a firm cannot provide any work for an employee, there is no financial incentive for them to be put on EWSS with no hours of work. All such employees would be made unemployed and put on the PUP. In contrast, in the UK the CJRS allows employers to partially or fully furlough employees. In this sense, the CJRS, whilst still a furlough scheme, has very much acted as an unemployment payment throughout the crisis. If CJRS is withdrawn too early though this effect will be significantly reduced.

To put these new payments in context it is worth attempting to compare them with the existing suite of payments in both the UK and Ireland. In order to do this, we look at 2020 earnings and welfare data for both the UK and Ireland and set benchmark replacement rates that would have applied to unemployed workers in the absence of the new covid payments. We then take the same income levels, average and 67% of the average, and apply the new covid payments to these. Using the new covid payments we can then calculate a new hypothetical replacement rate to compare with the pre-existing payments.

A photograph of a person in a cafe, seen from behind, wearing a dark shirt and apron, sweeping the floor with a broom and dustpan. The cafe has a modern aesthetic with a long counter, round tables, and a long cushioned bench along the wall. The floor is made of large, light-colored tiles. The image has a teal color overlay.

If instead the worker was placed on full furlough under the CJRS scheme, they would go on to receive 80% of their gross salary

Table 1.1 shows how the UK's unemployment payment would change if the applicant went from receiving Job Seeker's Allowance (JSA) to receiving a CJRS payment. In the first example, the worker was previously earning two thirds of the average wage. In 2020 that worker was receiving a gross salary of £28,011 resulting in a net salary of £22,687. Absent the CJRS, if they had become unemployed, that worker would then go onto to receive weekly payments of £94.30. The rate of JSA was increased by £20 as a temporary measure in 2020. When annualised, this payment amounted to £4925 per year, resulting in a net replacement rate of 22%.

If instead the worker was placed on full furlough under the CJRS scheme, they would go on to receive 80% of their gross salary, amounting to £22408. As CJRS payments are treated as employment income for tax purposes, this results in an annualised net payment of £18,879 and a resulting hypothetical replacement rate of 83%.

When we look at the experience of a worker previously earning the average wage we can see that the rate of payments to that worker under the JSA scheme are the same as those for the worker previously earning 67% of the average wage. Under the CJRS however that worker would receive an annualised payment of £28,800. This is less than 80% of that worker's previous gross salary, but payments under the CJRS are capped at £2,400 per month and so this limits the gross payments to an annualised figure of £28,800. After tax this leaves the worker with a net income of £23,226, resulting in a hypothetical replacement rate of 72%.

Table 1.1 Comparison of Net Replacement Rate between JSA and CJRS in UK 2020

2020	67% Average Wage				
	Gross Income	28011		Gross CJRS	22408
	Net income	22687		Net CJRS	18879
	Net replacement JSA	4925			
	Replacement Rate	22%		Replacement Rate	83%
2020	Average Wage				
	Gross Income	41807		Gross CJRS	28800
	Net income	32069		Net CJRS	23226
	Net replacement JSA	4925			
	Replacement Rate	15%		Replacement Rate	72%

OECD (2020) Benefits, Taxes and Wages, HMRC (2020)

Looking then to Ireland we can examine how an unemployed person would fare under the existing Jobseeker's benefit and the Pandemic Unemployment Payment using the equivalent income levels used in the UK example. Table 1.2 shows firstly the case of a worker who earns 67% of the average wage. In 2020 they received gross earnings of €31,279 resulting in a net income of €26,357. If they were to become unemployed, they would be entitled to €203 a week in Jobseeker's Benefit which would give them an annualised net income of €10,556. Jobseeker's benefit is subject to income tax, but

almost all recipients are entitled to tax credits which cancel out any tax liability. This then results in a replacement rate of 40%. Under the PUP, this worker would become entitled to the highest weekly payment rate of €350. This would result in a gross income of €18,200, and because the tax liability in this instance falls below that available tax credits, the resulting net income is also €18,200. This then implies a replacement rate of 69% for this worker.

If we look at the example for a worker on the average wage, we can see that they have previous gross earnings of €46,685 resulting in a net income of €35,095. Under the existing system of payments, the annualised net income that would result would be €10,556, resulting in a replacement rate of 30%. Once again, if that worker became unemployed under the PUP system they would be entitled to a gross and net income of €18,200. This would result in a net replacement rate of 52% for this worker.

Table 1.2 Comparison of Net Replacement Rate between JSB and PUP in Ireland 2020

2020	67% Average Wage				
	Gross Income	31279		Gross PUP	18200
	Net income	26357		Net PUP	18200
	Net replacement JSB	10556			
	Replacement Rate	40%		Replacement Rate	69%

2020	Average Wage				
	Gross Income	46685		Gross PUP	18200
	Net income	35095		Net PUP	18200
	Net replacement JSB	10556			
	Replacement Rate	30%		Replacement Rate	52%

OECD (2020) Benefits, Taxes and Wages, Department of Finance (2020)



There are a few things to bear in mind before we can analyse the figures in tables 1.1 and 1.2. Firstly, these replacement rates only apply to unemployment payments for the replacement of wages. Supports for housing and other unemployment assistance payments are not included. Secondly, in the case of the UK, CJRS payments are dependent on a continuing contract of employment with an employer. Absent a contract of employment, the worker would only be entitled to Jobseeker's Allowance.

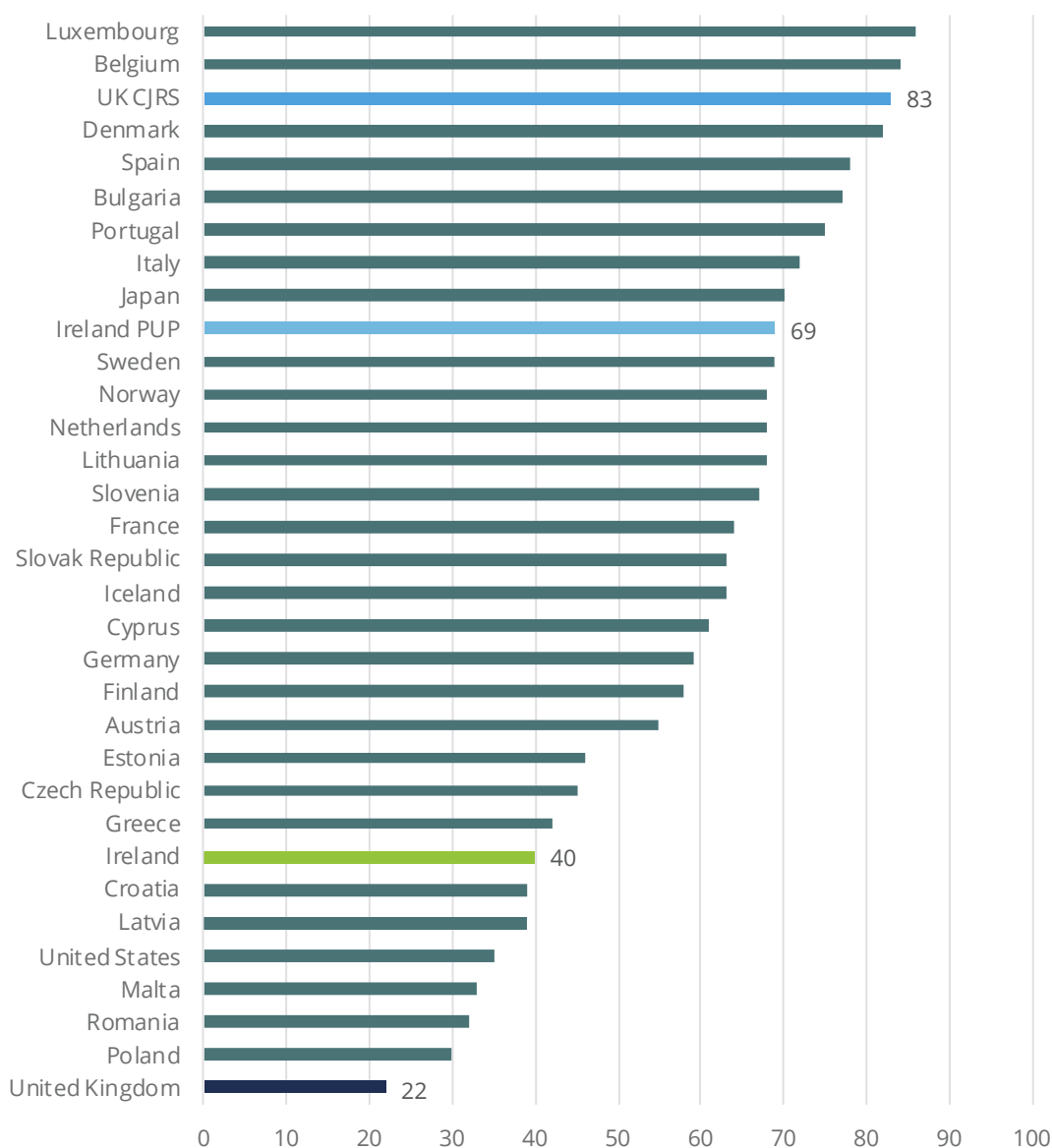
One of the most notable results from tables 1.1 and 1.2 is that unemployment payments in the UK were considerably less generous than in Ireland. However, under the new covid payments, that dynamic is reversed. Another notable feature is that in both the UK and Ireland, the new covid payments considerably raise the replacement rate for both. Moreover, in both cases, the percentage point increase in replacement rate is larger for the lower of the two income levels. In the UK, a worker on 67% of average earnings sees their replacement rate increase by 61 percentage points, while the increase for a person on average earnings is 57 percentage points. This is an important finding because it is often claimed that earnings linked payments benefit higher earners. What the CJRS scheme shows is that with an appropriate cap, this need not be the case. In Ireland those who previously earned 67% of the average wage see a 29-percentage point increase in replacement rate compared with a 22-percentage point increase for average wage earners.

It is not surprising that the new covid payments are more generous than those that they replaced. However, given that these payments are a temporary measure, there is an implicit assumption that they are not sustainable in the longer term. As mentioned previously, while the generosity of the CJRS and PUP may seem extraordinary relative to the existing suite of payments, they are far from extraordinary in comparison with European and OECD peers.

Charts 1.3 and 1.4 put the new covid payments in the context of existing European and OECD employment insurance schemes. Looking at the replacement rates for those who earned 67% of the average wage, chart 1.3 shows that under the CJRS, the UK goes from having the lowest replacement rate to having the third highest. Less dramatically, but significantly, Ireland goes from the middle of the lower half of the group to the middle of the upper half.

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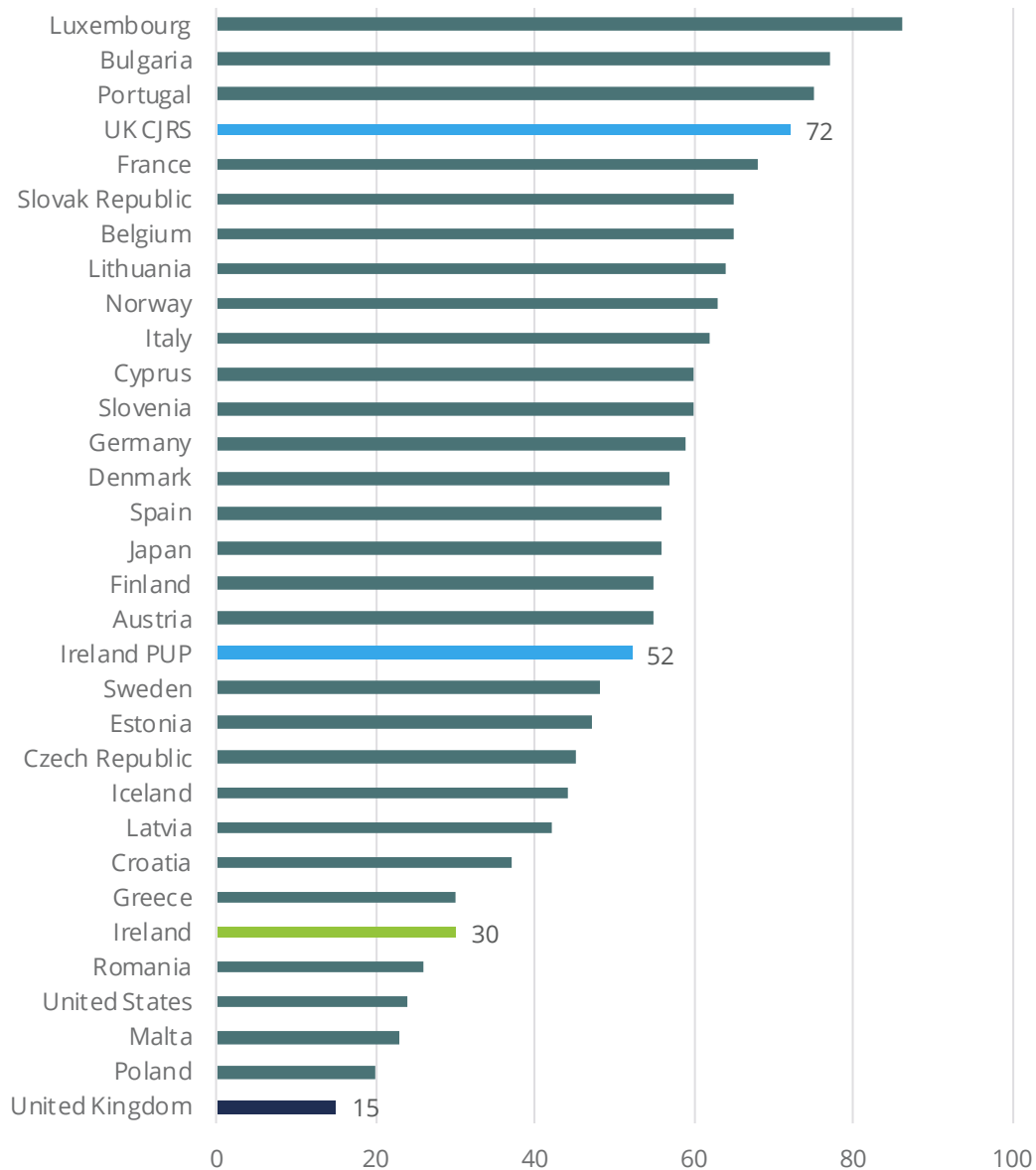
Chart 1.3 Net replacement rate in unemployment for 67% of Average Wage 2020 including CJRS and PUP



OECD (2020) Benefits, Taxes and Wages, DEASP (2020), HMRC (2020)

Chart 1.4 shows that for average income earners in UK, the jump in replacement rate under the CJRS is almost as big in comparative terms as that for the lower income group. Once again, the UK goes from having the lowest replacement rate to having the fourth highest. The change is more muted for Ireland, but it does go from having one of the lowest replacement rates, to being close to average. Incomplete data means that an OECD average is not available for 2020, but Ireland's 52% replacement rate is above the 2019 OECD average of 51% as seen in chart 1.4.

Chart 1.4 Net replacement rate in unemployment for Average Wage 2020 including CJRS and PUP



OECD (2020) Benefits, Taxes and Wages, DEASP (2020), HMRC (2020)

Charts 1.3 and 1.4 obviously present an imprecise comparison. Temporary covid payments are not the same as the long-established employment insurance schemes with which they are being compared. However, this imbalance is intentional. It is to show that far from being extravagant or extraordinary, the covid payments in the UK and Ireland, if they were to become permanent unemployment supports, would be quite ordinary.

Many of the countries that appear in the upper half of charts 1.1 to 1.4 operate unemployment insurance systems that bear resemblance to the CJRS. Luxembourg operates a system of supports with payments equal to 80% of previous earnings, exactly the same level as the CJRS. The PUP stands out as no other flat rate payment scheme matches the replacement rate that the PUP manages to achieve. This reflects the fact that in seeking to offer more generous payments during the pandemic, the Irish government sought to expand its existing welfare infrastructure, rather than to institute a new system.

From charts 1.3 and 1.4, it can be seen that the PUP achieves replacement rates that are most comparable with Sweden. In Sweden the inkomstbortfallsförsäkring (income-related benefit) provides 80% of pre-unemployment benefit for 200 days, falling to 70% for the following 100 days. Caps of SEK 910 (€87) per day for the first 100 days and SEK 760 (€73) for the remaining days apply. Such a model could apply to Ireland in the longer term as a more permanent scheme.

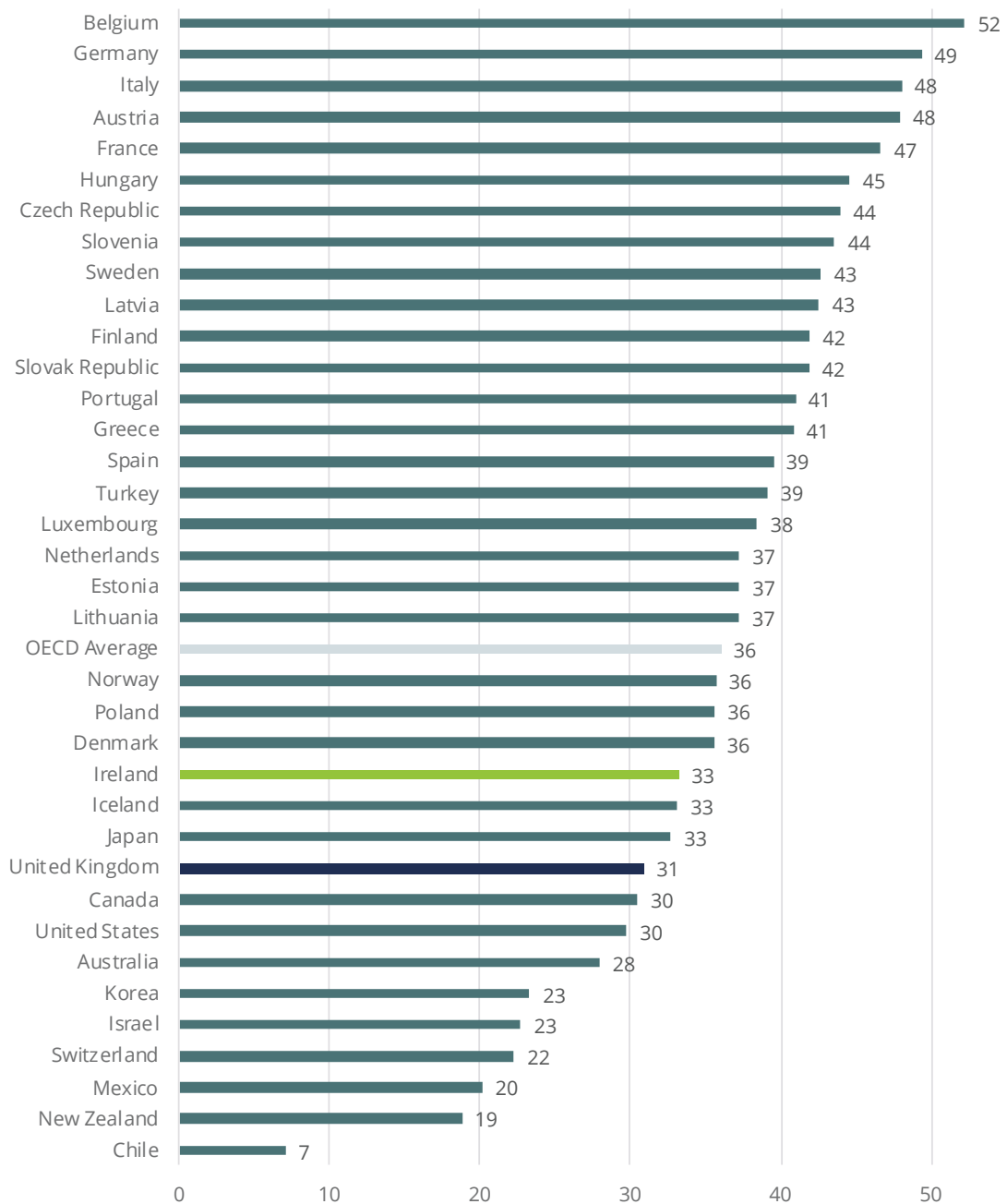
The obvious point that arises at this stage is that while more generous payments might be the norm in other countries, such reforms would require additional spending in the UK and Ireland. This is where we turn to next regarding the funding of unemployment insurance schemes among our comparator countries and the implications that these models would have for Ireland and the UK.

Funding Social Security

Spending on social security in most European countries is funded through a mix of general taxation and social contributions. Social contribution such as Pay Related Social Insurance (PRSI) in Ireland and National Insurance Contributions (NIC) in the UK are paid by both employees and employers. In the European Union, [over half \(55%\)](#) of expenditure on social security was financed by social contributions with the remainder coming from general government revenue. When we look at the taxation of labour in both the UK and Ireland it becomes clear why the social security systems in these countries are less generous than their peers.

Chart 1.5 shows income tax, employee social contributions and employer social contributions as a percentage of total labour costs for OECD countries. It can be seen that both the UK and Ireland are well below the OECD average and bottom of the table amongst their European peers. However, chart 1.5 obscures an imbalance in the shortfall of the taxation of labour that becomes clear when we separate out that which is paid by employers and that which is paid by employees.

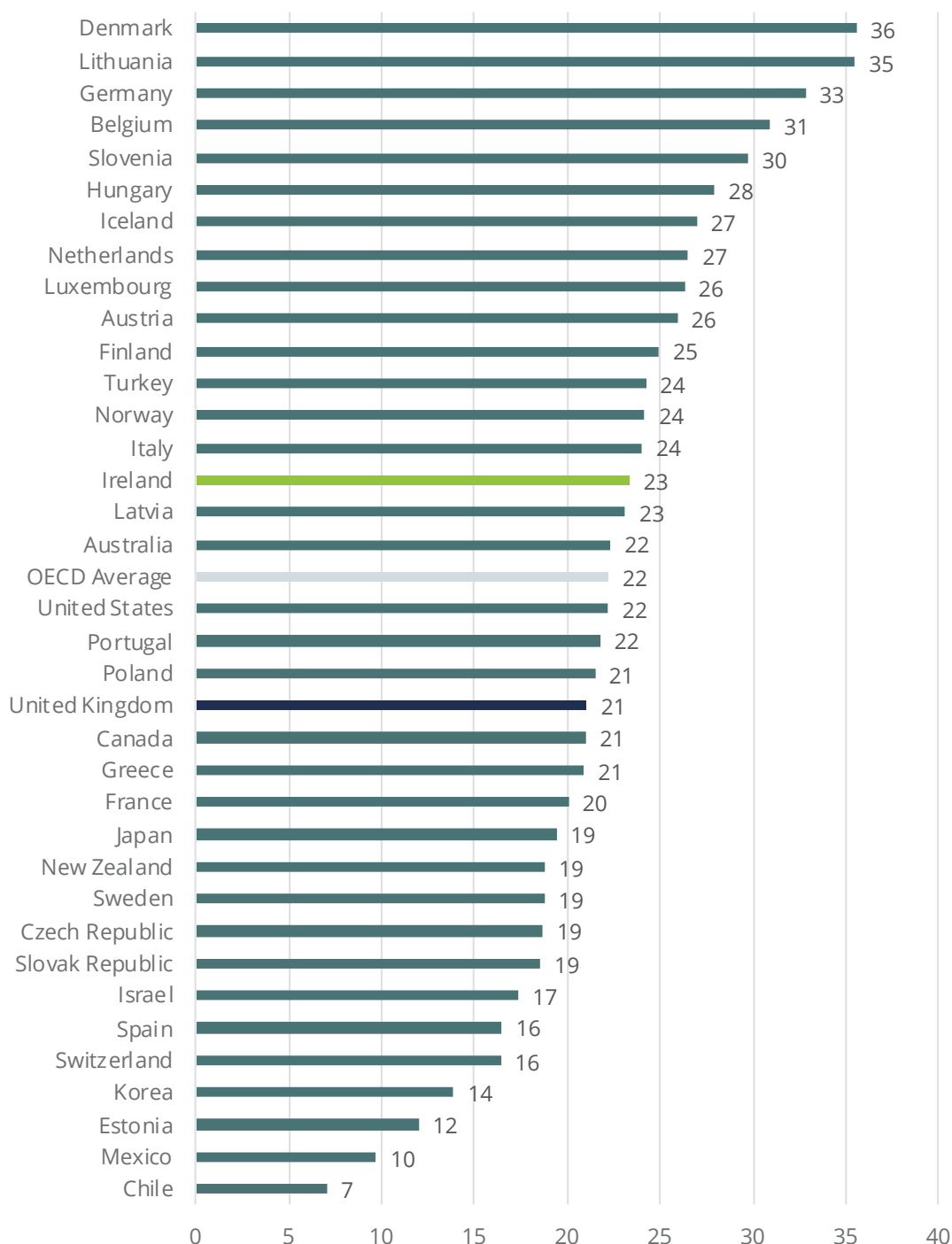
Chart 1.5 Income tax plus Employee and Employer social security contributions as a percentage of labour costs 2019



OECD (2020) *Taxing Wages*

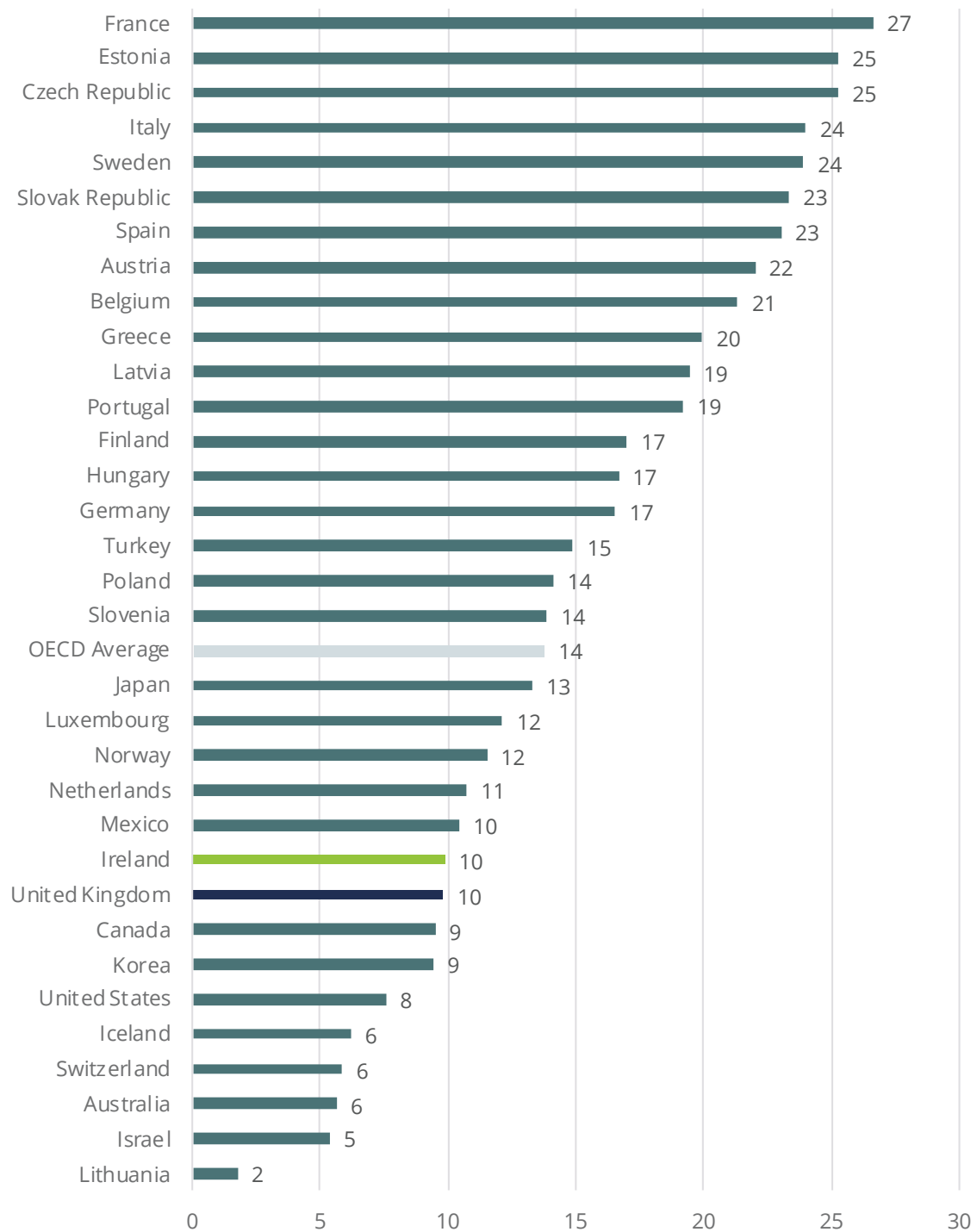
Chart 1.6 shows income tax and employee social contributions as a percentage of total labour costs. These are the two elements of labour taxation paid for by employees. As the chart shows, both the UK and Ireland are within a percentage point of the OECD average. Ireland is above the OECD average and both countries sit mid table in comparison to their European counterparts. By deduction then, the shortfall in labour taxation must occur in the portion paid by employers.

Chart 1.6 Income tax plus Employee social security contributions as a percentage of labour costs 2019



OECD (2020) *Taxing Wages*

Chart 1.7 shows employer social contributions as a percentage of total labour costs and both the UK and Ireland rank below the OECD average and every other EU member state and below every other European country bar Switzerland and Iceland.

Chart 1.7 Employer social security contributions as a percentage of labour costs 2019OECD (2020) *Taxing Wages*

Conclusion

For Ireland and the UK, the covid-19 pandemic has offered a glimpse of how an interventionist government can deal with the employment fallout from an economic crash. It should focus minds on how different the legacy from the great financial crisis may have been, if such swift and broad ranging policies were enacted between 2008 and 2010. Obviously, such a comparison is overly simplistic and the climate for government debt was far more hostile during that period. However, the experience should lead us to examine how systems of social security might be reformed for the future.

As this report shows, the financial supports made available to workers in the UK and Ireland during the pandemic may seem extraordinary in comparison to the status quo, but in comparison to what is provided in peer countries, they are quite ordinary. There does however need to be a conversation about how these policies might be funded. It is clear from comparisons with these peer countries that there is a clear tax gap with the UK and Ireland. The level of employer's social contributions in both countries stand in stark contrast to their peers. It is clear that this anomaly must be remedied.

Increasing taxes of any kind is not a harmless exercise and it is clear that there could be short term labour market disruption. Phasing-in and allowing for a period of adjustment are sensible guidelines for this policy change. However, it cannot be argued that this policy change would put either the UK or Ireland at any kind of disadvantage among their international competitors. As this report has shown, many of the most competitive European economies have achieved their success whilst operating a substantive social security system and the necessary levels of taxation to pay for it.

It should focus minds on how different the legacy from the great financial crisis may have been, if such swift and broad ranging policies were enacted between 2008 and 2010.



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