



Universal Credit: a preliminary analysis

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Background

- Universal Credit will be a substantial welfare reform, integrating all means-tested benefits and tax credits for working-age adults
- Fast-moving policy area
 - Consultation over the summer
 - Spending Review: £2bn to pay for introduction
 - White Paper in November 2010
 - Welfare Reform Bill in February 2011
 - Universal Credit to begin in 2013
- Government's view based on Centre for Social Justice report
 - Mirrlees review of tax system recommended integrating benefits and tax credits
(<http://www.ifs.org.uk/mirrleesreview/dimensions/ch2.pdf>)

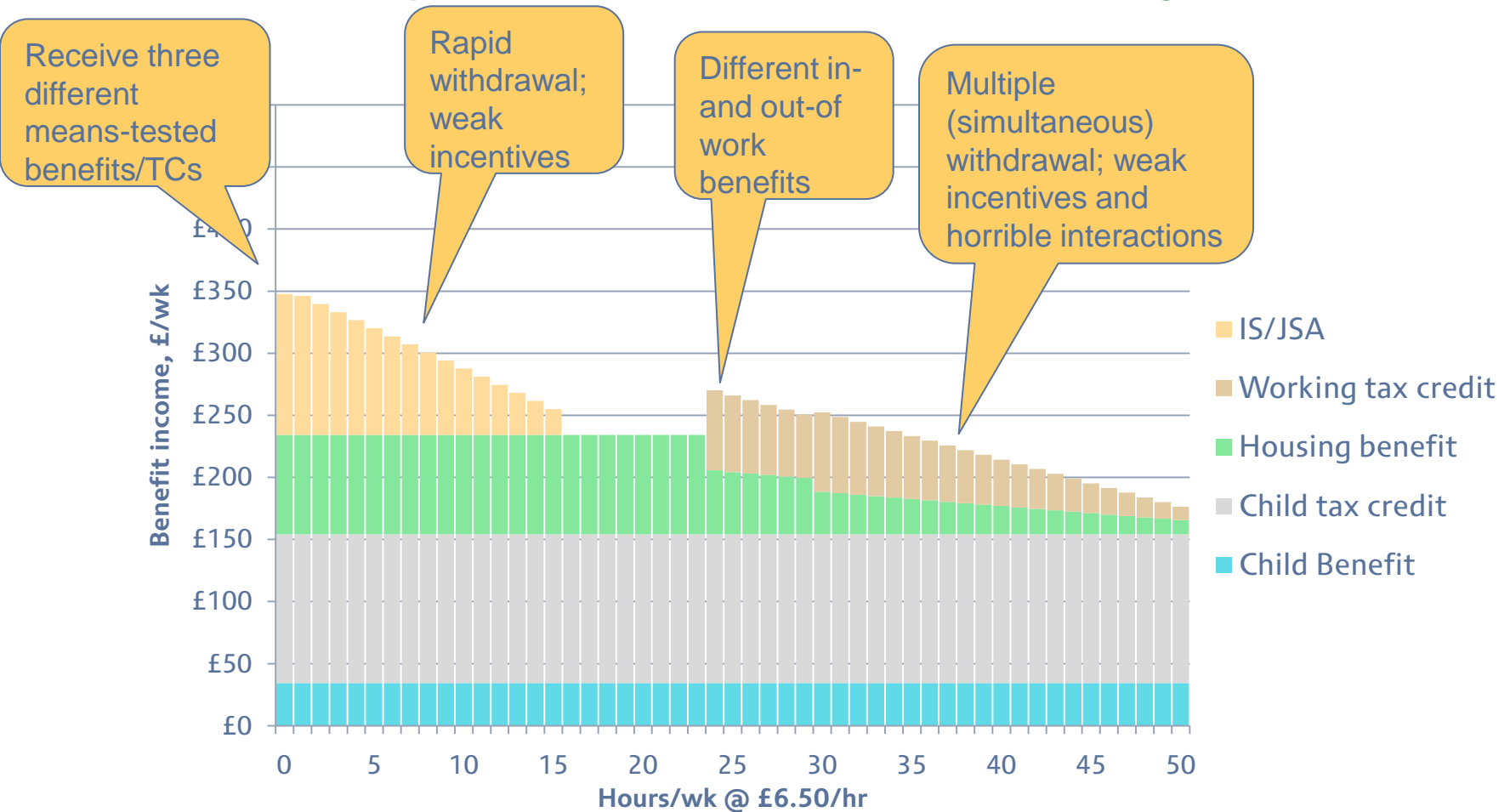
Outline

- What is Universal Credit
 - Government's objectives
 - How will it work?
- Our new empirical work
 - Winners and losers, and cost to government
 - Work incentives
- Not covering administration, operational details, conditionality or impact on poverty
- Based on details in White Paper, and is a preliminary assessment
 - Some of this analysis now redundant given Impact Assessment for WR Bill

What is Universal Credit?

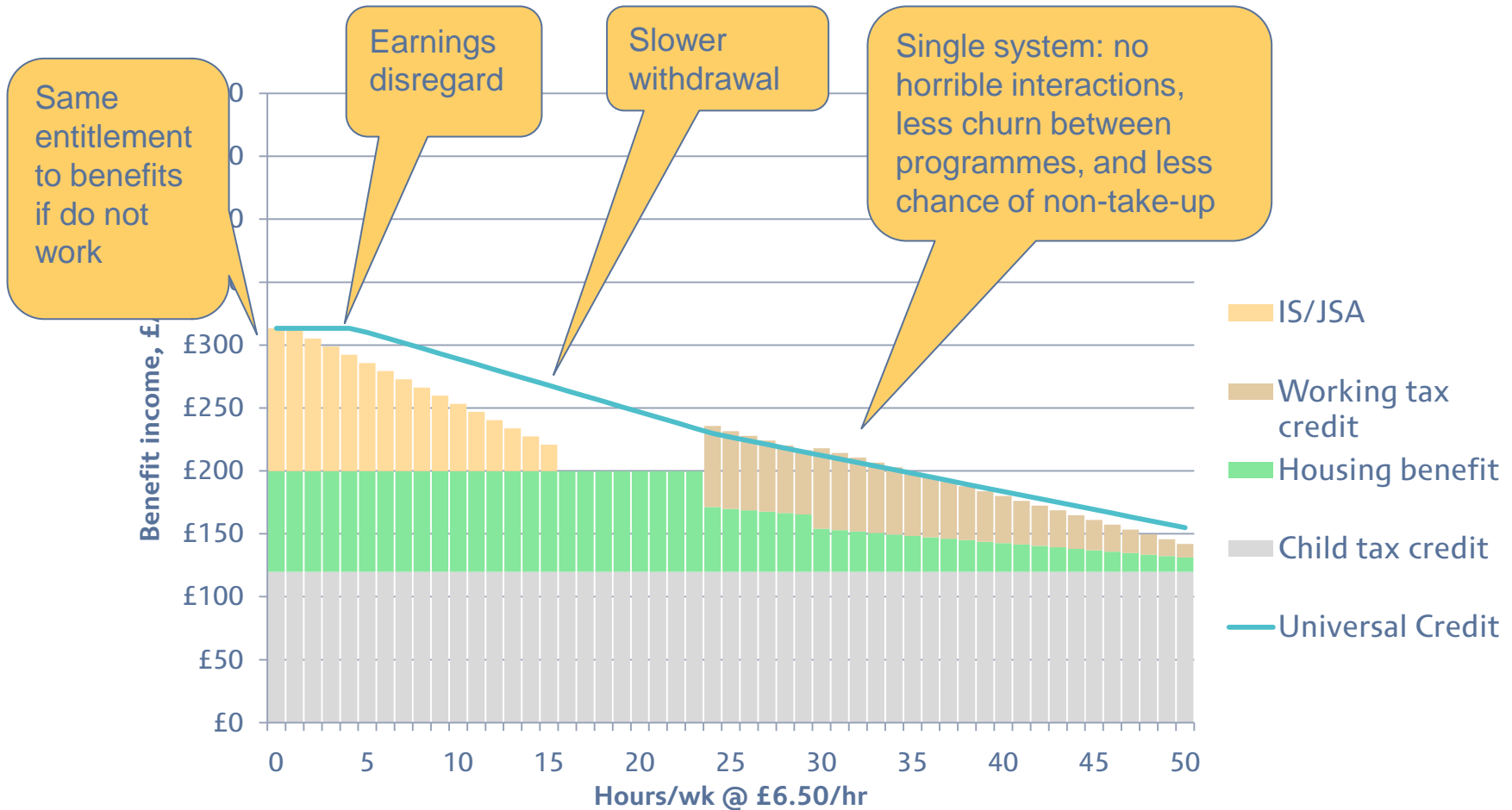
- Universal Credit is a means-tested benefit, based on family income, which will replace means-tested benefits and tax credits for working-age adults
 - Replaces Income Support, income-based Jobseeker's Allowance (JSA) and Employment and Support Allowance (ESA), Housing Benefit, Child Tax Credit, Working Tax Credit
 - Unclear what will happen to Council Tax Benefit
 - Pension credit not replaced
 - Administered by DWP, and paid monthly based on previous month's circumstances

Perceived problems with the current system



Assumes: couple with 2 children, 1 earner @ £6.50/hr, £80/wk LHA or eligible rent

The brave new world



Assumes: couple with 2 children, 1 earner @ £6.50/hr, £80/wk LHA or eligible rent. Ignores child benefit.

How is Universal Credit calculated

- Calculate maximum entitlement
- Calculate size of earnings disregard
- Calculate earned income, unearned income and imputed income from capital
- Calculate final award

Universal Credit: calculating maximum entitlement

Universal Credit	Current system	Example: couple, 2 children, LHA rate of £80/wk
Personal amount		
Child additions		
Housing addition		
Disability or carers addition		

Universal Credit: calculating maximum entitlement

Universal Credit	Current system	Example: couple, 2 children, LHA rate of £80/wk
Personal amount	Income support/ jobseekers allowance	£113.40/wk
Child additions		
Housing addition		
Disability or carers addition		

Universal Credit: calculating maximum entitlement

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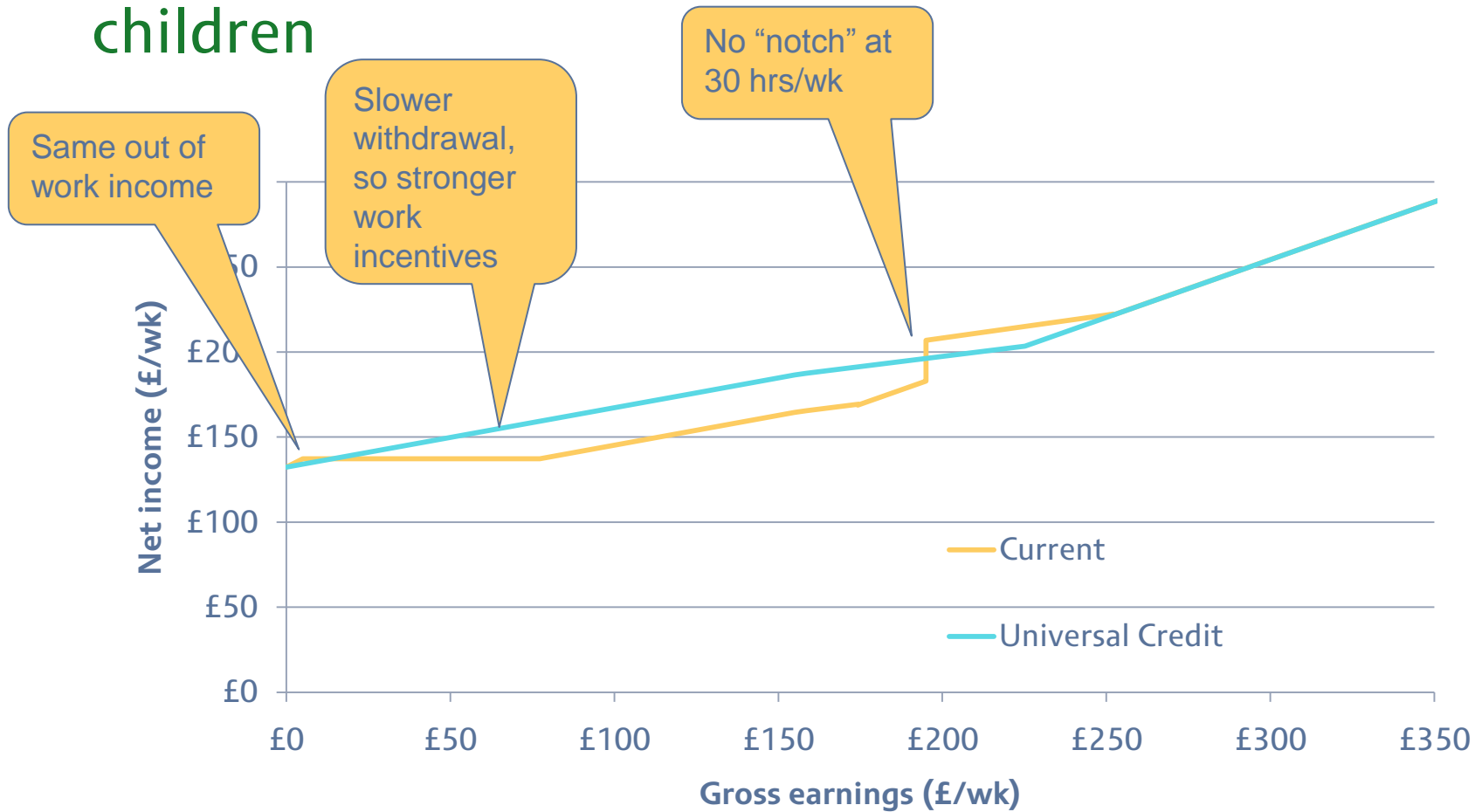
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Personal amount	Income support/ jobseekers allowance	£113.40/wk
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Housing addition	Housing benefit	£80/wk
Disability or carers addition	Disability premia in means-tested benefits	£0/wk

How is Universal Credit withdrawn as income rises?

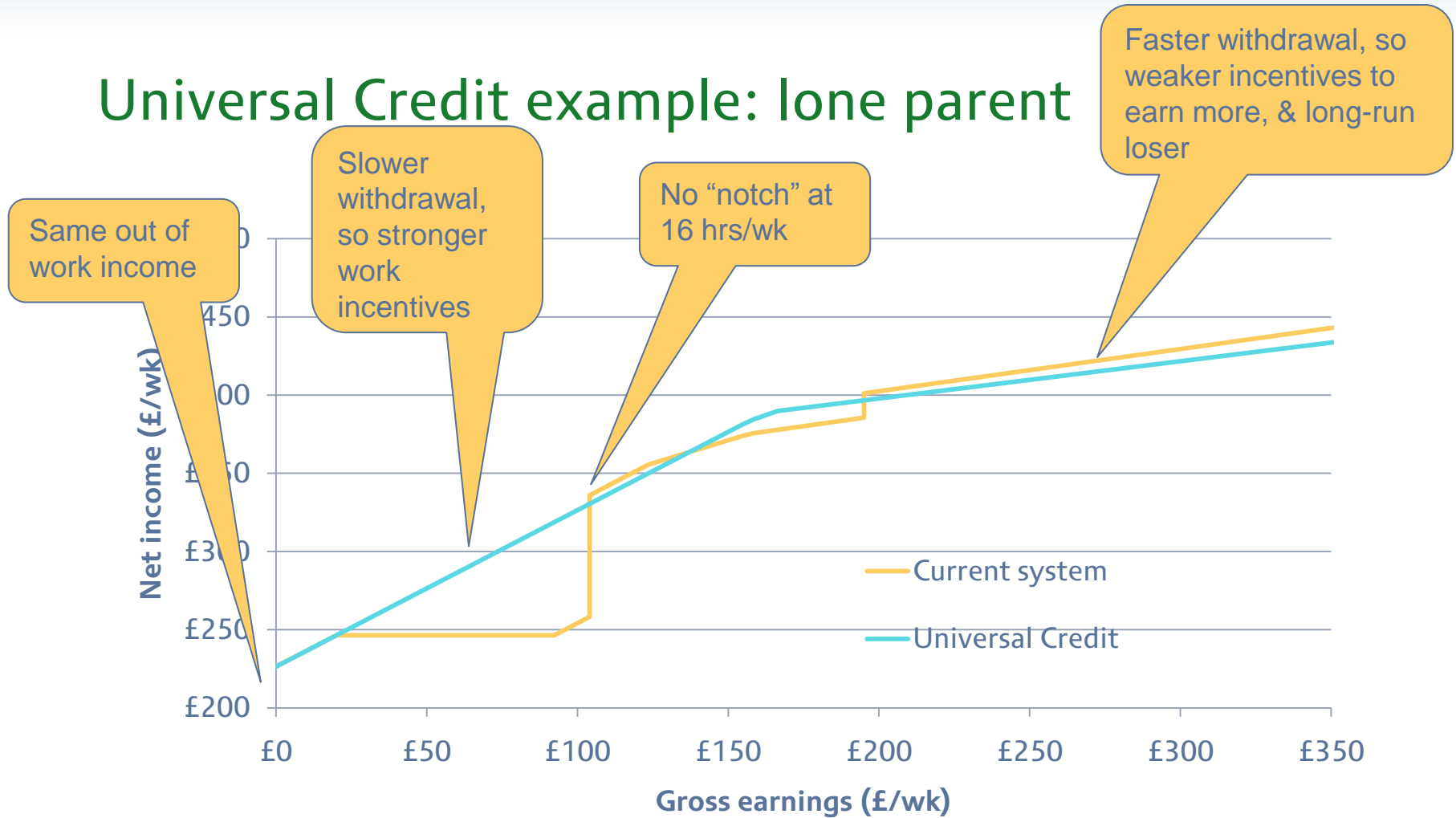
- Net-of-tax earned income subject to 65% withdrawal rate
 - **Lower** withdrawal rate than out-of-work means-tested benefits, so extends further up earnings distribution (and means WTC not needed)
 - **Higher** withdrawal rate than tax credits (65% of net earnings is greater than 41% of gross earnings)
 - The earnings disregard depends on family type & housing costs
- Unearned income (including income from some other benefits) subject to 100% withdrawal rate with no disregard
 - **Same** withdrawal rate as out-of-work means-tested benefits
 - **Higher** withdrawal rate than tax credits (100% is greater than 41%)
- Income from savings is imputed and capital rules mean those with savings > £16,000 get nothing
 - **Same** rules as out-of-work means-tested benefits
 - **Much harsher** than tax credits: £16,000 of savings would reduce tax credit eligibility by £1.42/wk

Universal Credit example: single adult, no children



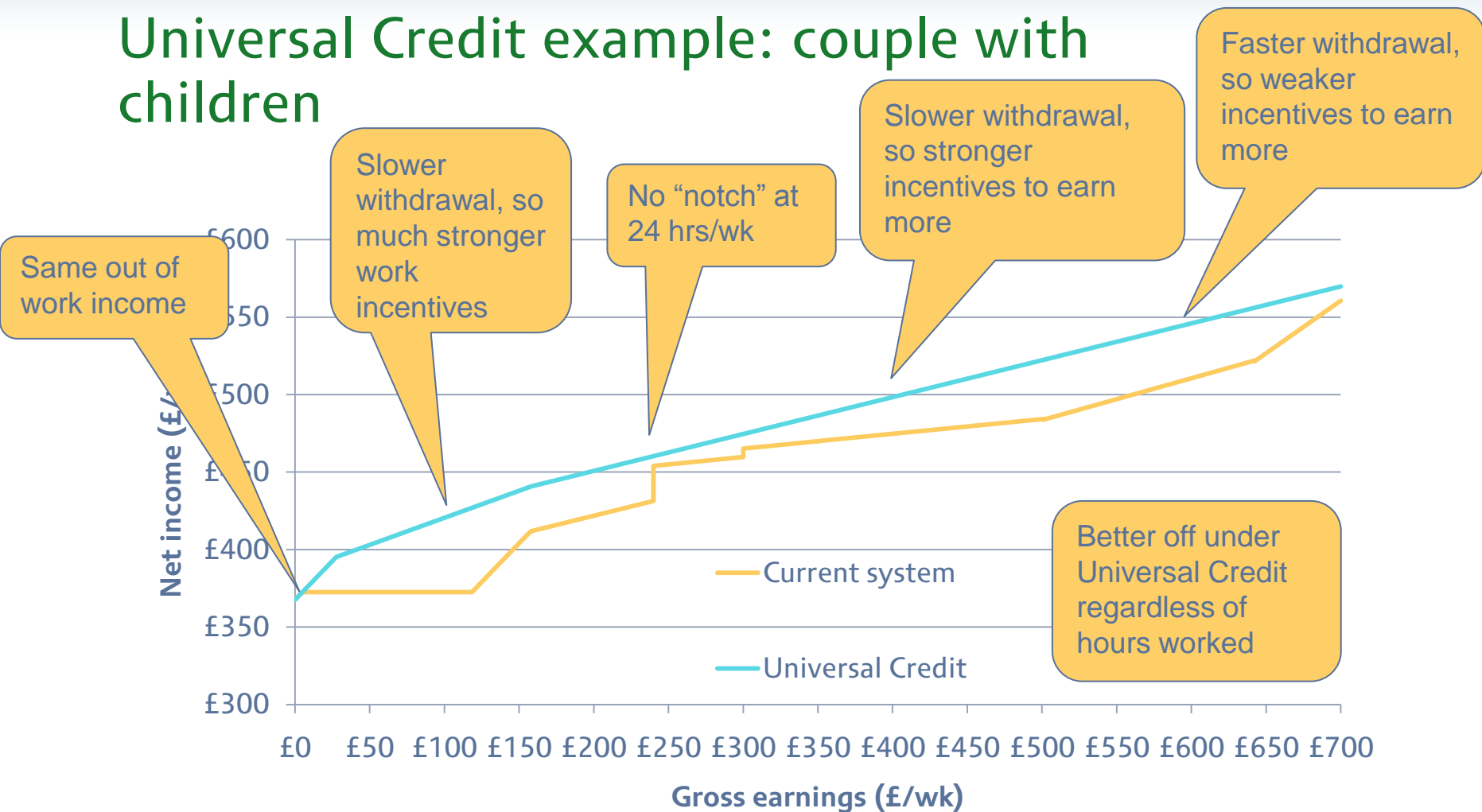
Assumes: £6.50/hr, £60/wk LHA or eligible rent

Universal Credit example: lone parent



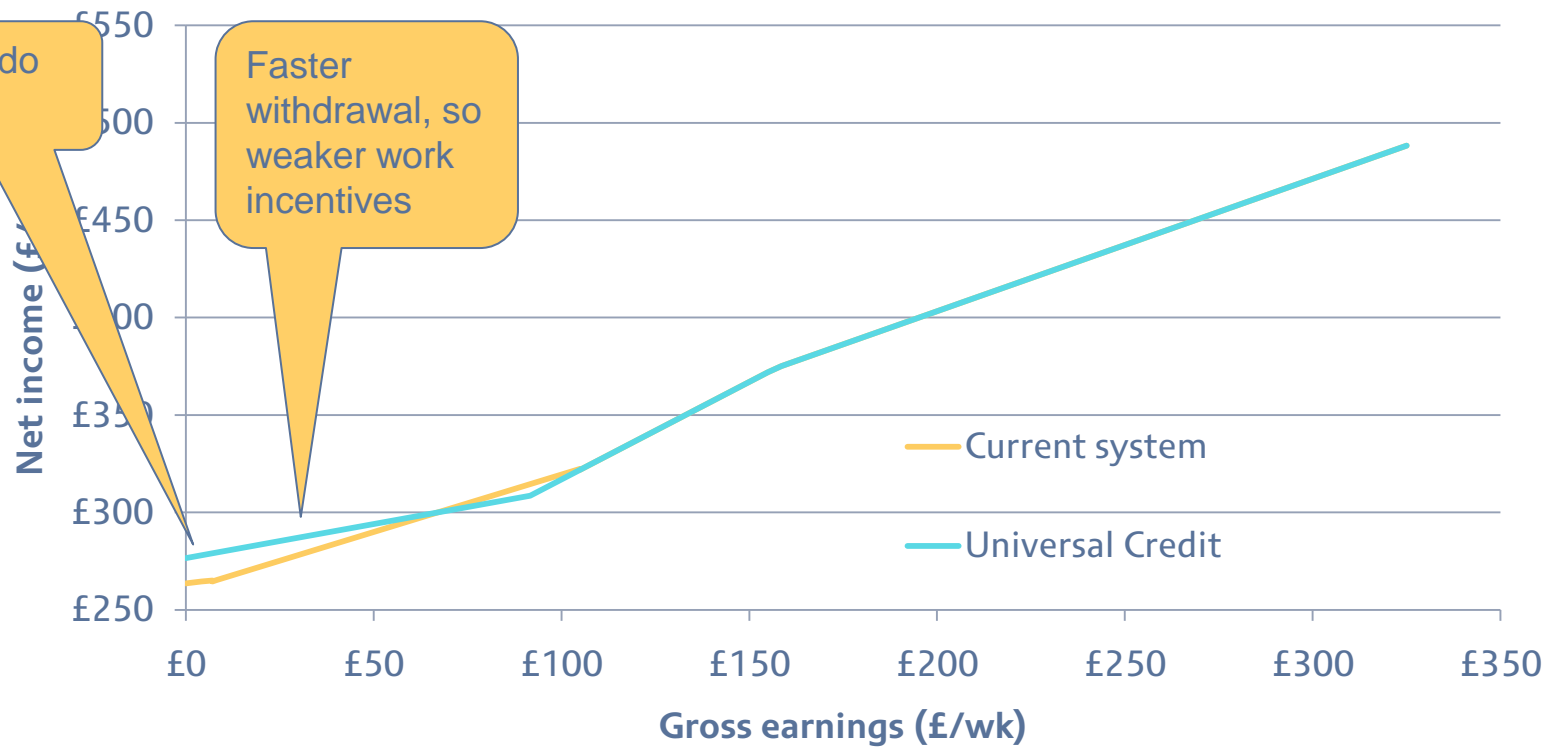
Assumes: 2 children, £6.50/hr, no rent

Universal Credit example: couple with children



Assumes: £10/hr, £100/wk LHA or rent

Universal Credit example: 2nd earner in couple without children



Assumes: Main earner on £245/wk, 2nd earner on £6.50, £80/wk LHA or rent

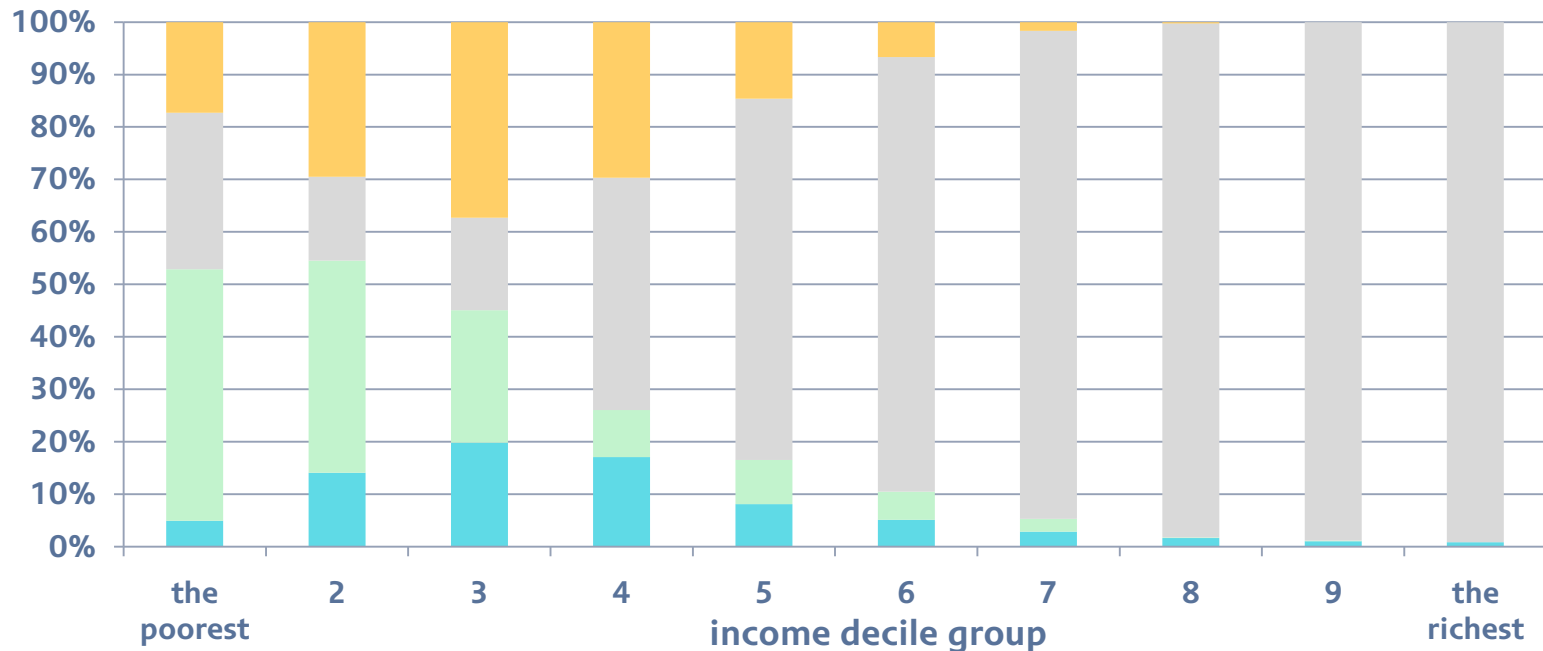
Timetable for transition

From October 2013	No new claims of out-of-work benefits: will claim Universal Credit instead Families leaving out-of-work benefits will claim Universal Credit
From April 2014	No new claims of tax credits: will claim Universal Credit instead
April 2014 to October 2017	Remaining claimants of benefits and tax credits moved to Universal Credit Transitional protection: families protected in cash-terms at point of transition while circumstances unchanged

Winners and losers

- 2.5 million working-age families will gain
- 1.4 million will lose out in the long run
- 2.5 million will receive as much payment as they do under the existing system
- Cost (given our assumptions)
 - Total gain of the winners is £3.6 billion per year
 - Total loss of the losers is £1.9 billion per year (ignoring transitional protection)
 - Long-run cost of £1.7 billion per year (WR Bill says £2 bn)
 - Short-run cost depends on how families are moved across and nature of transitional protection

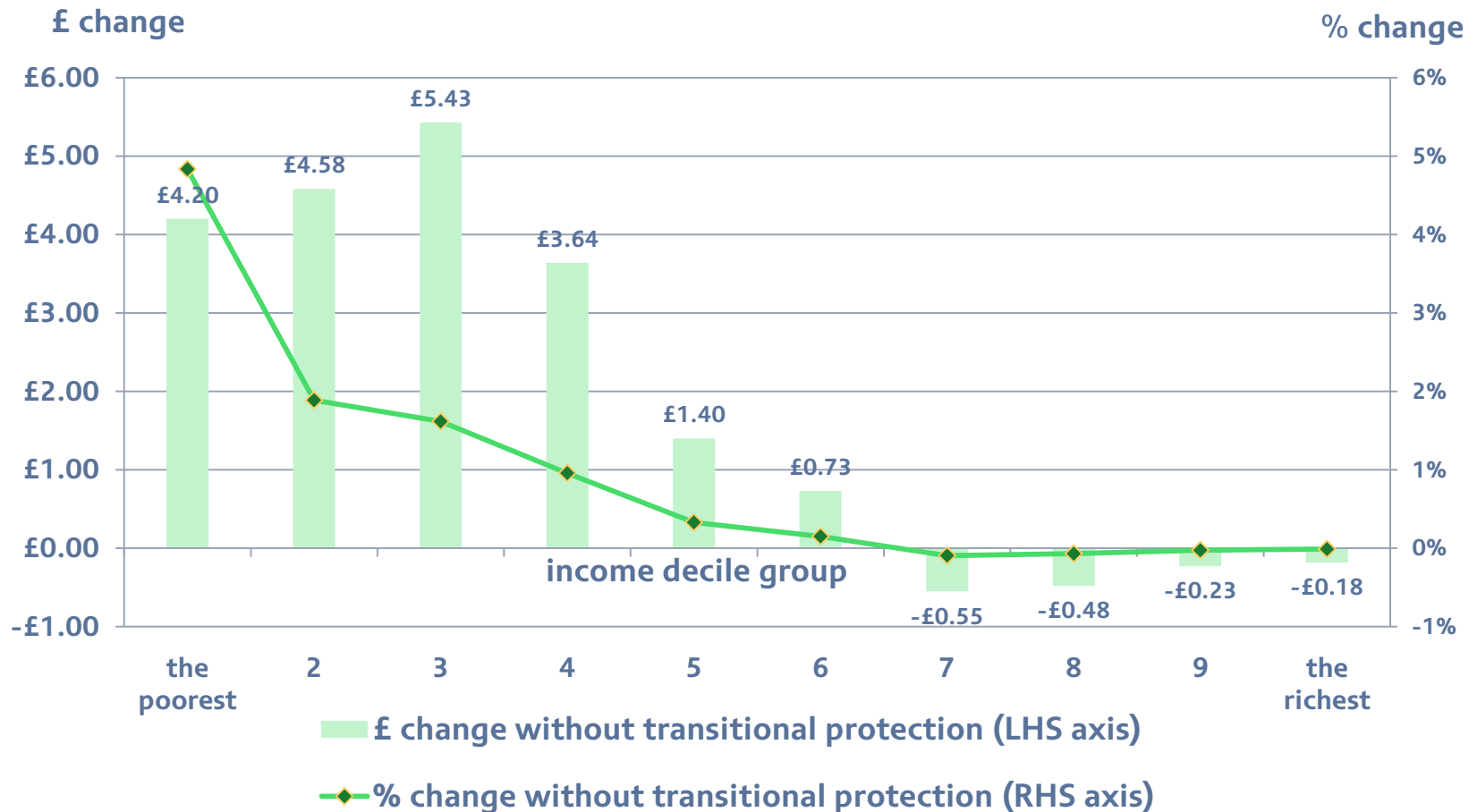
Winners and losers from Universal Credit



- loser (ignoring transitional protection)
- not affected because UC entitlement matches current entitlement to MTBs and TCs
- not affected and currently not receiving any means-tested benefits or tax credits
- winner

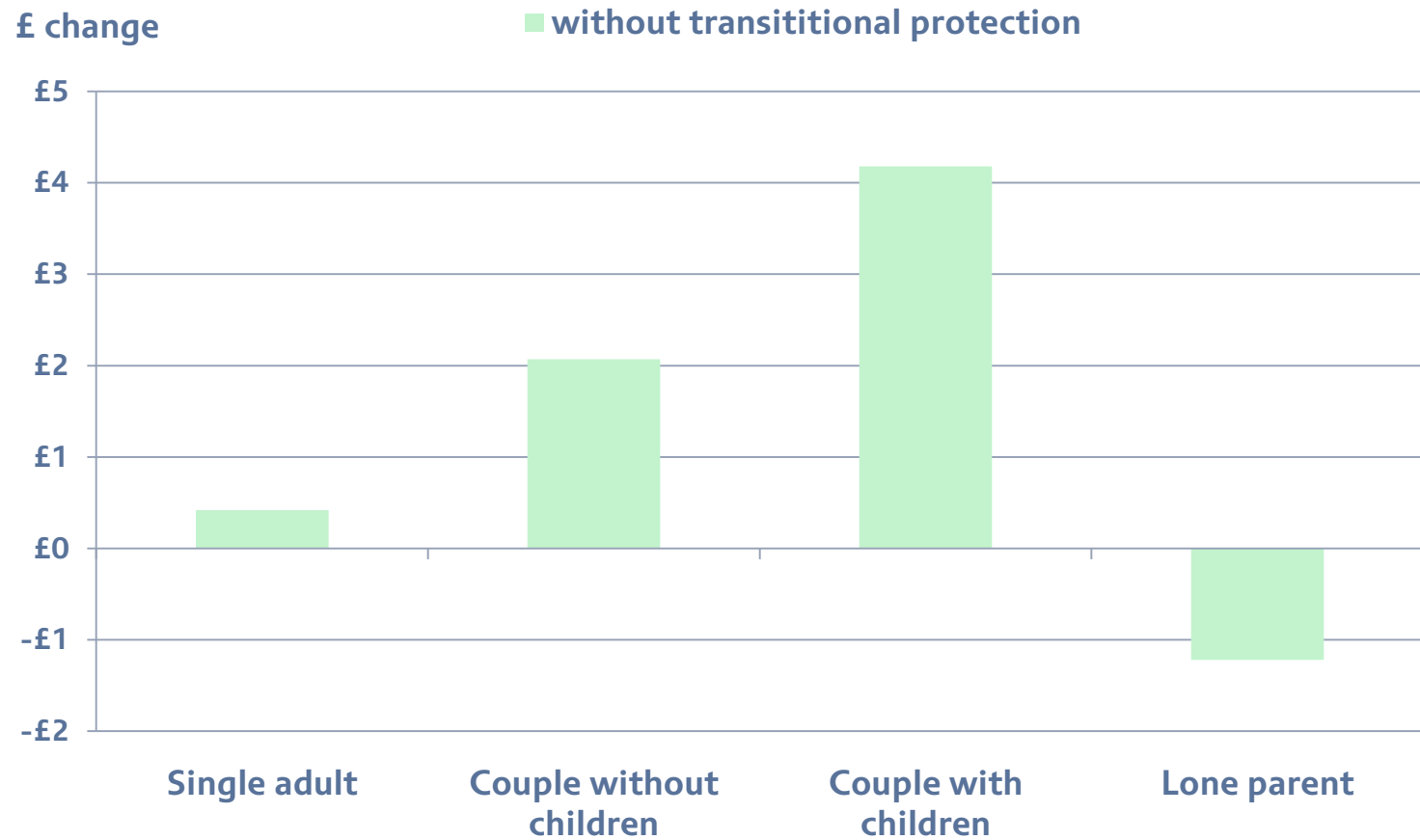
Notes: Income decile groups are based on equivalised family income using the McClements equivalence scale.
 Source: Authors' calculations using the IFS tax and benefit microsimulation model, TAXBEN, run on uprated data from the 2008–09 Family Resources Survey.

Change in income by income decile group



Notes: Income decile groups are based on equivalised family income using the McClements equivalence scale.
 Source: Authors' calculations using the IFS tax and benefit microsimulation model, TAXBEN, run on uprated data from the 2008–09 Family Resources Survey.

Change in income by family type



Change in income by family type and employment status (without transitional protection)

<i>Family type</i>	<i>Number of adults in work</i>	<i>Fraction of that family type</i>	<i>Change in income, %</i>
single adults	1	73%	0.1
	0	27%	0.4
couples without children	2	76%	<0.1
	1	19%	1.0
	0	6%	0.5
couples with children	2	61%	<0.1
	1	33%	1.7
	0	6%	-0.9
lone parents	1	56%	0.1
	0	44%	-1.0

•Personal amount under UC > WTC
•Gain from earnings disregards

Unearned income to be treated more harshly under UC than under CTC

Effect of Universal Credit on participation tax rates

- Universal Credit strengthens the incentive for single individuals to do low-paid work
- Universal Credit particularly strengthens the incentive for couples to have one person in work rather than none...
- ... but weakens the incentive for both members of a couple to work, rather than just one
- Why?
 - Universal Credit gives more support to single-earner couples than the current system, but this extra support is taken away more quickly when the second earner moves into work

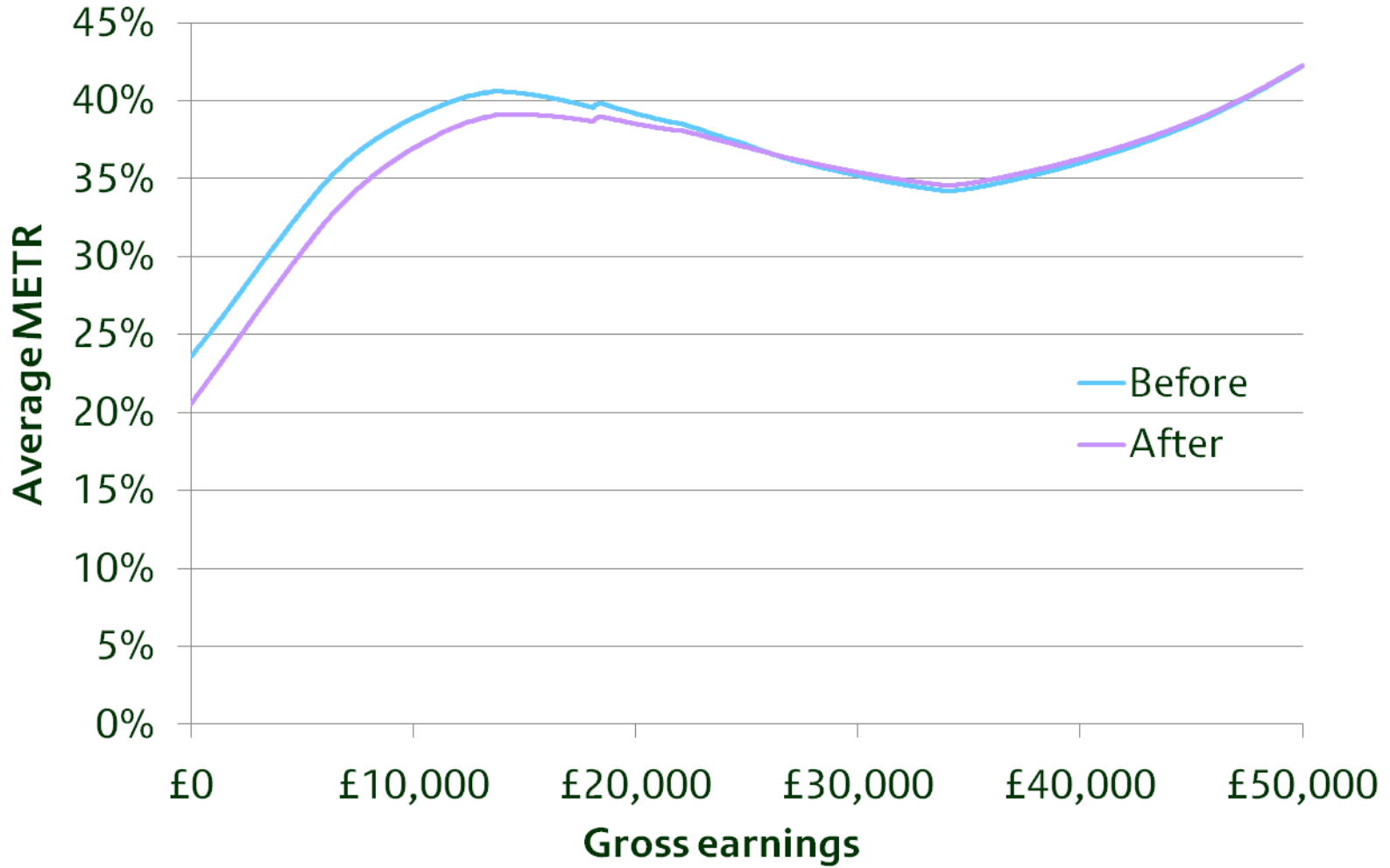
Changes in METRs among workers

- Around 1.7 million workers see their METRs fall, in particular
 - 600,000 see METR fall from between 77% and 96% to 76.2%
 - Taxpayers who face withdrawal of multiple benefits under the current system
 - 350,000 see METR fall from >80% to 65%
 - Non-taxpayers who face withdrawal of multiple benefits or an out-of-work benefit in the current system
 - 400,000 see METR fall from more than 70% to around 32%
 - Taxpayers who lose entitlement to tax credits
 - 200,000 see METR fall to zero
 - Second earners in couples who lose entitlement to benefits and tax credits

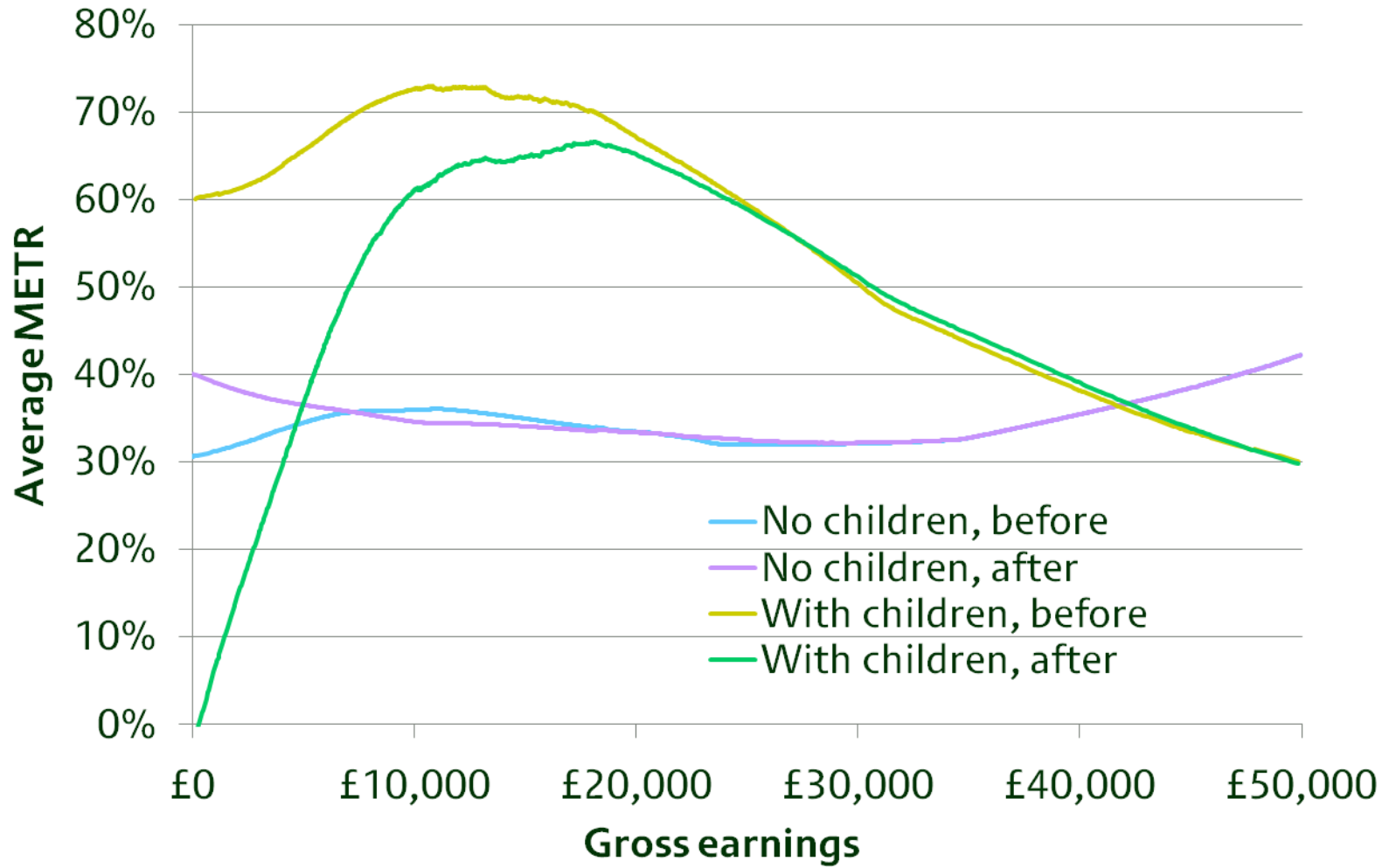
Changes in METRs among workers

- Around 1.8 million see their METRs increase, in particular
 - 900,000 see their METRs increase from 73% to 76.2%
 - Withdrawal rate of Universal Credit is higher than that for tax credits alone
 - 300,000 see their METRs increase from 32% to 76.2%
 - Taxpayers who become entitled to Universal Credit
 - 350,000 see their METRs increase from 0% or 41% to 65%
 - Second earners in couples who face withdrawal of Universal Credit, but are non-taxpayers

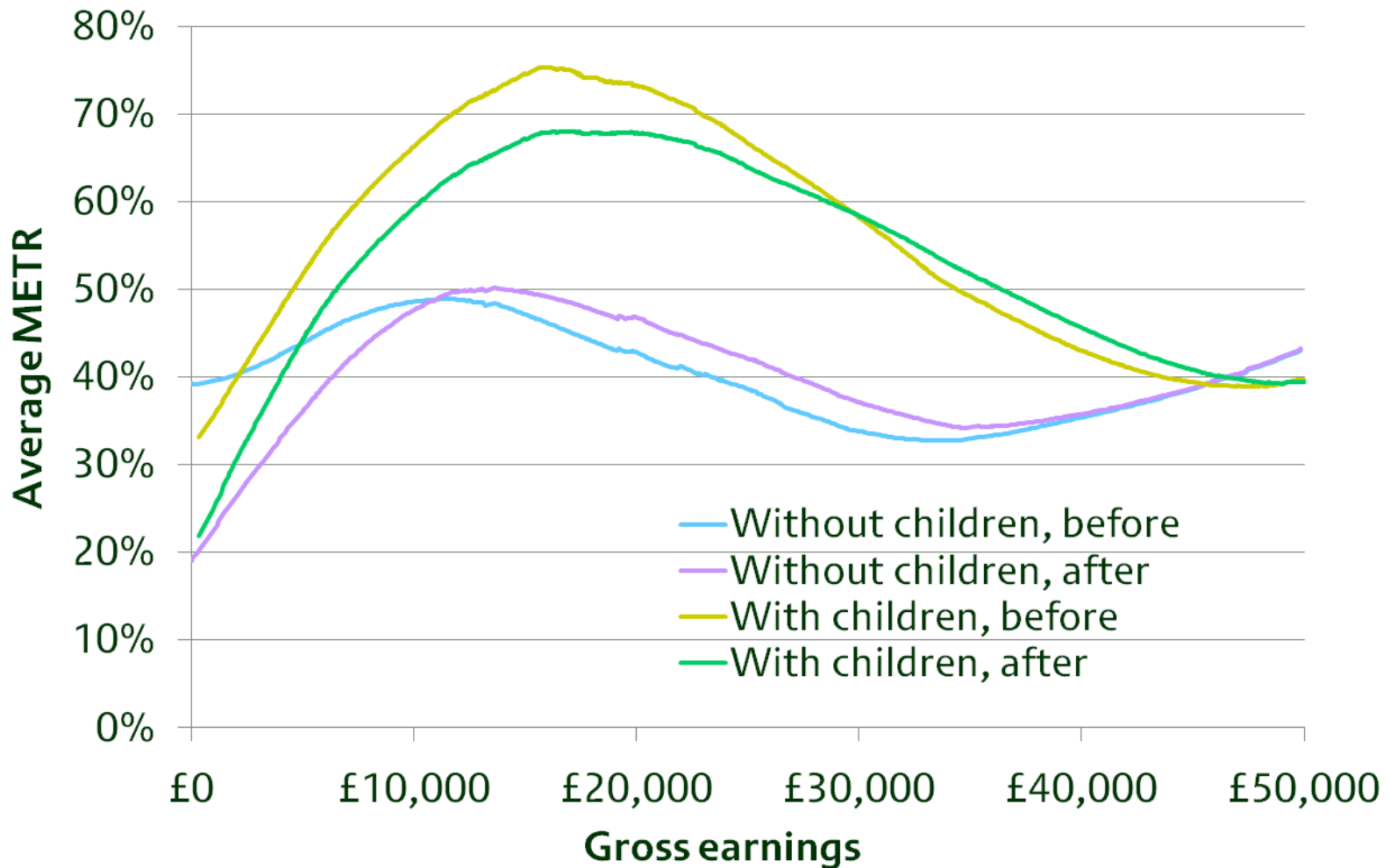
Average METRs by earnings



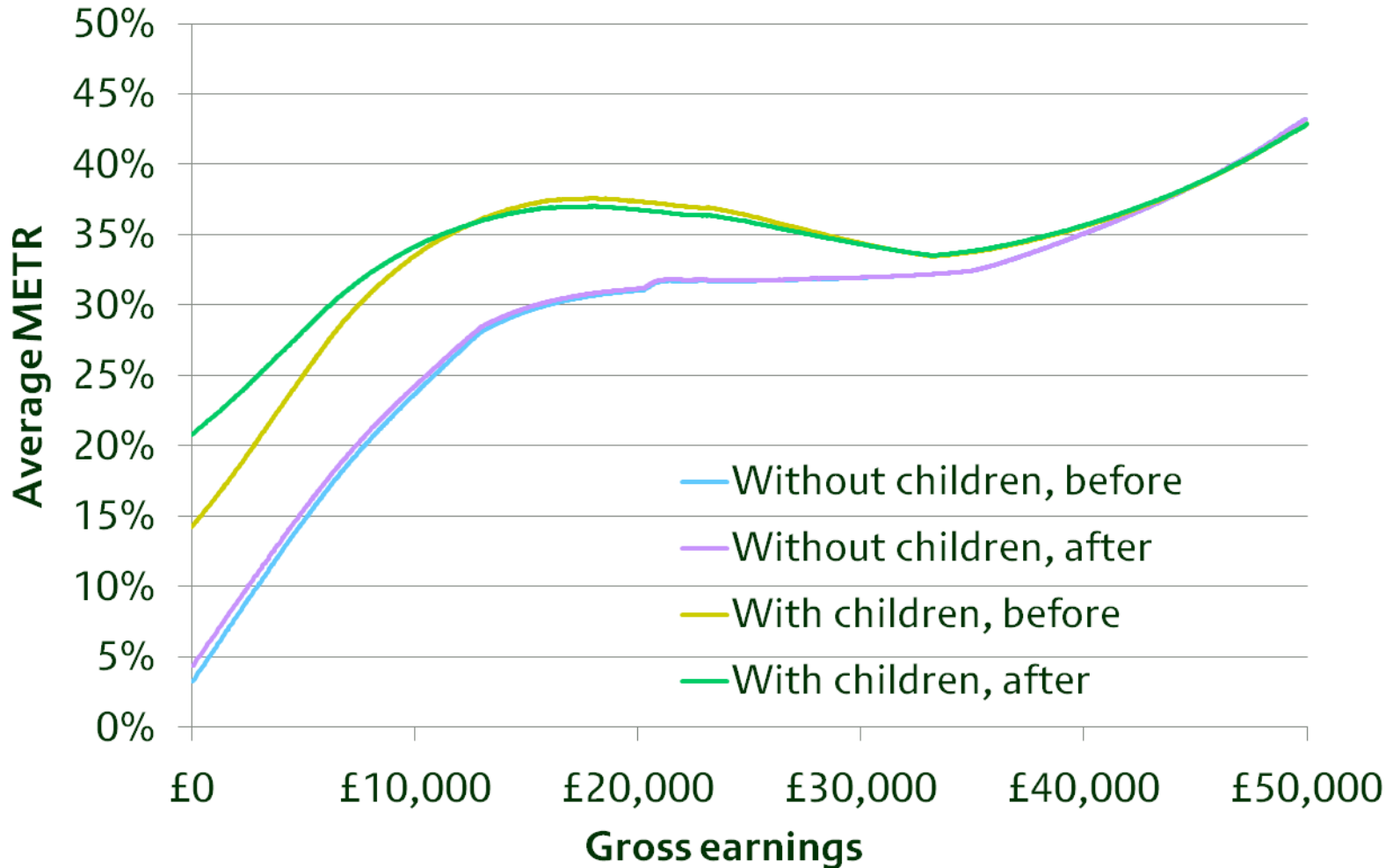
How does this vary by different types of worker? – single individuals



How does this vary by different types of worker? – single earner couples



How does this vary by different types of worker? – two-earner couples



Summary: impact on family incomes

- 2.5 million winners, 1.4 million losers, and 2.5 million not affected
- Cost £1.7 bn a year in the long run (or without transitional arrangements)
- Across the income distribution
 - Bottom six-tenths will, on average, be better off, with a progressive pattern. The richer ones will lose slightly on average.
- Different family types
 - Couples will fare better than single people
 - Lone parents will lose, on average, in the long run;
 - Couples with children have the highest average gain
 - But substantial differences in impact within each family type
- No simple explanation for pattern; reflects parameters chosen by government for Universal Credit

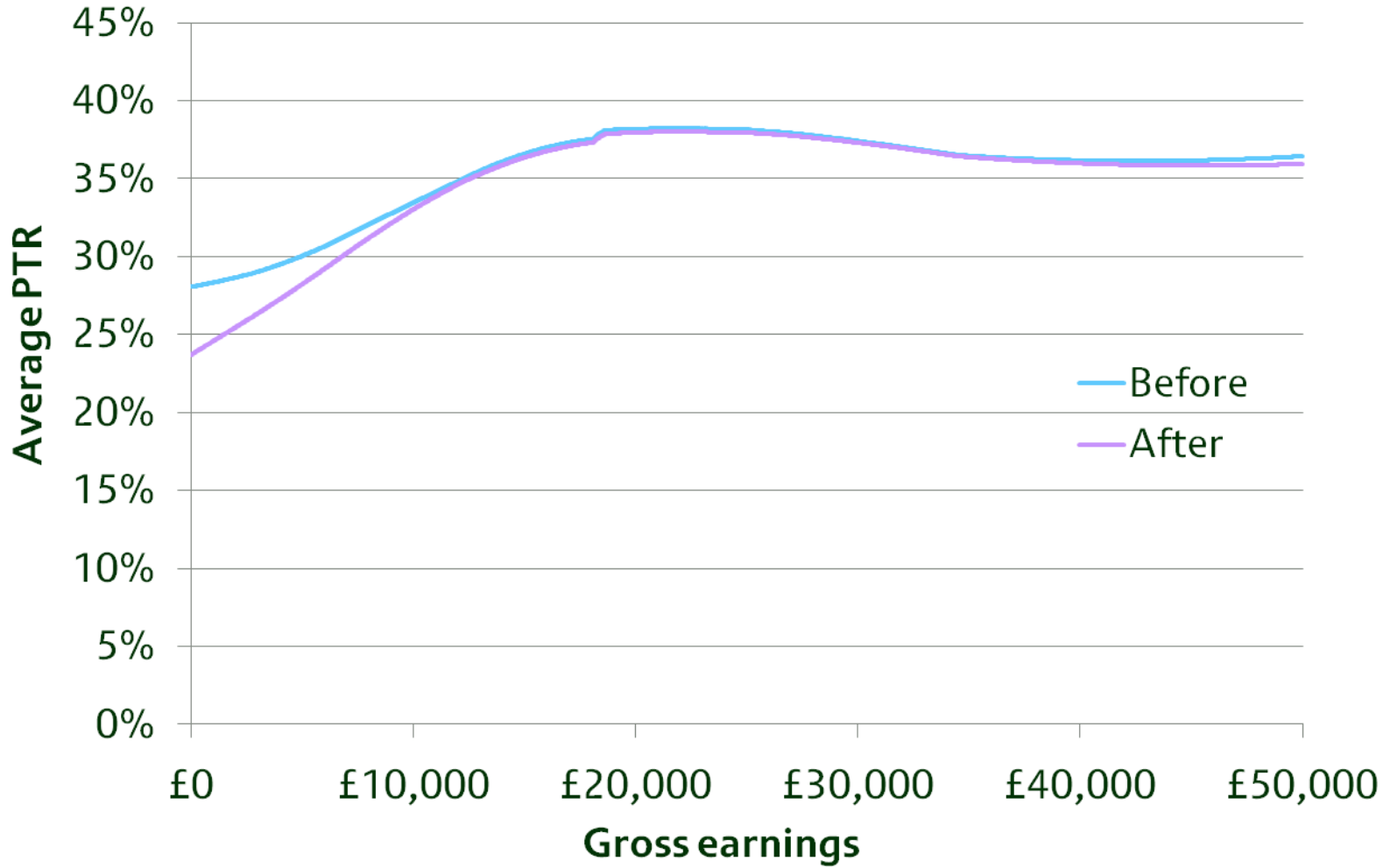
Summary: impact on work incentives

- Incentive to work for low earnings stronger under Universal Credit for single people and those in couples whose partner doesn't work
 - Higher earnings disregard and lower withdrawal rate than current out-of-work benefits
 - These individuals have the weakest work incentives under the current system
- However, Universal Credit will weaken incentive for couples to have both members in work rather than just one
 - This is because it will have a higher withdrawal rate than current tax credit system
- Similarly, those with weakest incentives to increase earnings at the moment (low earners with children) will see METRs reduced...
- ...but METRs increase slightly for those on higher earnings and for low-earners in 2-earner couples

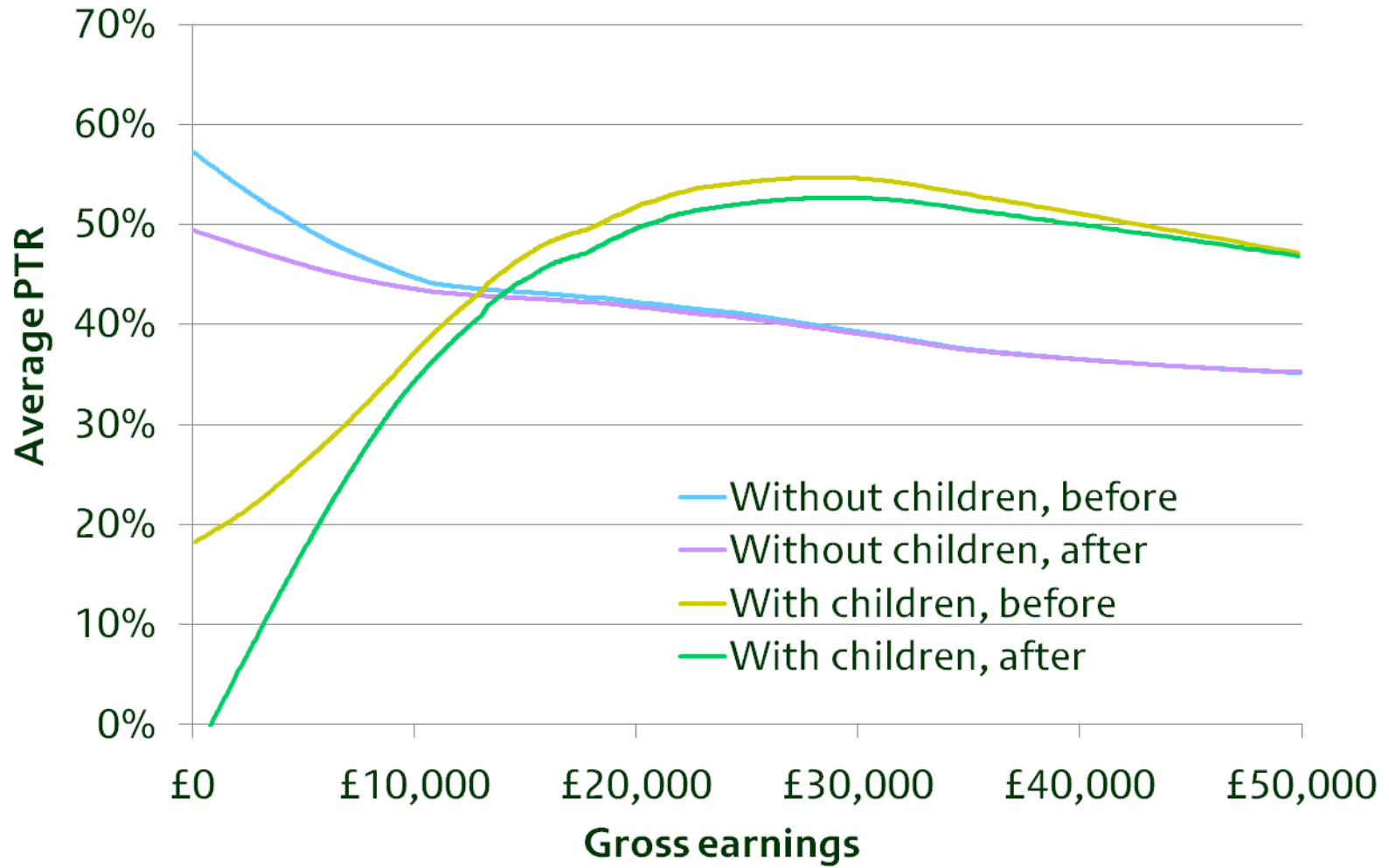
Concluding thoughts

- Many details unresolved, or unclear, in White Paper
- Some thorny policy issues include
 - Council tax benefit: inside or outside Universal Credit, and how to localise?
 - Childcare element of working tax credit: how to replace?
- Decisions also needed on
 - conditionality: who is subject, and how much Universal Credit to sanction
 - in-kind passported benefits
 - support for mortgage interest
 - disability additions
 - rates for students and those under 25

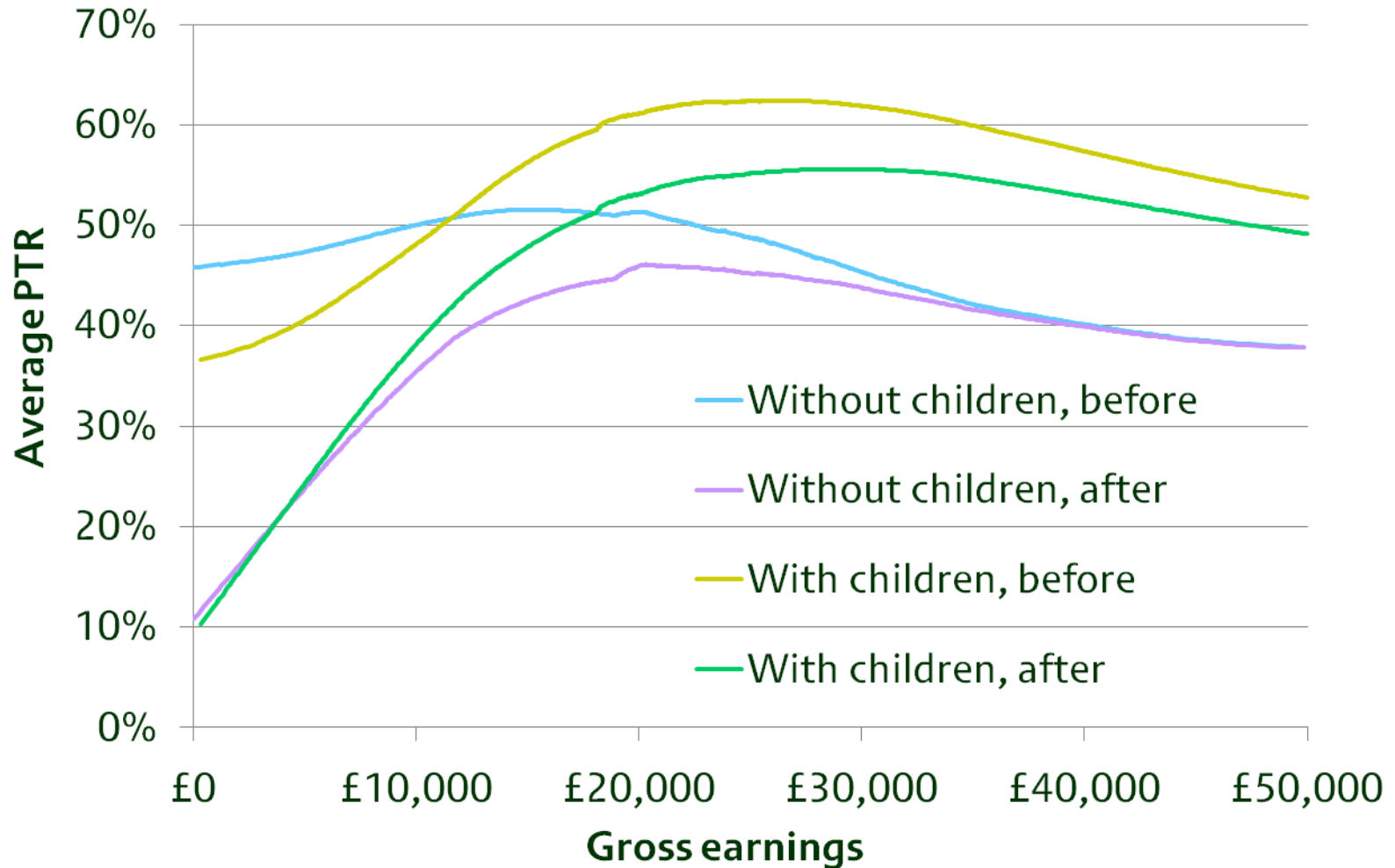
Average PTRs by earnings



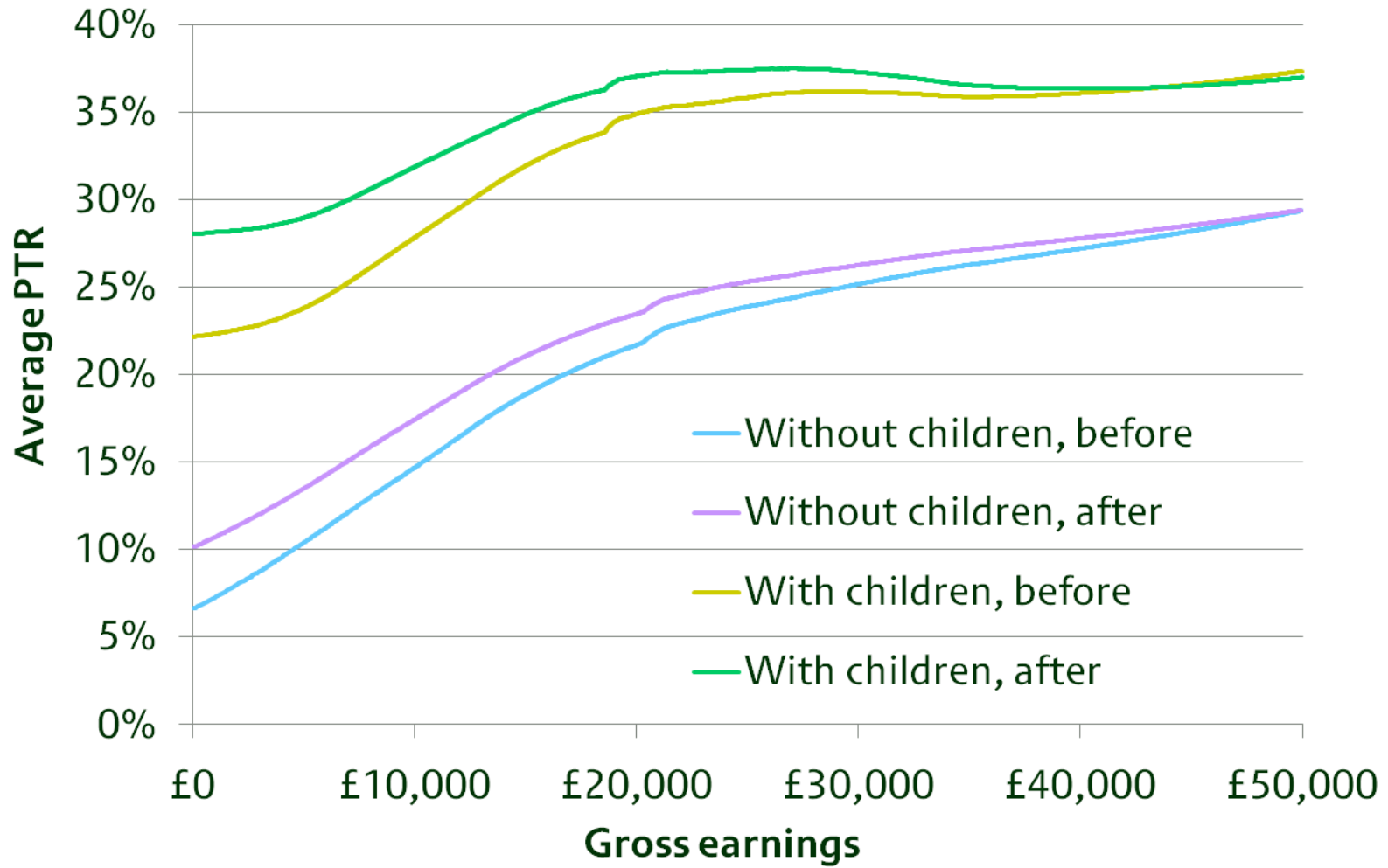
How does this vary by different types of individual? – single individuals



How does this vary by different types of individual? –in couple, partner doesn't work



How does this vary by different types of individual? –in couple, partner works



Universal Credit: full example of withdrawal

- Couple with 2 children, earning £400/wk, renting at £80/wk, savings of £10,000

Calculate maximum entitlement	
Calculate earnings disregard	
Calculate net earnings	
Calculate imputed income from capital	
Final calculation:	

Universal Credit: full example of withdrawal

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Final calculation:	$ \begin{aligned} &£313.30 \\ &-£16 \\ &-0.65*(£322.31 - £25) \\ &=£104.05/wk \end{aligned} $