



Making work pay:

Universal credit & low income working households

A report and recommendations
November 2012





Will low income working households really be better off with Universal Credit than under the current benefits system?

To consider this question we have looked at the benefit and tax system as it was in May 2010 before the government's programme of welfare cuts started, and the benefit and tax system as the government intends it to be in 2015

We have adjusted both systems for inflation to illustrate and compare how each system would affect a low income working household's income if it was in operation in 2013

Our findings and figures refer to the 'pre-reform' or 2010 system and the 'new' or 2015 system. They do not illustrate the actual current 2013 benefit system because it is a mid point in government's reform programme and does not enable a true comparison of pre- and post-reform systems

Our findings : a summary



Universal Credit will deliver improvements on the current system but not all low-earning working households will really be better off

ACHIEVING THE OVERALL POLICY AIM

With Universal Credit, households will benefit financially from increasing their earned income – which means there will be a better incentive to increase the number of hours worked

SOME GROUPS WILL SEE A CLEAR IMPROVEMENT

Couples without children across the whole income range will be better off than under the 2010 system

Single people aged under 25 across the whole income range will be better off than under the 2010 system

THE AMOUNT FOR INCOME DISREGARDS MATTERS

Government's intention to increase income disregards (the amount of earned income not counted when assessing Universal Credit claims) beyond the rates originally proposed in the White Paper makes a big difference

There will be an increased incentive for both adults in a couple to work

SOME OF THE IMPROVEMENTS RELY ON PREVIOUS CUTS

Many households will only be better off with Universal Credit because of benefit cuts made since 2010

Government's claims that households will be better off with Universal Credit than under the current system are true but only because of cuts they have already imposed

NOT ALL LOW INCOME GROUPS ARE BETTER OFF

Lone parents with one, two or three children will be worse off across the whole income range than under the 2010 system

Most two child families with a single earner (either a lone parent or in a couple) who earns less than the living wage will be worse off than under the 2010 system

Couples with three children will be worse off than under the 2010 system if their earned income is less than £300 per week

Our recommendations : a summary



Universal Credit could be improved, and additional actions would further improve circumstances for low earning households, especially those with children

GOVERNMENT SHOULD

- Boost earned income disregards in Universal Credit to give extra support to the lowest earners
- Set earned income disregards higher than those proposed in the 'Welfare the Works' white paper
- Guarantee to uprate Universal Credit in line with inflation
- Extend eligibility for free school meals and 'BT Basic' to low earning households
- Recognise that people on the lowest incomes will find it hard to improve their earned income because of the cost of childcare and the shortage of full time jobs in the current economy
- Encourage creation of greater opportunities for people in work to improve their employment circumstances
- Put extra resources into affordable childcare and sub-market housing
- Increase the £100 million transitional grant scheme for councils that build work incentives into their local Council Tax reduction scheme

Universal Credit : policy



With Universal Credit, the government aims to:

- **Make work pay**
 - So household income rises as people increase their wages
 - So people are better off in work than out of work
- **Simplify the benefits system**
 - So it responds faster and more smoothly to changes in circumstances

“Universal Credit will mean that people will be consistently and transparently better off for each hour they work and every pound they earn. Our reforms put work, whether full time, part time or just a few hours per week, at the centre of our welfare system”

(Iain Duncan Smith, Welfare that Works, November 2010)

Benefit reforms since 2010



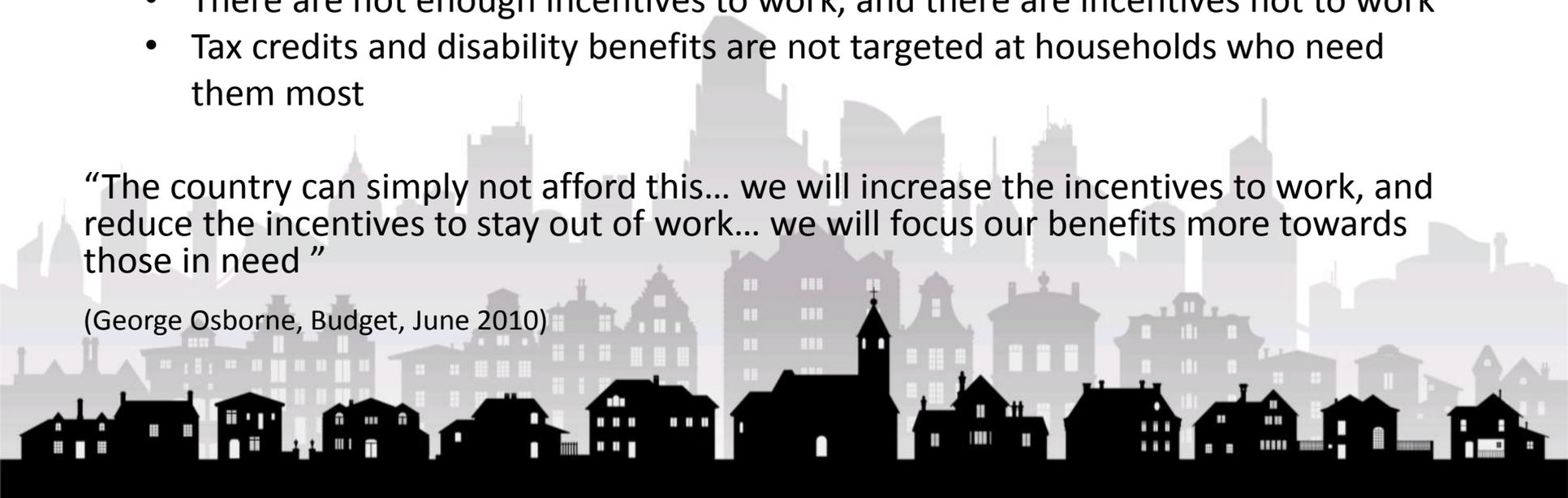
The government has made many changes to welfare benefits since June 2010

Reasons given for these changes are:

- 2000-2010 saw a 45% real terms increase in welfare spending
- The growth in welfare costs contributed to the UK's growing structural budget deficit
- Everyone across the income scale must make a contribution to helping reduce the debt
- There are not enough incentives to work, and there are incentives not to work
- Tax credits and disability benefits are not targeted at households who need them most

“The country can simply not afford this... we will increase the incentives to work, and reduce the incentives to stay out of work... we will focus our benefits more towards those in need ”

(George Osborne, Budget, June 2010)



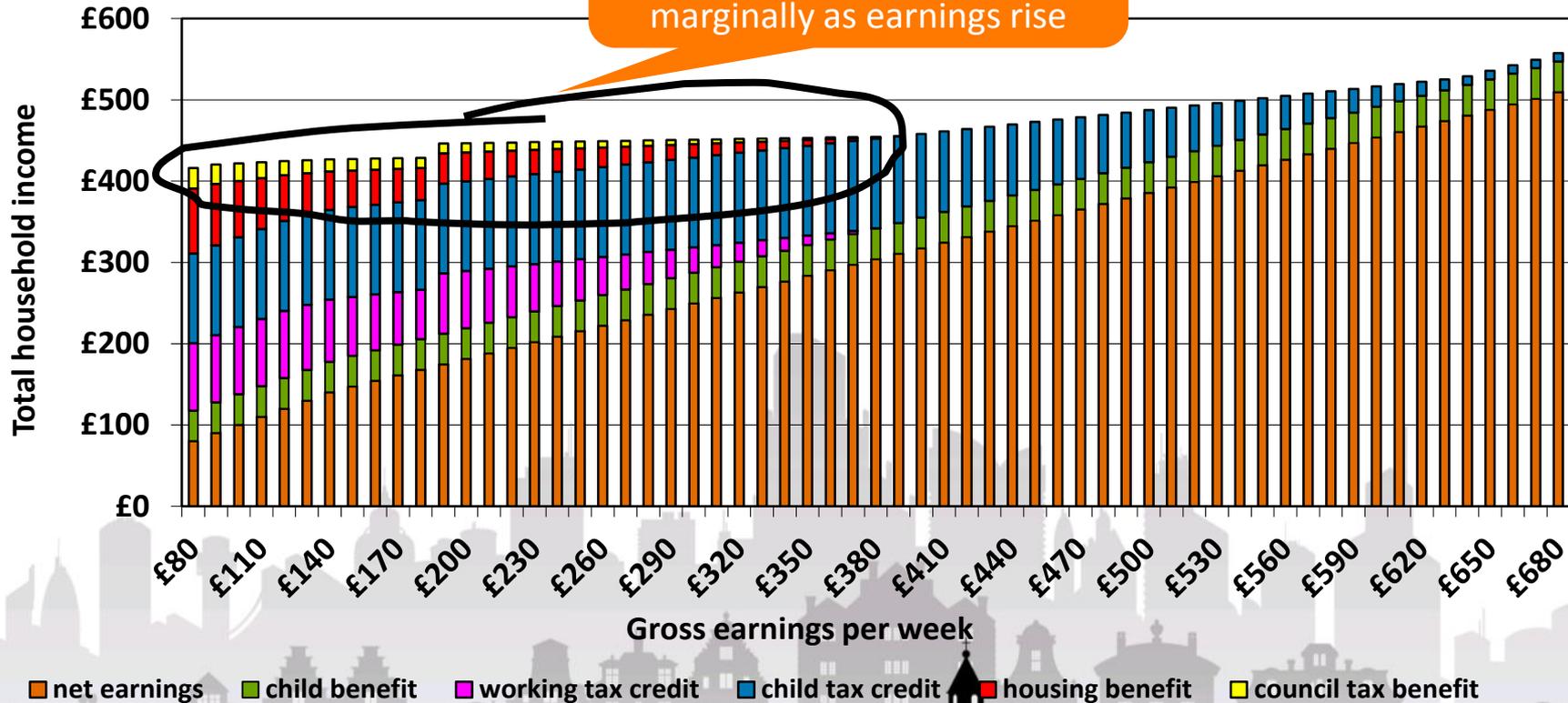
Pre-reform system for earners



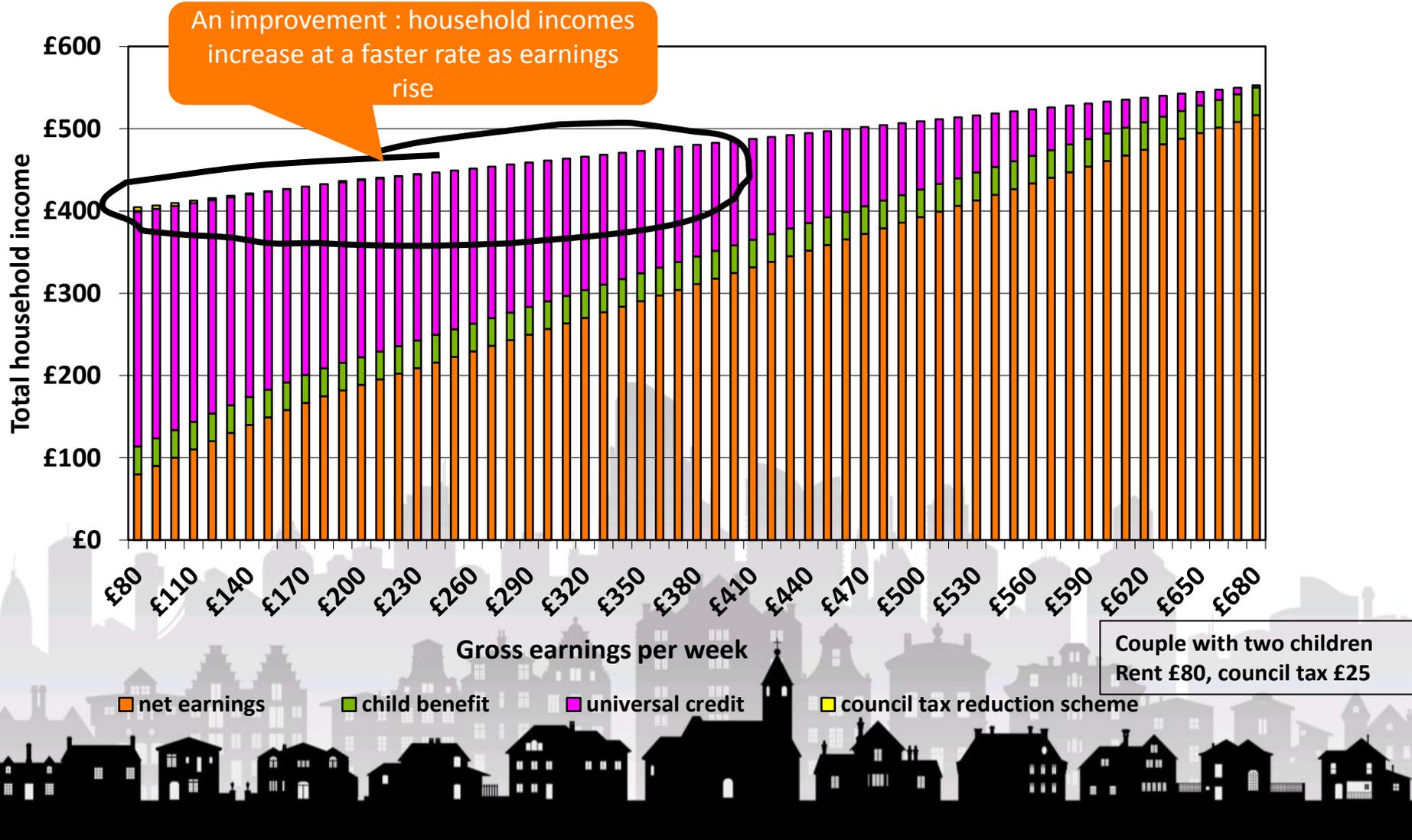
Couple with two children
Rent £80, council tax £25

The poverty trap : household income increases only very marginally as earnings rise

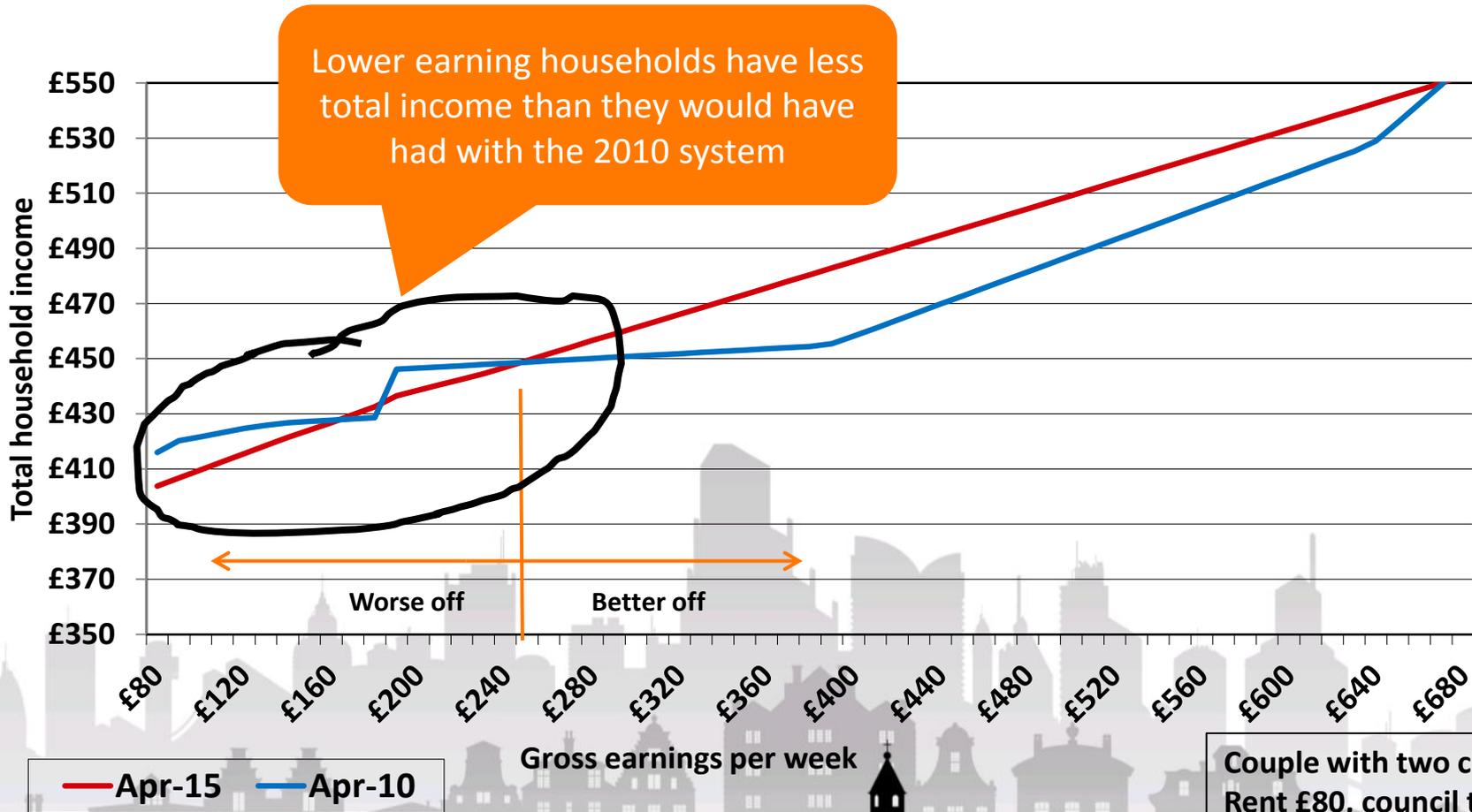
The graph shows the relationship between earned income and total household income



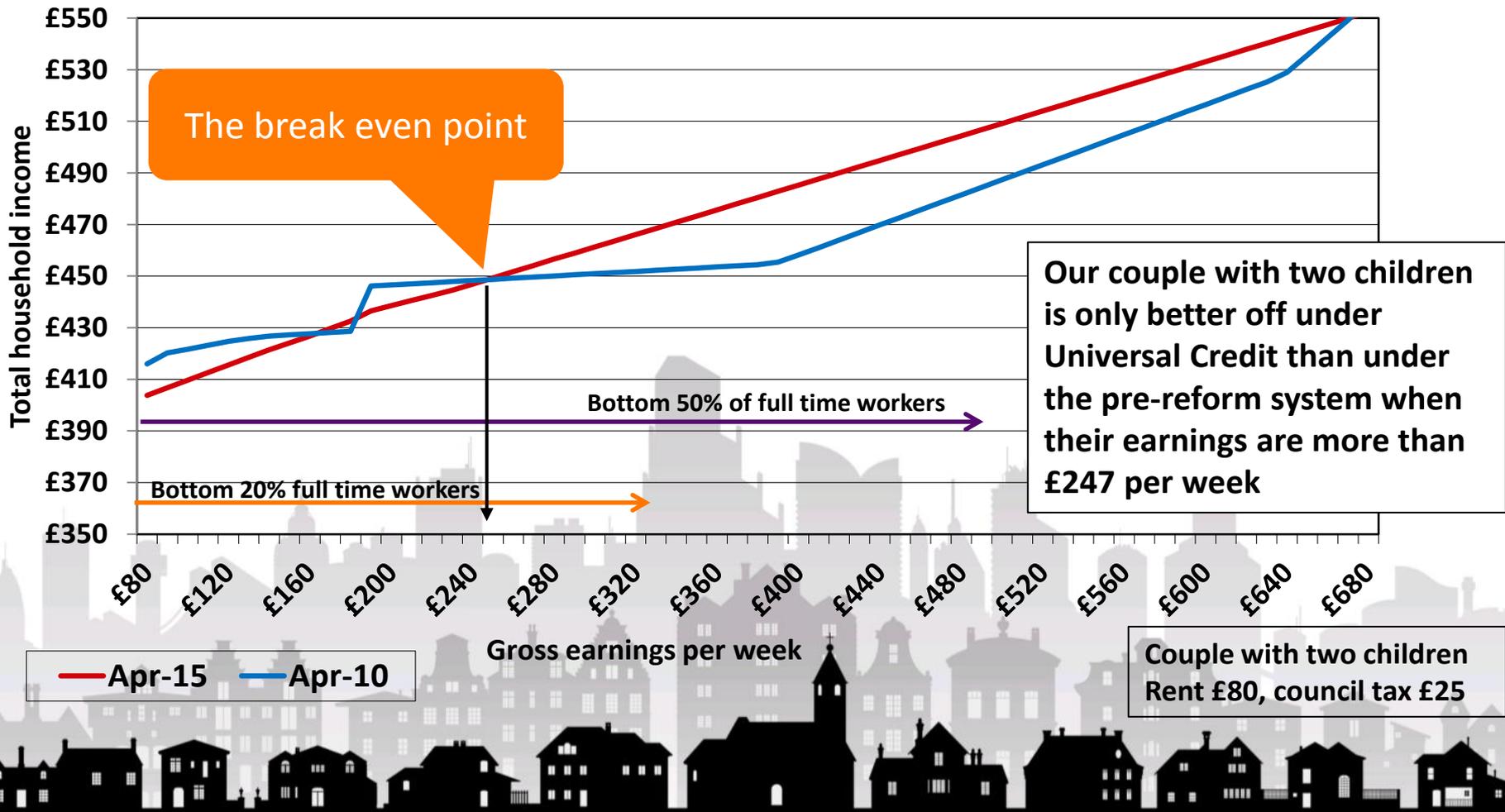
Universal Credit : an improvement



But not an improvement for everyone



The break even point



Break even points for different households



Household type	Approx. weekly break even weekly earnings
Couple , 1 child	£292
Couple, 2 children	£247
Couple, 3 children	£313
Lone parent , 1,2 or 3 children	Always worse off
Couple	Always better off
Single aged 25+	£362
Single aged under 25	Always better off

This table shows how much money different types of household have to earn before they are better off with Universal Credit than they would have been under the 2010 system

In each case we have assumed:

- Weekly rent of £80
- Weekly council tax of £25
- The household has a single earner working at least 30 hours per week
- Help with council tax from the local council (see appendix)
- Some earned income disregarded by DWP (see appendix)

Work more or get better pay?



Hours and wage	Earnings
16 hours @ minimum wage (£6.19)	£90.04
24 hours @ minimum wage	£148.56
30 hours @ minimum wage	£185.70
37.5 hours @ minimum wage	£232.13
16 hours @ UK living wage (£7.45)	£119.20
24 hours @ living wage	£178.80
30 hours @ living wage	£223.50
37.5 hours @ living wage	£279.38

This table shows gross earnings for someone who is paid the minimum wage and for someone who is paid the non-London living wage.

With the sole exception of an earner on the living wage working over 30 hours, the total earned income is less than £247 per week.

This shows that our single earner with a partner and two children cannot make themselves better off under Universal Credit than they would have been under the pre-reform system by increasing the number of hours they work – they would need to get a much better paid job.

Other pressures on income



Between 2008 and 2011 average full time earnings for the bottom 50% of earners rose between 4.5% and 5.5% (about 1.5% -1.8% pa)

BUT

- Over the same period CPI inflation increased by 10.2% (3.3% pa)
- CPI inflation for food and utilities was 14.5% (4.6% pa)
- The impact of increases in the cost of food and fuel is greater for poorer households

SO

Average full time earnings for the bottom 50% of earners declined in real terms by between 4.6% and 5.5% between 2008 and 2011

Lower income working households are worse off for two reasons: wages and benefits have both reduced in value since 2010



How many people will be worse off?



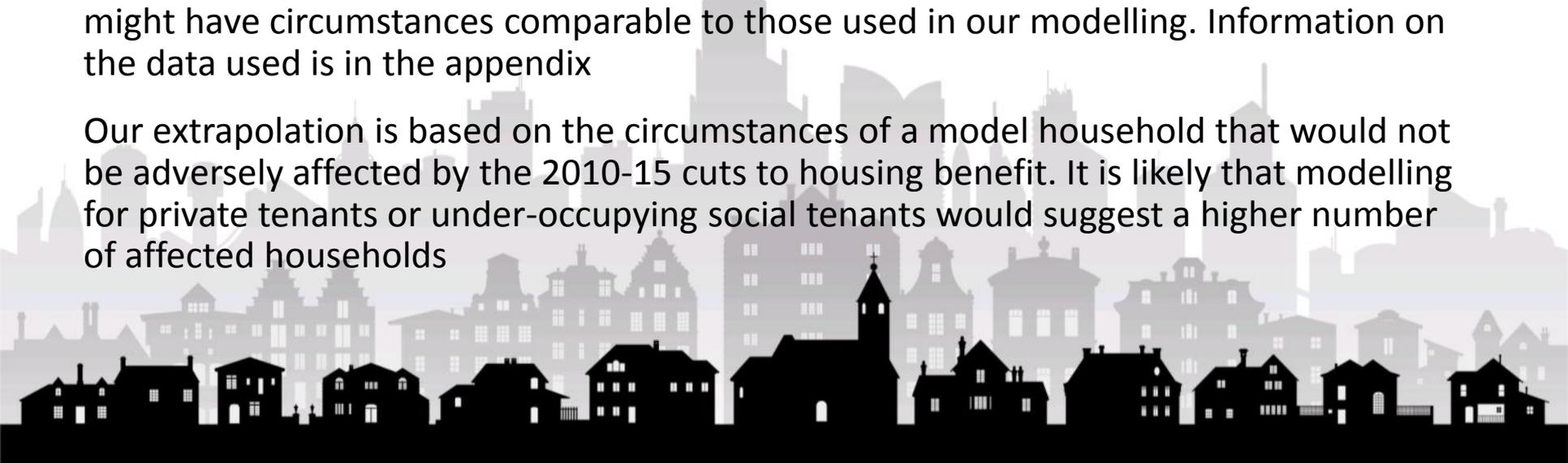
We estimate around 400,000 families in low paid work will be worse off with Universal Credit than under the pre-reform system

Why do we think this?

There is good government data on incomes and hours worked in the UK

Extrapolating from data provided by DWP gives an indication of how many households might have circumstances comparable to those used in our modelling. Information on the data used is in the appendix

Our extrapolation is based on the circumstances of a model household that would not be adversely affected by the 2010-15 cuts to housing benefit. It is likely that modelling for private tenants or under-occupying social tenants would suggest a higher number of affected households



Our priorities for action (1)



Announcements made in the Autumn Statement 2012 could make or break Universal Credit. There are easy steps government can take to build on the positive aspects of Universal Credit and ensure it is effective for the lowest paid working households

APPROACH TO INCOME DISREGARDS

Boost the earned income disregards to give extra support to the lowest earners and extend the range of households that benefit from Universal Credit

Resume the original plan to increase the minimum earnings disregards for the second and third child, to significantly extend the range of incomes over which most two parent households are better off

Ensure that earned income disregards remain higher than those specified in the 'Welfare that Works' white paper, and maintain the proposed additional earnings disregard for second earners. These features are central to the effectiveness of support and incentives offered by Universal Credit

UPRATING UNIVERSAL CREDIT

Uprate Universal Credit allowances in line with inflation otherwise people earning the lowest pay will continue to fall behind other employed people

LINKS TO ADDITIONAL FINANCIAL SUPPORT

Consider extending eligibility for fringe benefits and social tariffs (e.g. free school meals, BT Basic) to low paid working households to help offset the additional pressures faced due to the weak economy

Our priorities for action (2)



The government can, and should, make wider changes that will support the effectiveness of Universal Credit and achievements of its overall aims

HOUSING COSTS

Recognise that sub-market 'social' rents help to limit the range of incomes where households will live below the poverty line. The lower a household's housing costs are, the faster their household income increases in response to increases in earned income. In addition, lower housing costs mean lower overall costs of the Universal Credit system

REFORM OF COUNCIL TAX BENEFIT

Recognise the importance of help with Council Tax for the lowest earners by increasing the £100 million transitional grant scheme for councils that build work incentives into their local Council Tax reduction scheme

CHILDCARE AND EMPLOYMENT OPPORTUNITIES

Recognise that people on the lowest incomes will find it hard to improve their earned income because of the cost of childcare and the shortage of full time jobs in the current economy

Put extra resources into affordable childcare

Encourage creation of greater opportunities for people in work to improve their circumstances e.g. training provision to support career progression and ensuring availability of more full time jobs in the economy

In summary



Universal Credit has a number of very positive features but its design could be improved to help families on the lowest pay

The Autumn Statement is a critical time to make sure the new system works for all low income earners

If the right decisions are not taken now, government will create a system where low income earners are worse off than under the 2010 system, fixing the disadvantages of social immobility for this group



Appendix : research detail



Our findings are informed by a sophisticated model that calculates total household incomes based on earnings and family characteristics.

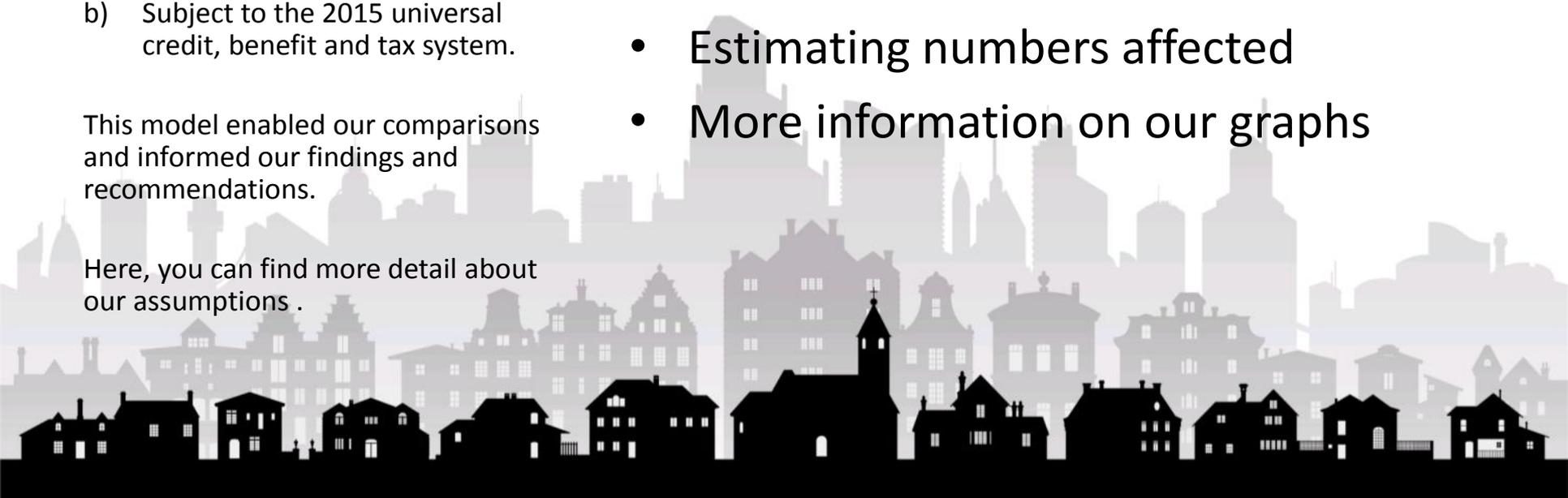
The model projects what would happen to a household 's income in 2013 if it was:

- a) Subject to the 2010 benefit, tax, and tax credit system
- b) Subject to the 2015 universal credit, benefit and tax system.

This model enabled our comparisons and informed our findings and recommendations.

Here, you can find more detail about our assumptions .

- 2010 system
- 2015 system
- Modelling operation in 2013
- Household financial needs
- Estimating numbers affected
- More information on our graphs



2010 system



- Low income households can claim child benefit, tax credits, housing benefit, council tax benefit
- Working Tax Credit eligibility
 - Claimant must work 16 hours with children or disability, 30 hours without
 - If a couple, only one claimant needs to work
- National Council Tax benefit scheme
- Personal tax allowances calculated as if the Coalition pledge to raise to £10,000 had not taken place

2015 system



- Low income households can claim child benefit, universal credit, local council tax reduction
- Work requirements for in-work Universal Credit
 - Claiming couples must work 24 hours per week in total, with at least one person working 16 hours
- Local Council Tax reduction scheme
- Personal tax allowances set at level announced in 2012 budget to meet Coalition pledge to raise to £10,000 by 2015

Modelling for comparison



We calculated what a household would receive in financial support and tax allowances for the 2010 system and the 2015 system, and then modelled them as if they were both operating in 2013

OUR APPROACH

Assumptions to model for 2010 rules

- 2013 applicable amounts for benefits using April 2010 rates increased using 2010 uprating policy as it stood before the June 2010 Budget
- Inflation based on ONS figures

Assumptions to model for 2015 rules

- Applicable amounts for Universal Credit are the same as April 2012 tax credit & child benefit, uprated by September 2012 CPI figures
- Earning disregards for Universal Credit as suggested by DWP in October 2011

Assumptions to model for 2013 rules for help with Council Tax

- Universal Credit counted in full as income. Any excess over the standard amount due to housing costs tapered away first and ignored until the tapered amount is equivalent to the full housing costs. Thereafter UC counted in full.
- Amount calculated as above with a 20% reduction on April 2012 council tax benefit entitlement applied

Our assumed households' circumstances

Rent = £80 per week

Council Tax = £25 per week

No disabilities

Home fully occupied (no spare rooms)

No childcare costs

Households' financial needs



	JRF *	DWP **
Single person	£192.59	£168.00
Couple	£301.74	£251.00
1 adult 2 children	£361.99	£269.00
2 adults 2 children	£454.52	£351.00

The table shows the two most widely used measures of how much money a household needs to live on after housing costs & childcare to achieve a reasonable quality of life / remain above the poverty line

Our hypothetical family does not hit either measure until their earned income passes £360 per week

This highlights an additional problem for Universal Credit – one which we do not explore further in this report

* Joseph Rowntree Foundation
Minimum Income Standards (July 2012)
<http://www.jrf.org.uk/focus-issue/minimum-income-standards>

** Department for Work and Pensions
Households below average income 2010/11

Estimating numbers affected

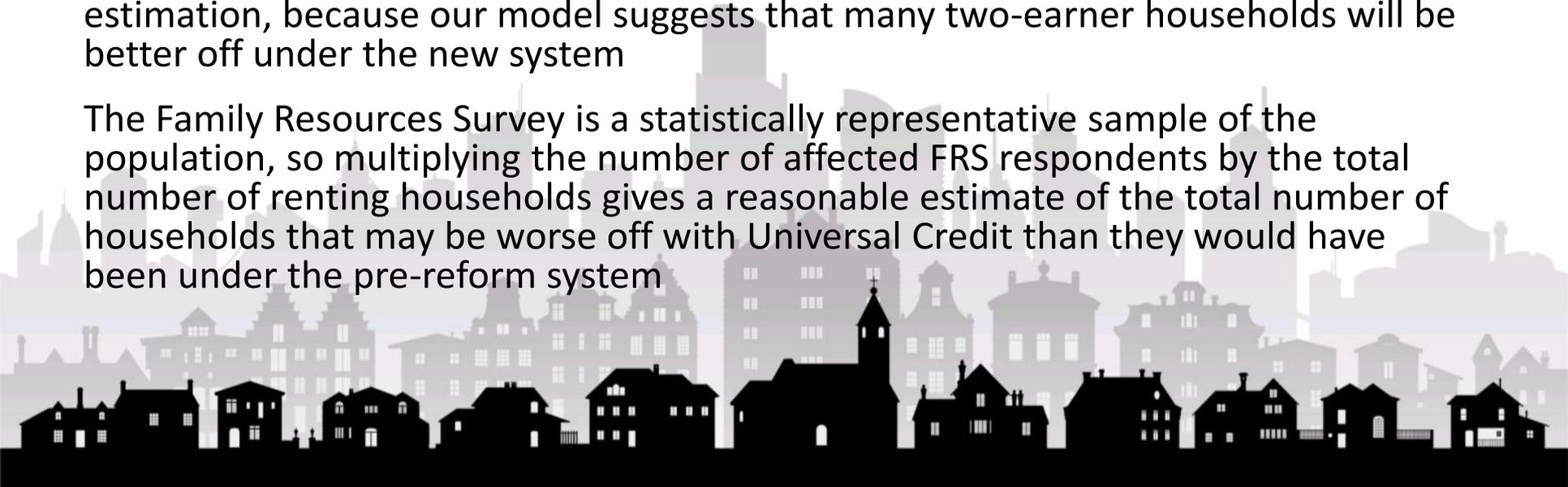


We have used raw data from DWP's Family Resources Survey to make our estimate. The FRS covers 25,000 households, and DWP uses this data for its own impact assessments

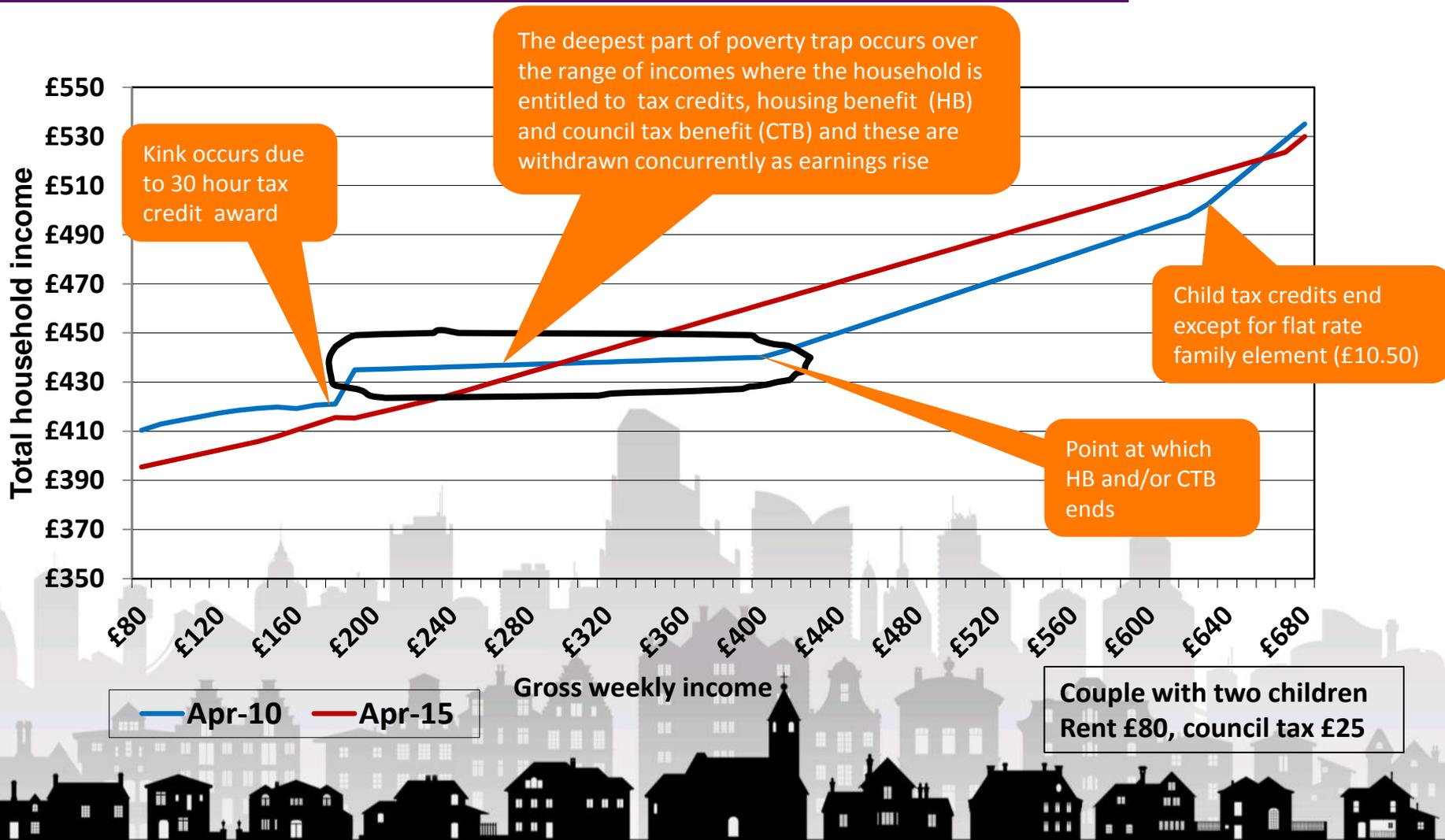
We identified the number of households in the FRS who receive Tax Credits and Housing Benefit, rent their home, and earn less than £300 per week. This is the profile of households that our model suggests will be worse off under the new system

We then filtered out households with two earners. This helps to prevent over-estimation, because our model suggests that many two-earner households will be better off under the new system

The Family Resources Survey is a statistically representative sample of the population, so multiplying the number of affected FRS respondents by the total number of renting households gives a reasonable estimate of the total number of households that may be worse off with Universal Credit than they would have been under the pre-reform system



Our graph explained



About CIH



Our purpose is simple - we want to transform lives by giving everyone working in housing the advice, tools and knowledge they need to be brilliant, and we want everyone to have a decent, affordable home in a thriving, safe community.

CIH is a registered charity and not-for-profit organisation. This means that the money we make is put back into the organisation and funds the activities we carry out to support housing work - last year we reinvested £11 million into the housing sector.

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