DEPARTMENT FOR WORK AND PENSIONS – WRITTEN EVIDENCE (EUC0115)

The economics of Universal Credit

1. The Government has been pleased to facilitate visits for the Committee to Jobcentres and other events to meet staff and claimants. The Government remains firmly committed to supporting all claimants of Universal Credit, and to ensuring that everyone can access the support that they need.

2. In considering Universal Credit, the principle of being better off in work than not working unless you cannot work was core in designing it, and is still at the heart of Universal Credit today. The legacy system was designed with the hardest cases in mind with rules that were then applied to the population as a whole, with the result that claimants were trapped on benefits or by cliff-edge rules such as not working beyond 16 hours.

3. As an example, a lone parent working 30 hours a week at National Living Wage and living in rented accommodation, could face a marginal deduction rate of just over 90% if they wanted to increase their hours or look for a better paid job. The equivalent rate in Universal Credit is 75%. 75% is the total marginal deduction rate including tax and National Insurance as well as the UC taper – that is the appropriate comparator with the 90% in the legacy system. When the policy design for the Universal Credit system was being developed, the UK had one of the highest rates of children growing up in homes where no one worked and it was found that this pattern repeated itself through the generations. Less than 60% of lone parents in the UK were in employment, compared to 70% or more in France, Germany and the Netherlands. Universal Credit was specifically designed to change that.

4. The 2010 white paper Universal Credit: Welfare that Works, noted that under the previous system:

"The welfare state has become a vast, sprawling bureaucracy that maintains, rather than really challenges, poverty:

> ***a.*** *more than one in four working-age adults in the UK does not work, and at least 2.6 million people spent at least half of the last ten years on some form of out-of-work benefit;*
> ***b****. around a fifth of families with children are in poverty at any one time and around two-fifths experienced poverty at some time in a four year period; and*
> ***c.*** *35 per cent of families remain in poverty when a parent enters work yet 2.4 million households now receive Working Tax Credit.*

To be effective and sustainable, public investment in tackling poverty must be about more than transferring money from those who have to those who have not. In the last decade, expenditure on working-age benefits and Tax Credits has risen from £52 billion in 1996/97 to £74 billion in 2009/10 14. Spending on *working-age Housing Benefit has increased by more than 25 per cent to £14.2 billion."*

5. To tackle this, the aim for Universal Credit is to prioritise the incentives of work in order to tackle poverty, and to provide underlying support for those who need it. Universal Credit is designed to be as simple as possible, straddling in and out of work cases, alleviating poverty, improving work incentives and increasing personal responsibility. The system is designed to replicate work to the furthest extent possible, in order to prepare people for employment. In Universal Credit, for example, payments are made monthly and include an element for housing costs, shifting responsibility to the claimant. Exceptions are included for those who might struggle with these aspects, like payment of rent direct to landlords or more frequent payment arrangements.

6. Creating a system like Universal Credit is a huge challenge and only possible if the rules are kept simple. A good example of this drive for simplicity is the length of the assessment period. In the economy as a whole, around 75% of people are paid monthly, a proportion that has been growing steadily over time as the economy shifts away from typical weekly or fortnightly paid jobs. A weekly assessment period would work for the minority of weekly-paid people, for anyone else such a system could result in significant fluctuations and overpayments. Anyone paid fortnightly, 4-weekly, or monthly could be paid Universal Credit for the weeks in which they did not receive their salary. For this and other reasons, (e.g. the HMRC real-time earnings feed, which is a monthly feed from employers) Universal Credit was designed around a monthly payment cycle. We accepted that the minority of claimants on non-monthly cycles might face a bigger budgeting challenge than the majority, and we would therefore need to support them through our Jobcentres and delivery partners, including budgeting support.

7. There are therefore some aspects of the system which are fundamental to it and deliberately designed to achieve its original objectives. This includes the mechanism of monthly assessment periods and, of course, the initial assessment period at the beginning of a claim.

8. There are various mechanisms, though, for making incremental improvements, ranging from regularly reported issues from operational delivery through teams of Service Improvement Leads, through to prioritised larger-scale requests which are impacted and governed through the Universal Credit Programme Governance structures. A good example of where we have responded to concerns was encouraging claimants to take up an advance payment. Around 60% of new claimants ask for and receive an advance of their entitlement, effectively meaning that they receive their annual payment in 13 smaller payments over a year, instead of 12. The intent here was to respond to concerns that the journey needed to be smoother at the start of a claim for some, and this has been achieved for many.

9. One of the unique aspects of Universal Credit is the support that it provides for those in-work to grow their hours or earnings. One of the benefits of the current model and, again, a feature designed to deliver its original objectives is that its sensitivity to changes in earnings enables the system to react

dynamically to changes in the working status of its claimants to an extent that has never been possible in the legacy system. This is contrary to the Tax Credits scheme, in which income is assessed annually and as a result has to contain an “income change disregard”, where earnings below a certain threshold level do not affect entitlement. As a result of this averaging being removed, Universal Credit will save £800million per year once fully rolled out, with a 10-year projection being a saving of £5.5 billion. Under previous systems, taking a low-paid job meant people running a large risk as Tax Credits are calculated and Housing Benefit adjusted over weeks and sometimes months. Many were simply not prepared to take that risk and remained trapped on benefits for many years as a result.

10. In terms of its applicability to the current labour market alongside its original objectives, the most recent labour market figures show that 130,000 more jobs in the UK are zero-hours contracts against the same time last year, and the rise of the gig economy has dominated discussions about the labour market for some time now. The indications are that this feature of the labour market will grow more prevalent and therefore the way that Universal Credit can automatically taper and adjust to earnings is designed for exactly that purpose. Under the previous system, benefit began to reduce after a very small amount of earnings at the rate of a pound of benefit for every pound earned. This was a huge disincentive to work legitimately for even a few hours because money earned over a small disregard would be lost through reduced benefits.

11. Many claimants are often already in debt prior to making their claim to Universal Credit. As all claims to Universal Credit outside of the Harrogate pilot are triggered by a “life event” leading to a change in circumstances – e.g. a job loss - it is likely that the claimant will already be experiencing financial difficulties. However, we also know that many claimants simply put off claiming, either because they simply do not want to claim benefits or are worried by what they have heard about Universal Credit. We want to encourage people to approach us for help as quickly as possible.

12. Therefore, another of the biggest current challenges to Universal Credit achieving its projected economic impact is the alleviation of unfounded fear in the system. Our evidence shows that claimants are delaying making a claim; are worried about Universal Credit as a result of stories on the internet and media, and are behaving accordingly. We are working to tackle those misperceptions in a range of ways.

13. We have consulted widely on various aspect of Universal Credit and have worked closely with stakeholders. Last year, the Department awarded Citizens Advice a grant of £39m to Citizens Advice to help vulnerable claimants who need support making their application to Universal Credit through the “Help to Claim” service. The Department will be evaluating the effectiveness of support to inform the future service. Last year, the Department also announced a £10m Universal Credit Transition Fund to encourage innovative approaches to supporting people in accessing the benefit system and preparing for work. The funding application process opened on 16 March 2020.

14.The Universal Credit Full Business Case (June 2018) [1] set out the range of economic benefits expected from Universal Credit. By 2026/27 Universal Credit is expected to realise £34bn in net economic benefits and £8bn of benefits per annum in steady state. This is primarily from increased employment and redistributive benefits as Universal Credit is better targeted on the with lowest incomes The main business case outcomes for Universal Credit are:

- **Delivering full employment** – Universal Credit will deliver 200k additional entrants into the Labour Market once fully implemented;
- **Reducing and preventing fraud, error** – Universal Credit will save approximately £1.3 billion in fraud and error (excluding sensitivity to changes in earnings reductions in Tax Credits);
- **Providing a safety net** – Universal Credit will allow the Department to tailor our offer to those who need it most, with extra assistance for vulnerable / complex claimants, and those with disabilities;
- **Increasing efficiency through automation** – Universal Credit will achieve savings representing a 29% reduction to the cost of administering the current legacy system (on a like for like basis), a saving of some £0.3 billion.

15. Since the publication of the business case, the Government has announced a significant increase to work allowances, equivalent to £1,000 per year, worth around £1.7bn per year by 2023/24. This is designed to further support work incentives and reduce in-work poverty. Aa a consequence of this the OBR expect Universal Credit to be on average more generous for claimants by £1.6bn in 2023/24.

16.Under Universal Credit, all of our work coaches are now trained to offer tailored, customised support to claimants, relevant to their own circumstances, to respond to their own needs and their local circumstances, including the local labour market. Universal Credit work coaches have the freedom and flexibility to make compassionate and sound judgements, and the tools at their disposal to support them in that, for the first time. Our digital journey is critical in this respect: not only does the Universal Credit digital system give claimants access to their records, payment breakdowns, deductions and decisions around the clock, but they can advise Work Coaches of any issues they encounter or request additional advice or support through their online journal at any time. This is important for the transformation journey as we seek to automate and remove the transactional aspects of our interactions with our claimants and spend our time with them providing the best support for them to find work.

17.In terms of our scope and plan, Universal Credit is currently on budget and to date, the Universal Credit system has cost £1.3bn to build. Universal Credit delivery is not yet finished though: we are improving and embedding it constantly and will continue to do so until and after a steady state is reached and all claimants are moved across. There are considerable social policy goals that this system is specifically designed for. We find, though, that often the issues that claimants are unhappy with relate not to Universal Credit itself but to their personal circumstances or the level of benefit available to them.

[1] https://www.gov.uk/government/publications/universal-credit-programme-full-business-case-summary

18. The current employment figures speak for themselves. The number of people in work is up by over 3.8 million since 2010 and the employment rate is at a record high at present of 76.5%. Both unemployment level and youth unemployment level have almost halved in the same period. And whilst the number of "zero hours" jobs has risen recently, the majority of the increase in employment in the last year has come from permanent work. Compared to 2010, there are over 1 million fewer workless households and at a record low, 730,000 fewer children in workless households.

19. Early evidence suggested Universal Credit claimants are 4 percentage points more likely to be in work within 6 months than JSA claimants and we do know that the freedoms and flexibilities afforded to our work coaches to find the right path for individuals to move into work as part of the Universal Credit design are working.

16 March 2020