BRIGHT BLUE – WRITTEN EVIDENCE (EUC0070)

The economics of Universal Credit

In February 2019, Bright Blue published a report, *Helping hand? Improving Universal Credit,* which explored the impact of the unique and key design features of Universal Credit (UC) on current claimants during three critical stages: accessing UC, managing on UC, and progressing on UC. It proposed original policies to minimise some of the common challenges faced by a sizeable minority of claimants, and to ensure some of the positive experiences of many claimants can also be enjoyed by others. Our research was based on a broadly representative sample of 40 interviews with UC claimants, conducted in August 2018.

How well has Universal Credit met its original objectives?

Our research allows us to comment on views and experiences of claimants in relation to three original objectives: rewarding work and personal responsibility, creating a fair system that protects those greatest in need, and creating a simpler system.

Rewarding work and personal responsibility

The single 'taper rate', which is one of the key tools in ensuring that working more always pays for UC claimants, was broadly well received. Among claimants that we have interviewed, most understood that as their earnings increased, the amount of their UC award would be gradually withdrawn. Most suggested this was broadly fair. But some felt that the taper rate was punitive.

There was also widespread recognition of the need for ensuring personal responsibility through conditionality and resulting sanctions. For many interviewees, an obligation for claimants to seek employment was just common sense. There was an implicit acceptance of the notion of rights and responsibilities; that in return for financial support from the state, claimants should accept certain obligations.

But while there was a general acceptance among claimants that sanctioning is necessary, some claimants argued that either the level of sanctions or the conditions under which it could be imposed, were punitive.

A fair system that protects those in greatest need

Most claimants are coping with and adapting to UC, and have positive experiences and attitudes. However, our research showed that groups of claimants were more likely to struggle or face issues. Such claimants tended to be older, self-employed, long-term unemployed, or had physical or mental health problems.

In our research, the initial waiting period of at least five weeks emerged as the design feature that a majority of interviewees had the most concern about, particularly for those belonging to one of the groups identified as more likely to face issues. Interviewees spoke of the stress induced by this initial waiting period. Only a handful of interviewees said they had enough savings to cover their expenses in this period. Most interviewees had to rely on family and friends for financial support. Some even fell into rent arrears and took on commercial debt. This aspect of UC appears to be the most likely to fail those who are in greatest need.

A simpler system

Among our interviewees, there was a clear majority preference for the single payment model that UC introduces. Interviewees said that it helped them to keep better track of their household cash flow. Many interviewees also spoke positively about having to deal with only one government agency.

<u>Does Universal Credit's design adequately reflect the reality of low-paid work?</u>

There were several elements in relation to low-paid workers in our primary research that we wish to highlight for this inquiry: monthly payments in arrears, self-employment on UC and removal of hours-based threshold.

Monthly payments in arrears

The monthly payment model is intended to replicate how frequently most workers typically receive their salary. Our interviewees were divided as to whether monthly payment in arrears was an improvement compared with the more frequent payments paid under the legacy system. There were some interviewees who coped significantly better than others in managing their income over a longer period. For UC recipients in regularised work, monthly payment was seen as mostly working well and serving to top up their income at the end of the month. In fact, interviewees with recent experience of a monthly wage were the most likely to speak positively about the monthly payment model.

However, while our fieldwork observed that many were adapting to the monthly payment, there was a significant minority – especially those who were unemployed – who struggled. Older claimants and those who are divorced or single, also spoke about the immediate challenges in needing to adapt to a new budgeting cycle, though many believed that they will eventually be able to manage it.

However, it should also be noted that wider evidence does suggest that a monthly wage is far from universal for those on very low income. For new UC claimants, fewer than two in five will have been paid monthly in employment. And around 60% of new UC claimants were paid weekly or fortnightly before moving onto UC.[1] Indisputably, for many claimants, monthly payment of UC is not reflective of the way they receive their salary from work.

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[1] Resolution Foundation, "Universal remedy", https://www.resolutionfoundation.org/app/uploads/2017/10/Universal-Credit.pdf (2017), 6.

Self-employment on UC

Previous research by Bright Blue estimated that 20% of self-employed resided in a low-income household, twice as many as employees.[2] There are three main design elements of UC that affect self-employed claimants that we have examined in our research: that those in receipt of UC should be 'gainfully' self-employed; the Minimum Income Floor (MIF); and, the surplus earnings and loss rule.

First, UC is available only to self-employed claimants deemed to be gainfully self-employed. A claimant is considered gainfully self-employed if they can demonstrate their work is regular and organised, that it is their main job, and that they expect to make a profit. While none of our self-employed interviewees described difficulties proving themselves to be gainfully self-employed, there was little evidence that work coaches met the specialised needs of self-employed interviewees, with some stating that their work coach could not offer effective advice.

Second, self-employed claimants' awards are subject to, after 12 months, a 'Minimum Income Floor'. This means that when their award is calculated, their earnings are assumed not to fall beneath a certain level. If a claimants' earnings fall beneath the MIF, their entitlement will not be increased to reflect the lower earnings, with MIF being set at the equivalent of 35 hours worked per week at the National Minimum Wage for most claimants.

None of our self-employed interviewees were subject to the MIF, and awareness and understanding of the MIF was low. Some claimants who were aware of it raised concerns about the length of the 12-month grace period, stating it was not long enough to allow nascent businesses to get off the ground. Furthermore, in previous Bright Blue research, income volatility came through as the top challenge self-employed individuals in low income households face.[3] If a self-employed claimant has months of very low earnings, which go beneath the MIF, their benefit entitlement will be less than an employee on an equivalent income.

Third, there is also an earnings ceiling, known as 'Nil UC Threshold', for entitlement to UC. The surplus earnings rule means that monthly income that is more than £2,500 over the 'Nil UC Threshold', such as profits from self-employed income, is used in future calculations of a claimant's UC award, counting as additional earnings. While this rule was not mentioned by any interviewees, the additional amount over the threshold for the rule to apply will reduce from £2,500 to £300 in April 2020, potentially affecting a significant number of self-employed claimants with very volatile income.

Removal of hours-based thresholds

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[2] Bright Blue, "Standing alone", https://brightblue.org.uk/wp-content/uploads/2017/03/StandingAlone2.pdf (2016), 8.
[3] Bright Blue, "Standing alone", p.12.

Under the legacy system, a claimant's eligibility for out-of-work benefits (IS and JSA) and in-work benefits (Working Tax Credit) depends on the number of hours worked. In contrast, claimants can receive UC for any hours worked. The removal of hours-based thresholds for receiving benefits was noted by many interviewees, who explicitly mentioned not having to reach and maintain a specific number of hours. This change was received positively, partly because it was perceived to be enabling greater flexibility in working patterns.

<u>If Universal Credit does not adequately reflect the lived experiences of low-paid workers, how should it be reformed?</u>

To address the issues we have identified in relation to this inquiry, we suggest the following recommendations on improving Universal Credit.

All new claimants of UC should receive a one-off upfront 'helping hand' payment.

We recommend that all new UC claimants should be offered a one-off 'helping hand' payment of equal to at least 25% of their estimated initial UC award. This 'helping hand' would be paid as soon as possible after successfully registering on UC to the claimant's chosen bank account, would be non-repayable, and could only be received once by a claimant over a long time period. This one-off 'helping hand' payment will help to alleviate the financial impact of the delay for the initial UC award.

Enable claimants, through their online accounts to and personalise the default frequency and destination of their future UC awards.

Upon first claiming for UC, claimants should be automatically enrolled into the default positions: monthly payments, a single payee, and all money paid directly to them. Through their online accounts, claimants should be granted the power to change the frequency and distribution of their UC. This would enable claimants to have control to over how they receive their UC awards, allowing them to modify frequency of payments to fit the way they receive other income and budget for expenses.

Extend the 12-month exemption from the Minimum Income Floor (MIF) for self-employed UC claimants, so a further separate 12 months of exemption can be claimed at any point in their lifetime while an individual is on UC, after approval from a claimant's work coach.

While the MIF serves an important purpose, it fails to recognise that even established, profitable forms of self-employment regularly generate a fluctuating income. Income volatility is a marked feature of self-employment, especially seasonal businesses. we recommend that UC claimants are given an additional but separate 12 months' exemption from the MIF. Self-employed claimants will be able to choose which months the exemption will apply. They will determine the months for any point in their lifetime when they are on UC. To ensure that UC is not used to prop-up unprofitable businesses, this exemption should only be granted if approved by the work coach.

About Bright Blue

Bright Blue is an independent think tank that champions liberal conservatism. Our work is guided by five research themes: social reform; immigration and integration; ageing society; green conservatism; and human rights. We were shortlisted for the 2016, 2017 and 2018 and 2019 UK social policy think tank of the year and UK environment and energy think tank of the year in the prestigious Prospect Magazine annual awards.

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