Universal Credit: *Inclusion* briefing

What is it going to cost?

It will cost £2.6bn in additional benefit expenditure. There will be a £2bn cost owing to entitlement changes and a further £2.6bn cost from an increased take-up of benefits (because of targeting and 'automatic passporting'). The savings made from reduced fraud, error, and overpayments will offset this by £2bn.

How will it work?

The reforms are designed to restructure the benefits system, to create one single income-replacement benefit for working age adults. This will bring together the current system of means-tested out of work benefits, Tax Credits and support for housing. It will be introduced in October 2013, with a phased four year roll out.

What is the baseline for the model?

The baseline that has been used for Universal Credit is the 'current benefits and Tax Credits system, assuming the current system incorporates all of the changes announced up to and including the 2010 Spending Review'.[1]

Who are the winners from the new Universal Credit system?

A total of 2.7 million households will see an increase in their entitlements; 85% of the higher entitlements will go to households in the bottom two quintiles; 1.1 million households will experience an increase in income of £25 or more.

The bottom two deciles of the income distribution will see increases in entitlement of around £4.40 and £5.40 a week, but higher if increased levels of take-up are assumed (bottom two deciles gain around £10 and £6 more a week). There will be lower gains for households higher up the income distribution.

It is estimated that Universal Credit will lift around 950,000 people out of poverty, including 350,000 children and 600,000 working-age adults. The number of workless households will fall by 300,000.

Will there be any losers?

Yes. There will be 1.7 million households with lower entitlements under Universal Credit. Of those, 1.2 million are found in the bottom two quintiles. As many as 400,000 households will see a reduction in incomes of £25 or more.

There are considerable differences in the changes to entitlement measured by family type and household tenure. For instance, 400,000 single no children households will see higher entitlements, while 600,000 will see a loss. However, couples with children will tend to benefit more from the changes.

Households with lower entitlements will be in one or more of these categories:

- in receipt of a large amount of Working Tax Credit
- not receiving Housing Benefit/Council Tax Benefit
- have a low disregard
- possess some capital savings.

Are there any transitional arrangements?

Yes. At the point of transition onto the new system, there will be full cash protection for individuals who would otherwise experience a reduction in income.

The value of the transitional protection will lessen over time, as people move off Universal Credit or their situation changes. Consequently, in the long-term, there will be some households who receive a notionally lower level of benefits.

How will work incentives be improved?

The government has said Universal Credit will increase the incentive to start work and do extra hours, as there will be lower participation tax rates (PTRs, the incentive people have to enter work) and marginal deduction rates (MDRs, the incentive people have to progress through work, i.e. doing more hours).

The number of households facing PTRs over 70% for working 10 hours per week will fall by around 1.1 million under Universal Credit. Similarly, those engaged in 16 hours of work will see their PTRs over 70% fall by over 900,000.The PTR for second earners will generally be higher under Universal Credit. Up to 330,000 second earners will see a weakening in their work incentives.

No in-work households will face a MDR of above 76.2% under the new Universal Credit system. The 700,000 people who currently have MDRs above 80% will see their MDR reduced to 76.2% or lower. However, some 2.1m individuals will have higher MDRs under Universal Credit. The median increase will be around four percentage points.

Around 1.5m individuals will have lower MDRs under Universal Credit with a median reduction of 20 percentage points.

What is 'individualised' conditionality?

Universal Credit will institute personalised conditionality. This will be tailored to the individual circumstances of claimants. In all cases, couples will be required to make a joint claim. For couples with children, one partner will be subject to the same conditions as a single person, while the other would be treated as the lead carer.

Inclusion analysis

Key headline points

1. *Inclusion* supports a streamlined and less complicated benefits system.
2. Changes to the level of Council Tax support for low-income households could have a considerable impact on Universal Credit's work incentives. Details of the changes are yet to be released.
3. The future arrangements for childcare support are crucial in getting families into and progressing through work. The government have yet to set out the full details.
4. We welcome the reduction in high marginal withdrawal rates, but will examine closely the impact on work incentives for 2.1 million people who will experience higher rates.
5. *Inclusion* will closely assess Universal Credit's impact on reducing both in and out of work poverty.

The model

- We welcome the creation of a simpler and more streamlined benefits system. The government's anticipation that this will lead to increased take-up is an equally positive development. The new system has been widely endorsed across the political spectrum.

- However, care should be taken in estimating future take-up levels, as there are several factors, like public awareness and attitudes, which influence rates.

Council Tax Benefit changes/baseline figures

- In calculating the distributional impact of Universal Credit, the government assumed the current rate of Council Tax Benefit (CTB). However, it was announced in the spending review that the benefit will abolished and replaced with grants to local authorities in April 2013. The current level of spending will be reduced by £500m.

- The Institute for Fiscal Studies (IFS) has raised serious misgivings about the changes and the effect these will have on Universal Credit. It argues they: run counter to the principles of Universal Credit; may potentially lead to a 'postcode lottery'; create perverse incentives for councils to encourage low-income households to move to different areas; and, with over 100 local authorities designing and administering their own measures, will cause marked variations around the country.

- Mike Brewer, IFS welfare specialist, said 'it would make the calculations over whether the unemployed would be better off taking a job than remaining on benefits more difficult'.[2]

- Any changes to the level of Council Tax support for low-income households could have a considerable impact on the working incentives of Universal Credit. We will study any developments to CTB closely.

Childcare payments

- Recently conducted research by the Daycare Trust found nursery place prices rose twice as fast as wages last year. Once the arrangements for childcare support are confirmed, we will carefully assess the implications for parent households and Universal Credit.

- The exact details of how Universal Credit will be administered have not been released. If an online approach is adopted, we urge the government to account for the circumstances of some low-income households, who may lack internet access. A variety of methods should be used.

Work incentives

- We strongly welcome the reduction in those facing extremely high withdrawal rates (i.e. losing 90% of every pound they earn while in work). However, we are concerned at the potential effect of higher withdrawal rates for 2.1 million households, who will experience an average withdrawal rate increase of 4%. We will examine closely the impact this may have on in-work incentives.

- The Resolution Foundation has warned of the possible negative impact on low-to-middle income working households. It has calculated that a couple with one full-time worker and two children will keep only 24 pence in the pound for earnings between around £8,000 and £32,000 a year. The same family would currently keep 10 pence in the pound for earnings between £11,000 and £17,000, rising to 30 pence in the pound for earnings up to £30,000.

- The Joseph Rowntree Foundation has emphasised the importance of demand-side measures and job creation in delivering successful outcomes for Universal Credit: 'Jobs need to pay enough, training needs to be available to allow for progression and we must remember the need for flexible and affordable child-care that enables parents to work. To make a real difference, we need to tackle poverty in a holistic and comprehensive manner.'[3]

Poverty & Fairness

- The government predicts that 950,000 individuals will be lifted out of poverty, including 350,000 children. We will closely follow and study the progress that Universal Credit makes on this front.

- The Social Market Foundation has highlighted how Universal Credit will penalise working families who have saved for their futures. Under the new rules, 400,000 families who are currently receiving tax credits will lose their entire eligibility as households with savings of £16,000 or more will no longer be eligible. An additional 200,000 families with savings between £6,000 and £16,000 will lose some of their entitlement.

- Kate Wareing, Oxfam's UK Poverty Director, has warned the welfare system must continue to support people in need: 'The government must make sure the safety net welfare provides is not being pulled from under our feet. Iain Duncan Smith has largely ignored warnings that people will be forced into destitution, and we want to see real action on his commitment that no one needs to live below the poverty line.'[4]

- It was announced that at the point of transition to Universal Credit, existing claimants would 'receive full cash protection against their losses'.[5] We ask the government to clarify whether this is in line with inflation or nominal 'cash terms'.

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1. Department for Work and Pensions (2011) *Impact Assessment – Universal Credit* www.dwp.gov.uk/docs/universal-credit-wr2011-ia.pdf

2. Timmins, N. (2010) 'IFS sees threat to universal benefit plan', *Financial Times*, 21 October www.ft.com/cms/s/0/959266dc-dd4e-11df-9236-00144feabdc0.html#axzz1EswQ9IgH

3. Joseph Rowntree Foundation (2001)*Response to the Welfare Reform Bill,* media release, 18 February www.jrf.org.uk/media-centre/response-welfare-reform-bill

4. Oxfam (2011) *Oxfam response to the publication of the Welfare Reform Bill*, media release, 17 February www.oxfam.org.uk/applications/blogs/pressoffice/2011/02/17/oxfam-response-to-the-publication-of-the-welfare-reform-bill/?v=media

5. Department for Work and Pensions (2011) *op. cit.*