The Austerity Generation: the impact of a decade of cuts on family incomes and child poverty

November 2017

Child Poverty Action Group
30 Micawber Street
London N1 7TB
www.cpag.org.uk

Registered charity number 294841

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Written by Josephine Tucker

Analysis commissioned from the Institute for Public Policy Research was carried out by Carys Roberts and Alfie Stirling. Additional analysis was carried out by Josephine Tucker.

With thanks to Jane Ahrends, Jonathan Bradshaw, Giselle Cory, Lizzie Flew, Alison Garnham, Moussa Haddad, Imran Hussain and Clare McNeil.

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Summary

This report sets out the cumulative effect of a decade of cuts to social security on the incomes of families with children, at population and household level, and subsequent increases in poverty rates. It examines both cuts within the legacy benefit and tax credit system, the introduction of universal credit, and changes to universal credit since it was first introduced.

The losses are alarming, and will damage the life chances of hundreds of thousands of children growing up under austerity. Cuts in both the legacy and universal credit systems will hit families with children harder than any other group across the population. Lone parents with children will be £1,940 a year worse off on average as a result of cuts in the legacy benefit system, and £2,380 worse off as a result of universal credit cuts, compared to what universal credit first promised.

Families already at the greatest risk of poverty will lose most: not just lone parents but families already on low incomes, larger families, families with young children, and families where someone is disabled. Families with four or more children will be more than £4,000 a year worse off because of cuts in the legacy benefit system, and more than £5,000 worse off following cuts to universal credit (compared with its original design). Lone parents, single earner families, families with more than two children and young parents also lose out across the decade in the move from the 2010 tax credits system to today's universal credit.

Cuts to universal credit have substantially reduced the rewards from work for many families. Cuts and freezes to work allowances will leave lone parents worse off by £710 a year on average, and couples £250 a year on average, across the population. They also hit 'just about managing' families in the second and third income deciles particularly hard. In order to make up the losses from work allowance cuts, a couple already working full time on the 'national living wage' would have to work 17 extra days a year, and a lone parent an extra 41 days a year –in effect, a fourteen month year.

A couple with two young children, with one full-time and one part-time earner on the 'national living wage', will be over £1,200 worse off a year as a result of cuts to universal credit. A lone parent with two young children, starting work at 12 hours a week on the 'national living wage', will see their effective hourly wage rate reduced from £5.01 to £4.18 an hour by universal credit cuts.

Cuts in the legacy benefit system will push 700,000 children into poverty (after housing costs) and 500,000 into severe poverty (before housing costs). Cuts to universal credit – which originally promised to lift 350,000 children out of poverty – will now mean a million more children in poverty than under its original design, and 900,000 more in severe poverty.

Failure to uprate benefits in line with inflation will be responsible for 300,000 additional children in poverty under universal credit, with the freeze of the child element alone responsible for 100,000 additional children in poverty. The two-child limit will be responsible for 200,000 children in poverty.

Finally the report examines possible improvements to universal credit which would help restore its poverty-reducing potential, in addition to reversing cuts, as well as additional forms of support for childcare. Restoring the value of children's benefits, and in particular, applying a triple lock, would bring large child poverty gains, while restoring the work allowances, and introducing a second earner work allowance for couples, would boost the incomes of families and help make work pay.

1. Introduction

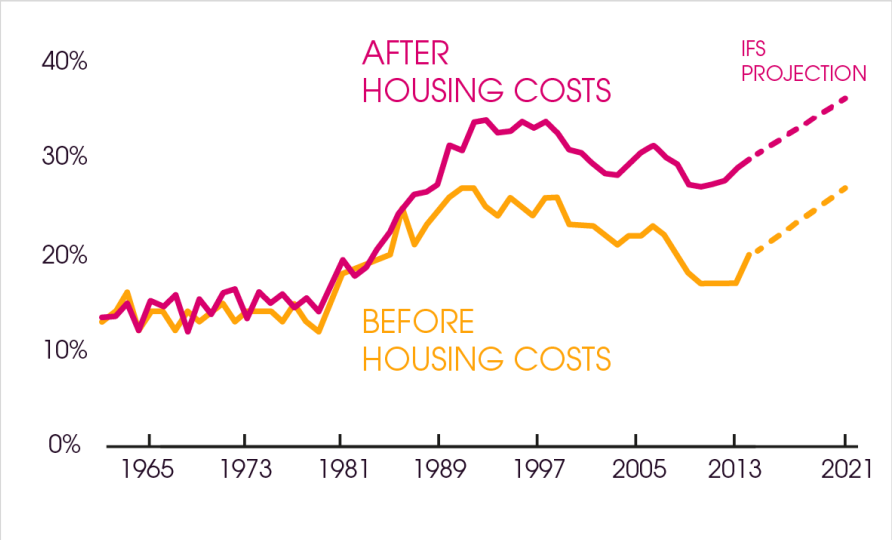
1a. Our intention: to understand the effect of a decade of social security cuts on family incomes and child poverty

This report aims to set out the cumulative effects of a decade of cuts to social security on the incomes of families of different types and with different working patterns. It covers both changes to the tax credit and legacy benefit system since 2010, looking ahead to 2020, and the introduction and subsequent changes to universal credit. The analysis allows us to isolate the effect of specific cuts on family incomes and on child poverty rates. Finally it models the effect of several possible changes to universal credit, in addition to reversing cuts, which could help restore its poverty-reducing potential and improve the rewards from work for parents. Our particular focus is on families with children, and the impact of changes on child poverty.

Our starting point is the social security system inherited by the coalition government when it came to power in 2010. Child poverty was at a 13-year low, at 27 per cent (after housing costs), thanks to policies enacted since the mid-1990s: the introduction of a minimum wage, establishment of a more progressive tax and benefit system, protection and real-terms increases for benefits targeted at children, a childcare strategy, the Sure Start programme, and measures to encourage parental employment, particularly for lone parents. The Child Poverty Act had just been enshrined in law, with cross-party support, committing the new government to further poverty reduction over the coming decade.

However, child poverty instead plateaued for several years and then started to rise, reaching 4 million or 30 per cent of children in 2015/16 (after housing costs), the latest year for which figures are available. Projections indicate that under current policies child poverty will rise to 5.1 million (36 per cent) after housing costs by the end of the Parliament in 2021/22 (Figure 1.1).

Figure 1.1 Actual and projected percentage of children in poverty, 1960s to 2020s



Source: historical data from Department for Work and Pensions, *Households below average income: an analysis of the income distribution, 1994/5-2015/16*, 2017; projections from A Hood and T Waters, *Living standards, poverty and inequalities in the UK: 2016-17 to 2021-22*, Institute for Fiscal Studies, 2017

Throughout this report we will use poverty rates after housing costs unless otherwise stated, as this is the most accurate way to capture the real living standards of those on low incomes.

This study isolates the effect of changes to the social security system. Analysis of incomes and poverty rates is projected to 2020, assuming that all other policies - minimum wage rates, childcare policy and so on - are as we expect them to be in 2020, based on current law and government announcements at the time of analysis in early 2017.

Our purpose in isolating the effect of changing social security policy in this way is to understand clearly the effect of these changes and inform future decisions about the design of the social security system. It also serves to demonstrate just how much has been lost compared with what could have been achieved, had the level of adequacy provided by the 2010 tax credit and benefits systems been retained.

Finally we model a range of improvements to universal credit which could help to prevent and reverse the coming increase in child poverty.

1b. What about the personal tax allowance, 'national living wage' and childcare support?

Our design leaves this analysis open to the charge that it focuses mainly on cuts, and ignores the effect of other measures which directly or indirectly boost family incomes, principally the introduction of the so-called 'national living wage', increases in the personal tax allowance, and the extension of free childcare. However it has been established that these do not come close to compensating for the effect of social security cuts – a conclusion which the government has not challenged.

The IFS calculated that the combined tax and benefit reforms proposed in the 2015 budgets – which included increasing the personal allowance to £12,500 by 2020/21 alongside £13 billion in cuts to social security - would reduce the income of the average household, nationwide, by £455 a year. [1] (Some of the cuts to tax credits were reversed after opposition in the House of Lords, but cuts of a similar nature and scale have been made to universal credit meaning that in the long run the effect on incomes will be similar.)

According to their analysis the average household would lose £470 a year from benefit changes in the legacy (tax credit) system, a further £5 from the introduction of universal credit, and £70 from changes to indirect taxation (e.g. tobacco duty and insurance premium tax), while gaining £89 from changes to direct taxes.

Not only are the gains from direct tax changes much smaller than the losses from benefit cuts, but they do not, in general, accrue to poorer households. The overall effect is that households in lower income deciles will see the greatest reductions in income, with the bottom decile losing almost £750 a year (around 6 per cent of their net income) and the second decile losing more than £1,250 a year (more than 7 per cent of their net income), while the second richest decile made a net gain.

As the IFS noted, 'many poorer households do not pay income tax in the first place and so do not benefit from increases in the personal allowance. Moreover, higher rate taxpayers gain more than

[1] J Browne, *The Impact of Proposed Tax, Benefit and Minimum Wage Reforms on Household Incomes and Work incentives,* Institute for Fiscal Studies, 2015.

basic rate taxpayers from the government's changes to income tax as a result in increases in the higher rate threshold'.

Analysis by the Resolution Foundation of tax and benefit changes introduced in 2017/18 (when many of the cuts announced in 2015 took effect) tells a similar story, showing that households in the top half of the income distribution stand to make a net gain – with the greatest gains going to the richest ten per cent – while the bottom three deciles would see losses.[2]

The introduction of the 'national living wage' also has a limited effect in offsetting the effect of cuts. The IFS noted that overall the 'national living wage' would compensate for just over a quarter (27 per cent) of the losses from tax and benefit changes.[3] The increased income expected to go into workers' pockets from the 'national living wage' is around £4 billion, set against around £13 billion in cuts to social security since 2015 alone. Furthermore, the largest cash gains from raising the minimum wage go to households in the middle of the income distribution, partly because those who do not work at all cannot benefit from changes in wages and also because many people who saw their wage increased have higher-earning partners. For households in the poorest twenty percent of the population, the 'national living wage' compensates on average just 6 per cent of losses from the cuts to benefits announced in 2015. This does not even consider the cuts already made between 2010 and 2015.

Neither the personal tax allowance changes nor the 'national living wage' are targeted at families with children, and they are of most benefit to people well above the poverty threshold. The extension of free childcare will bring substantial benefits to some households, but again the government spend on this offer pales in comparison with cuts to benefits that support families with children. The estimated cost of increasing free childcare from 15 to 30 hours to working parents of three and four year olds is £585 million a year in 2020/21, compared with £10.5 billion in cuts to benefits for families with children alone.[4]

Overall it is clear that the compensation offered by these policies is limited, and, despite the rhetoric, not well targeted at low income households.

1c. Cuts to working-age benefits since 2010

In his first budget in June 2010, then-chancellor George Osborne announced spending reductions of £32 billion a year by 2014/15, of which £21bn was to come from so-called 'welfare reform'. Social security was a prime target of austerity, and the government presented existing levels of spending as 'unaffordable'. There were initial promises to use some of the savings from planned cuts to fund above-inflation increases in child tax credit, recognising that children merit protection from poverty, but this was partially reversed two years later when it was announced that most benefits and tax credits would instead be uprated by just one per cent, in line with the public sector pay cap.

[2] D Finch, *The government's £1bn tax and benefit giveaway will leave poorer households worse off*. Resolution Foundation, 2017.
[3] J Browne, *The Impact of Proposed Tax, Benefit and Minimum Wage Reforms on Household Incomes and Work incentives,* Institute for Fiscal Studies, 2015.
[4] C Beatty and S Fothergill, *The uneven impact of welfare reform: The financial losses to places and people,* Sheffield Hallam University Centre for Regional Economic and Social Research, 2016

Cuts made between 2010 and 2015 remove around £14.5 billion a year from the social security budget,[5] by both reducing the value of benefits and restricting entitlement (Table 1.1). With pensioner benefits protected by the triple lock, the weight of these cuts has fallen heavily on working-age people and families with children. Significant cuts were made by simply failing to uprate benefits in line with costs of living, first by changing the inflation measure from RPI to CPI, and then through a series of decisions to uprate benefits and tax credits below inflation.

Since 2015 the squeeze on spending on social security for working-age families has intensified, with nearly £13 billion of further cuts announced in the 2015 summer budget and subsequent statements (Table 1.2).[6] These cuts systematically de-link benefit entitlement from the actual costs faced by families. By 2020 we therefore expect £27 billion less spending on social security than a decade earlier, an unprecedented reduction in spending .

Table 1.1 Cuts and changes to benefits and tax credits in the Coalition era, 2010-2015 (excluding the introduction of universal credit)

	Change	Date effective	Details and previous estimates of impact[7]
Included in our analysis			
1	Health in Pregnancy grant abolished*	April 2011	One-off payment of £190 to women during pregnancy who were receiving health advice from a doctor or midwife.
2	Local housing allowance caps introduced for homes of different sizes*	April 2011 (new claims) January 2012 (all claims)	An estimated 21,000 households lost an average £3,848 a year, 80% of which were in London.
3	Local housing allowance rates capped at 30th percentile of local market rates (previously median)*	April 2011 (new claims) January 2012 (all claims)	An estimated 775,000 lost an average of £468 a year in 2012 (with larger households losing more).
4	Child element of tax credits increased from £2,300 to £2,555 a year	April 2011	The child element was increased by £3.45 a week above inflation.
5	Childcare payments in tax credits reduced from 80% to 70%	April 2011	Affected families with two or more children could lose up to £1,560 a year.
6	Increase in the tax credit taper (rate at which tax credits are withdrawn above an earnings threshold of £6,420) from 39% to 41%	April 2011	Estimated 3.5 million households affected; variable losses dependent on award and earnings.
7	Basic and 30 hour elements of working tax credit frozen for three years	April 2011	4.9 million working families lost out by £88 (basic element) or £154 a year compared with RPI uprating.
8	Disregard for in-year income rise in tax credits reduced from £25,000 to £10,000	April 2011	Claimants to face an immediate reduction in tax credits if their income increased by more

[5] See 4

[6] C Beatty and S Fothergill, *The uneven impact of welfare reform: The financial losses to places and people,* Sheffield Hallam University Centre for Regional Economic and Social Research, 2016

[7] Unless otherwise stated information is from H Aldridge, P Kenway, T MacInnes and A Parekh, *Monitoring poverty and social exclusion 2012,* Joseph Rowntree Foundation, 2012 (Appendix)

			than £10,000 during the year.
9	Child benefit frozen for three years	April 2011	Cost a family with 2 children over £180 a year by 2012/13, compared with RPI uprating.[8]
10	Baby element of child tax credit abolished (and proposed Toddler Element never implemented)	April 2011	Baby element worth £545 a year withdrawn (claimed by 470,000 families in April 2011).
11	Family element of child tax credit withdrawn for families earning more than £40,000 (previous threshold £50,000)	April 2011	Family element worth £545 a year withdrawn.
12	Most benefit levels (except state pension) uprated by Consumer Price Index rather than Retail Price Index	April 2011	Disability elements were often protected.
13	Sure Start maternity grant restricted to first child*	April 2011	Around 150,000 families a year no longer be eligible for a £500 payment for second and subsequent children.
14	Working hours required for a couple with children to qualify for working tax credit increased from 16 to 24 a week	April 2012	An estimated 200,000 households lost up to £3,900 a year.
15	£2,500 disregard for in-year fall in income introduced (reduced from £25,000)	April 2012	Tax credit awards only to be increased if income falls by more than £2,500 compared with the previous year's income.
16	50-plus element working tax credit abolished	April 2012	Additional element for claimants aged over-50, payable for a year after moving into work, scrapped.
17	Family element of tax credits to be withdrawn immediately after child element	April 2012	Family element no longer to be available to all families earning up to £40,000
18	Entitlement to income support for lone parents limited to parents of under-5s while those with older children must claim jobseeker's allowance.†	May 2012	100,000 claimants affected. If they moved to jobseeker's allowance there would be no loss of entitlement, but requirements for job seeking.
19	12-month time limit imposed for claiming contributory Employment Support Allowance, for those in the work-related activity group	May 2012	700,000 to be affected by 2015/16, expected to lose an average £1,872 a year.
20	Households earning over £41,300 no longer entitled to child tax credit (reduced from £50,000)	April 2012	An estimated 600,000 households lost an estimated £545 a year.
21	Child benefit reduced for households with earnings over £50,000 and removed completely for households earning over £60,000	January 2013	840,000 households to lose entitlement completely, and 360,000 to see their child benefit tapered.
22	Most working-age benefits and tax credits to be uprated by 1% each year for the next three years	April 2013	Some disability-related payments were protected. At the time expected to cost one in eight households £0.90 a week, saving the government £0.2bn in 2013/14.[9]
23	Disregard for in-year income rise in tax credits reduced from £10,000 to £5,000	April 2013	Claimants to face an immediate reduction in tax credits if their income increased by more than £5,000 during the year.
24	Local housing allowances to be uprated in line with Consumer Price Index rather than market rents*	April 2013	Expected to affect around 1.4 million recipients of housing benefit and to save the government £250 million in 2014/15 alone.[10]

[8] Trades Union Congress, *Child Benefit: a bad case of neglect?* TUC 2013

[9] Department for Work and Pensions, *Impact Assessment: Social Security Benefits Uprating Order 2013*, January 2013.

[10] Department for Work and Pensions, *Impact Assessment: Housing Benefit – uprating local housing allowance rates by CPI from April 2013*, March 2012

25	Benefit cap introduced, limiting total benefit payments for out of work and low-hours working-age households to £26,000 a year for families with children (£18,200 without)	April 2013	By May 2015, 62,571 households had been capped, of which almost half were in London.[11]
26	Child benefit to increase by 1% a year for two years	April 2014	On top of the earlier freeze, this meant child benefit was worth £3.60 less per week for a first child and £2.45 for subsequent children in 2015/16 than under RPI uprating.[12]
27	Local housing allowances to be uprated by 1% a year for two years, with provision for high rent areas*	April 2014	In 2015/16, private rental prices rose by 2.6%[13] but LHA increases were limited to 1%.
Not included in our analysis			
28	Rate of support for mortgage interest cut from 6.08% to 3.63%, with provision for future reductions if average interest rates fell by 0.5% or more	October 2010	Reduced to average mortgage rate. Available estimates suggest 250,000 people were affected in 2010.[14]
29	Child Trust Fund scrapped	January 2011	Government contributions of £500 per child (for low income families) or £250 per child (for all others) scrapped.
30	Non-dependant deductions increased in housing benefit, council tax support and other income-based benefits calculations (for other adults in the household)	April 2011 (new claims) January 2012 (all claims)	300,000 Housing Benefit and Council Tax Benefit claimants had claims adjusted.
31	£15 weekly excess (for housing benefit claimants with rents below the Local Housing Allowance) abolished	April 2011 (new claims) January 2012 (all claims)	Top-up scrapped so that housing benefit could no longer exceed the level of rent.
32	Migration from incapacity benefit to Employment Support Allowance†	2011 onwards	375,000 were expected to lose entitlement by 2014 following reassessment.
33	Local housing allowance reduced to single room rate (from one bedroom rate) for single claimants under 35 (previously under 25)	January 2012	Estimates suggested 63,000 claimants would lose an average of £2,132 a year.
34	Replacement of Disability Living Allowance with Personal Independence Payment	2013 onwards	500,000 expected to lose entitlement due to more stringent eligibility rules.
35	Social Fund (which includes Community Care Grants and Crisis Loans) abolished and localised as a discretionary fund. Many local authority schemes have not survived	April 2013	In 2009/10 more than 260,000 Community Care Grants were awarded averaging £437, and 2.7 million Crisis Loans were provided.
36	'Bedroom tax' (under-occupancy penalty) introduced, reducing the housing benefit payable to social housing tenants deemed to have one or more spare bedrooms	April 2013	Expected to affect around 660,000 housing benefit claimants in the social rented sector.[15]
37	Council Tax Benefit abolished and replaced by localised Council Tax Support	April 2013	Many councils have introduced minimum payments for households who would

[11] Department for Work and Pensions, *Benefit cap quarterly statistics: GB households capped to March 2015*, August 2015.
[12] Trades Union Congress, *Eroding Child Benefit*, June 2015.
[13] Office for National Statistics, *Statistical bulletin: Index of Private Housing Rental Prices, Great Britain: April 2016,* May 2016
[14] Channel 4 News, *CutsCheck: Mortgage interest payment help – the quiet cut,* 2010
[15] Department for Work and Pensions, *Impact Assessment, Housing Benefit: Under occupation of social housing*, June 2012.

	schemes, with a 10% budget cut		previously have been exempt, in some cases of 30 per cent a year.[16]
38	Seven waiting days introduced for unemployed claimants	October 2014	New claimants must wait 7 days before entitlement to jobseeker's allowance or employment and support allowance begins.
39	Energy prices – support to vulnerable households	2014	Additional payments to help vulnerable households meet energy bills.
40	Genuine Prospect of Work test	January 2014 (new arrivals), May 2015 onwards (all EEA nationals)	EEA nationals now required to demonstrated 'genuine prospect of work' in order to claim right of residence as a jobseeker for more than 91 days (or 6 months if previously worked)[17]
41	Tightening of working tax credit tests for the self-employed	April 2015	To claim working tax credit on basis of self-employment, businesses must show they are 'genuine and effective'.
42	Carers Allowance earnings limit increased from £102 to £110 a week	April 2015	Carers could now claim Carers Allowance if working 16 hours at the minimum wage.
43	Savings credit threshold within pension credit increased by 5.1% and maximum amount payable reduced	April 2015	Reduces the number of pensioners eligible and restricts payments to maximum of £14.82 a week for a single person and £17.43 a week for a couple, in order to finance above-inflation increases in the guarantee credit.[18]
44	Restriction on repeat claims of Employment Support Allowance	April 2015	Provision allowing a reclaim of ESA after ending a claim scrapped.
45	Bereavement benefits reform (announced 2014)	April 2017	New bereavement support payment to replace Widowed Parents Allowance, Bereavement Allowance and Bereavement Payment (see Table 1.2 below)

* Changes not in the model but calculated manually in this analysis.

† Changes assumed to be fully implemented in the model for all scenarios.

Table 1.2 Cuts and changes to benefits and tax credits in the Conservative era, 2015 -2020 (excluding the introduction of universal credit)

	Change	Date effective	Details and previous estimates of impact
Included in our analysis			
1	Most working-age benefits and child benefit frozen for four years	April 2016	A low-income family with two children will be almost £2,800 a year worse off by 2020 than in 2010 due to the freeze, or more if inflation rises.[19]
2	Benefit cap reduced from £26,000 a year to £20,000, or £23,000 in London, for couples and single parents (£13,400, or £15,410 in London, for single people)	From November 2016	Expected to affect 88,000 households with 244,000 children.[20]

[16] S Ashton, M Francis and A Woudhuysen, *Still too poor to pay: three years of localised council tax support in London*, Child Poverty Action Group and Zacchaeus 2000 Trust, 2016

[17] M Williams, *Genuine Prospect of Work – is this test lawful?* Child Poverty Action Group, 2015

[18] House of Commons Library, *2015 Benefit Uprating*, Standard Note SN07054, 2014.

[19] End Child Poverty, *Feeling the Pinch*, 2017

[20] Department for Work and Pensions, *Welfare Reform and Work Act: Impact Assessment for the benefit cap*, August 2016.

3	Family element of tax credits (payable to families with children) abolished for new claims*	April 2017	Expected to affect around 970,000 families in 2019/20, who will not receive the family element worth up to £545 a year.
4	'Two child limit' restricts eligibility to child tax credit and housing benefit to two children per family (only affects third and subsequent children born after April 2017) with limited exceptions. *	April 2017	An estimated 640,000 families with around 2 million children will miss out on payments worth up to £2,780 per third or subsequent child.[21]
5	Local housing allowances frozen for four years.	April 2016	It has been estimated that by 2020, there will be a gap of more than £50 a month between LHAs and private rents in more than 50% of the country, and a gap of more than £200 a month in 15% of the country.[22]
6	Income rise disregard in tax credits reduced to £2,500.		Claimants to face an immediate reduction in tax credits if their income increased by more than £5,000 during the year.
Not included in our analysis			
7	Changes to Personal Independent Payment assessment criteria	From March 2017	Estimated to affect up to 339,500 people (3,000 by changes to daily living activity assessment, 336,500 by changes to mobility assessment criteria).[23]
8	Permitted work limit removed in Employment and Support Allowance, and sanction levels reduced from 40% to 20%.	April 2017	Claimants working fewer than 16 hours a week, earning up to £120 a week, can continue to do so and still claim ESA after 52 weeks.
9	Work-related activity component of Employment Support allowance abolished for new claimants, reducing the level of award to claimants assessed as fit to undertake work-related activity, to the same level as Jobseeker's Allowance	April 2017	New ESA claimants will miss out on £1,510 a year. Expected to affect around 500,000 families.[24]
10	Widowed Parent's Allowance and other bereavement benefits replaced with Bereavement Support Payment	April 2017	91% of newly widowed parents will receive support for a shorter time than under the previous system. 75% will lose out in cash terms, by £12,000 on average for a working parent.[25]
11	Housing benefit backdating limited to four weeks	April 2016	Previously housing benefit could be backdated by up to six months.
12	Support for Mortgage Interest converted to a loan	April 2018	Expected to affect 170,000 households who will lose on average £1,500 a year.[26]

*Applied to all claims in the analysis, i.e. treated as a long run effect in the modelling.

[21] Her Majesty's Treasury/Department for Work and Pensions, *Welfare Reform and Work Bill: Impact Assessment of Tax Credits and Universal Credit, changes to Child Element and Family Element*, July 2015

[22] Shelter, *What could be the impact of freezing local housing allowance for four years – and who might be left out in the cold?* Method Note, 2015

[23] House of Commons Library, *Spring Budget 2017: Background briefing*, Briefing Paper Number 7913, 2017

[24] Department for Work and Pensions, *Welfare Reform and Work Bill: Impact Assessment to remove the ESA Work-Related Activity Component and the UC Limited Capability for Work Element for new claims*, July 2015

[25] Childhood Bereavement Network, *Briefing on Changes to Bereavement Benefits*, January 2017

[26] C Beatty and S Fothergill, *The uneven impact of welfare reform: The financial losses to places and people,* Sheffield Hallam University Centre for Regional Economic and Social Research, 2016

2d. The promise of universal credit

At the same time as cuts being made in the tax credit and legacy benefit system, the introduction of universal credit began in 2013. Universal credit originally promised to lift 350,000 children and 600,000 adults out of poverty by increasing their entitlements,[27] and to improve the rewards from work. The 2010 White Paper 'Welfare that works' explained that under universal credit 'people will generally keep more of their earnings for themselves and their families than is currently the case', and that 'no-one will experience a reduction in the benefit they receive as a result of the introduction of Universal Credit'.[28] Universal credit was supposed to transform the benefits system and its principal architect, Iain Duncan Smith, has called it 'the biggest change since Beveridge introduced the welfare system'.[29]

Universal credit was designed to smooth transitions into (or out of) work, as claimants would not have to claim a different set of benefits when they started (or ended) a job. It was also intended to eradicate the cliff-edges in the tax credit system at particular hours of work - eligibility for working tax credit and support with childcare costs begins at 16 hours of work a week, for example, leading to very poor rewards from work for those working less than this. Eligibility for particular elements of universal credit is not linked to earnings or hours of work. In these ways it was intended to help avoid both the unemployment trap (where people do not become better-off if they move into work) and the poverty trap (where it is hard to increase income by earning more, because benefit withdrawals offset increased wages). Universal credit also sought to eliminate very high taper rates resulting from the withdrawal of both tax credits and housing benefit at certain levels of earnings.

Early analysis of universal credit in its original design, by the IFS, concluded that universal credit ought to eliminate 'very weak work incentives' overall.[30] It found that universal credit would 'strengthen the incentive to work at all, on average, particularly for… low-earning single people and primary earners in couples', who under tax credits face very weak incentives to work unless they can reach 16 hours a week. But universal credit was also expected to 'weaken incentives to work for (potential) second earners in couples' who would see universal credit withdrawn more quickly than tax credits because they have no separate earnings disregard before universal credit is withdrawn.

Universal credit was designed to reward couples with children in particular, with sixty-seven per cent of couples with children in rented accommodation expected to see their entitlement increase in the move to universal credit, compared with just 29 per cent of lone parents who would see an increase. While couples with children were expected to see an average £3.60 increase in weekly entitlements, lone parents expected a small reduction on average.[31] This was justified as a step towards eliminating the so-called 'couple penalty' in the benefit system.

However analysis which takes into account the costs involved in living separately rather than in a couple, not only changes in benefit receipt, has highlighted that in reality the couple penalty was restricted to families in very particular circumstances, while many families would have faced a severe

[27] Department for Work and Pensions, *Welfare Reform Bill Universal Credit, Equality impact assessment*, March 2011
[28] Department for Work and Pensions, *Universal Credit: Welfare that works*, White Paper, 2010.
[29] Daily Telegraph, *Iain Duncan Smith: My welfare reforms are Beveridge for today, with a hint of Tebbit*, 6 November 2010
[30] M Brewer, J Browne, W Jin, *Universal credit: a preliminary analysis*. Institute for Fiscal Studies, 2011.
[31] Department for Work and Pensions, *Universal Credit Impact Assessment*, October 2011

'separation penalty' if they had split up.[32] There are also many reasons why lone parents might require additional support, for example their greater risk of poverty and the difficulty of increasing income through work when one parent must manage both work and childcare.

Disabled people and families with a disabled child also stood to be made worse off by universal credit, as payments for disabled children, disabled working adults and severely disabled people were all lower in universal credit than in the legacy benefit system. This analysis does not focus on the impact of cuts on disabled people in particular, but we note that these have been severe.

This analysis also does not deal with other design features of universal credit, such as the waiting time for a first payment, the intensified conditionality and sanctions regime, and the shift from a range of weekly and fortnightly payments to a single monthly assessment and payment made to one member of a family. We focus on the adequacy and poverty-reducing potential of universal credit, how this has changed over time, and whether the promises of universal credit will be delivered.

2e. Changes and cuts to universal credit

Since its initial design, universal credit has been subject to a succession of changes and cuts which have substantially reduced its adequacy overall (Table 1.3).

Table 1.3 Changes to universal credit since it was first legislated

	Change (all included in our analysis)	Date effective	Details
1	Benefit cap introduced.	April 2013	Limits total annual benefit receipt for claimants earning less than a threshold amount per month, to £26,000 for couples or families with children (£18,200 for single people).
2	Work allowances frozen	April 2014	Freezes the amount claimants can earn before universal credit starts to be withdrawn, rather than uprating in line with earnings or costs.
3	Work allowances reduced	April 2016	Reduces the amount claimants can earn from work before universal credit starts to be withdrawn, to £192 for families with children who rent their homes (and claim housing support through universal credit) and £397 for those who do not, and to £0 for non-disabled adults without children. This costs renting couples with children up to £234 a year and renting lone parents up to £554 a year.
4	Four year freeze of most universal credit rates (and other working-age benefits)	April 2016	Freezes the value of the main elements of universal credit, as well as child benefit, rather than uprating in line with inflation.
5	Childcare subsidy increased from 70 to 85 per cent	April 2016	Increases the proportion of childcare costs that can be claimed back through universal credit from 70 per cent to 85 per cent (up to a ceiling).
6	Benefit cap lowered	November 2016	Reduces the limit on total benefit receipt for claimants earning below the earnings threshold to £20,000 each year, or £23,000 in London for couples and families with children (or £13,400 and £15,410 respectively for single people without children).

[32] D Hirsch, Does the tax and benefit system create a 'couple penalty'? Joseph Rowntree Foundation, 2012

7	Minimum age introduced for the housing element	April 2017	18-21-year-olds will no longer be eligible for the housing element of universal credit, unless limited exceptions apply.
8	Higher rate child element for first child abolished	April 2017	Removes the premium paid for the first child (equivalent to the family element in tax credits) worth £545 a year.
9	Child element restricted to two children per family	April 2017	Limits the award of child elements to two children per family, unless very limited exceptions apply. This is worth up to £2,780 per child.
10	Taper rate reduced	April 2017	Reduces the rate at which universal credit is withdrawn when claimants' earnings exceed the work allowance, from 65p to 63p in the pound.
11	Higher earnings threshold introduced for benefit cap†	April 2017	Threshold raised from £430 a week to the equivalent of 16 hours a week at the 'national living wage'.

† Change assumed to be fully implemented in the model for all scenarios.

At the same time, other benefits which may be received alongside universal credit have also been subject to cuts. Child benefit was uprated at 1 per cent a year from April 2014 and then frozen for four years in April 2016. Council tax support (previously council tax benefit) was localised and in many cases reduced. And substantial reductions were made to local housing allowances as detailed in Tables 1 and 2 above.

Following these cuts to universal credit, the Office for Budget Responsibility has confirmed that 'universal credit is now less generous on average than the tax credits and benefits system it replaces' and that spending will be reduced by around £3.1 billion compared with the legacy system.[33] The Institute for Fiscal Studies calculated in February 2016 that, in moving on to universal credit, an estimated 2.1 million working families will lose out (by £1,600 a year on average) and only 1.8 million working families will gain (by £1,500 a year on average).[34] The government has not responded meaningfully to requests for a revised estimate of the impact of universal credit on child poverty.[35]

[33] Office for Budget Responsibility, *Welfare Trends Report,* October 2016, p.26
[34] J Browne, A Hood and R Joyce, *Universal credit cuts support for working families, but helps make work pay where current system creates worst problems*, Institute for Fiscal Studies, February 2016
[35] Houses of Parliament, *Universal Credit: Written question – 31250*, 2016

2. Overview of methods

CPAG commissioned the Institute for Public Policy Research (IPPR) to conduct modelling of the impact of cuts and changes to social security on family[36] incomes and poverty rates at population level, and at household level for a series of model families.

The population level analysis was carried out using the IPPR tax benefit model, which uses data from the UK Family Resources Survey (FRS) to assess the fiscal and distributional impact of changes to the tax and benefit system. This modelling was carried out in 2016 using the latest available FRS data at that time, i.e. 2014/15 data, and forecasts from the November 2016 autumn statement. The most significant change since then has been that inflation forecasts have been revised upward, meaning that our analysis probably underestimates the effect of sub-inflationary uprating decisions and freezes.

The population level analysis compares three scenarios in a tax credit 'world' (assuming, for the purposes of modelling, no transition to universal credit):

- TC2010: the benefits and tax credits system inherited by the Coalition government in May 2010.
- TC2015: benefits and tax credits system inherited by the Conservative government in May 2015.
- TC2016: the benefits and tax credits system as legislated at the end of 2016, assuming full implementation of all changes regardless of the actual planned date of implementation.

It also compares two scenarios in a universal credit 'world' (assuming full transition to universal credit, and ignoring the temporary effect of transitional protection):

- UC2013: universal credit as originally legislated and other benefits as legislated in 2013.
- UC2016: universal credit as legislated at the end of 2016, assuming full implementation of all changes regardless of the actual date of implementation.

All scenarios were compared at a particular point in time: Scenarios TC2010 and TC2015 were compared in 2015/16; TC2010 and TC2015 were compared with TC2016 in 2020/21; and UC2013 was compared with UC2016 also in 2020/21. Income changes are expressed in nominal terms.

Within each of these scenarios the model is used to isolate the effect of specific cuts and changes, for example the effect of uprating decisions or the two child limit, on poverty rates and family incomes.

It is also used to model the effect of a variety of hypothesised changes to universal credit on family incomes and poverty rates, for imagined scenarios in which these had been applied since 2013/14:

- Addition of a second earner work allowance (at either 100 percent or 50 percent of the first earner work allowance)
- Under-25 rates raised to the same level as the over-25 allowance
- Taper rate reduced to 55 per cent.
- Triple lock applied to child benefit (in a universal credit system)
- Triple lock applied to the child element
- Tripe lock applied to both child benefit and the child element.
- All of the above (with both work allowance levels)

[36] Benefit unit

- A ‘full overhaul’ of universal credit in which all cuts are reversed, all above hypothetical changes are included plus increased support for childcare costs, and higher rates for disabled children.

The analysis does not include the temporary transitional protection provided for people moving from one benefit to another, discretionary hardship or crisis payments which families may be able to claim in emergencies, or schemes put in place by the governments of Scotland or Northern Ireland which currently provide some (but limited) mitigation through supplementary payments.

Apart from in the TC2010/TC2015 comparison, incomes are projected to 2020/21 based on projected wage rates as well as tax and benefit changes due to come into force by 2020/21.

Further details of the tax-benefit model are available in recent IPPR reports.[37]

The income effects of both actual and hypothetical policy changes are presented by income decile, by family structure, by the number of children, by age of youngest children, by the presence of disability in the family, by working status and by region of the UK. Income changes are given as averages across the whole population in order to show distributional effects, meaning that they depend on both the scale of losses to individual families and the extent to which families in each group are affected by the cuts. The latter is a function both of the number of families claiming benefits or tax credits in each group, and the size of their claims. For poverty calculations the poverty line is recalculated for each scenario to reflect the effect of the policies in question on median incomes.

The household level analysis complements the population level analysis by providing insight into the actual losses facing particular families. It was carried out by IPPR using the Resolution Foundation micro-simulation model, which allows household income to be analysed for specified in-work families under both real and hypothesised tax and benefit policies and is designed for use alongside IPPR’s tax benefit model. In this analysis household incomes are calculated for 2020/21, taking account of policies implemented between the time of analysis and the end of the decade, but expressed in 2015/16 prices to permit comparison with the 2015/16 poverty line and current costs of living.

The household level analysis is used to model the incomes of eight model families under scenarios TC2010, TC2015, TC2016, UC2013 and UC2016, for a variety of working patterns and with and without childcare costs, revealing the effect of changes on the rewards from work for different household types. It is further used to model the effect of various hypothesised increases in in-work support for families, either through changes to universal credit or increased support for childcare:

- UC2016 plus a second earner work allowance (at 100 per cent of the first earner work allowance)
- UC2016 with the taper rate reduced from 63 per cent to 55 per cent
- UC2013 with the ‘full overhaul’ described above (with a second earner work allowance at 100 per cent of the first earner work allowance)

All the analysis presented below is derived from these models unless otherwise stated.

[37] For example see R Gunson, S Thompson and A Stirling, *Scotland’s missing pay growth: The economic and fiscal impacts of weak wages since the financial crisis*, Institute for Public Policy Research, 2016.

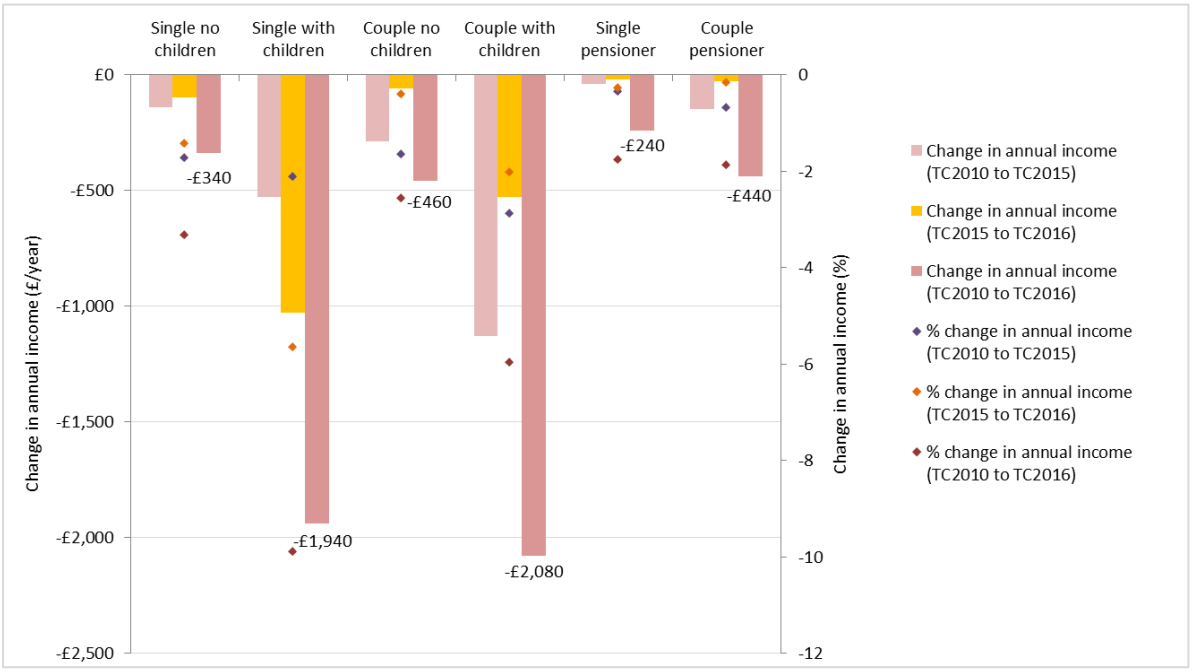
3. What have changes meant at population level?

The following section presents population-level estimates of the impact of changes on family incomes. Those affected will thus be facing greater losses than these averages, and in many cases much greater.

3a. Cuts hit families with children harder than those without children, especially lone parents

Comparing family types, in both the tax credit and universal credit systems, families with children have taken the biggest financial hit from the cuts on average – more than single adults or couples without children, and much more than pensioners. Cuts made in the coalition era affect both couples and lone parents but since then – and if we consider cuts to universal credit - lone parents have seen particularly dramatic reductions in support. Of course families with children tend to have larger awards than people without children, and are more likely to receive benefits and tax credits.

Figure 3.1 Average change in annual income for all families resulting from cuts to benefits and tax credits (TC2010 to TC2016) by family type



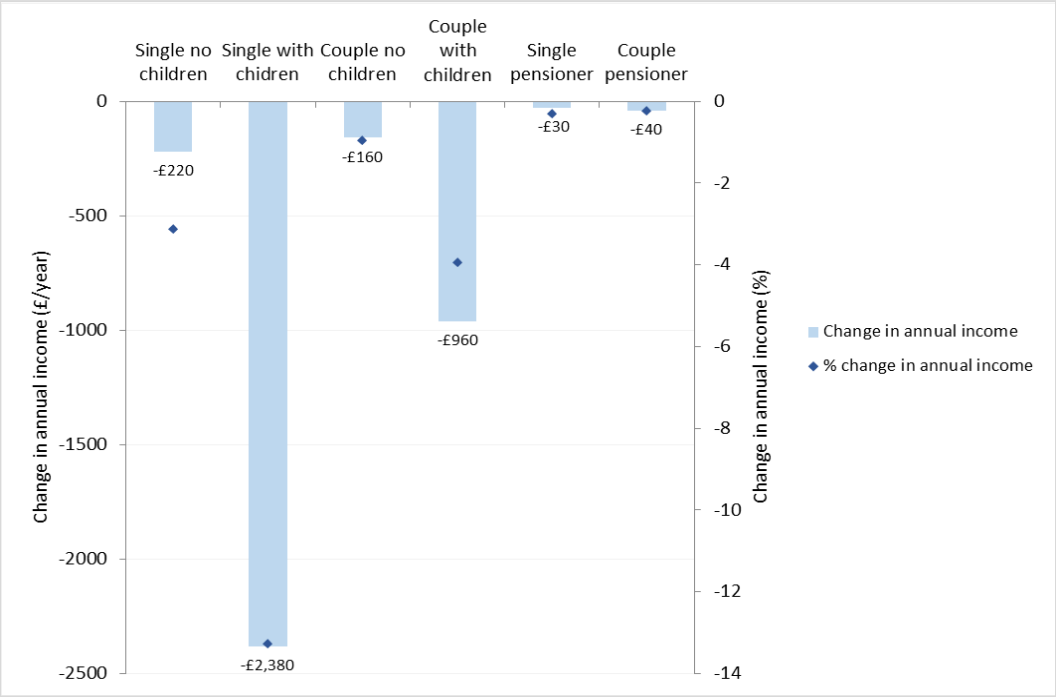
Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Reforms in the tax credit system are projected to leave lone parent families on average almost 10 per cent worse off (£1,940 a year) than they would have been had the 2010 system been retained, while couples with children will be on average almost 6 per cent (or £2,080 a year) worse off (Figure 3.1)

Cuts to universal credit are projected to leave couples with children four per cent (£960 a year) worse off on average than under universal credit as originally designed, and lone parents more than 13 per cent (£2,380 a year) worse off. In contrast pensioner couples or single pensioners will be 0.3 per cent (£40 or £30 a year respectively) worse off (Figure 3.2).

Children in lone parent families already face almost twice the risk of poverty of those in couple families, with a poverty rate of 47 per cent (after housing costs) compared with 24 per cent for children in couple families.[38] This is projected to rise to 63 per cent under current policies,[39] undoing all progress since 1997.

Figure 3.2 Average change in annual income for all families from changes to universal credit and child benefit (UC2013 to UC2016), by family type



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

The above analysis provides averages across the population, meaning that for people claiming universal credit the effect of cuts may be much more severe.

3b. Families already at greater risk of poverty will lose most

In addition to lone parents, other groups of families also face higher poverty risks, including those already on a low income, larger families, families with young children, families where someone is disabled, and those living in more deprived regions of the UK. All these groups face disproportionate impacts from the cuts.

This is in part because they have greater reliance on support from the benefits system, meaning cuts will increase and deepen their disadvantage. But some cuts have also specifically targeted particular at-risk groups, for example cuts to the child element of universal credit and tax credits, the two-child limit on these payments, and the benefit cap which largely affects families with children.

[38] Department for Work and Pensions, *Households Below Average Income 1994/5 to 2015/16, Table 4_5db*, March 2017.
[39] A Hood and T Waters, *Living standards, poverty and inequality in the UK: 2016-17 to 2021-22,* Institute for Fiscal Studies, 2017

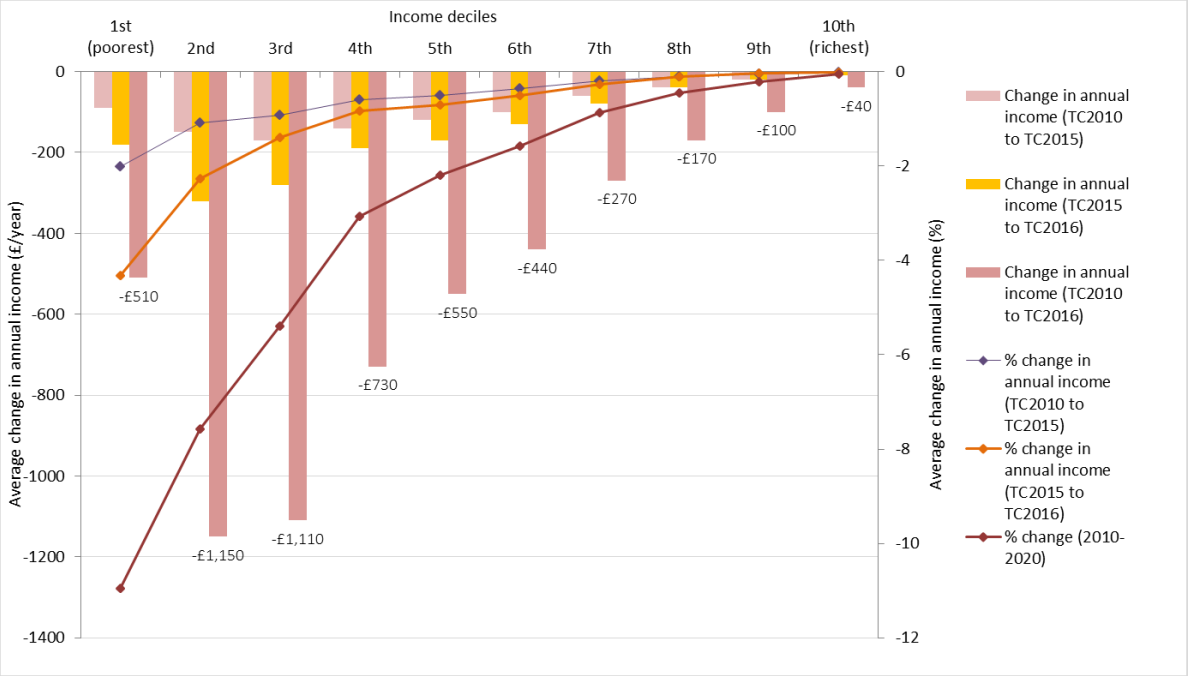
Families on the lowest incomes

The cuts in both systems disproportionately affect lower income deciles, with the poorest 10 per cent expected to lose the greatest proportion of their income.

Families in the poorest two deciles are projected to be more than 8 per cent worse off in 2020/21, on average, than they would have been if the social security policies inherited in 2010 had been maintained. The 'just about managing' don't do very well either: families in the third decile are set to be nearly 6 per cent worse off and those in the fourth decile more than 4 per cent worse off in the TC2016 than in the TC2010 scenario. For the second and third deciles these losses amount to over £1,200 a year of lost income. Both rounds of cuts (2010-2015 and 2015-2020) were regressive in their impact but the gradient is especially steep for cuts enacted since 2015 (Figure 3.3).

As noted in section 1, families in the lowest income decile are also least likely to gain from the increase in the personal tax allowance and 'national living wage'. The IFS estimated that the introduction of the 'national living wage' would increase average household incomes in the lowest income decile by just £45 a year, and the personal tax allowance increases even less[40].

Figure 3.3 Average change in annual income for all families resulting from cuts to benefits and tax credits (TC2010 to TC2016) by equivalised income decile



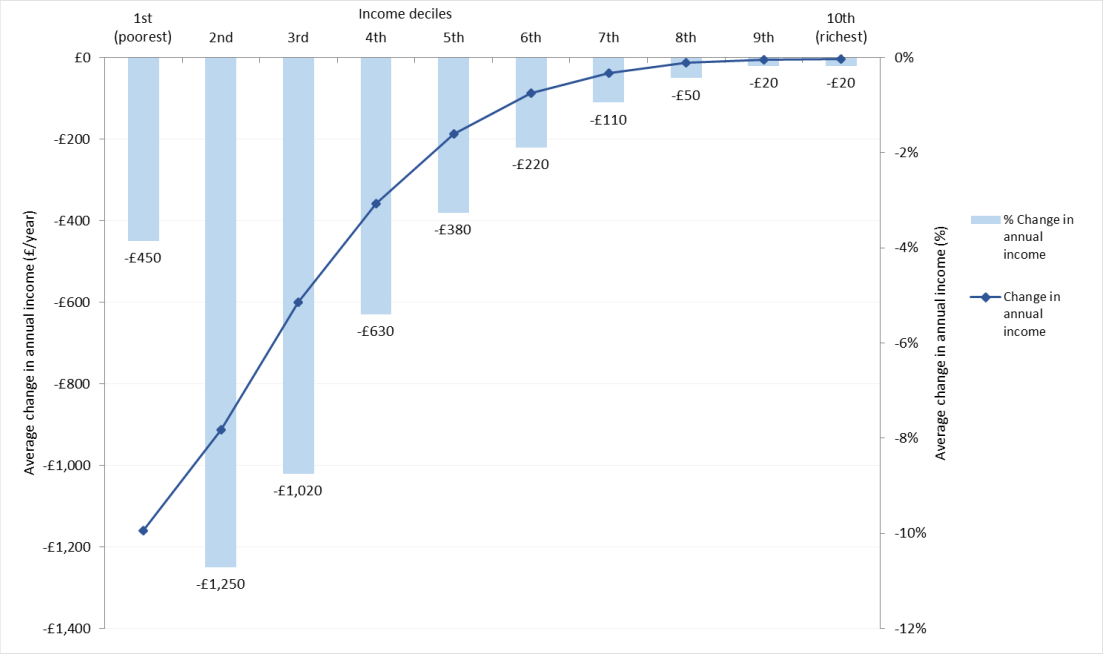
Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Cuts to universal credit have been more steeply regressive, with the poorest 10 per cent expected to lose 10 per cent of their income (or £450 a year) on average. Again families in the second decile lose out the most from the cuts in cash terms, with the average family in this group set to be £1,250 worse off a year, or nearly 8 per cent of their income (Figure 3.4).

[40] J Browne, *The impact of proposed tax, benefit and minimum wage reforms on household incomes and work incentives*, Institute for Fiscal Studies, 2015

The third and fourth deciles will be worse off by £1,020 and £630 a year (5 and 3 per cent) respectively. In contrast those in the richest 20 per cent are typically only affected by cuts to child benefit, if at all, and stand to be just £20 a year worse off (less than 0.05 per cent) on average.

Figure 3.4 Average change in annual income for all families from changes to universal credit and child benefit (UC2013 to UC2016) by equivalised income decile



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Larger families

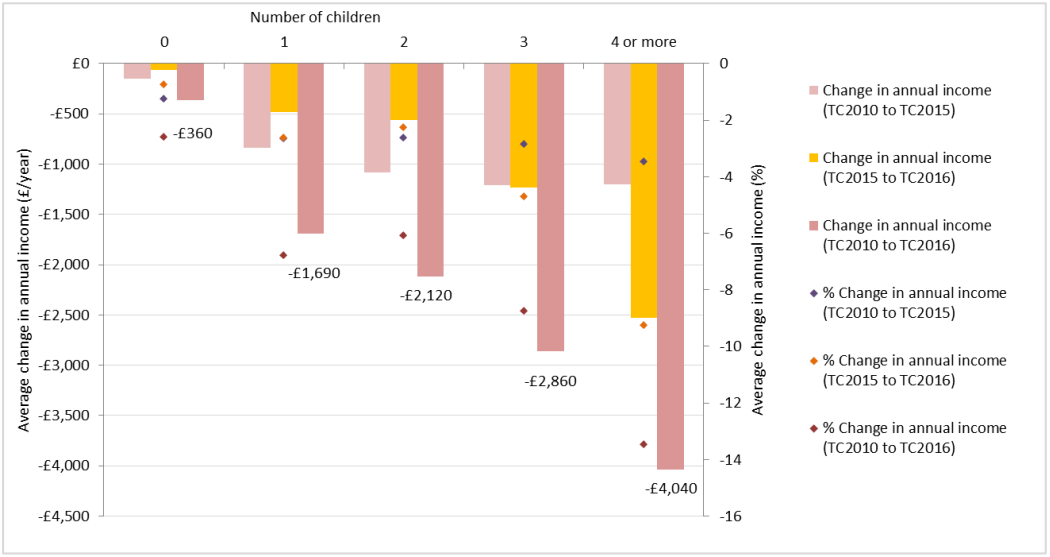
The child poverty rate (after housing costs) is 39 per cent in families with three or more children, compared with 27 per cent and 26 per cent for families with one or two children respectively.[41] The risk of poverty among children in larger families has increased year on year over the last three years for which data exists, from a low of 33 per cent in 2012/13. In 2016 the IFS projected that *absolute* child poverty[42] (before housing costs) would rise by around 600,000 by 2020/21, entirely among families with three or more children, especially those in lone parent families. A third of the impact is due to the two-child limit in tax credits and universal credit.[43]

In the tax credit system, by the end of the decade, families with four or more children are projected to be 13.5 per cent or £4,040 a year worse off on average as a result of cuts to tax credits and other benefits (in the TC2016 scenario), than they would have been in the absence of these cuts (under TC2010). Those with three children will be almost 9 per cent (£2,860 a year) worse off, and those with two children about 6 per cent (£2,120 a year) worse off.

[41] Department for Work and Pensions, *Households Below Average Income 1994/5 to 2015/16, Table 4_5db*, March 2017.
[42] For the purposes of official measures of poverty, as first set out in the Child Poverty Act 2010, absolute poverty refers to an equivalised net income below 60 per cent of an adjusted base amount, with the base year currently 2010/11.
[43] J Browne and A Hood, *Living standards, poverty and inequality in the UK: 2015-16 to 2020-21*, Institute for Fiscal Studies, 2016

Cuts made between 2010 and 2015 caused fairly similar percentage losses for families with one to three children, with families with four or more children losing only slightly more. But cuts made since 2015 will cause huge losses for larger families – more than £2,400 a year or 8 per cent of income for a family with four or more children, in that five year period alone. Across the decade this amounts to a loss of over £4,000 for these families on average; for some families in receipt of tax credits the losses will be much greater (Figure 3.5).

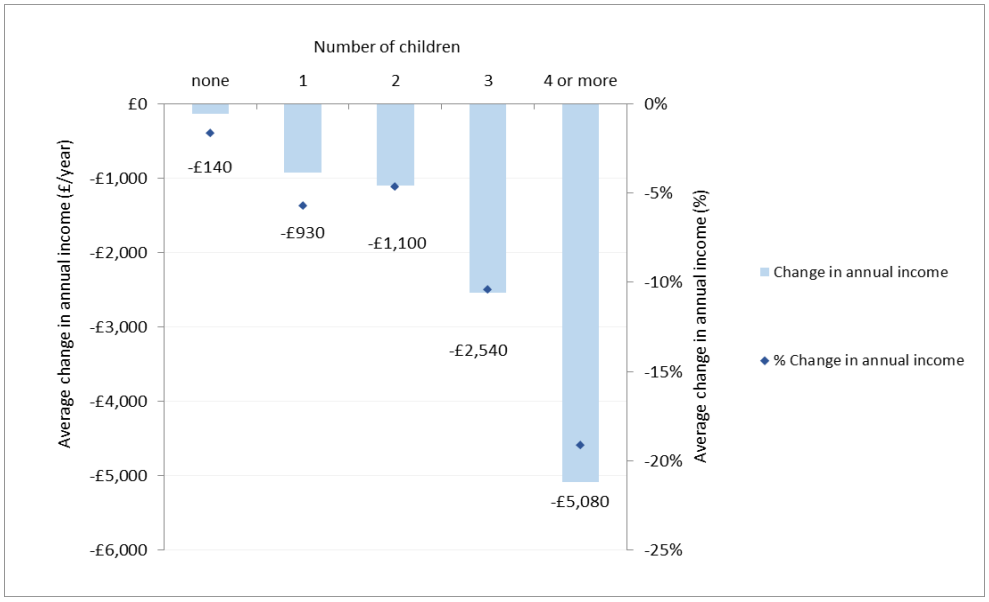
Figure 3.5 Average change in annual income for all families with children from cuts to benefits and tax credits (TC2010 to TC2016), by number of children



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

The picture is similar in universal credit. Under UC2016 the average family with three children will be 10 per cent (£2,540 a year) worse off and the average family with four or more children 19 per cent (£5,000 a year) worse off than under UC2013 (Figure 3.6).

Figure 3.6 Average change in income for all families with children from changes to universal credit and child benefit (UC2013 to UC2016) by number of children



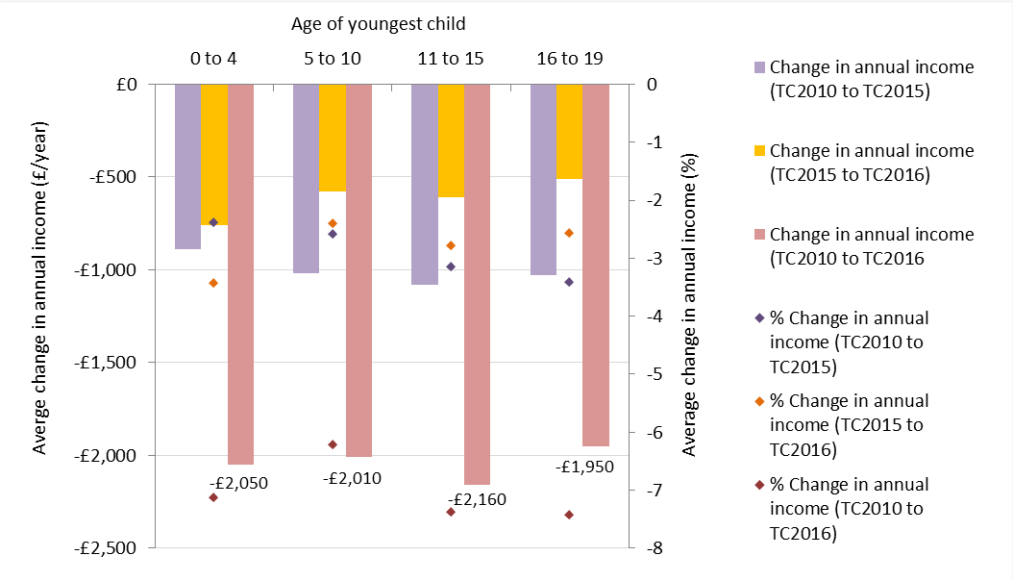
Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Families with young children

In the tax credit system, there are similar losses for families with children of different ages, though families with under-5s lose out slightly more than those with only older children in the second half of the decade (Figure 3.7).

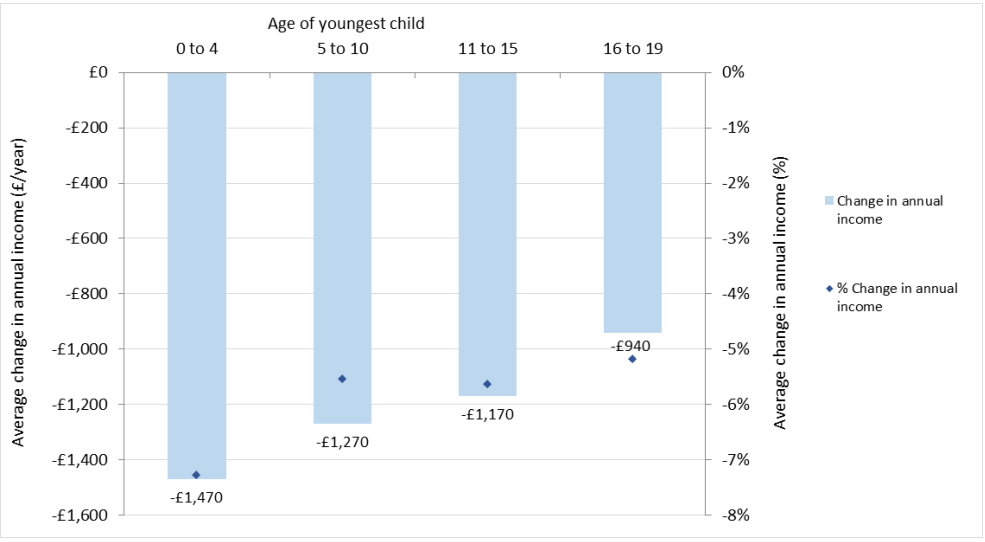
Cuts to universal credit, however, will affect families with youngest children most severely, with families with a child under five standing to be more than 7 per cent (£1,470 a year) worse off on average as a result of cuts between UC2013 and UC2016, and a family with a youngest child aged 16 to 19 more than 5 per cent (£940 a year) worse off (Figure 3.8).

Figure 3.7 Average change in annual income for all families with children resulting from cuts to benefits and tax credits (TC2010 to TC2010), by age of youngest child



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Figure 3.8 Average change in annual income for all families with children resulting from cuts to universal credit and child benefit (UC2013 to UC2016) by age of youngest child



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

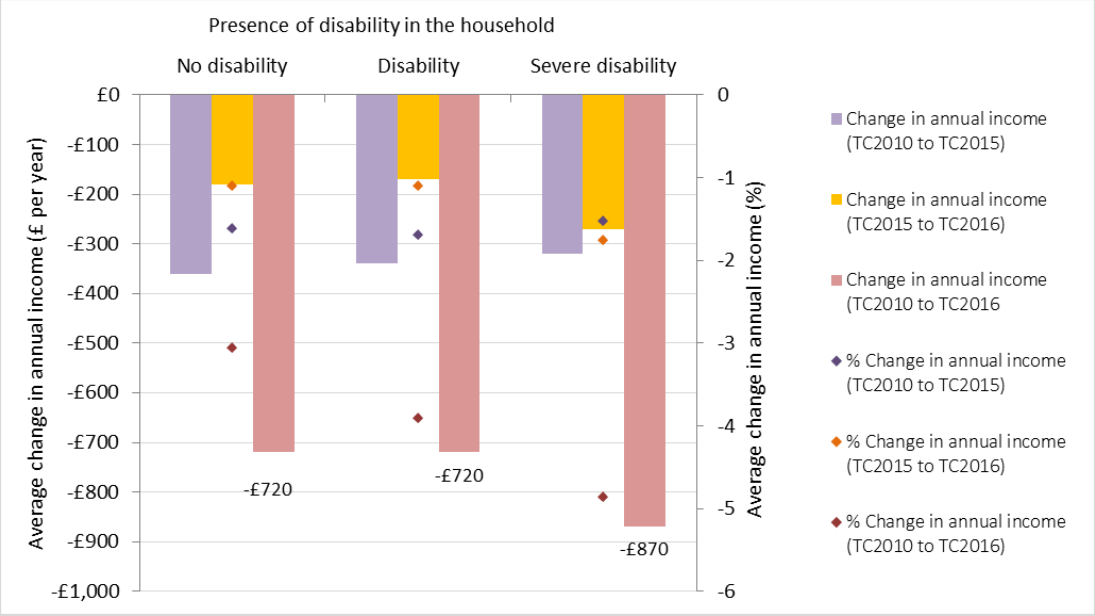
The risk of child poverty is already highest among families with an under five, at 35 per cent, compared with 24 or 27 per cent in families where the youngest child is aged 5-10 or 11-15 respectively[44]. This gap has already widened considerably since 2010/11 with child poverty increasing considerably more among families with an under five than in other families; in 2010/11 child poverty in families with an under five stood at 30 per cent compared with 26 or 25 per cent in families where the youngest child was aged 5-10 or 11-15 respectively.[45]

Families where someone is disabled

In both the tax credit and universal credit systems, families containing an individual with a severe disability will see a greater reduction in their expected income than either those with no disability or those with a disabled (but not severely disabled) family member (Figures 3.9 and 3.10).[46]

Children living in a family where someone is disabled currently have a poverty risk (after housing costs) of 36 per cent, compared with 27 per cent in families where no one is disabled.[47] Again this gap has widened since 2010/11 when the child poverty risk for these groups stood at 33 per cent and 25 per cent respectively.

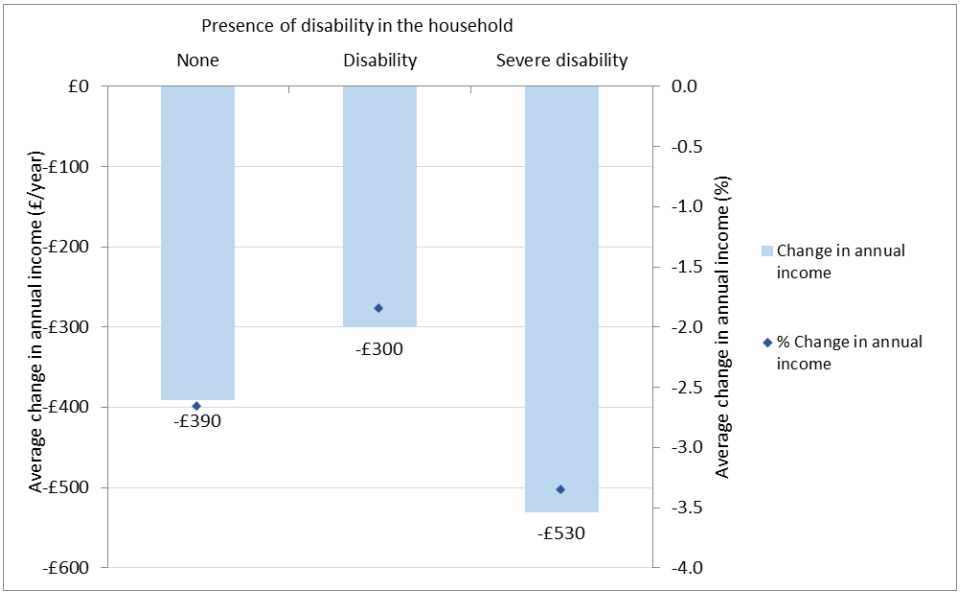
Figure 3.9 Average change in annual income for all families from changes to benefits and tax credits (TC2010 to TC2016) by presence of disability in the family



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

[44] Department for Work and Pensions, *Households Below Average Income 1994/5 to 2015/16, Table 4_6db*, March 2017.
[45] Department for Work and Pensions, *Households Below Average Income. An analysis of the income distribution 1994/5 – 2010/11, Table 4.6db*, June 2012
[46] 'Severe disability' is defined as 'core disability' as per the Equality Act 2010. 'Disability' includes some progressive diseases that are not substantially affecting day-to-day tasks in the present.
[47] Department for Work and Pensions, *Households Below Average Income 1994/5 to 2015/16, Table 4_5db*, March 2017.

Figure 3.10 Average change in annual income for all families due to cuts to universal credit and child benefit (UC2013 to UC2016) by presence of disability in the family



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit mode

Disadvantaged regions

Average losses are fairly evenly spread around the country under both systems, but some poor areas seem to be hard hit: the West Midlands, North West and Northern Ireland will see families become worse off by more than £800 a year comparing TC2010 and TC2016. The greatest losses are in Northern Ireland (but this does not take account of the scheme of supplementary payments provided in Northern Ireland to mitigate some of the cuts, for example for families affected by the benefit cap).

The same regions see the largest losses due to universal credit cuts, along with London; in these areas the average family will be more than £450 a year worse off under UC2016 than UC2013. Again, this does not incorporate the limited mitigation available in Northern Ireland.

The regional effects are driven by a combination of variations in wage levels and employment rates, costs of housing, and rates of benefit receipt. Poverty rates are included in the tables below for context.

Table 3.1 Average changes in annual income for all families resulting from cuts to benefits and tax credits (TC2010 to TC2016) by region.

	Average change in annual income (£/year)	Average percentage change in annual income (%)	Child poverty rate 2013/14 -2015/16
North East	-£720	-4.7	28
North West and	-£800	-3.5	30
Yorkshire and Humberside	-£770	-4.3	29
East Midlands[48]	n/a	n/a	29
West Midlands	-£800	-4.4	33
Eastern	-£690	-3.5	25
London	-£710	-3.6	37
South East	-£740	-3.3	25
South West	-£780	-3.7	26
Wales	-£780	-4.4	30
Scotland	-£710	-3.8	23
Northern Ireland	-£900	-5.2	26

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Table 3.2 Average changes in annual income for all families from cuts to universal credit and child benefit (UC2013 to UC2016) by region

	Average change in annual income (£/year)	Average percentage change in annual income (%)	Child poverty rate 2013/14 -2015/16
North East	-£400	-2.8	28
North West and	-£460	-3.0	30
Yorkshire and Humberside	-£420	-3.1	29
East Midlands	-£440	-2.6	29
West Midlands	-£450	-3.0	33
Eastern	-£330	-2.1	25
London	-£470	-3.6	37
South East	-£370	-2.1	25
South West	-£410	-2.6	26
Wales	-£410	-2.8	30
Scotland	-£330	-2.3	23
Northern Ireland	-£510	-3.4	26

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

3c. Both working and non-working families lose out

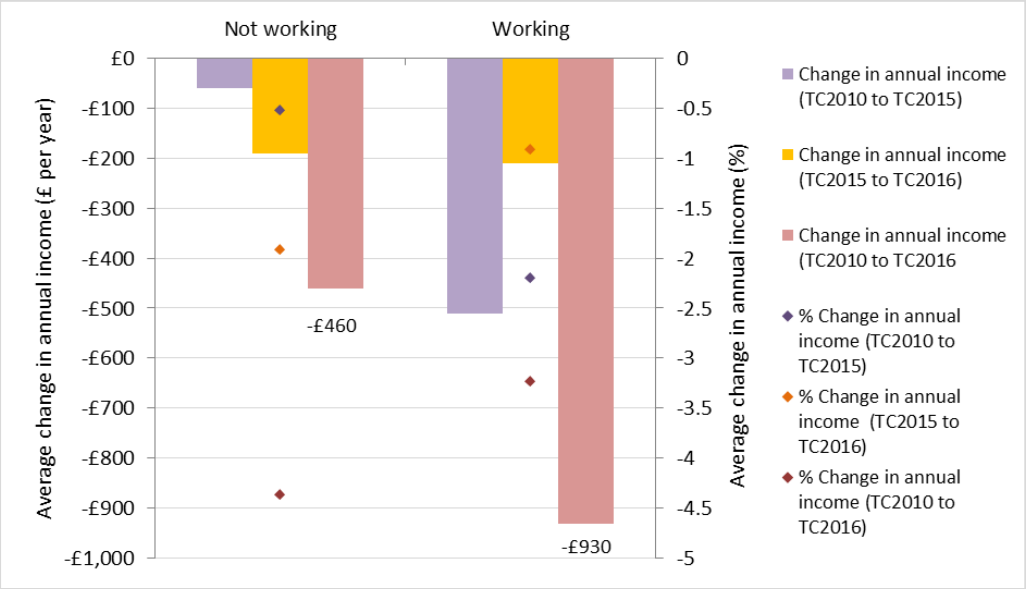
In either system, the cuts affect working families more than non-working families on average in cash terms (Figure 3.11 and 3.12).[49] Working families stand to lose on average £930 a year from cuts in a tax credit system, or £420 a year in a universal credit system. Cuts to universal credit work allowances

[48] Not reported due to sample size.

[49] 'Working' is defined according to the International Labour Organisation definition of having carried out any paid work within a reference period.

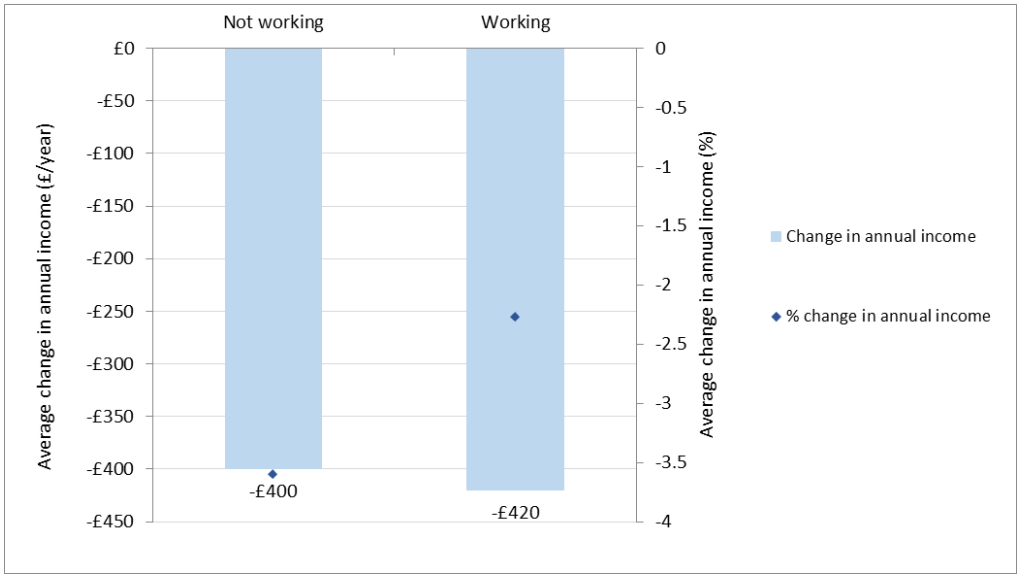
have targeted working families in particular. But many in both groups – low-income working families who rely on in-work benefits, and out-of-work families of working age - stand to lose considerably more than the average figures given here. And those not working are losing more in percentage terms over the decade, and some of those reliant on out-of-work benefits may have perilously low incomes close to a destitution level.[50]

Figure 3.11 Average change in annual income for all families from changes to benefits and tax credits (TC2010 to TC2016) by working status



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Figure 3.12 Average change in annual income for all families from cuts to universal credit and child benefit (UC2013 to UC2016), by working status



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

[50] S Fitzpatrick, G Bramley, F Sosenko, J Blenkinsopp, S Johnsen, M Littlewood, G Netto and B Watts, *Destitution in the UK*, Joseph Rowntree Foundation, 2016

Under the coalition government, non-working families were relatively protected from cuts, although they were subject to sub-inflationary uprating of out-of-work benefits, and some non-working families were affected by the benefit cap from 2013. This has changed since 2015, when we have seen out-of-work benefits (as well as children's benefits available to out-of-work families) frozen at a time when inflation is rapidly rising, and the benefit cap has been reduced by £6,000 a year leading to a 240 per cent increase in the number of families capped.[51] As pensioner benefits have been largely protected, non-working families of working age will have seen very substantial losses.

3d. Many cuts specifically target families with children

Some of the cuts are specifically targeted at families with children, and some at particular groups of families who are already at higher risk of poverty. The two-child limit only affects families with three or more children, who are already at an elevated risk of poverty. The benefit cap affects out-of-work families or those working very few hours, and mainly affects lone parents with young children. The family element of tax credits and the first child premium in universal credit have been removed, and various cuts have been made to support provided for new babies or young children (see below).

The two-child limit

The two-child limit is expected to affect 640,000 families by 2020/21,[52] and when fully rolled out in universal credit is likely to affect around 870,000 families, with at least 2.9 million children (based on the number of families with three or more children claiming tax credits in 2015/16).[53]

Our modelling indicates that the two-child limit will cost families with three children on average £460 a year, and families with four or more children on average £1,210 – 2 per cent and almost 5 per cent of their income respectively – in a tax credit system (Figure 3.13).

In a universal credit system the two-child limit is expected to cost the average family with three children £530 a year, and the average family with four or more children £1,180 a year (Figure 3.14). These are average losses across the population meaning that for those families affected the losses can be much greater, at up to £2,780 a year for each third or subsequent child. See below and the real-life example in Box 3.1.

CPAG carried out further analysis to estimate the average losses *per family affected by the two child limit*, comparing average losses from the policy at population level (using output from the IPPR tax-benefit model) with an estimate of the number of families affected by the two-child limit (derived from comparing national data on the number of families with three or more children in the population, with tax credit statistics showing the number of such families who claim child tax credit).[54]

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[51] Department for Work and Pensions, *Benefit cap: number of households capped to May 2017*, August 2017

[52] Her Majesty's Treasury/Department for Work and Pensions, *Welfare Reform and Work Bill: Impact Assessment of Tax Credits and Universal Credit, changes to Child Element and Family Element*, July 2015

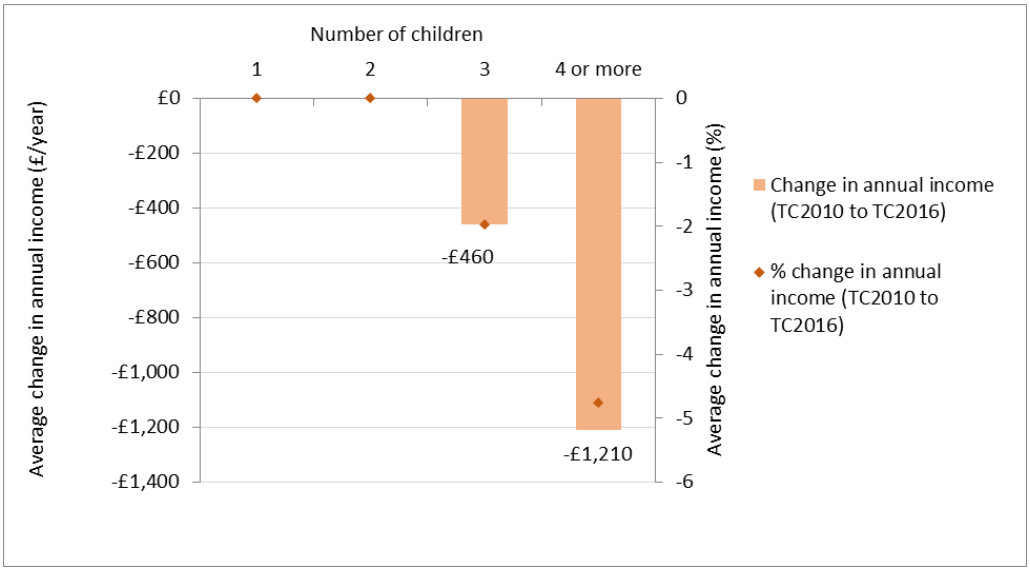
[53] HM Revenue and Customs, *Child and Working Tax Credits statistics: finalised annual awards – 2015 to 2016*, *Table 2.2*, June 2017

[54] These are estimates only because they assume that 2014/15 FRS data (on which the IPPR tax-benefit model) and more recent DWP tax credit statistics are fully compatible, and that the profile of universal credit claimants will be similar to that of child tax credit claimants.

This analysis should be treated with some caution as it assumes that these datasets are fully compatible with each other and with the 2014/15 FRS data used in the IPPR tax-benefit model, but it suggests that the average loss from the two-child limit, for affected families, would be:

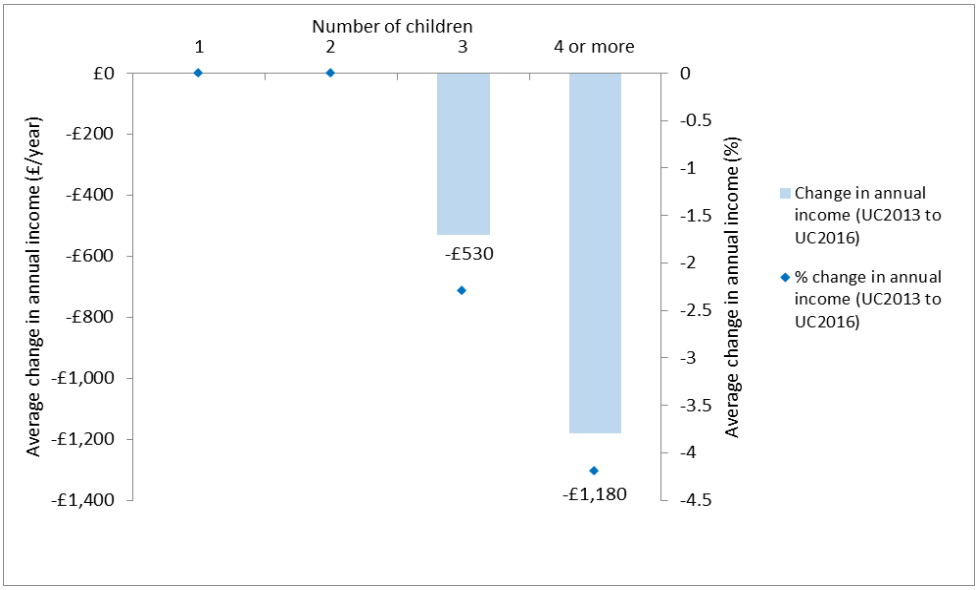
- £689 a year in a universal credit world and £795 in a tax credit world for families with three children, in 2020.
- £1,184 a year in a universal credit world and £1,214 a year in a tax credit world for families with four or more children, in 2020.

Figure 3.13 Average change in annual income for all families with children from the two-child limit in a tax credit system (TC2010 to TC2016), by the number of children.



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Figure 3.14 Average change in annual income for all families with children resulting from the two-child limit in universal credit (UC2013 to UC2016), by the number of children



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Box 3.1 Rebecca's story – the impact of the two-child limit

Rebecca has two daughters aged seven and four. Her former partner passed away from heart disease in 2013. In 2016 Rebecca became pregnant, and her son was born in August 2017.

Her son's father does not live with the family so Rebecca claims a number of benefits - including child tax credit - as a single mother. Her son is subject to the two-child limit, and she receives no child tax credit award for him. Rebecca suffers from epilepsy and learning disabilities.

Rebecca and her children are 11 per cent worse off than they would have been before the two-child limit was introduced, losing £46 a week or £2,416 a year. Rebecca's income now puts her family £126 a week below the poverty line.

Rebecca's name has been changed to protect her identity.

The benefit cap

A small minority of families are hit by the benefit cap – 68,000 at the last count, including 48,000 lone parents[55]. The benefit cap will cost the average lone parent family £230 a year in the tax credit system (TC2016 compared with TC2010) and £290 a year under universal credit at population level. Given that currently around one in forty lone parents is affected by the cap at a given time, this means that individual losses can be huge, as discussed further below.

Families with more children are again hardest hit on average. In the universal credit system the benefit cap will cost to cost the average family with three children £460 a year, and the average family with four or more children £1,200 a year (Figure 3.16), with smaller but substantial losses in the tax credit system (Figure 3.15).[56]

These are similar average losses to those caused by the the two-child limit at population level, but the two child limit is expected to affect around ten times as many families meaning that individual losses from the benefit cap will again typically be much higher.

Further analysis by CPAG estimated the average losses *per lone parent family affected by the benefit cap*, by comparing average losses from the cap at population level (using output from the IPPR tax-benefit model as detailed above) with an estimate of the proportion of lone parents in the population affected by the benefit cap (derived from comparing benefit cap statistics with national data on the number of lone parent families with dependent children in the population).

This analysis should be treated with some caution as it assumes that these datasets are fully compatible with each other and with the 2014/15 FRS data used in the IPPR tax-benefit model, but it suggests that the average loss, from the benefit cap alone, for capped lone parent families, would be:

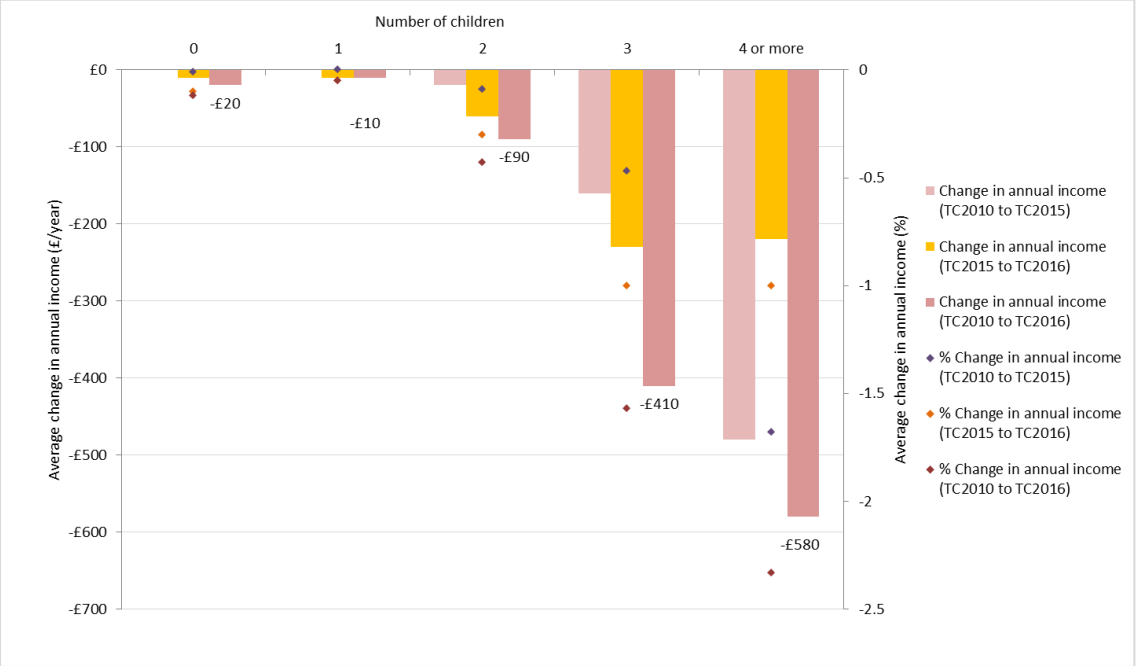
- £11,500 a year in a universal credit world in 2020;
- £9,100 in a tax credit world in 2020.

[55] Department for Work and Pensions, *Benefit cap: number of households capped to May 2017*, August 2017

[56] NB the sample of families with four or more children affected by the benefit cap in both tax credits and universal systems is small, and only just reportable.

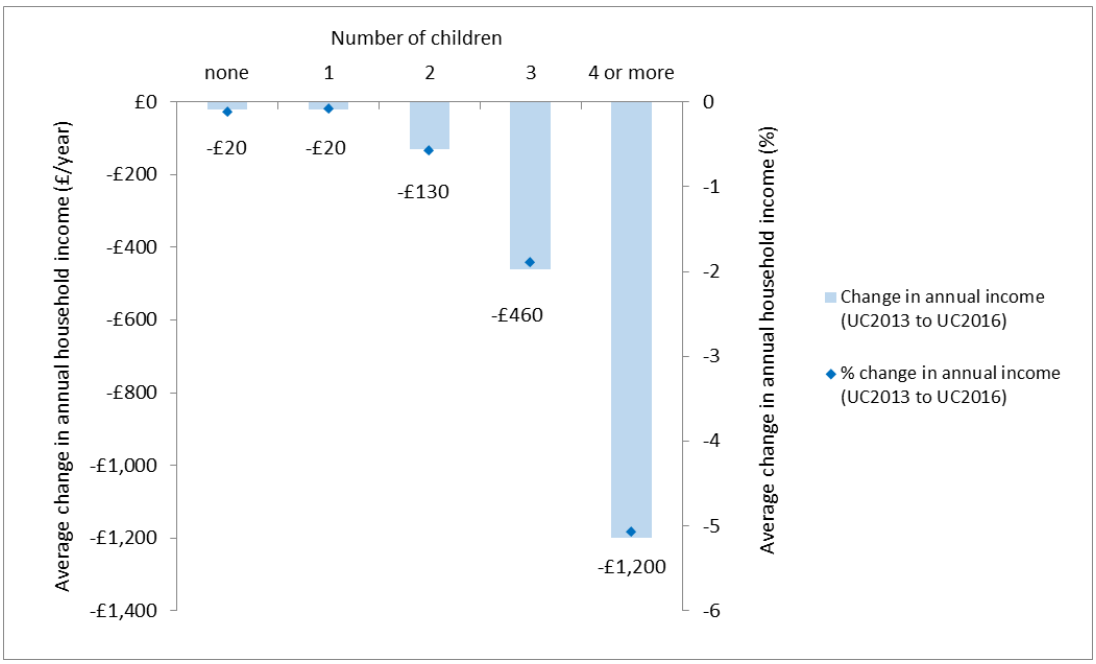
The extent of losses is also illustrated by the real-life example of Amanda's family, in Box 3.2. The benefit cap costs this family more than a third of its income.

Figure 3.15 Average change in income for all families resulting from the benefit cap in a tax credit system (TC2010 to TC2016), by the number of children in a family



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Figure 3.16 Average change in family income for all families resulting from the benefit cap in universal credit (UC2013 to UC2016), by the number of children in a family



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Box 3.2 Amanda's story – a lone parent affected by the benefit cap

Amanda has a son and daughter aged nine and 13, and was working as a care worker until having twins. She is separated from their father. Amanda was not able to work while caring for two babies under one, one of whom had health problems, as a single parent, and did not receive maternity pay.

Amanda claimed child tax credit, child benefit, income support and housing benefit. In the absence of the benefit cap she would have received £230 a week in housing benefit towards her rent for a small three-bedroom home. The benefit cap meant that this was reduced to £30 – a loss of £200 a week or over £10,400 a year, 34 per cent of the family's income.

Amanda's name has been changed to protect her identity.

Losses due to the benefit cap are greater in the universal credit system than in the tax credit system. This appears to be for two main reasons. First, as the cap within universal credit extends beyond housing costs (the whole award can be reduced, not just the housing element), some families are brought into the cap under universal credit who do not claim much (or any) housing element. Second, more families are brought into the scope of the cap, particularly those with children, because the earnings condition for becoming uncapped is based on earnings equivalent to a set number of hours at the 'national living wage', and will rise as the 'national living wage' rises, becoming harder to achieve.

Other cuts to support for first and young children

We also examine the effect of a collection of cuts to benefits designed to support parents of babies and young children: the scrapping of the baby element and later the family element of tax credits, the abolition of the Health in Pregnancy grant and the restriction of Sure Start maternity grants to the first child in a family, and the decision to withdraw the family element of tax credits immediately after the child element (previously the family element was available to all families earning up to £40,000 even if they had no entitlement to other tax credit elements).

These cuts cost the average family between £470 and £580 a year depending on the number and age of children, in the tax credit system. The same bundle of cuts was not modelled for the universal credit system because they came into effect before 2013, meaning the loss of the Health in Pregnancy grant and the restriction of Sure Start maternity grants are already included in the UC2013 scenario.

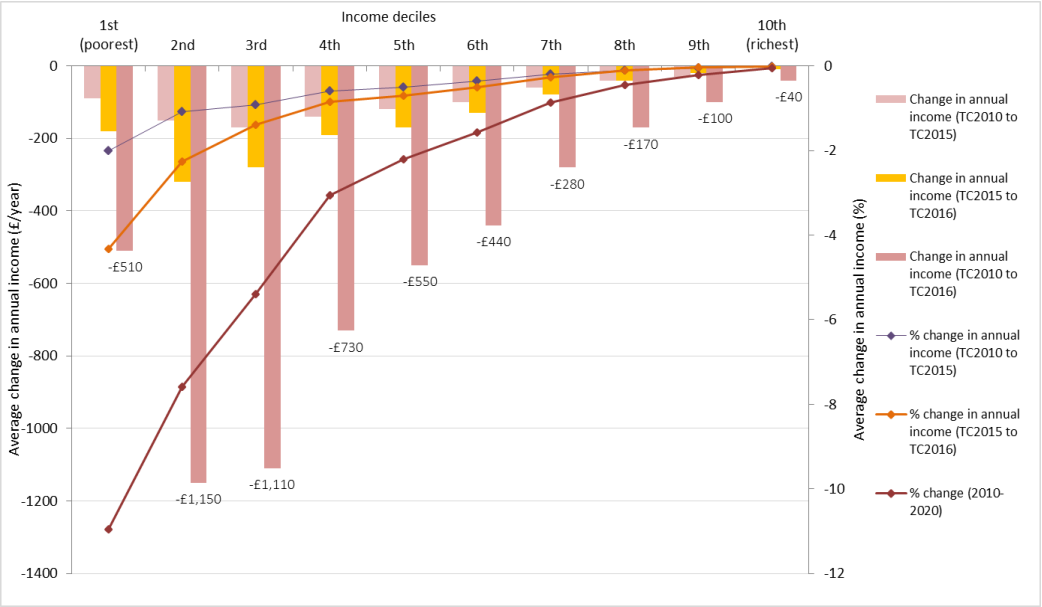
In a universal credit system the loss of the first child premium (equivalent to the family element in tax credits, and worth up to £545 a year to any given family) will cost the average lone parent family £420 a year, or 2.6 per cent of their income, and the average family with one child £160 a year.

3e. Failure to uprate benefits adequately causes large losses

Figures 3.17 and 3.18 show the substantial role of sub-inflationary uprating decisions in the losses to families. These compound over time creating very heavy losses when looked at over a time horizon of

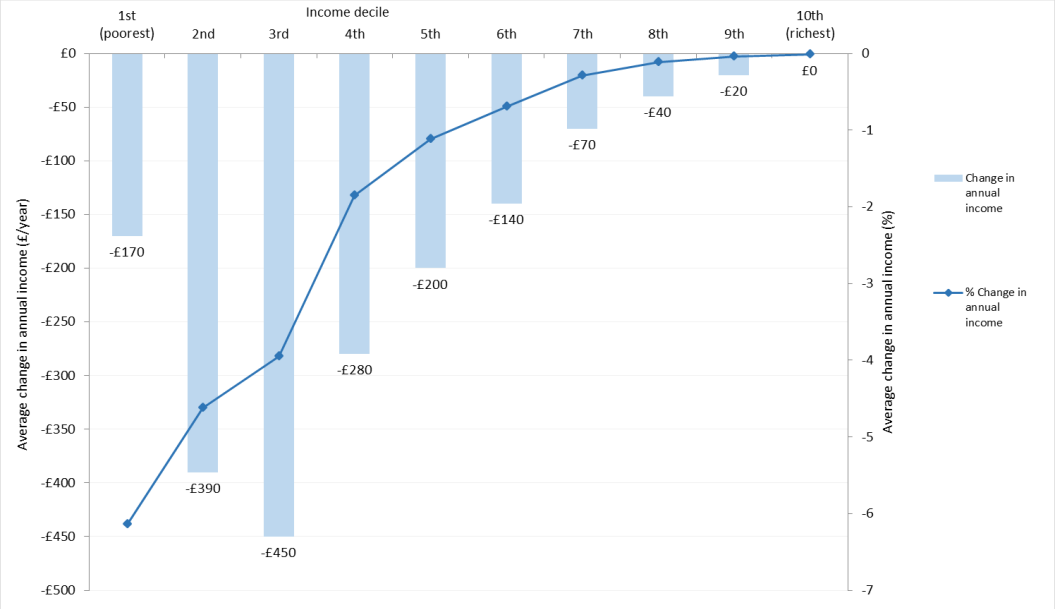
seven to ten years, particularly with inflation projected to rise considerably in the coming years.[57] In fact these are likely to be underestimates of the effect of uprating decisions, as inflation forecasts have been revised upward since this analysis was conducted.

Figure 3.17 Average change in annual income for all families from sub-inflationary uprating of benefits in a tax credit system (TC2010 to TC2016) by equivalised income decile.



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Figure 3.18 Changes in income for all families resulting from the failure to uprate universal credit and child benefit (UC2013 to UC2016) by equivalised income decile



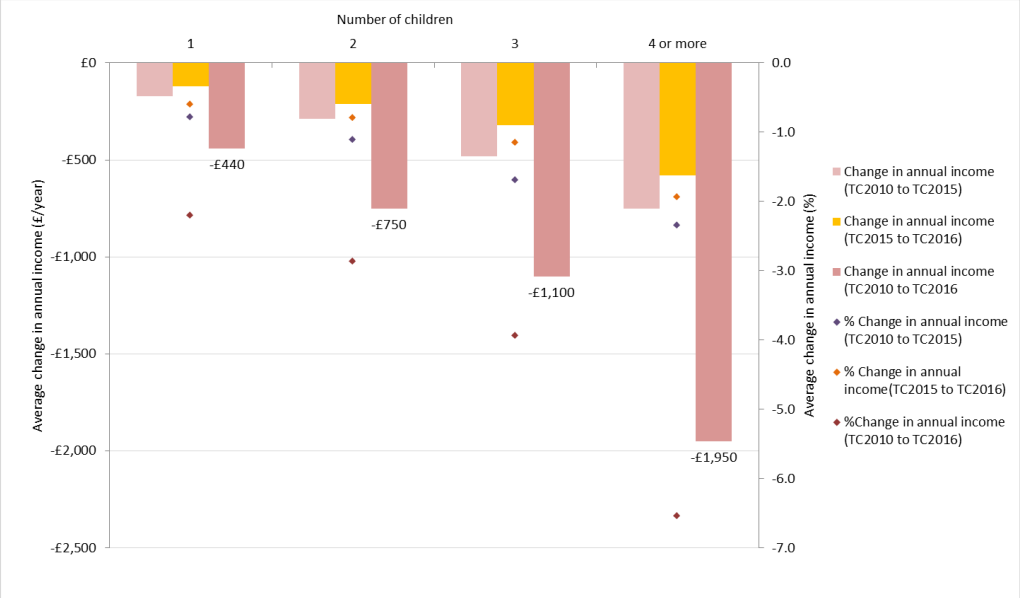
Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

[57] To calculate losses purely due to uprating decisions we have manually subtracted the increase in child tax credit rates made in 2011/12, cuts to universal credit work allowances in 2016/17 and the reduction in the first child element in universal credit made in 2017/18 where relevant.

The four-year freeze to universal credit, plus child benefit uprating policy, will cost the average single parent family £710 a year and the average couple with children £430 a year in a universal credit system. For a family with three children, the effect of uprating decisions outweighs the effect of the two-child limit or the benefit cap when averaged at population level, though for families affected by the benefit cap this is likely to be much more significant. Working families will be on average £190 a year worse off as a result of the freeze and uprating decisions in universal credit and child benefit.

In a tax credit system, uprating decisions for child benefit and child tax credit alone would leave the average family with three children £1,100 a year worse off and the average family with four or more children £1,950 a year worse off than under the 2010 system (TC2010), on top of the effect of other cuts (Figure 3.19). Child benefit rates are expected to be 24 per cent lower in 2020 than had they been uprated by RPI since 2010, and child tax credit rates 11 per cent lower.[58]

Figure 3.19 Average change in annual income for all families with children from sub-inflationary uprating of children's benefits in a tax credit system (TC2010 to TC2016), by number of children

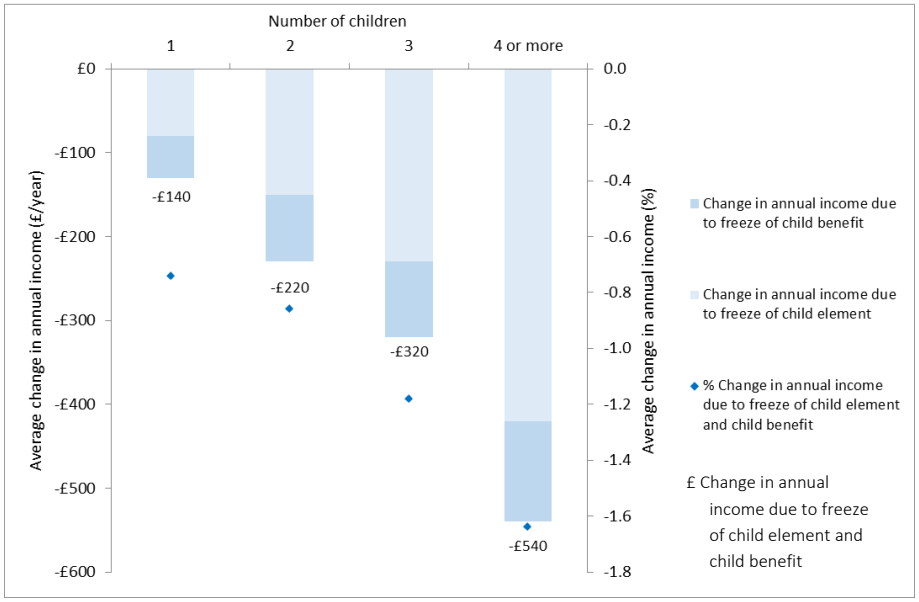


Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

The freeze of the child element in universal credit will cost the average family with three children £230 a year, and the average family with four or more children £420 a year (Figure 3.20). If the freeze to child benefit is added, this rises to £320 a year for families with three children, and £540 a year for families with four or more. The freeze of the child element costs the average couple with children £100 a year and the average lone parent family £230 a year (£170 and £300 a year respectively with the freeze of child benefit also included).

[58] End Child Poverty, *Feeling the Pinch*, 2017

Figure 3.20 Average change in annual income for all families with children resulting from the freeze to the child element of universal credit and child benefit (UC2013 to UC2016) by the number of children in a family



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

3f. Cuts to local housing allowances have broken with actual rents

In 2010, local housing allowances (the amount of rent which can be paid in housing benefit for tenants in the private rented sector) were set at the median of local rents. Their level was reduced to the 30th percentile of rents in 2011. Following this, LHAs were uprated by just one per cent a year for two years from April 2014 (with some provision for high rent areas), and frozen for four years from April 2016. Yet since 2011 rents in the private rented sector in Great Britain have increased by 15.1 per cent nationally, and 11 per cent if London is excluded.[59]

Cuts to LHAs in the tax credit system have led to substantial reductions in the incomes which families claiming housing benefit (whether out of work or in low-paid work) can expect and left support behind actual rents in many cases. The cuts to LHAs alone would make the average lone parent family £220 a year (1 per cent) worse off in 2020/21 compared with what they could have expected under the TC2010 system. Families with young children are affected more than those with older children, with families with a child under five becoming £160 a year worse off on average. And larger families are affected more than smaller ones: the average family with one child is set to be £100 a year worse off as a result of LHA cuts, and the average family with four or more children £180 a year worse off.

[59] Office for National Statistics, *Index of Private Housing Rental Prices, Great Britain: August 2017*, September 2017

Table 3.3 Average changes in annual income for all families resulting from cuts to local housing allowances, in a tax credit system (TC2010 to TC2016) by region.

	Average change in annual income between TC2010 and TC2016 scenarios	
	Cash change (£/year)	Percentage change
North East	-£40	-0.3
North West and Merseyside	-£50	-0.3
Yorkshire and Humberside	-£40	-0.3
East Midlands	-£50	-0.3
West Midlands	-£40	-0.3
Eastern	-£40	-0.2
London	-£80	-0.4
South East	-£40	-0.2
South West	-£60	-0.3
Wales	-£60	-0.4
Scotland	-£30	-0.2
Northern Ireland	-£50	-0.3

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Perhaps unsurprisingly, the cuts have a greater effect in London than in other regions: the average family in London stands to be £80 worse off as a result. Given that only one in five of London's families claim housing benefit,[60] it is clear that individual families may see much greater losses. Indeed, analysis by the Chartered Institute for Housing in 2016[61] found that local housing allowances now fall below the 30th percentile of private local rents in most rental areas in the country. In the worst cases they have fallen more than £60 a week below the 30th percentile, and in some areas the LHA for certain sizes of property is now worth less than the 10th percentile of available rents, meaning less than 10 per cent of locally available properties could have rent fully covered by housing benefit.

The cuts to local housing allowances also apply in universal credit. However, there were too few families on universal credit claiming a housing element of universal credit in the 2014-15 FRS to model their effect in a universal credit system.

3g. Cuts to universal credit work allowances have harmed working families and reduced the rewards from work

One of the most heavily criticised of the changes to universal credit was the decision to reduce work allowances (the amount which can be earned from work before awards are reduced) in April 2016. These were reduced as shown in Table 3.4. Similar cuts were proposed in tax credits but reversed following criticism. Lone parents not claiming housing costs see the most dramatic reduction.

[60] Housing benefit caseload in May 2017 was 756,019 in London (Department for Work and Pensions, *Housing Benefit caseload statistics: data to May 2017,* August 2017) and GLA projections indicate the total number of households in London to be around 3,640,000 in 2017 (Greater London Authority, *2016-based household projections*, London Datastore, 2016)
[61] Chartered Institute of Housing, *Mind the gap: the growing shortfall between private rents and help with housing costs,* 2016

Table 3.4 Changes to work allowances

	Work allowance level (£ / month) Before April 2016	From April 2016	Resulting loss of income* (£/year)
Claimants receiving housing costs			
Single person (no children)	£111	£0	£839
Couple (no children)	£111	£0	£839
Couple with children	£222	£192	£227
Lone parent	£263	£192	£537
Person with limited capability for work	£192	£192	-
Claimants not receiving housing costs			
Single person (no children)	£111	£0	£839
Couple (no children)	£111	£0	£839
Couple with children	£536	£397	£1,051
Lone parent	£734	£397	£2,548
Person with limited capability for work	£647	£397	£1,890

* For claimants with monthly net earnings at least equal to the relevant original work allowance. Claimants earning less than the old work allowances, but more than the new allowances, will lose proportionally less (63 per cent of their earnings above the new work allowance).
Source: Authors' calculations

Cuts to work allowances not only reduce the financial incentive for claimants to start work or increase earnings, potentially lowering the 'sweet spot' for working,[62] they also reduce overall awards for claimants who earn more than the new lower allowances, as a greater portion of their award is subject to the taper. In addition to the outright cut, work allowances were frozen in 2014 and again following the cuts, further reducing their value.

At a population level these cuts will cost the average lone parent £570 a year, and the average couple with children £180 a year (see Table 3.5) rising to £710 and £250 respectively when the freeze of work allowances is also included. For lone parents the average loss will be between 3 and 4 per cent of annual income. However as with all these cuts it is clear that for some families the actual loss is much higher. Work allowance cuts have the greatest impact in cash terms on families in the 2nd and 3rd income deciles, as they hit low-paid working families hard (Figure 3.21). The percentage impact is, however, highest for the poorest decile.

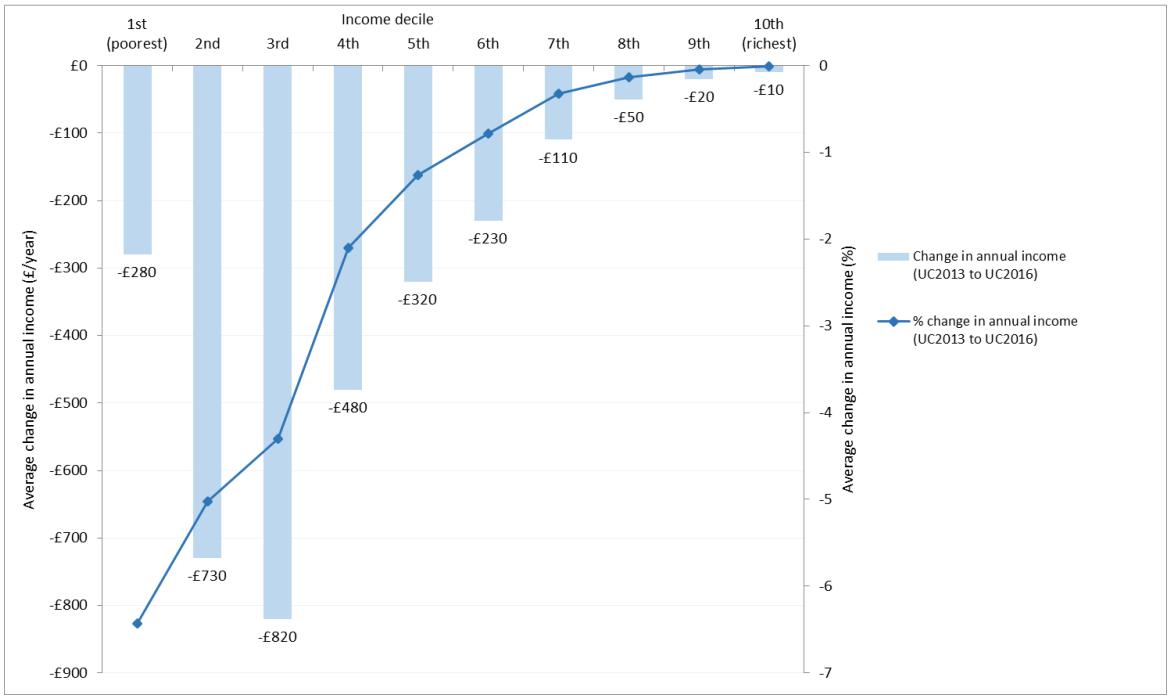
Table 3.5 Effect of work allowance cuts on incomes of all lone parents and couples with children

	Average change in annual income resulting from work allowance cuts £/ year	Percentage
Work allowance cuts only		
Couples with children	£180	0.8%
Lone parents	£570	3.1%
Work allowance cuts and freeze		
Couples with children	£250	1.1%
Lone parents	£710	3.8%

[62] D Finch, *Universal Challenge: Making a success of Universal Credit*, Resolution Foundation, 2016

The reduction in the taper rate from 65 to 63 per cent does little to compensate for these cuts. At the time of the announcement of the reduced taper rate, the Treasury briefed that a lone parent with one child and no housing costs, earning £15,000 a year, would gain £170 a year from the lower taper rate.[63] However the same parent loses more than £2,500 a year from cuts to the work allowances.

Figure 3.21 Average changes in annual income for all families resulting from work allowance freezes and cuts in universal credit (UC2013 to UC2016) by equivalised income decile



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

The government suggested that families could make up for work allowance cuts by working 'three to four additional hours a week at the national living wage to which they are entitled'.[64] However as the examples in Box 3.3 show, this will simply not be true for many families.

[63] HM Treasury, *Autumn Statement 2016: some of the things we've announced*, News story, 23 November 2016

[64] Department for Work and Pensions, *Government response to SSAC Occasional Paper 15: Universal Credit: priorities for action*, 21 December 2015

Box 3.3 The impact of work allowance cuts

For renting couple families the threshold at which UC starts to be withdrawn has been reduced by £30 a month; for renting lone parents it has been reduced by £71 a month. UC is withdrawn at the rate of 63p in the pound for all earnings above the work allowance, after tax and national insurance.

So the work allowance cuts mean that couple families lose 63 per cent of £30 a month, i.e. £18.90 a month, and lone parents will lose 63 per cent of £71 a month, i.e. £44.73 a month.

A full-time worker earning £7.50 an hour (the National Living Wage in 2017/18) will take home just £1.89 per additional hour they work:

- After deductions of 32p in the pound for income tax and national insurance, their net hourly wage is £5.10.
- After UC deductions of 63p in the pound of their net earnings, their effective hourly take home pay is £1.89.

In order to recoup £18.90 a month, a couple would have to work 10 additional hours a month, adding up to 17 extra working days a year. A lone parent would have to work 24 extra hours a month, or 41 extra days a year to recoup the £44.73 they have lost. That is nearly two additional months of full-time work in a year, which is clearly unrealistic for a parent already working full time.

3h. Cuts will put up to a million more children in poverty

Cuts in the tax credit system

Tables 3.6 and 3.7 show the additional number of children and working-age adults expected to fall into poverty between 2010 and 2020 as a result of cuts in the tax credit system. This can also be read as the number who would be kept from poverty by the reversal of cuts. As this modelling does not include the transition to universal credit, this is not a projection of poverty figures in 2020. Its purpose is to demonstrate the extent to which cuts to tax credits and other benefits in the tax credit system are poverty-producing, compared with the system as it stood in 2010, which could have been maintained through to 2020. All poverty figures are rounded to the nearest hundred thousand.

Overall, the cuts are expected to put 600,000 additional children into poverty[65] after housing costs (700,000 before housing costs) in a tax credit system. Restoring the uprating of children's benefits and compensation for past years of inadequate uprating would keep 400,000 children from poverty after housing costs (also 400,000 before housing costs). Reversing the package of cuts affecting young children would keep 100,000 children from poverty (200,000 before housing costs) and reversing the two-child limit or the benefit cap would each keep an estimated 100,000 children from poverty (either before or after housing costs). Just as importantly, these measures would also reduce the poverty gap (how far families fall below the poverty line).

An alarming number of children are also expected to enter severe poverty (with an income below 50 per cent of the median) as result of the cuts. These figures are only available on a before housing costs basis. As a whole the cuts will mean an additional 500,000 children in severe poverty; 400,000

[65] The poverty threshold is 60 per cent of median income, equivalised for household composition.

would be in severe poverty as a result of sub-inflationary uprating of children's benefits, and 100,000 as a result of each of the two-child limit, the benefit cap and the package of cuts affecting young children.

These effects on severe poverty show the cuts are not just pushing people slightly below the poverty line, but will drive a large number of families into deep poverty.

The cuts also create additional poverty among working-age adults, particularly uprating decisions, but the impact on child poverty is greater.

Table 3.6 Additional child poverty effect of cuts to benefits and tax credits

	Children in poverty (<60% median income) AHC			Children in poverty (<60% median income) BHC			Children in severe poverty (<50% median income) BHC		
	Total	Under-5s	Over-5s	Total	Under-5s	Over-5s	Total	Under-5s	Over-5s
TC2010-TC2015									
All cuts 2010-2015	100,000	-	100,000	100,000	-	100,000	100,000	-	100,000
All uprating decisions	100,000	100,000	100,000	100,000	-	100,000	100,000	-	100,000
Uprating of children's benefits	200,000	100,000	100,000	100,000	100,000	100,000	100,000	-	100,000
Uprating of child benefit	-	-	-	-	-	-	100,000	-	-
Uprating of child tax credit	100,000	100,000	100,000	100,000	-	100,000	100,000	-	-
Cuts affecting young/first children	-	-	-	-	-	-	-	-	-
Benefit cap	100,000	-	100,000	100,000	-	-	-	-	-
TC2015-TC2016									
All cuts since 2010	500,000	100,000	300,000	600,000	200,000	400,000	400,000	100,000	300,000
All uprating decisions	200,000	-	200,000	200,000	100,000	200,000	200,000	100,000	100,000
Uprating of children's benefits	100,000	-	100,000	100,000	100,000	100,000	100,000	-	100,000
Uprating of child benefit	-	-	-	-	-	-	-	-	-
Uprating of child tax credit	100,000	-	100,000	100,000	-	100,000	100,000	-	-
Cuts affecting young/first children	100,000	-	100,000	200,000	100,000	100,000	100,000	100,000	100,000
Benefit cap	-	-	-	100,000	-	100,000	100,000	100,000	100,000
Two-child limit	100,000	-	-	100,000	100,000	100,000	100,000	100,000	100,000
TC2010-TC2016									
All cuts since 2010	600,000	200,000	400,000	700,000	300,000	500,000	500,000	200,000	400,000
All uprating decisions	800,000	200,000	600,000	900,000	300,000	600,000	600,000	200,000	400,000
Uprating of children's benefits	400,000	100,000	300,000	400,000	100,000	300,000	400,000	100,000	300,000
Uprating of child benefit	100,000	-	100,000	100,000	100,000	100,000	100,000	-	100,000
Uprating of child tax credit	300,000	-	200,000	300,000	100,000	200,000	300,000	100,000	200,000
Cuts affecting young children	100,000	-	100,000	200,000	100,000	100,000	100,000	-	100,000
Benefit cap	100,000	-	-	100,000	-	100,000	100,000	-	100,000
Two-child limit	100,000	-	-	100,000	100,000	100,000	100,000	100,000	100,000

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model. Numbers may not sum due to rounding.

Table 3.7 Additional working-age poverty effect of cuts to benefits and tax credits (TC2010 to TC2016)

	Adults in poverty (<60% median income) AHC	Adults in poverty (<60% median income) BHC	Adults in severe poverty (<50% median income) BHC
TC2010-TC2015			
All cuts 2010-2015	-	200,000	200,000
All uprating decisions	100,000	100,000	100,000
Uprating of children's benefits	100,000	100,000	100,000
Uprating of child benefit	-	-	-
Uprating of child tax credit	100,000	100,000	-
Cuts affecting young/first children	100,000	100,000	-
Benefit cap	-	-	-
TC2015-TC2016			
All cuts since 2010	400,000	500,000	400,000
All uprating decisions	200,000	300,000	200,000
Uprating of children's benefits	100,000	100,000	-
Uprating of child benefit	-	-	-
Uprating of child tax credit	100,000	100,000	-
Cuts affecting young/first children	100,000	100,000	100,000
Benefit cap	-	100,000	100,000
Two-child limit	100,000	100,000	100,000
TC2010-TC2016			
All cuts since 2010	700,000	800,000	700,000
All uprating decisions	700,000	900,000	700,000
Uprating of children's benefits	200,000	300,000	200,000
Uprating of child benefit	100,000	100,000	-
Uprating of child tax credit	200,000	200,000	200,000
Cuts affecting young children	-	100,000	100,000
Benefit cap	100,000	100,000	100,000
Two-child limit	100,000	100,000	100,000

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

N.B. some changes are not included in the poverty analysis as these are not part of the IPPR model and family losses had to be modelled manually: principally cuts to local housing allowances but also cuts to the Sure Start Maternity Grant and the abolition of the Health in Pregnancy Grant. This means that the overall poverty impacts of the cuts may be underestimated.

Cuts in the universal credit system

Universal credit was introduced with the promise of reducing poverty. However our analysis indicates that the cuts to universal credit will be heavily poverty-producing. Were universal credit to be fully implemented by 2020 (ignoring transitional protection and any possible dynamic effects), there would be a million more children in poverty (after housing costs) following the cuts than there would have been had the 2013/14 system been retained.

Again this is not a child poverty projection for 2020, but a comparison of the two universal credit systems and an indication of the extent to which universal credit has been hollowed out and its promise of poverty reduction abandoned.

The freeze of most elements of universal credit and inadequate uprating of child benefit alone would mean an additional 300,000 children in poverty, and work allowance cuts and the two-child limit each an additional 200,000 children (before or after housing costs). The removal of the first child premium and the freeze of the child element will together put 200,000 children into poverty after housing costs (300,000 before housing costs). The cuts will also put 900,000 working-age adults into poverty after housing costs (800,000 before housing costs).

The effects on severe poverty (incomes below 50 per cent of the national median, before housing costs) are particularly alarming, with 900,000 children and 800,000 adults expected to be pushed into severe poverty by the cuts. Reversing the work allowances would keep 200,000 children and 200,000 adults from severe poverty. Restoring the child element (both the first child premium and uprating) or scrapping the benefit cap would each protect 200,000 children and 100,000 adults from severe poverty. Again all of these policies would also reduce the poverty gap.

Again there are large numbers of families facing severe losses and being driven into deep poverty; cuts are not simply moving people from just above to just below the poverty line.

Tables 3.8 and 3.9 show the effects on child and adult (working-age) poverty of cuts to universal credit. As noted above, these do not include the effect of cuts to local housing allowances within universal credit which will probably to increase the poverty impacts of the cuts.

Table 3.8 Additional working-age poverty effect of cuts to universal credit and child benefit (UC2013 to UC2016)

	Adults in poverty (below 60% median income) (AHC)	Adults in poverty (below 60% median income) (BHC)	Adults in severe poverty (below 50% median income) (BHC)
All cuts since 2013	900,000	800,000	800,000
All uprating decisions	300,000	400,000	300,000
Freeze of child benefit and child element	100,000	100,000	100,000
Freeze of child benefit	-	-	-
Freeze of child element	100,000	100,000	100,000
Removal of the first child premium	100,000	100,000	100,000
Cuts to the child element (first child premium and freeze)	200,000	300,000	100,000
Work allowance cuts and freeze	300,000	300,000	200,000
Benefit cap	-	100,000	100,000
Two-child limit	100,000	100,000	-

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Table 3.9 Additional child poverty effect of cuts to universal credit and child benefit (UC2013 to UC2016)

	Children in poverty (below 60% median income) (AHC)			Children in poverty (below 60% median income) (BHC)			Children in severe poverty (below 50% median income) (BHC)		
	Total	Under-5s	Over-5s	Total	Under-5s	Over-5s	Total	Under-5s	Over-5s
All cuts since 2013	**1,000,000**	300,000	700,000	**1,000,000**	300,000	700,000	**900,000**	300,000	600,000
Universal credit freeze and child benefit uprating	**300,000**	100,000	200,000	**400,000**	100,000	200,000	**200,000**	100,000	100,000
Freeze of child benefit and child element	**200,000**	-	100,000	**100,000**	100,000	100,000	**100,000**	-	100,000
Freeze of child benefit	**-**	-	-	**-**	-	-	**-**	-	-
Freeze of child element	**100,000**	-	100,000	**100,000**	-	100,000	**100,000**	-	-
Removal of the first child premium	**100,000**	-	100,000	**200,000**	100,000	100,000	**100,000**	-	100,000
Cuts to the child element (first child premium and freeze)	**200,000**	100,000	200,000	**300,000**	100,000	200,000	**200,000**	100,000	100,000
Work allowance cuts and freeze	**200,000**	100,000	200,000	**200,000**	100,000	200,000	**200,000**	-	100,000
Benefit cap	**100,000**	-	100,000	**100,000**	-	100,000	**200,000**	-	100,000
Two-child limit	**200,000**	100,000	100,000	**200,000**	100,000	100,000	**100,000**	-	100,000

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model. Numbers may not sum due to rounding.

4. What do changes mean for particular households?

This section presents analysis of the impact of cuts on the incomes of specific model households (listed in Box 4.1), under a range of working patterns.

We modelled net incomes *after housing and childcare costs* both for families who do not pay any childcare costs (for example because grandparents provide childcare) and for those who rely entirely on paid childcare if they work outside the hours of school or free childcare provision. We assume that the latter group claim the childcare element of tax credits or universal credit which partially subsidises costs. In reality many families use a patchwork of free and paid childcare: their income would be somewhere in between our 'with childcare costs' and 'no childcare costs' models.

We consider families in both an average cost area (assuming average childcare costs[66] and rent at the national average local housing allowance) and those in a high-cost area (using London childcare costs and local housing allowances for outer London). In reality some families will face rents which exceed their local housing allowance cap, as discussed, meaning their income (after housing costs) would in fact be lower. Families are assumed to be renting privately.

The analysis in this section allows us to explore how expected incomes have changed for families in different circumstances due to cuts and changes to benefits, both within the tax credit or universal credit system and in the move from tax credits to universal credit, and also how the rewards from work have changed.

We focus on families with children aged either two or primary school age, in order to explore the effect on family incomes of having to manage childcare costs either for a young child not yet eligible for thirty hours of free childcare a week, or for child requiring childcare before and after school and during school holidays. This also allows us to model the hypothetical effects of additional childcare support targeting these groups (discussed later in section 5c).

Box 4.1 Model families

Family 1. Lone parent over 25 on 'national living wage', two children (two and five), average cost area.
Family 2. Lone parent over 25 on median wage, two children (two and five), average cost area.
Family 3. Lone parent over 25 on 'national living wage', one child (two), average cost area.
Family 4. Couple both over 25, on 'national living wage', two children (two and five), average cost area.
Family 5. Couple both over 25, on 'national living wage', two children (two and five), high cost area.
Family 6. Couple both under 25, on minimum wage, two children (two and five), average cost area.
Family 7. Couple both over 25, on 'national living wage', three children (two, five and seven), average cost area.
Family 8. Couple both over 25, on the median wage, two children (two and five), high cost area.

[66] Childcare costs are based on the 2016 Family and Childcare Trust Childcare Costs Survey, uprated to 2020/21 using CPI, which provides both national average costs for children of different ages, and costs in London which are used for the high-cost scenarios.

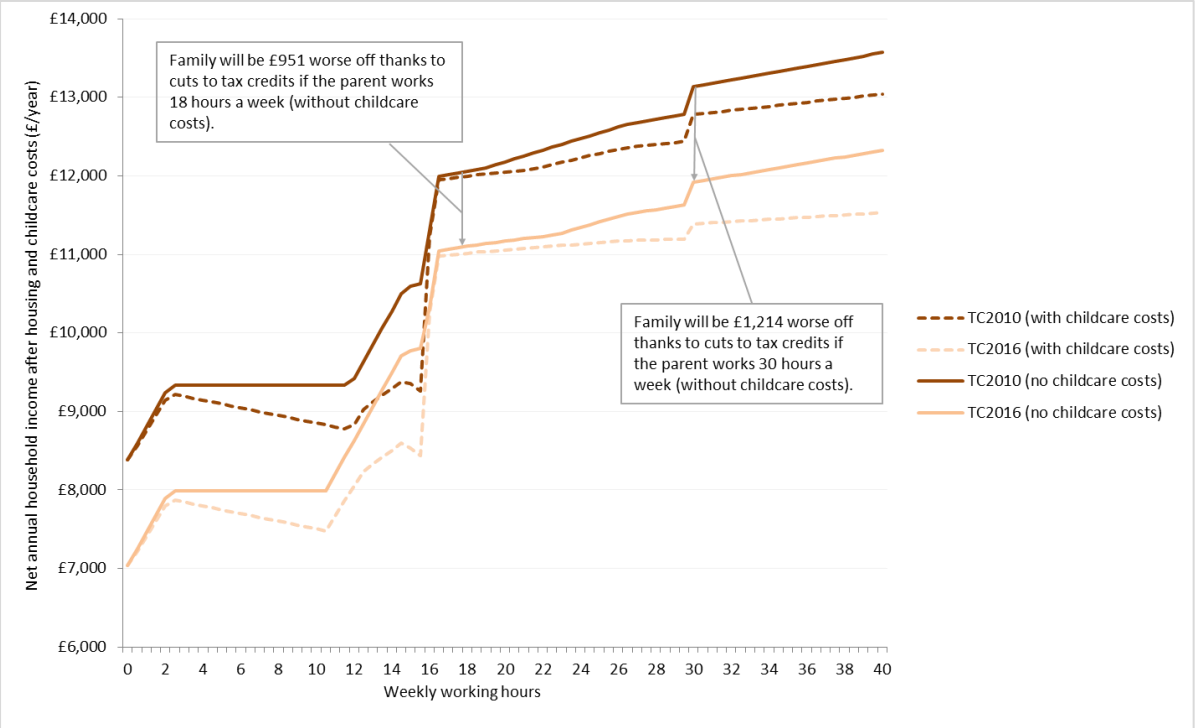
4a. Cuts in the tax credit system make everyone worse off

The effect of changes to the tax credit and legacy benefits systems since 2010 has been a straightforward reduction in family incomes, for all family types and regardless of hours worked.[67] Losses for our model families range from around £800 to around £2,700 depending on family structure and working pattern. Families 3 and 4 are presented as examples.

Family 3. Lone parent with one child aged two, earning the 'national living wage', average-cost area

This family would be £1,346 a year (16 per cent) worse off in 2020 if the parent did not work but instead stayed at home to look after their child. If working 18 hours a week they would be £951 a year (8 per cent) worse off in 2020 without childcare costs, or £981 a year worse off with childcare costs. If the parent works 30 hours a week they would be £1,214 a year (9 per cent) worse off without childcare costs (£1,390 a year or 11 per cent with childcare costs).

Figure 4.1 Effect of tax credit and legacy benefit cuts on the income of a lone parent with two children working up to 40 hours a week on the 'national living wage'



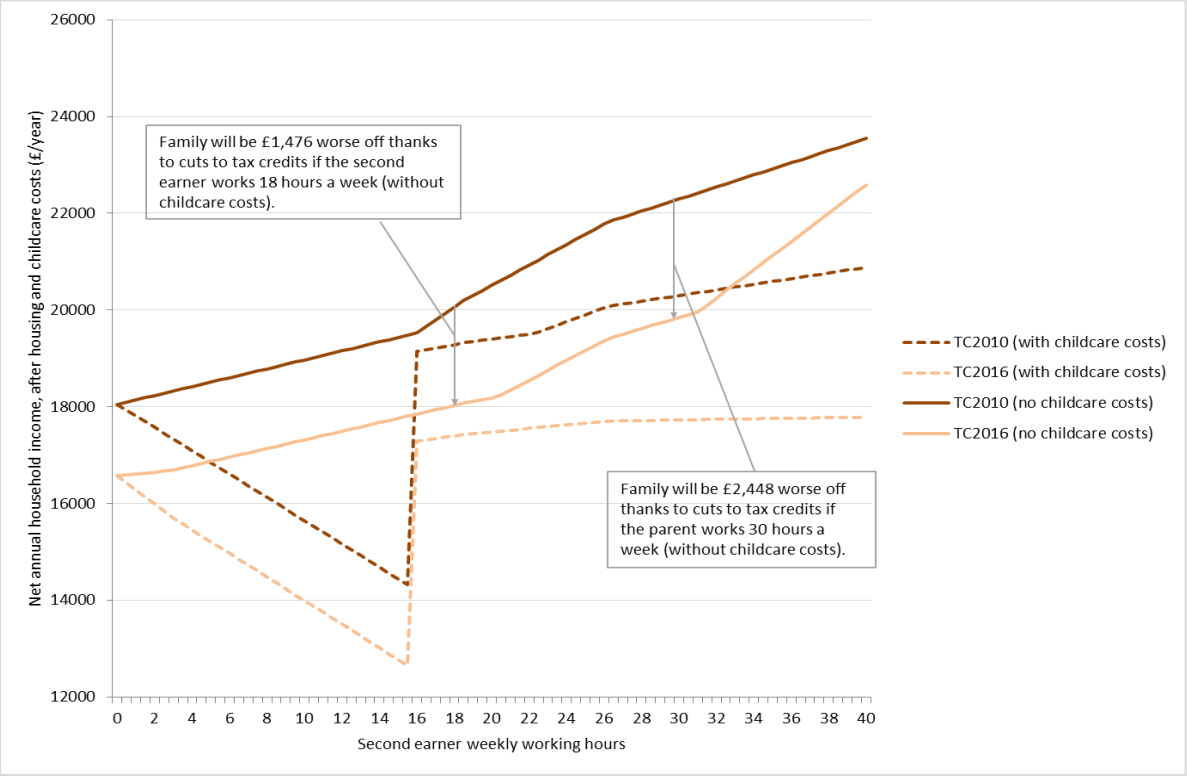
Source: IPPR analysis using the Resolution Foundation micro-simulation model

Family 4. Couple with two children, both earning the 'national living wage' in an average-cost area

This typical 'just about managing' family would be £1,476 a year (8 per cent) worse off in 2020 under TC2016 than TC2010 if one parent works full time and the second stays at home with the children. This loss could only be recouped by the second earner starting work at 19 hours a week or more, with no childcare costs. If the family needed paid childcare, they could not recoup this loss even if the second earner worked 40 hours a week (Figure 4.2).

[67] There was an increase in the value of the child element in 2011/2012 but this is outweighed by the effect of cuts.

Figure 4. Effect of tax credit and legacy benefit cuts on the income of a couple with two children, with one full-time earner and a second earner working up to 40 hours a week, both on the 'national living wage'



Source: IPPR analysis using the Resolution Foundation micro-simulation model

If the second earner already worked 30 hours, they would be £2,448 a year (11 per cent) worse off in 2020 without childcare costs, and £2,572 (13 per cent) worse off with childcare costs.

The reduced support for childcare costs also means that the incentives for a second earner in this family to work more than 16 hours have become almost non-existent if they have to pay for childcare.

4b. The promises of universal credit have been broken for many families

Universal credit in its original design promised to make most families better off than under the 2010 tax credit and benefit system, even though some of the cuts to tax credits and other benefits early in the decade fed into universal credit's initial design, and despite other cuts being made in universal credit from the outset, in particular to disability-related payments and rates for young parents.

Our modelling shows that couples with two children and either one or two earners would have been better off under UC2013 than TC2010, i.e. if they had moved on to universal credit in its original design, unless the parents were under 25 or if they had fairly high childcare costs (in the case of our model families, where families have one two year old and one primary school aged child and both

work full time, or with one two year old and two primary school aged children and the second earner works at least 16 hours a week). In universal credit the lower under-25 rate of the standard allowance was extended to parents (unlike in tax credits), meaning families with young parents tend to lose out in the transition.

Working lone parents would have been better off under UC2013 than TC2010 at most hours of work if they had no childcare costs, or if they worked fewer than 16 hours (before eligibility for childcare costs kicks in under tax credits) with childcare costs.

This fits with the stated intentions of universal credit to incentivise shorter hours of work as a first step for lone parents (back) into the workplace, and to be more generous to couples than lone parents compared with the tax credit system. However the change could be viewed as punitive to those staying at home with very young children (as lone parents not in work would have lost out) or those facing high childcare costs.

Yet universal credit today (UC2016) looks very different than before the cuts (UC2013). Families with more than two children will see the most dramatic reduction in incomes thanks to policies such as the two-child limit on payments. Cuts and changes to universal credit (and child benefit) since its introduction also penalise lone parents, whether working or not, including those with very young children, as well as couples with young children where only one parent works, or where a second earner does not work a large number of hours.

The government has argued that the changes to universal credit have improved work incentives, and when the work allowances were cut, the government suggested that families could make up the loss by working a few more hours each week.[68] Worked examples in Box 3.3 showed that this would not be possible for some families, and our household-level analysis bears this out.

These families will, in many cases, be completely unable to make up for these losses by working a few extra hours. They would have to increase their hours significantly just to maintain the same level of income, which – even if possible – would mean compromising time spent with their young children. In some cases the difference in income between the two systems is so great that it cannot be recovered by simply working more hours, without a stepchange in pay rates. If families pay for childcare they will also face higher outgoings if they increase their hours, as 15 per cent of childcare costs are not covered by universal credit, and childcare costs mean that the returns from working extra hours can be low.

The only giveaways which have come in return for cuts tend to benefit families who earn higher amounts and/or work longer hours. Cuts have been made to the level of the main elements of universal credit (how much it pays per adult and child) and work allowances (how much families can earn before universal credit is withdrawn) while giveaways have come in the form of increased support for childcare and a slightly reduced taper rate (the rate at which universal credit is withdrawn as earnings increase). Overall these giveaways are worth much less than the cuts, so do not compensate for losses. However, a small number of families who claim a large amount of childcare and have higher earnings from work may be better-off after the changes overall despite the cuts.

[68] Department for Work and Pensions, *Government response to SSAC Occasional Paper 15: Universal Credit: priorities for action*, 21 December 2015

Overall it is clear that the effect of changes to universal credit has been to significantly reduce the income it promised for families, except for those with one or two children who are working a high number of hours (or earning relatively high wages) and claiming childcare costs for a siginifcant number of hours of childcare a week. This may be regarded as a work incentive, but for families with young children it may simply not be possible or desirable to increase hours to the extent needed to recoup the losses. Importantly, work allowance cuts have also reduced the gains for working extra hours or moving into work for some families, especially lone parents.

Universal credit cuts leave lone parents worse off and reduce their rewards from work

All the lone parent families we modelled lose out considerably from universal credit cuts. Only a lone parent working close to 40 hours a week and using very large amounts of paid childcare (47 hours a week for their two year-old and 18 hours a week for their five year-old) would see enough benefit from the increased childcare subsidy to offset the effect of cuts, but this is an unlikely circumstance. A lone parent with one pre-school child would still be worse off as a result of the cuts even if working 40 hours a week and relying on paid childcare for everything outside the free nursery entitlement.

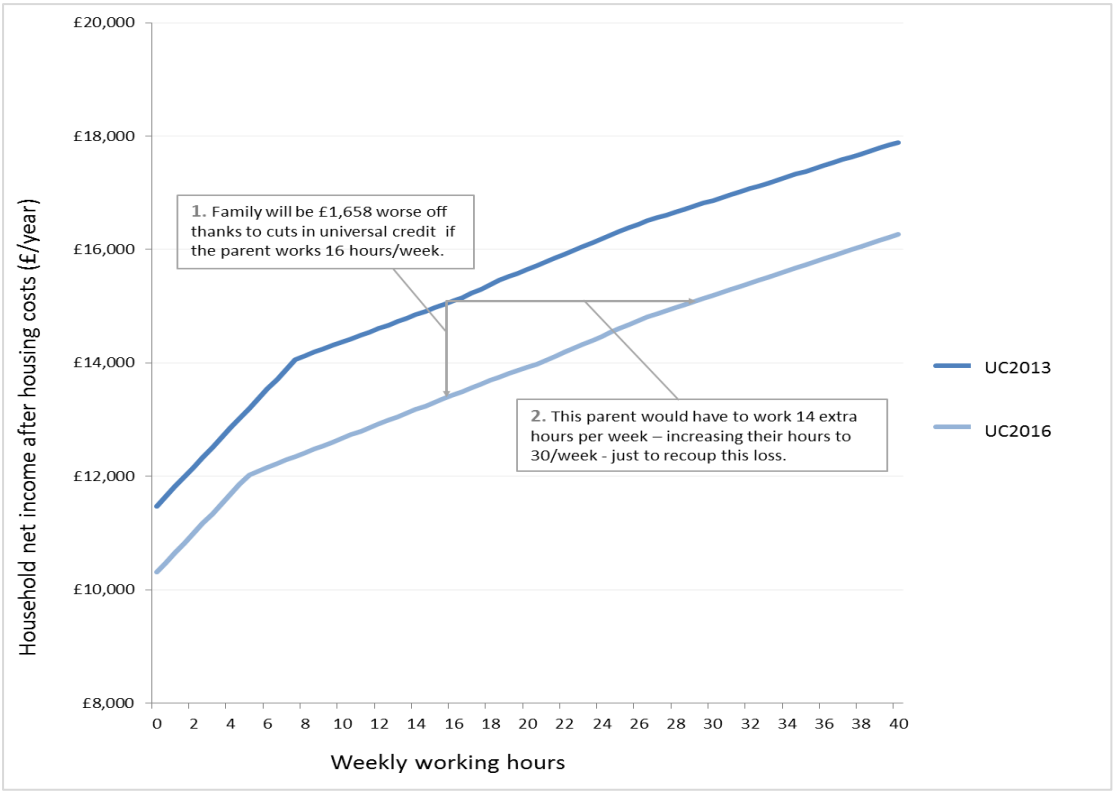
Family 1. Lone parent of two children aged two and five, working for the 'national living wage', renting privately in an average-cost area

Without childcare costs

This family would be substantially worse off in 2020 as a result of cuts to universal credit, regardless of whether the parent worked and for how many hours. If not working, in order to look after their young children, they would be 10 per cent (£1,167 a year) worse off as a result of the cuts. The cash loss would be the same if they worked up to 5 hours a week; at this very small number of hours, the parent is not yet affected by the large reduction in the work allowances for lone parents.
If this lone parent worked more than 5 hours a week, their award would start to be tapered under UC2016 because of the lower work allowance. Under UC2013, they could have worked around eight hours a week before withdrawals started. Working between eight and 40 hours a week, their overall income is reduced by all the cuts to universal credit and the only 'compensation' – the slight reduction in the taper rate announced in 2016 – has minimal effect, leaving the family between £1,619 and £1,743 worse off overall.

If working 16 hours a week this family would be £1,658 worse off in 2020 under UC2016 than UC2013. They would have to work 14 extra hours a week – two whole days – just to recoup this difference (Figure 4.3) almost doubling their hours to 30 a week.

Figure 4.3 Effect of universal credit cuts on the income of a lone parent with two children working up to 40 hours a week on the 'national living wage'



Source: IPPR analysis using the Resolution Foundation micro-simulation model

The heavy cuts to the work allowance have also meant that the rewards for starting work are reduced. Table 4.1 shows the effective hourly earnings that this parent would take home in 2020, after deductions, universal credit withdrawals and rent payments, if starting work at 12 or 24 hours a week, as well as the effective tax rates in terms of pence lost for every pound of gross earnings. This is again assuming the parent does not have to pay for any childcare over the free provision.

Effective hourly earnings here refers to additional income per hour worked, comparing incomes when not working with incomes when working 12 or 24 hours, after all deductions and rent payments. Effective tax rate means the deduction rate on the additional income gained when moving into work at 12 or 24 hours a week, including tax, national insurance, universal credit withdrawals and rent payments.

Table 4.1 Effective hourly earnings have reduced, and effective tax rates increased, for a lone parent with two children entering work on the 'national living wage', without childcare costs

	Family income (£/year)		Effective hourly earnings		Effective tax rate	
Weekly hours	UC2013	UC2016	UC2013	UC2016	UC2013	UC2016
0	£11,476	£10,308	n/a	n/a	n/a	n/a
12	£14,610	£12,925	£5.01	£4.18	39%	49%
24	£16,185	£14,468	£3.76	£3.32	50%	56%

Source: CPAG analysis of IPPR modelling output

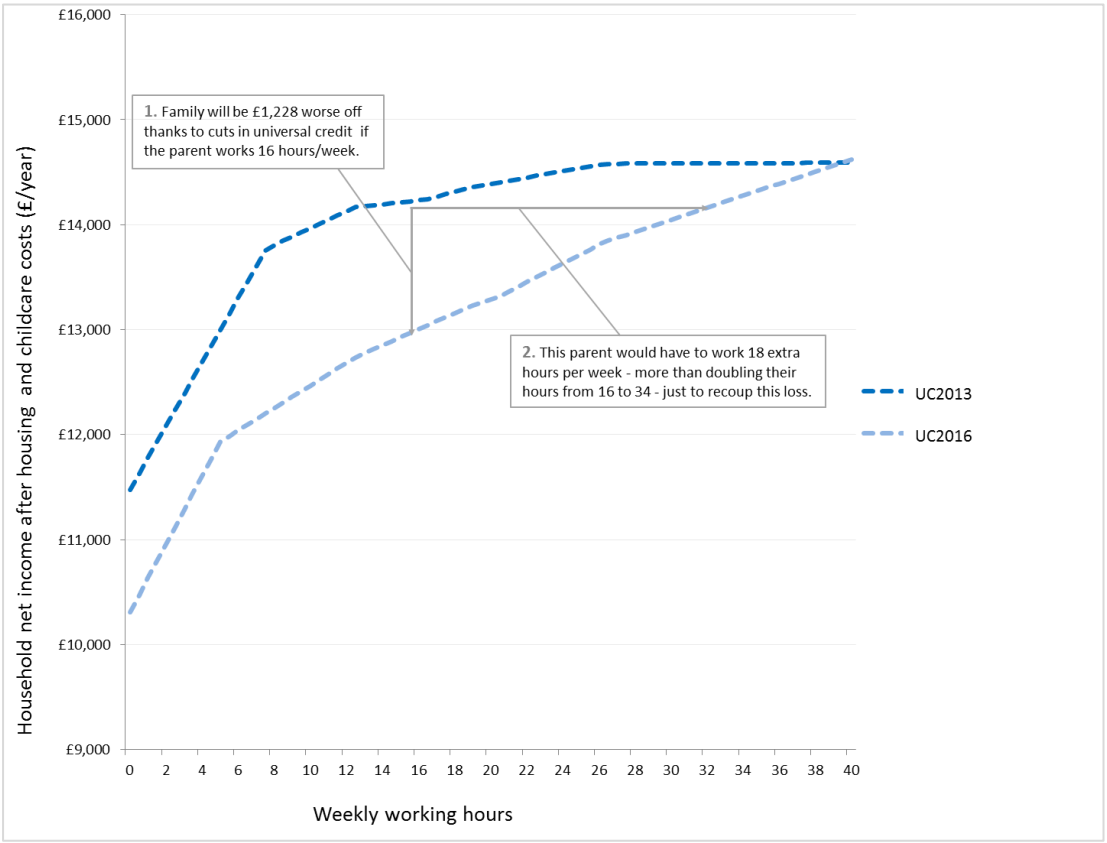
Only if this parent is already working longer hours will they see any improvement in hourly returns from work, for example if they moved from 24 to 30 hours a week they would now take home £2.30 an hour on average for the additional hours worked, compared with £2.18 under the old system, and keep 2p more in the pound earned. This improvement is, however, of very limited help when you consider that if working 30 hours a week they will still be more than £1,600 worse off than in the absence of the cuts.

The introduction of the 'national living wage' increased gross hourly pay for minimum wage earners over 25 by 80p an hour (from £6.70 to £7.50 an hour), but the work allowance cuts have cut the effective *take-home pay* for this lone parent by 83p an hour.

With childcare costs

If the family had childcare costs they would still be worse off in 2020 under UC2016 than UC2013, regardless of working hours (we have modelled up to 40 working hours a week), but the difference is not as stark because of the increased childcare subsidy in UC2016. However, overall the family's income once in work would be lower than if they did not have to pay for childcare, as they still have to pay a proportion of the childcare cost. As this cost increases as with hours of work, it is harder for this family to increase their income by working more hours. If working 30 hours a week, this family will have a net income (after childcare costs) of £14,047 under UC2016, compared with £15,189 for an identical family who have free childcare.

Figure 4.4 Effect of universal credit cuts on the income of a lone parent with two children working up to 40 hours a week on the 'national living wage', with childcare costs



Source: IPPR analysis using the Resolution Foundation micro-simulation model

If the parent in this example worked 16 hours a week, the family would be £1,228 worse off in 2020 as a result of the cuts to universal credit, after rent and childcare costs. They would have to more than double their working hours to 34 a week –18 additional hours - just to recoup this (Figure 4.4).

As this parent's hours increase, the difference between UC2016 and UC2013 narrows because the increased support for childcare and the lower taper compensates partially for the cuts. But they would have to work 40 hours a week to reach a point where their overall income is unaffected by the cuts, something many parents would not find compatible with caring for children aged two and five.

The large reduction in work allowances for lone parents also reduces the rewards they would experience from entering work at between six and 18 hours a week. If entering work at 12 hours a week (hours which might be compatible with the government's offer of 15 hours free childcare for two year-olds whose parents claim universal credit, allowing for a small amount of travel time), their effective hourly income (after withdrawals of universal credit, rent and childcare payments) will be £3.79 an hour under UC2016, compared with £4.24 under UC2013. Their effective tax rate will be 54 per cent instead of 49 per cent.

If they went into work at more than 18 hours/ week, their effective hourly income would be higher under universal credit today than under the pre-cuts version, thanks to increased support for childcare. For example if they entered work at 24 hours, their effective hourly income would be £2.65 under universal credit today compared with £2.43 before the cuts (after all deductions plus rent and childcare payments). However they would still be £880 a year worse off overall. See Table 4.2.

Even with the increased childcare subsidy in universal credit, and the government's offer of 15 hours free childcare a week for two-year-olds, childcare costs (along with universal credit withdrawals) still mean that the rewards from working more hours would be very limited for this parent. If they doubled their hours from 10 to 20 a week, their net income would increase by just £820 a year or £16 a week. Universal credit was intended to encourage in-work progression by ensuring people would always be better off if they increased their hours. Yet it is clear that some lone parent families will see extremely low rewards from working more hours, and could end up 'stuck' in low hours of work.

Table 4.2 Overall income, effective hourly earnings, effective tax rates for a lone parent entering work on the 'national living wage', with childcare costs

	Family income (£/year)		Effective hourly earnings		Effective tax rate	
Weekly hours	UC2013	UC2016	UC2013	UC2016	UC2013	UC2016
0	£11,476	£10,308	n/a	n/a	n/a	n/a
12	£14,126	£12,683	£4.24	£3.79	49%	54%
24	£14,511	£13,631	£2.43	£2.65	71%	68%

Source: CPAG analysis of IPPR modelling output

The picture is similar for our other lone parent model families. For a lone parent on the median wage (Family 2), the change in the taper has a greater effect, meaning that if they worked for 37 or more hours a week and claim childcare costs they would be slightly better off in 2020 on UC2016 than UC2013. For a lone parent on the 'national living wage' with just one child (Family 3), childcare costs are not high enough for the increased subsidy to compensate for cuts, even working 40 hours a week,

and the family will simply be worse off by between about £288 a year (if working 40 hours) and £1,457 a year (if working 8 hours a week).

The government has argued that cuts to universal credit must be considered in the context of other policies designed to assist parents to work, often citing the increased support for childcare. Additional childcare hours for three- and four- year-olds, and the increased subsidy in universal credit compared with tax credits, are important steps and ones which CPAG and others campaigned hard to achieve, but our model families illustrate the limitations of existing support for childcare when families have an older or younger child, who may simply be worse off regardless of how many hours they work.

Effect of universal credit cuts on couple families

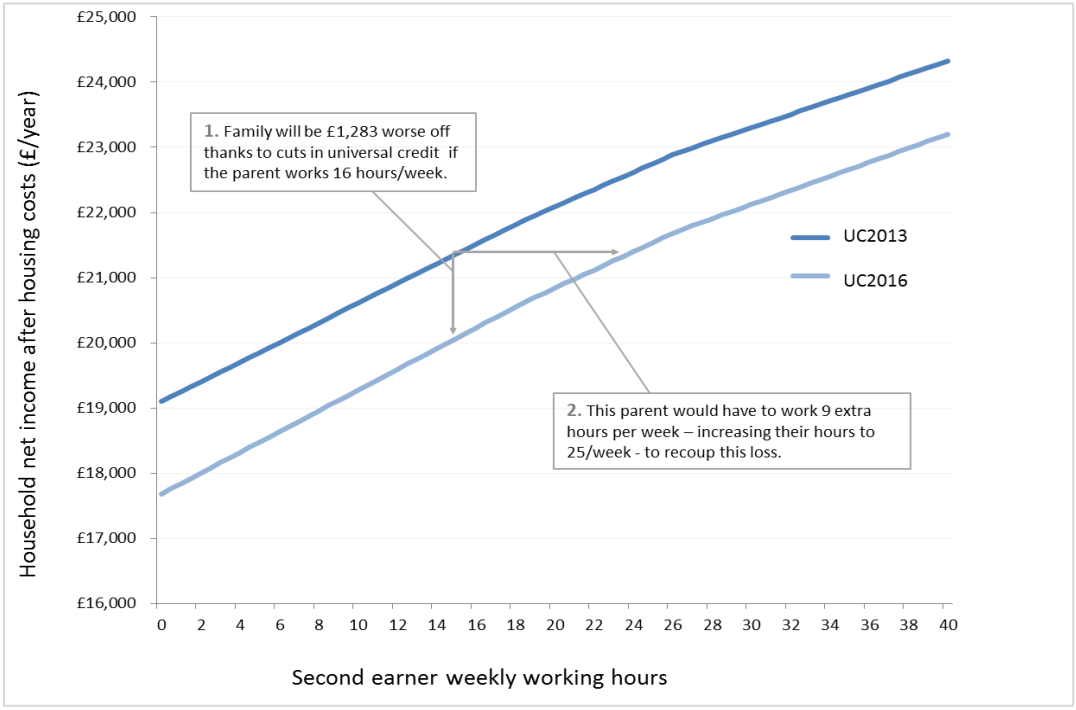
Here we assume that each family already has one full time earner working 37.5 hours a week, and examine the effect of variations in second earner working hours on total net household income.

Family 4. Couple both working for the 'national living wage', with two children aged two and five, renting privately in an average-cost area

Without childcare costs

The family would be more than £1,400 worse off under UC2016 than UC2013 if only one parent worked, and if they had no childcare costs they would be worse off by a similar amount with the second parent in work at any number of hours. The losses become marginally smaller if the second earner works more hours because of the reduced taper rate in UC2016. If the second earner works 16 hours a week, the family would be £1,283 worse off a year as a result of the cuts, for example. They would have to work nine additional hours a week to recoup this amount (Figure 4.5).

Figure 4.5 Effect of universal credit cuts on the income of a couple with two children, with one full-time earner and a second earner working up to 40 hours a week, both on the 'national living wage'



Source: IPPR analysis using the Resolution Foundation micro-simulation model

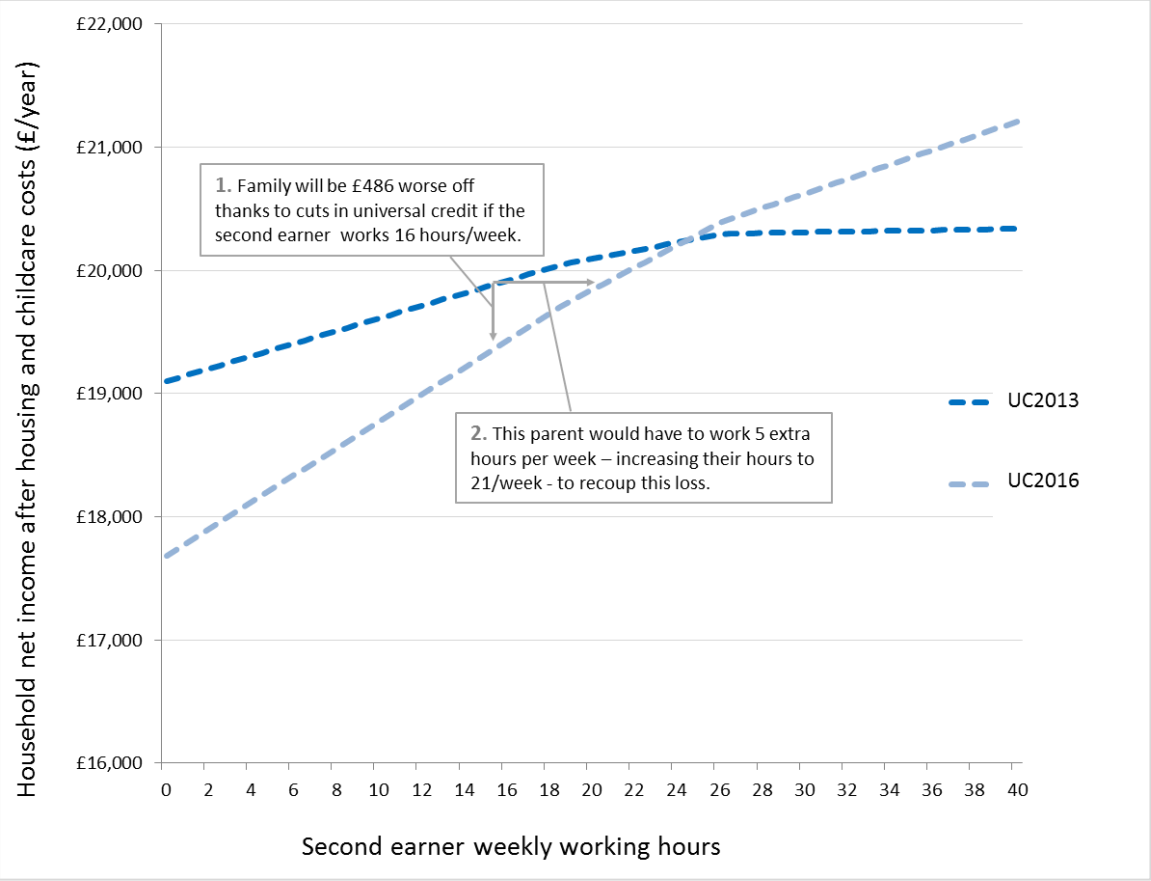
With childcare costs

If the family had childcare costs, they would lose out somewhat less from the changes to universal credit. If the second earner works 16 hours a week this family would be £486 a year worse off in 2020 under UC2016 than under UC2013, and they would have to work five additional hours a week to recoup this loss (see Figure 4.6).

Were the second earner in this family to move into work (from not working) at 16 hours a week, the family would have an effective take-home income from this work of £2.10 an hour compared with £0.98 an hour under UC2013 – a reduction in the effective tax rate from 88 per cent to 75 per cent. However they would remain worse off by £486 than under UC2013.

At smaller numbers of hours, the difference is greater because the family requires less childcare, and benefits less from the increased subsidy. Conversely if the second earner works 25 hours a week or more using paid childcare, they would be better off under UC2016 than UC2013. This tipping point would require them to use 29 hours a week of childcare for their two-year-old and 11 hours a week for their five-year-old.

Figure 4.6 Effect of universal credit cuts on the income of a couple with two children, with one full-time earner and a second earner working up to 40 hours a week, both on the 'national living wage', with childcare costs



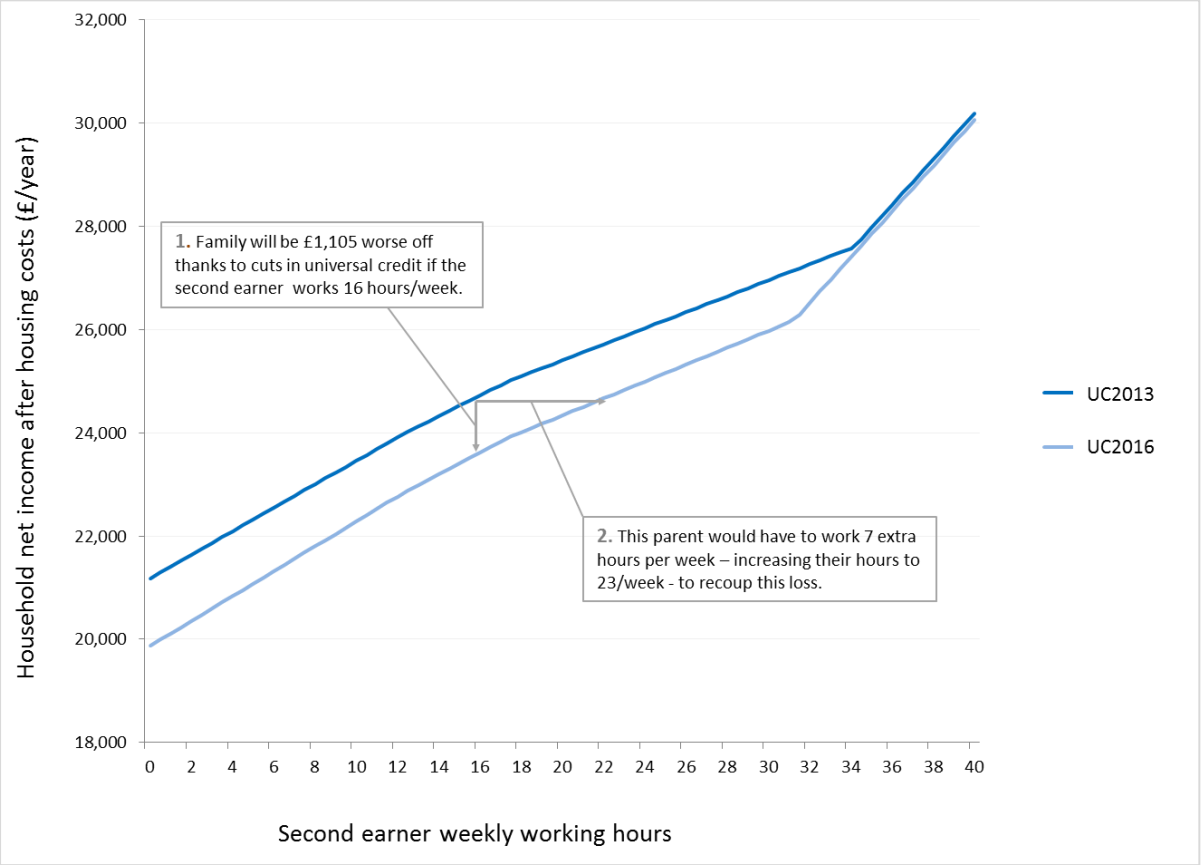
Source: IPPR analysis using the Resolution Foundation micro-simulation model

Family 8. Couple both working for the median wage, with two children aged two and five, in a higher-priced area (outer London)

Without childcare costs

If the family does not have childcare costs (Figure 4.7) they would again be worse off in 2020 under UC2016 than UC2013, by between around £980 and around £1,300 a year, whether they have a single earner or a second earner working up to 30 hours a week. If the second earner worked 16 hours a week, the family would be £1,105 a year worse off, and they would have to work seven additional hours each week to recoup the difference.

Figure 4.7 Effect of universal credit cuts on the income of a couple with two children, with one full-time earner and a second earner working up to 40 hours a week, both on the median wage, in a high-cost area



Source: IPPR analysis using the Resolution Foundation micro-simulation model

If the second parent started work at 16 hours a week, from not working, their effective hourly income would be £4.50 under UC2016. This is slightly better than £4.25 an hour under UC2013, but overall the family will still be worse off by £1,105 than they would have been under UC2013.

If the second earner worked 31 or more hours a week the family would move out of entitlement to universal credit under UC2016 and consequently gain more income from each further additional hour of work (as there are no universal credit withdrawals), so the difference between the systems narrows. After 35 hours a week they would have no universal credit entitlement under UC2013 either. The difference in their income would then be just £128 a year, the result of child benefit cuts.

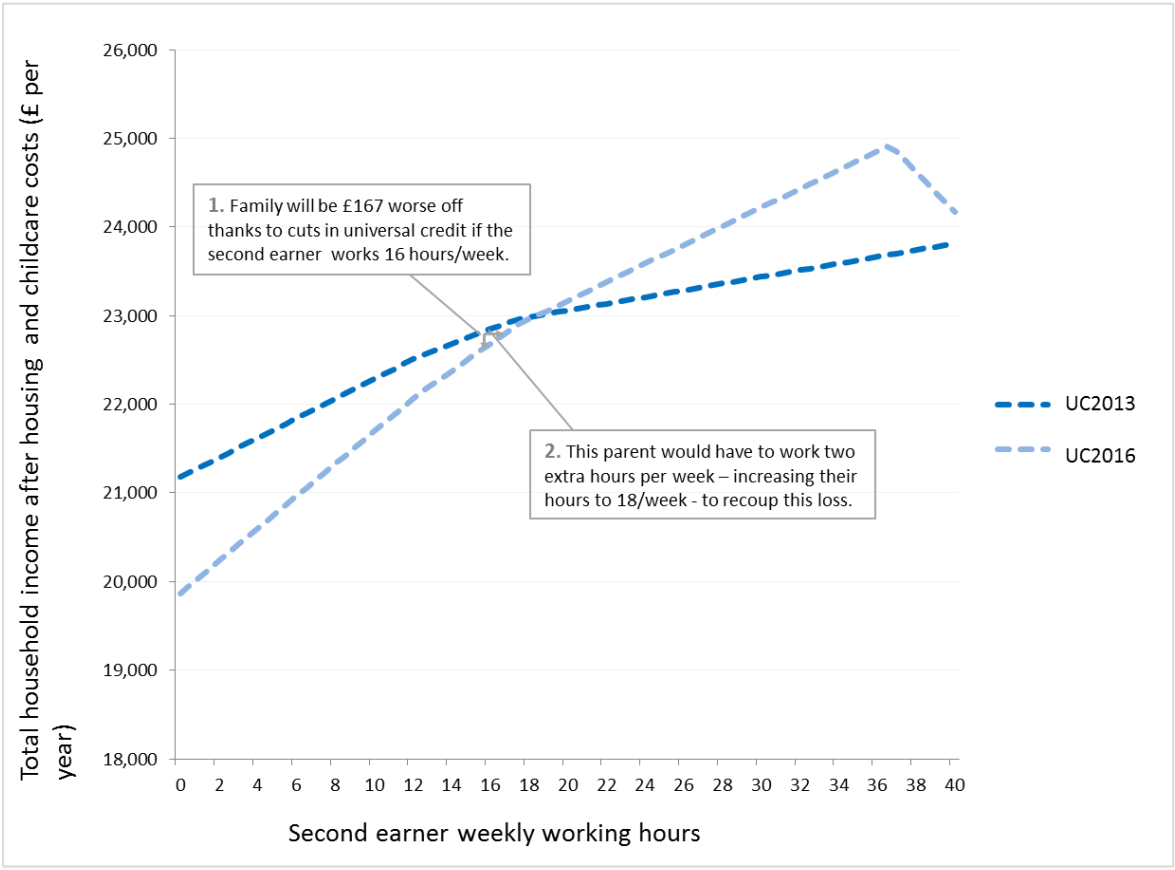
With childcare costs

If the family has childcare costs (Figure 4.8), the combination of the increased childcare subsidy (as childcare costs are higher) and the greater effect of the taper rate on this family (as their hourly earnings are higher) means that the 'break-even point' between UC2013 and UC2016 occurs when the second earner works 18 hours, using 22 hours a week of childcare for their two-year old and nine for their five-year-old.

If only one parent worked the family would be £1,308 worse off in 2020 under UC2016, and if they had childcare costs the second earner would have to work eight hours a week to recoup this. If the second earner worked 16 hours a week, the family would be worse off to a lesser extent (£167 a year) and would have to work two extra hours a week to recoup this difference.

If the potential second earner entered work at 16 hours a week, they would take home an effective hourly income of £3.37 an hour compared with £2 an hour under UC2016. But overall the family's income would, as in the previous example, still be lower.

Figure 4.8 Effect of universal credit cuts on the income of a couple with two children, with one full-time earner and a second earner working up to 40 hours a week, both on the median wage, in a high-cost area, with childcare costs



Source: IPPR analysis using the Resolution Foundation micro-simulation model

Family 7. Couple with three children, on the National Living Wage, in an average-cost area

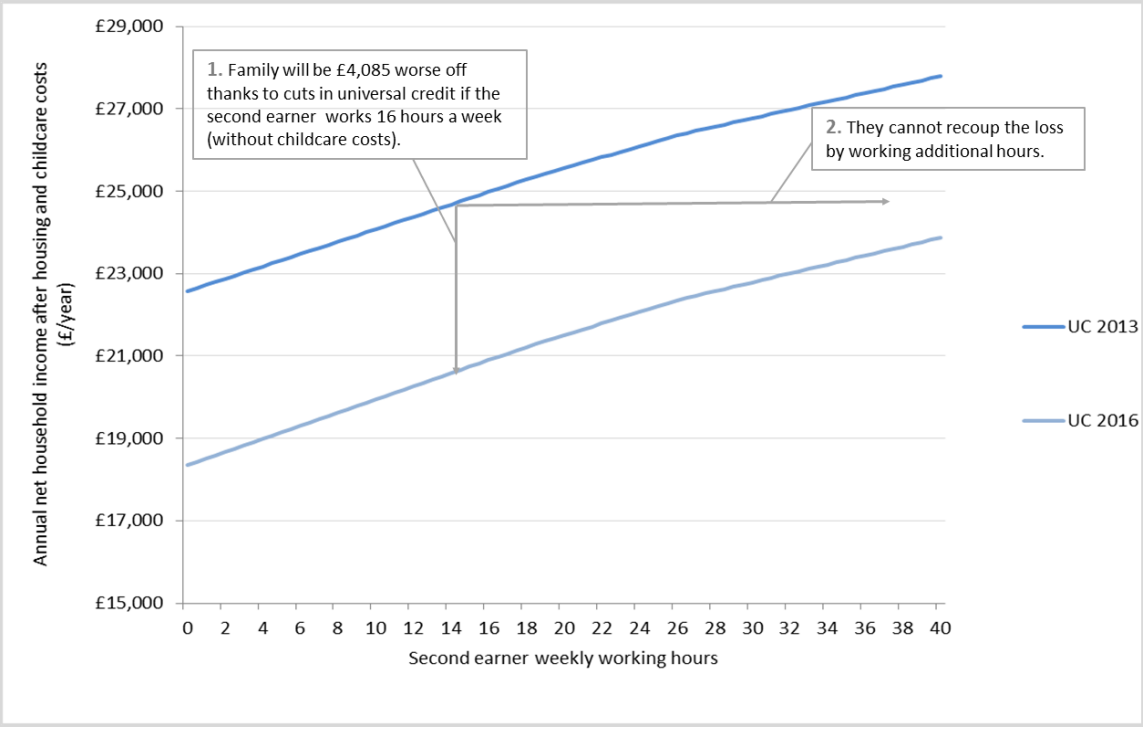
This family sees much greater losses from cuts to universal credit than those with one or two children, as a result of the two-child limit and other reductions in support for children. The additional subsidy for childcare does not come close to offsetting these losses, even though childcare costs are higher.

Without childcare costs

Regardless of the working hours of the second parent, this family would be between £3,900 and £4,300 worse off in 2020 under UC2016 than UC2013 without childcare costs, losing 14 to 18 per cent of the income they could have expected before the cuts. With a single earner they would have an overall household income (after rent) of £18,349 compared with the £22,571 they could have expected under UC2013. The second parent would have to start working almost full time - at least 28 hours a week - to attain the same income.

If the family already had a second earner working 16 hours a week they would be 16 per cent (£4,085 a year) worse off under UC2016 than UC2013, and could not make up this loss even by increasing their hours to 40 a week (Figure 4.9).

Figure 4.9 Effect of universal credit cuts on the income of a couple with three children, with one full-time earner and a second earner working up to 40 hours a week, both on the 'national living wage'



Source: IPPR analysis using the Resolution Foundation micro-simulation model

With childcare costs

If this family used paid childcare the losses would still be very large. With a second earner working 16 hours a week with childcare costs the family would be £3,378 a year (14 per cent) worse off in 2020 under UC2016 than UC2013, and again they could not recoup this difference even by working 40 hours a week.

It is clear that work is now less likely to offer this family – already facing higher than average risks of poverty - a route out of poverty. It is true that under UC2016 the additional take-home income from

an extra hour of work is considerably higher thanks to the increase in support for childcare, but this is poor compensation when at any number of working hours this family remains much worse off.

Are many families really likely to gain from changes to universal credit?

As described above, the only families to benefit from the changes to universal credit since 2013 are those with up to two children, using significant amounts of childcare. This in effect probably means having at least one child aged under three. The lower the wage rate, the more childcare they have to use for the increased subsidy and taper rate to offset cuts.

Lone parents currently make up more than half (54 per cent) of families with children claiming child tax credit, and we can expect this to be similar under universal credit. They are likely to be worse off as a result of cuts in most cases. 15 per cent of families are couples with three or more children, who will lose out from the cuts in spite of increased support for childcare.[69]. A further third (32 per cent) of child tax credit claimants are couple families with one or two children, who could theoretically be better off if they use enough paid childcare.

Our model lone parent families would have to be using upward of 45 hours per week formal childcare for a child aged under three (at age three more free childcare becomes available) *and* more than 17 hours per week for a primary school aged child[70] to be better off under UC2016 than UC2013, though the equivalent costs might be reached if using slightly fewer hours if they had two very young children, as hourly costs are higher. Very few lone parents will be in this situation: fewer than half of lone parents with a child aged under three are in work, and just one in five work full time, including those on maternity leave who would not need childcare.[71] Of those lone parents who work full time, many will use informal childcare (e.g. from grandparents) for at least some of the hours.

Couples with one or two children are more likely to use enough childcare to offset the effect of cuts to universal credit, as their earnings are higher with two people in work and they need to use fewer hours of childcare to reach this break-even point. However, the numbers expected to benefit are still small. First, a minority of families will have a child under three at any point in time (and from an individual household perspective, any benefit from the increased childcare support while children are young will be temporary). Second, only two-thirds of couples with a child under three have both parents in work (again including people on maternity leave or a career break who would not require childcare) and only 31 per cent have both parents in full-time work.[72]

Finally, most children under three do not in reality spend long hours in formal childcare. Our family 4 (two children, both parents earning the 'national living wage') only start to be better off under UC2016 when their two-year-old is in formal childcare for 30 hours a week and their five-year-old for 12 hours a week. Family 8 (both parents earning the median wage but in a higher childcare cost area) would only be better off with their two-year-old in formal childcare for 22 hours a week and their five-year-old for 9 hours a week. If they had just one child, they would have to use even longer hours.

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[69] HM Revenue and Customs, *Child and Working Tax Credits statistics: finalised annual awards – 2015 to 2016, Tables 2.1 and 2.2*, June 2017

[70] Childcare hours are given for a typical term time week, to allow comparison with data from the Childcare and early years survey of parents. More hours would be needed in school holidays and this is reflected in the annual costs.

[71] Office for National Statistics, *Families and the labour market, England, LFS and APS datasets, Table 8*, September 2017

[72] Office for National Statistics, *Families and the labour market, England, LFS and APS datasets, Table 9*, September 2017

National survey data shows that 61 per cent of two-year-olds attend some form of formal childcare but only 37 per cent attend formal childcare *only*, with the rest using informal childcare some of the time. Among two-year-olds who spend time in formal childcare, children attend for an average of 18.5 hours a week, suggesting that it would be relatively rare to spend 30 hours or more in this setting.[73] It is likely to be couples with relatively higher earnings and those in areas where childcare costs are high who benefit most from the additional subsidy, because their additional pay is larger for each extra hour worked and/or the additional 15 per cent of childcare costs paid is worth more.

4c. Those already most at risk of poverty lose most in the move to universal credit

In the long run, the story of this decade will not be of movement between different versions of the tax credit system, or from the early version of universal credit to its current incarnation, but from the tax credit and legacy system as it stood in 2010 (TC2010 scenario) to universal credit as it looks today (UC2016 scenario). It is therefore these systems we compare next.

Broadly speaking, those who lose from the transition are families which already face a greater risk of poverty: lone parents, young parents, and larger families. The biggest winners are those with relatively high earnings; median wage earners in couples do better in the transition than those on the 'national living wage'. The following sections discuss these groups in turn and compare their incomes against the 2015/16 poverty line for a family of their size.[74]

Lone parents and the transition to universal credit

As other analysis has indicated, lone parents fare badly from the transition, yet lone parents make up almost half of families claiming tax credits. The only circumstance in which a lone parent will be significantly better off under UC2016 than TC2010 is if they work in mini-jobs of more than a few hours a week but less than 15, and require paid childcare to do so.

A lone parent who works more or less than this, or who does not require paid childcare because their children are older or they have informal help, would almost always be worse off under UC2016. For our lone parent family 1, with two children, earning the 'national living wage', the difference is often more than 10 per cent and in some cases 18 per cent or up to £2,876 a year. For families 3 (with one child, earning the 'national living wage') and 2 (with two children, earning the median wage), the losses are not quite so severe but can still reach 16 per cent (more than £1,300 a year) or 13 per cent (more than £1,700 a year) respectively. In some cases the changes push these families below the poverty line.

It is also worth remembering that the lone parents in our example families have a two year-old child and are therefore not required to seek any work under universal credit. However if they did not work because they choose to stay and home and look after their young child, they would be more than £1,500 a year worse off in 2020 under UC2016 than under TC2010.

Tax credits were explicitly designed to incentivise work of 16 hours or more. Universal credit was in part designed to smooth work incentives and promote mini-jobs. However the rewards for increasing hours have been substantially reduced by the cuts to universal credit, as discussed above. As others

[73] Department for Education, *Childcare and early years survey of parents: 2014 to 2015, Table 2.3 and Table 2.8*, March 2016
[74] Department for Work and Pensions, *Households Below Average Income 1994/5 to 2015/16, Table 2_2db*, March 2017.

have warned[75] this could lead to lone parents choosing to work fewer hours or even reducing their working hours. Recent DWP analysis found that lone parents on universal credit on average wanted to work 25 hours a week, but that awareness of how different working patterns would affect their income was low.[76]

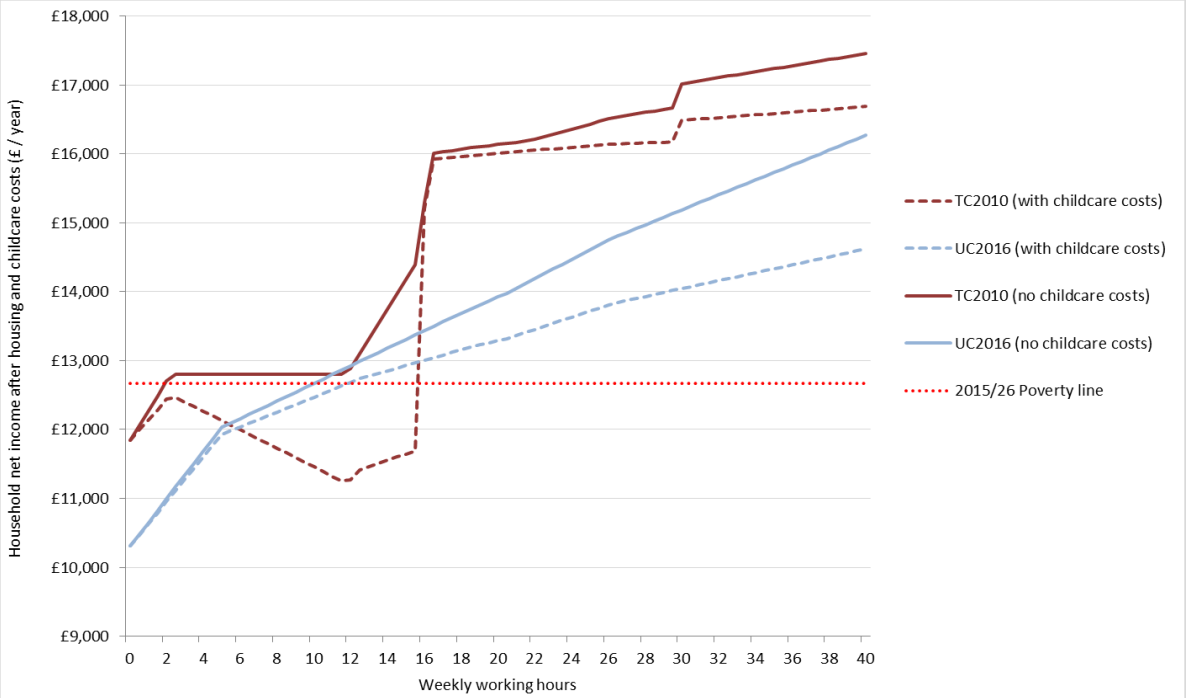
This change in incentives may explain the adoption of in-work conditionality, and the new conditionality requirements for lone parents with children aged three or four to look for work.

The following graphs show how several of our model lone parent families fare in the transition. For reference we have also included a line representing the 2015/2016 poverty line (after housing costs) for each family.

Lone parents with two children, earning the 'national living wage' (Family 1)

This family would become notably worse off in this transition under most combinations of working hours and childcare use. If they were not working – which they are not required to do under either the universal credit or tax credit system – they would be £1,538 a year (13 per cent) worse off in 2020. They would fall £2,634 a year below the poverty line under UC2016 (a 19 per cent gap), almost three times the gap under TC2010 (£826 a year, or 7 per cent), in other words these families are being pushed considerably deeper into poverty. See Figure 4.10.

Figure 4.10 Effect of the transition from the 2010 tax credit system to today's universal credit on the income of a lone parent with two children, working up to 40 hours on a week on the 'national living wage'



Source: IPPR analysis using the Resolution Foundation micro-simulation model

[75] D Finch, *Universal Challenge: Making a success of Universal Credit*, Resolution Foundation, 2016
[76] Department for Work and Pensions, *Universal Credit Test and Learn Evaluation: Families. Findings from qualitative and quantitative research with claimants*, 2017

If they worked 18 hours a week, they would be £2,380 a year (16 per cent) worse off under UC2016 than under TC2010, or £2,805 a year (18 per cent) if using paid childcare. Their income under TC2010 would have placed them £3,396 (27 per cent) above the poverty line, or £3,290 (26 per cent) if using paid childcare, but under UC2016 they would have an income just £1,016 (8 per cent) above the poverty line or £484 (4 per cent) in 2020 if using paid childcare. A lone parent with a part-time job will now barely escape poverty under UC2016, and if they took one of the mini-jobs which universal credit was intended to promote, they could still find themselves beneath the poverty line.

Even if working 30 hours a week they stand to be £1,829 a year (11 per cent) worse off under UC2016 than TC2010, or £2,438 a year (15 per cent) worse off if using paid childcare. They would be 20 per cent above the poverty line (£2,516 a year) under UC2016, or just 11 per cent (£1,374 a year) if using paid childcare, compared with 34 per cent (£4,345 a year), or 32 per cent (£3,812) with childcare costs, under TC2010.

This is the sort of family which was once supposed to be helped by welfare reforms, at least according to rhetoric just before the Coalition came into power, but in reality they have become much worse off (see Box 4.2).

Box 4.2 'A single mother with two kids'

In 2009, David Cameron argued for changes to the tax credit system, saying 'if you're a single mother with two kids earning £150 a week the withdrawal of benefits and the additional taxes mean that for every extra pound you earn, you keep just 4 pence. What kind of incentive is that?'

For our model family 1 (a lone parent with two children), earning £150 a week means working about 18.5 hours a week. Although the effective tax rate they would face in that situation has indeed been reduced under universal credit, as shown in Figure 4.10 that same family would still be £2,336 a year worse off.

Lone parents with one child, earning the 'national living wage' (Family 3)

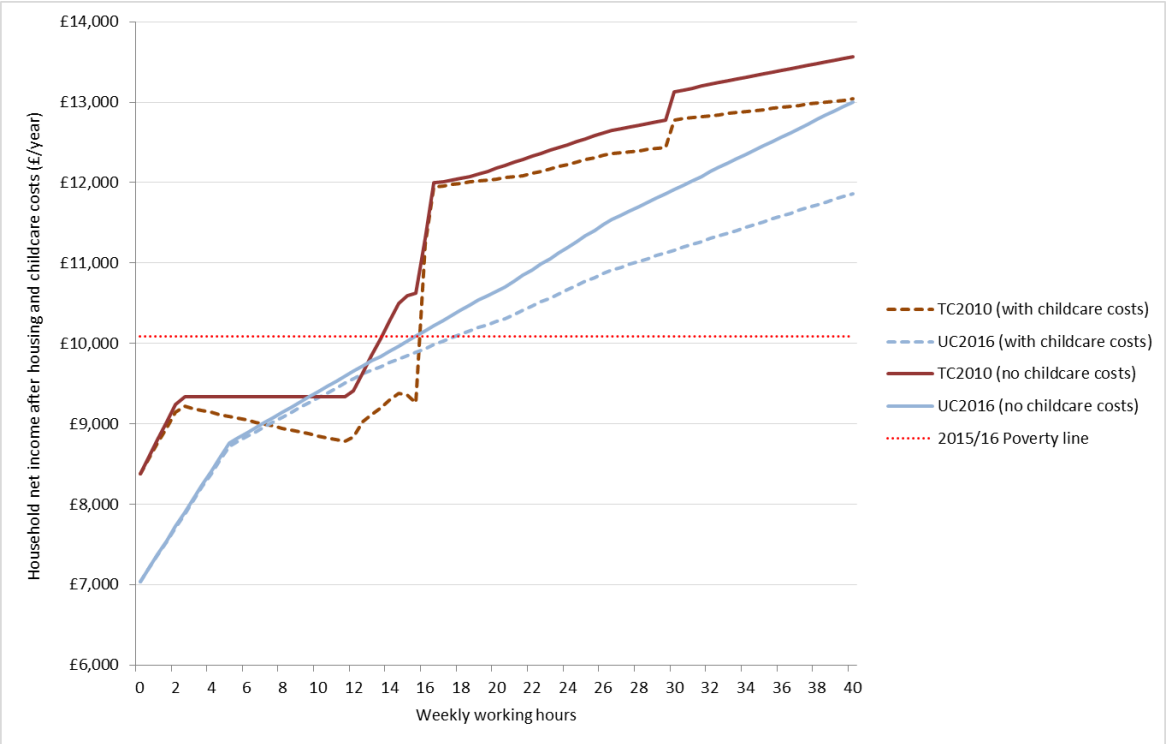
A lone parent with just one child also becomes worse off in this transition under most combinations of working hours and childcare use. If not working they would be £1,344 a year (16 per cent) worse off in 2020 under UC2016 than TC2010. They would be pushed almost twice as far below the poverty line, with an income £3,050 (30 per cent) short of the poverty line, compared with a £1,706 (17 per cent) shortfall under TC2010. See Figure 4.11.

If working 18 hours a week they would be £1,637 a year (14 per cent) worse off in 2020 under UC2016 than TC2010, or £1,877 a year (16 per cent) if they use paid childcare. Under TC2010 they would have had an income £1,968 a year (20 per cent) above the poverty line, or slightly less (£1,908 or 19 per cent) if using paid childcare. But under UC2016 an 18-hour job barely takes their income over the poverty line – just £330 a year or 3 percent above – if they do not use childcare and leaves them virtually on the poverty line (just £31 a year above) if they pay for childcare.

If working 30 hours a week the gap narrows slightly for those not using paid childcare but they remain £1,215 a year (9 per cent) worse off under UC2016 than TC2010, with an income £1,830 (18 per cent) above the poverty line rather than £3,046 (30 per cent) above. But if they used paid childcare they

would be £1,618 (13 per cent) worse off under UC2016 than TC2010, and would have an income just £1,075 a year (11 per cent) over the poverty line rather than £2,693 a year over (27 per cent).

Figure 4.11 Effect of the transition from the 2010 tax credit system to today's universal credit on the income of a lone parent with one child, working up to 40 hours on a week on the 'national living wage'



Source: IPPR analysis using the Resolution Foundation micro-simulation model

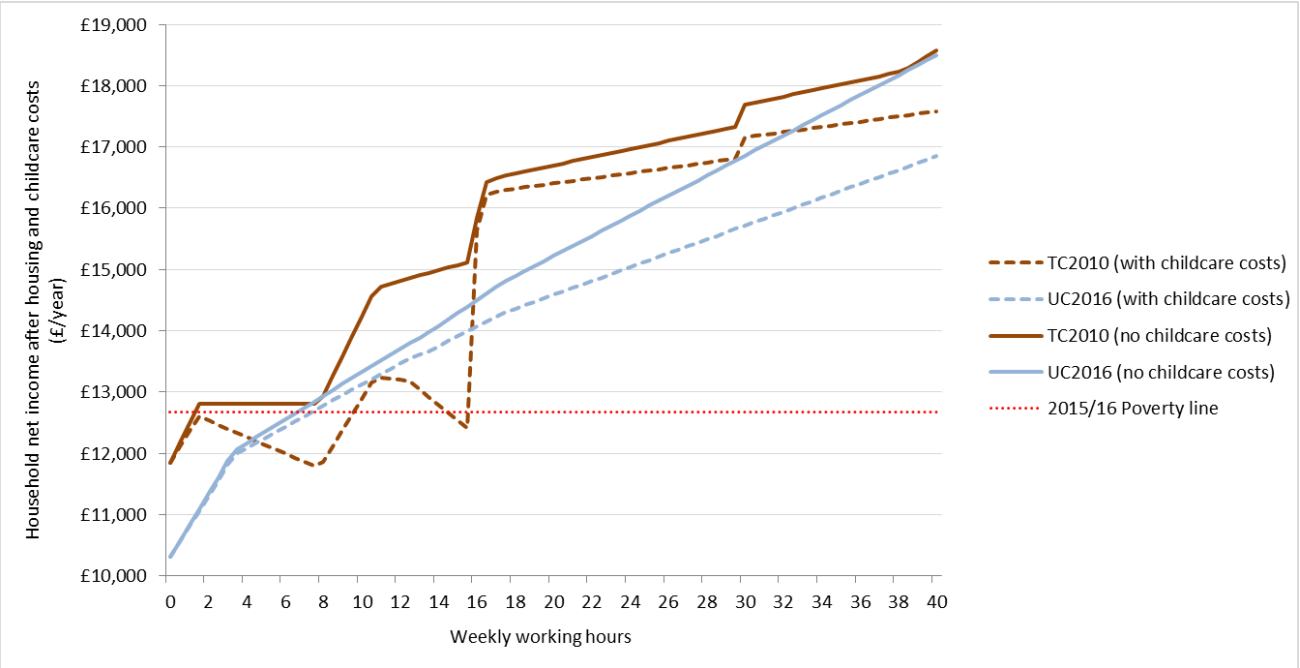
Lone parents with two children, earning the median wage (Family 2)

A slightly higher-earning lone parent loses out less in the transition than Family 1, which is identical except for a lower hourly wage rate, because their higher earnings mean that their benefit award is smaller both in absolute terms and as a percentage of their income.

If not working this is effectively the same family as Family 1. If they work 18 hours a week, however, they still stand to be £1,677 a year (10 per cent) worse off under UC2016 than under TC2010, or £1,960 a year (12 per cent) if they rely on paid childcare. Under UC2016 they will be £2,219 a year (18 per cent) above the poverty line, or just £1,687 (13 per cent) above if they use paid childcare, compared with an expected income £3,896 (31 per cent) above the poverty line under TC2010 (£3,648 or 29 per cent if using paid childcare). See Figure 4.12.

As this parent increases earnings by working more hours a week, the benefits of the single taper rate under universal credit (which has eliminated the very highest effective marginal tax rates faced by some families under the tax credit system) mean that the difference in income between the two systems reduces. But even if this parent works 40 hours a week they will still be slightly worse off under UC2016 than TC2010 if they do not use paid childcare, and £734 a year (4 per cent) worse off if they do use paid childcare).

Figure 4.12 Effect of the transition from the 2010 tax credit system to today's universal credit on the income of a lone parent with two children, working up to 40 hours on a week on the median wage



Source: IPPR analysis using the Resolution Foundation micro-simulation model

Overall the picture is of substantial reductions in income for most lone parents, moving them either deeper into poverty or closer to the poverty line, particularly for those either not working to look after young children or those working on low wages.

Couple families and the transition to universal credit

Our model couple families with children all lose out from the move from the 2010 system of tax credits and legacy benefits to the 2016 system of universal credit if they have a single earner and a stay at home parent.

For two-earner couples there is a mixed picture of winners and losers. Families with two children and parents who are over 25, and both working, typically do better under universal credit, even after the cuts, especially if they are using paid childcare. However families with two working parents aged under-25, and families with three or more children, stand to be much worse off regardless of working hours or childcare use. Currently 32 per cent of couple families with children claiming tax credits have three or more children so stand to lose out substantially from the transition. [77]

Again low-earning families (with a single earner on the 'national living wage') lose out under UC2016 compared with remaining in the 2010 tax credit system; however those with a higher earner (one or two earners on the median wage) stand to be better off under UC2016 than TC2010, even after the cuts to universal credit.

[77] HM Revenue and Customs, *Child and Working Tax Credits statistics: finalised annual awards – 2015 to 2016, Table 2.2*, June 2017

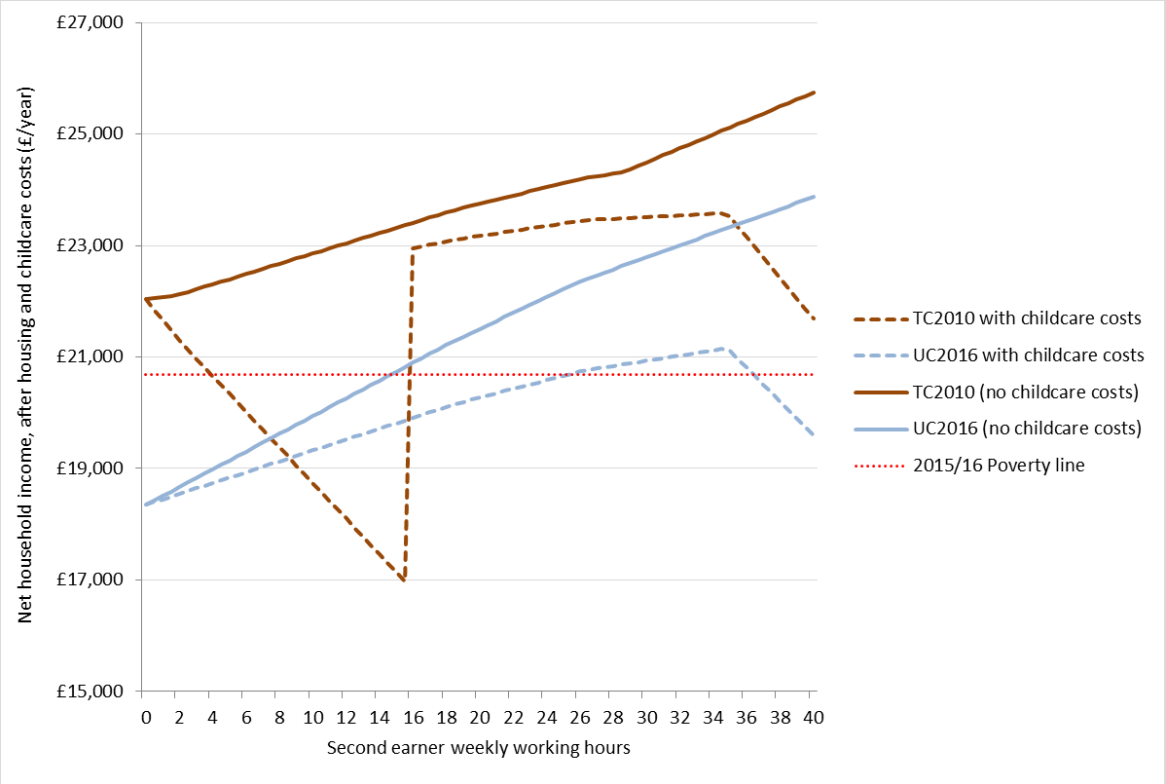
Couples with three children (Family 7)

Couples with three children, earning the 'national living wage' (our Family 7), would have received a substantial income boost under universal credit, as first designed, compared with the tax credit system. However, following deep cuts to universal credit and the introduction of the two-child limit they would now be considerably worse off under UC2016 than under TC2010 in 2020, almost regardless of their working pattern. The only exception is if the second earner works between eight and 16 hours a week and claims childcare costs, as under tax credits there would have been no entitlement to a childcare subsidy if working fewer than 16 hours. If only one parent in this family worked (with one staying at home to look after their three young children), or if the second earner worked a small number of hours without incurring childcare costs, this family would be pushed below the poverty line by the transition from TC2010 to UC2016 (see Figure 4.13).

With a single earner, this family would be £3,962 (17 per cent) worse off in 2020 under UC2016 than TC2010. Rather than having an income £1,350 (7 per cent) above the poverty line, they would be pushed £2,341 (11 per cent) below the poverty line.

The second parent would have to move into work at 24 hours a week without any childcare costs to recoup this loss under UC2016, and could never recoup it if they have to pay for childcare to work, even by working 40 hours a week.

Figure 4.13 Effect of the transition from the 2010 tax credits system to today's universal credit on the income of a family with three children, with one full-time earner and a second earner working up to 40 hours a week on the 'national living wage'



Source: IPPR analysis using the Resolution Foundation micro-simulation model

With a second earner working 18 hours a week they would be £2,377 a year (10 per cent) worse off under UC2016 than TC2010 if they did not use paid childcare, or £2,970 a year (13 per cent) with childcare costs. Under TC2010 they would be £2,902 a year (14 percent) above the poverty line, or £2,383 a year (12 per cent) if using paid childcare. However under UC2016 they would be just £525 a year (3 per cent) above the poverty line, and if using paid childcare they will have an income below the poverty line (by £586 a year or 3 per cent).

If the second earner worked 30 hours a week they would be £1,706 (7 per cent) worse off under UC2016 than TC2010 if they did not require paid childcare, or £2,575 a year (11 per cent) worse off with childcare costs.

Under UC2016 this family would need one full-time earner and a second earner working at least 15 hours a week to meet the poverty line if they have no childcare costs, rising to at least 25 hours a week if they have childcare costs.

Young parents with two children, earning the national minimum wage (Family 6)

Young families also fare badly in the transition to universal credit because of the decision to introduce a lower under-25 rate of the standard allowance in universal credit, even for parents of children, while the income they require for a decent standard of living is no lower simply because of their age. As a result young families will be at increasing risk of poverty, especially if they have a single earner or a second earner working part time.

Young parents would have lost out from the introduction of universal credit even before the cuts, but the cuts to universal credit will reduce their incomes still further. Minimum wage workers under 25 have also not benefited from the uplift in the minimum wage with the introduction of the (over-25) 'National Living Wage'. Our Family 6 is a couple, both under 25, with two children, earning the under-25 national minimum wage. They stand to be much worse off under UC2016 than TC2010 unless the second earner works between 12 and 15 hours a week and the family pays for childcare.

While under TC2010 this family could have escaped poverty with a second earner working just 4 hours a week (or 16 hours if they required paid childcare), under UC2016 the second earner would have to work 17 hours a week (with no childcare costs) or 23 hours a week (if paying for childcare) to reach the poverty line (see Figure 4.14).

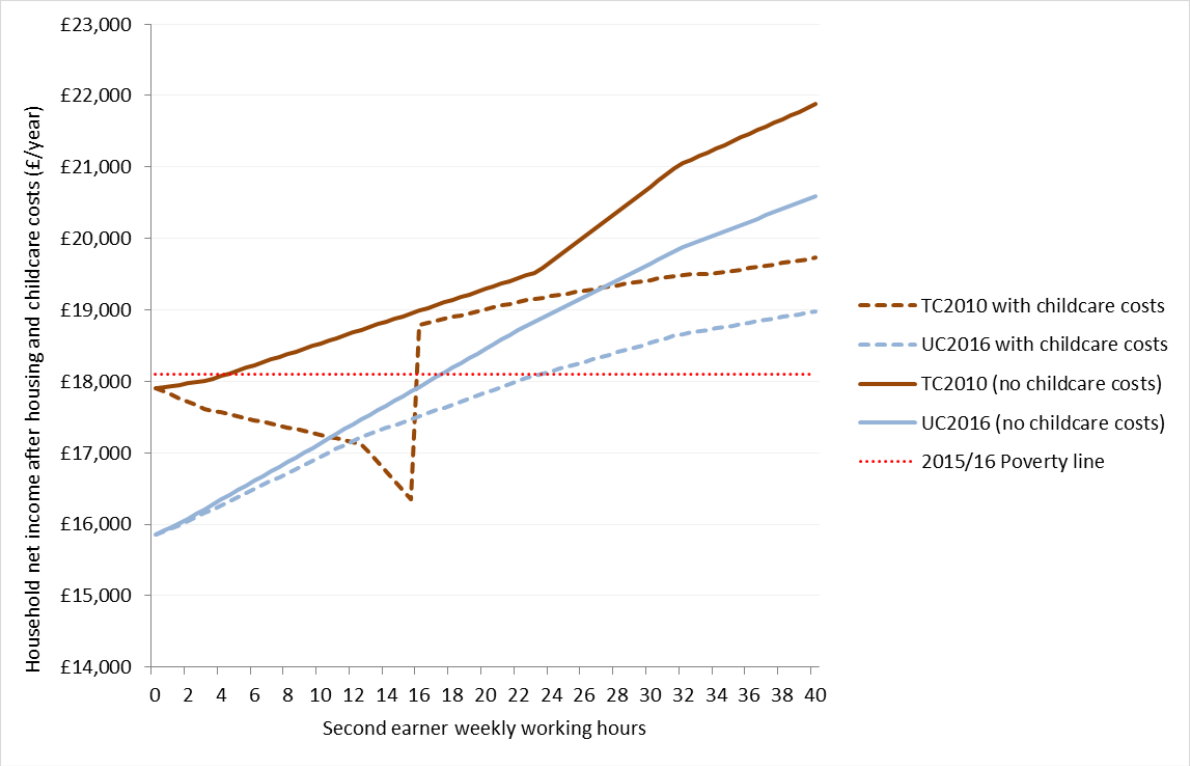
If this family has a single earner, they would be £2,048 (11 per cent) worse off in 2020 under UC2016 than TC2010. Under TC2010 they would have an income just below the poverty line (£199 a year or 1 per cent below the line), but under UC2016 this falls to £2,257 or 12 per cent below the poverty line. The second parent would have to work 16 hours a week under UC2016 just to recoup this difference, or 21 hours a week if they have to pay for childcare.

If the second parent works 18 hours a week, they would be £951 a year (5 per cent) worse off in 2020 under UC2016 than TC2010 if they can access free childcare, or £1,125 a year (6 per cent) worse off if they use paid childcare. Under TC2010 they would have an income £1,036 a year (6 per cent) above the poverty line, or £796 a year (4 per cent) above if using paid childcare. Under UC2016 this falls to just £84 a year above the poverty line with no childcare costs – only just escaping poverty – and if

they pay for childcare they remain £430 a year (2 per cent) below the poverty line, which is worse off than they would have been under TC2010 with just one earner.

If the second parent worked 30 hours a week, they would be £1,073 a year (5 per cent) worse off under UC2016 than TC2010 if they could use free childcare, or £882 a year (also 5 per cent) with childcare costs.

Figure 4.14 Effect of the transition from the 2010 tax credits system to today's universal credit on a couple aged under 25, with two children, with one full-time earner and a second earner working up to 40 hours a week, both on the national minimum wage



Source: IPPR analysis using the Resolution Foundation micro-simulation model

In contrast, couples over 25, with two children, either do not lose (much), or tend to gain under UC2016 compared with TC2010.

Couple with two children, earning the 'national living wage', with average housing and childcare costs (Family 4)

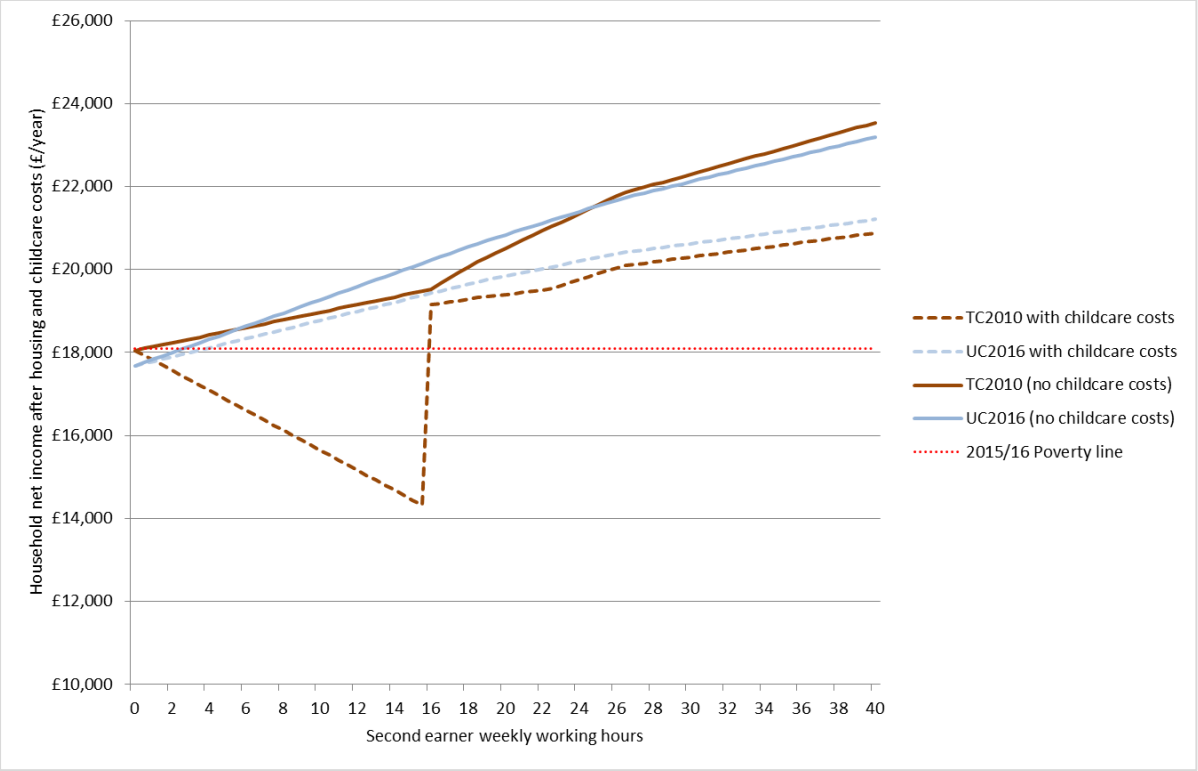
Families with a single 'national living wage' earner (over 25) and two young children would have gained considerably from the introduction of universal credit in its original form. However, since cuts to universal credit they now stand to be worse off in 2020 under UC2016 than under TC2010. With a single earner this family would be £373 (2 per cent) a year worse off under UC2016 than TC2010 in 2020, and will slip from virtually on the poverty line (£51 a year below) to £424 a year below the poverty line (see Figure 4.15).

Where the second earner can move into work without incurring childcare costs, the rewards from having a second earner in work are fairly similar under TC2010 and UC2016, but better for TC2010 (by up to £341 a year) if working low or high numbers of hours, and better for UC2016 (by up to £694 a year) if working between six and 24 hours a week.

If the family used paid childcare they would be better off under UC2016 than under TC2010 with a second earner working any number of hours. If working below 16 hours the difference is substantial, up to almost £5,000 a year, because there is no eligibility for childcare subsidy in working tax credit if the second earner works fewer than 16 hours. If the second earner works 16 hours a week or more, the difference is between about £300 and £500 a year.

Unless the second earner works more than 24 hours a week and uses paid childcare, however, they will not see the gains they were initially promised by the introduction of universal credit. When working more hours than this, the increased support for childcare under UC2016 compared with UC2013 starts to offset the cuts, making UC2016 the best system for a couple family using large amounts of childcare.

Figure 4.15 Effect of the transition from the 2010 tax credits system to today's universal credit on a couple with two children, with one full-time earner and a second earner working up to 40 hours a week, both on the 'national living wage'



Source: IPPR analysis using the Resolution Foundation micro-simulation model

Except in the case of a second earner in a mini-job of less than 16 hours a week and using paid childcare, however, the income gains for this family arising from the transition from TC2010 to

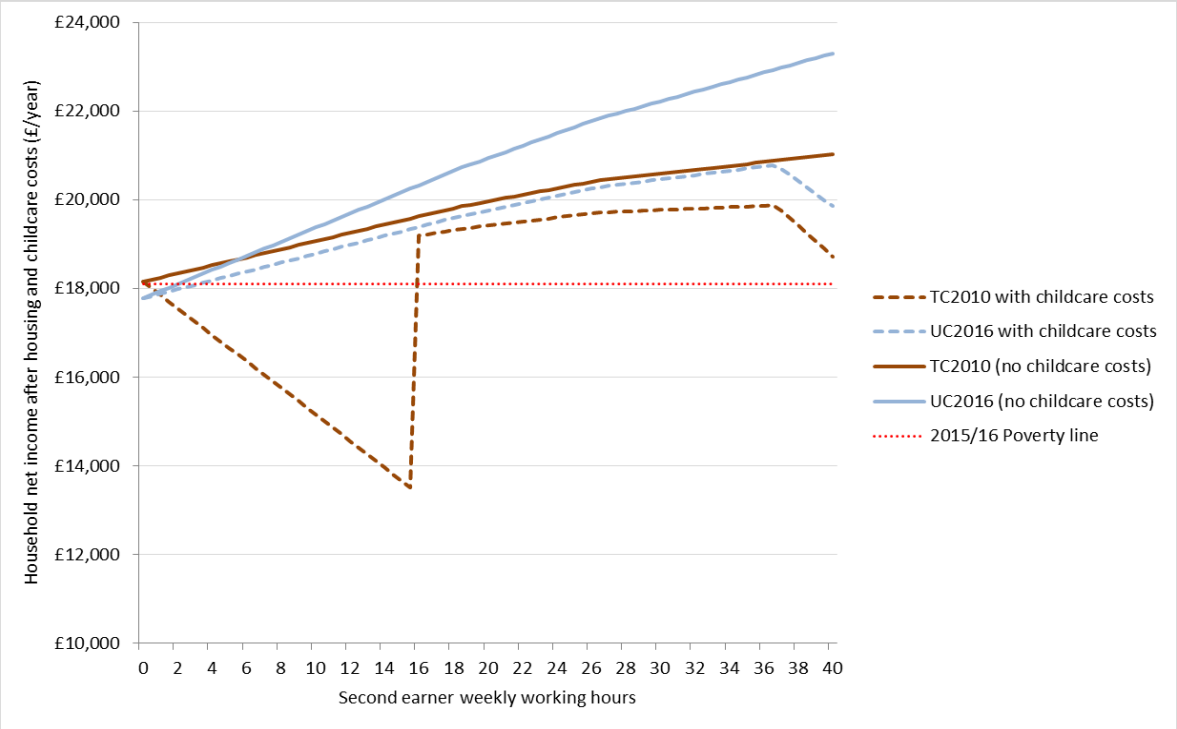
UC2016 are small compared with the losses faced by the single parents, young parents and larger families discussed above.

Couple with two children, earning the 'national living wage', with high housing and childcare costs (Family 5)

For a family in an identical situation but living in a higher cost area (outer London), the way in which their higher housing benefit award is tapered in the legacy system, as well as the taper applied to their tax credits, depresses the rewards from a second earner starting work or increasing their hours under TC2010. In contrast universal credit applies a single taper meaning that if the second earner worked seven hours or more this family would be better off under UC2016 than TC2010 whether or not they use paid childcare (see Figure 4.16).

If they used paid childcare they would be better off under UC2016 than TC2010 at any number of second earner working hours, particularly if working fewer than 16 hours. Again this family would have been better off under UC2013 than UC2016 if they had a single earner or a second earner who works fewer than 21 hours or can work without requiring paid childcare, but better off under UC2016 if the second earner works more than 21 hours and they require paid childcare.

Figure 4.16 Effect of the transition from the 2010 tax credits system to today's universal credit on a couple with two children, with one full-time earner and a second earner working up to 40 hours a week, both on the 'national living wage', in a high-cost area



Source: IPPR analysis using the Resolution Foundation micro-simulation model

With a single earner this family will be £373 a year (2 per cent) worse off under UC2016 than under TC2010. Under TC2010 they would have had an income virtually on the poverty line (£49 above) but under UC2016 their income will be £324 (2 per cent) below the poverty line.

If the second earner worked 18 hours a week they would be £840 a year (4 per cent) better off under UC2016 than TC2010 with no childcare costs, and £277 a year (1 per cent) better off under UC2016 than TC2010 with childcare costs.

If the second earner worked 30 hours a week they would be £1,630 a year (8 per cent) better off under UC2016 than under TC2010, if they did not use paid childcare, and £691 a year (3 per cent) with childcare costs. Under TC2010 their income would be £2,485 a year (14 per cent) above the poverty line, or £1,664 a year (9 per cent) above with childcare costs. Under UC2016 this rises to £4,115 a year (23 per cent) above the poverty line, or £2,355 a year (13 per cent) above with childcare costs.

Couple with two children, earning the median wage, with high housing and childcare costs (Family 8)

A higher-earning couple (both on median wage) with two children again do considerably better from universal credit relative to tax credits, *and* lose somewhat less from universal credit cuts than a lower-earning couple, as they are compensated more by the change to the taper rate. If this family claims childcare costs the additional subsidy available under universal credit today means that they would be better off under UC2016 than any of the other systems if the second earner worked 19 or more hours a week. If not using paid childcare, this family retains entitlement to universal credit with a second earner working up to 31 hours, considerably more than under the tax credit system where they would have moved out of entitlement from tax credits at 16 hours a week and housing benefit at 22 hours work a week.

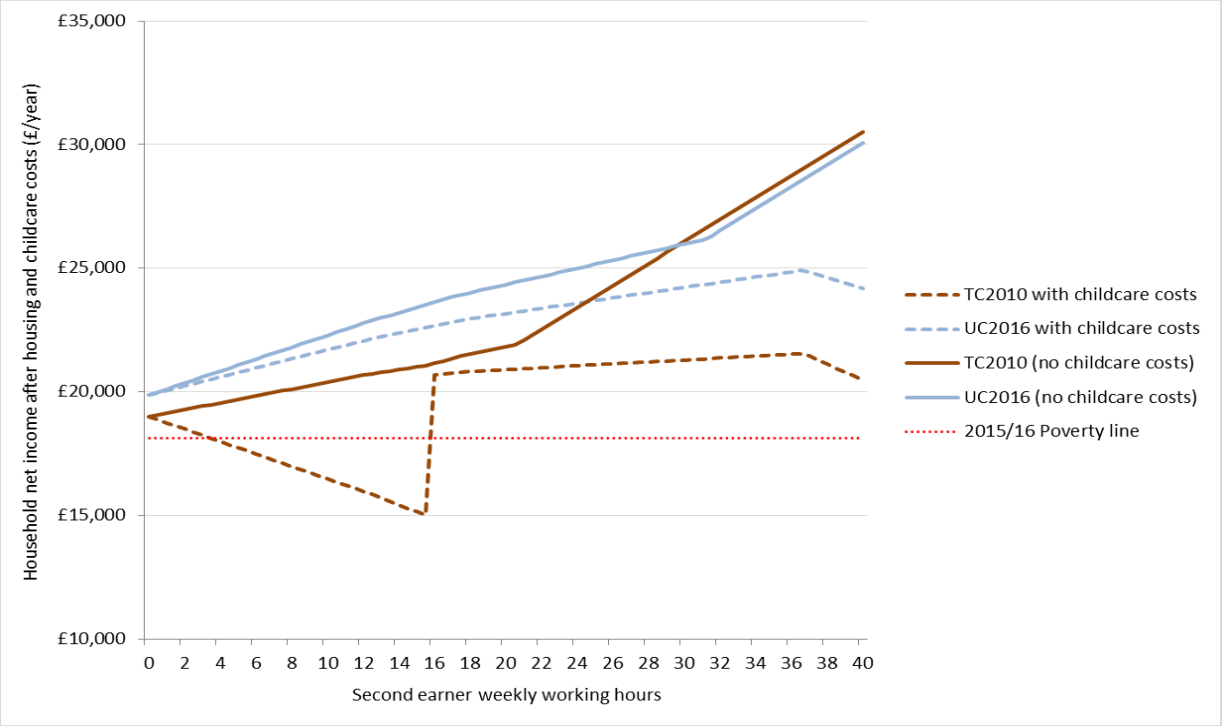
If the second earner works more than 31 hours and there are no childcare costs, the only difference in their income between the TC2010 and UC2016 systems relates to the reduction in the value of child benefit (due to failures to uprate in line with inflation). This still amounts to £446 a year in 2020.

With a single earner this family will be £874 a year (5 per cent) better off under UC2016 than TC2010, with an income £1,765 (10 per cent) above the poverty line rather than £891 (5 per cent) above.

If the second earner works 18 hours a week they will be £2,492 a year (12 per cent) better off under UC2016 than TC2010 without childcare costs, or £2,136 a year (10 per cent) better off with childcare costs.

If the second earner works 30 hours a week they have a very similar income under the two systems if they do not have childcare costs (£98 a year more under TC2010 than UC2016). However if they do have childcare costs they would be £2,934 a year (14 per cent) better off under UC2016 than TC2010. See Figure 4.17.

Figure 4.17 Effect of the transition from the 2010 tax credits system to today's universal credit on a couple with two children, with one full-time earner and a second earner working up to 40 hours a week, both on the median wage, in a high-cost area



Source: IPPR analysis using the Resolution Foundation micro-simulation model

Table 4.3 and Figure 4.18 summarise the impacts of the transition from a tax credit system to universal credit on our model families. Table 4.3 shows the differences in income for our model families in different working patterns under TC2010 and UC2016, and the percentage of the 2015/16 poverty line attained.

Figure 4.18 shows how the annual incomes (after housing and childcare costs) have changed between TC2010 and UC2016 for a selection of our model families, at different numbers of working hours. It is immediately apparent that lone parent families (Family 1), young families (Family 6) and families with more than two children (Family 7) stand to lose out substantially, unless the working hours of the lone parent or second earner fall within a small window below 16 hours a week and they pay childcare costs.

In contrast, couples over 25 (Families 4 and 8) either benefit from the change or lose much less. Family 8 - the higher earning couple – is the only family which can expect significant gains if they do not pay childcare costs.

The rationale for this policy choice is not clear, given that the three groups who will be most penalised by the transition are already those where parents and children are at a greater risk of poverty.

Table 4.3 Net household incomes after housing and childcare costs, and percentage of 2015/16 poverty line (AHC), for families under the 2010 tax credit system and today's universal credit

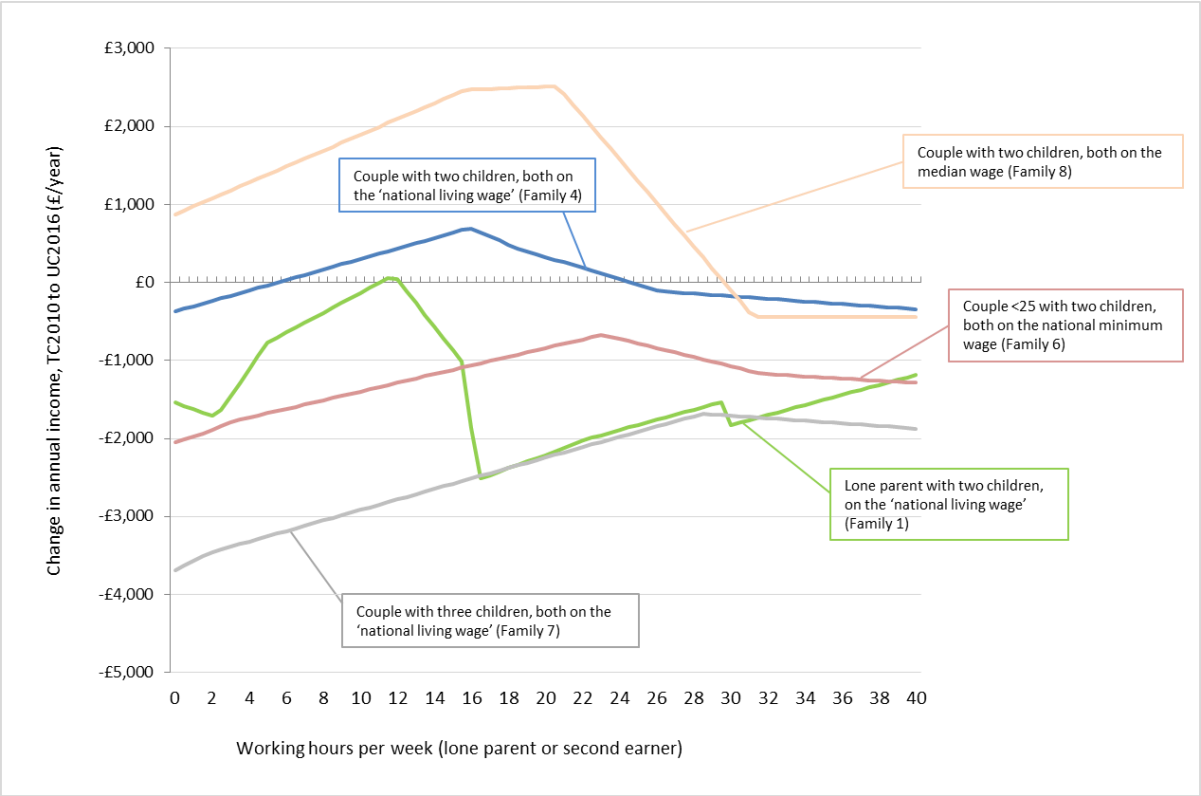
Lone parent families									
Family	Working hours	Using free childcare				Using paid childcare			
		TC2010		UC2016		TC2010		UC2016	
		Net annual income	Income as % of the poverty line	Net annual income	Income as % of the poverty line	Net annual income	Income as % of the poverty line	Net annual income	Income as % of the poverty line
1	0	£11,847	93%	£10,308	81%	n/a	n/a	n/a	n/a
	12	£12,884	102%	£12,295	102%	£11,270	89%	£12,683	100%
	24	£16,359	129%	£14,468	114%	£16,096	127%	£13,631	108%
	40	£17,455	138%	£16,272	128%	£16,685	132%	£14,621	115%
2	0	£11,847	93%	£10,308	81%	n/a	n/a	n/a	n/a
	12	£14,813	117%	£13,711	108%	£13,199	104%	£13,469	106%
	24	£16,966	134%	£15,876	125%	£16,575	131%	£15,039	119%
	40	£18,570	147%	£18,500	146%	£17,584	139%	£16,850	133%
3	0	£8,380	83%	£7,036	70%	n/a	n/a	n/a	n/a
	12	£9,417	93%	£9,652	96%	£8,836	88%	£9,565	95%
	24	£12,473	124%	£11,195	111%	£12,227	121%	£10,668	106%
	40	£13,569	135%	£12,999	129%	£13,040	129%	£11,865	118%
Couple families									
Family	Working hours	Using free childcare				Using paid childcare			
		TC2010		UC2016		TC2010		UC2016	
		Net annual income	Income as % of the poverty line	Net annual income	Income as % of the poverty line	Net annual income	Income as % of the poverty line	Net annual income	Income as % of the poverty line
4	0	£18,053	100%	£17,680	98%	n/a	n/a	n/a	n/a
	12	£19,155	106%	£19,591	108%	£15,167	84%	£18,993	105%
	24	£21,353	118%	£21,398	118%	£19,758	109%	£20,202	112%
	40	£23,543	130%	£23,202	128%	£20,884	115%	£21,208	117%
5	0	£18,153	100%	£17,780	98%	n/a	n/a	n/a	n/a
	12	£19,255	106%	£19,691	109%	£14,562	80%	£18,987	105%
	24	£20,260	112%	£21,498	119%	£19,603	108%	£20,090	111%
	40	£21,026	116%	£23,302	129%	£18,724	103%	£19,853	110%
6	0	£17,905	99%	£15,857	88%	n/a	n/a	n/a	n/a
	12	£18,683	103%	£17,397	96%	£17,149	95%	£17,167	95%
	24	£19,675	109%	£18,954	105%	£19,193	106%	£18,141	100%
	40	£21,877	121%	£20,591	114%	£19,729	109%	£18,981	105%
7	0	£22,041	107%	£18,349	89%	n/a	n/a	n/a	n/a
	12	£23,041	111%	£20,260	98%	£18,100	87%	£19,519	94%
	24	£24,045	116%	£22,067	107%	£23,354	113%	£20,585	99%
	40	£25,743	124%	£23,871	115%	£21,685	105%	£19,597	95%
8	0	£18,995	105%	£19,869	110%	n/a	n/a	n/a	n/a
	12	£20,665	114%	£22,763	126%	£15,972	88%	£22,059	122%
	24	£23,417	129%	£24,995	138%	£21,052	116%	£23,587	130%
	40	£30,510	169%	£30,064	166%	£20,466	113%	£24,170	134%

Source: CPAG analysis of IPPR modelling output

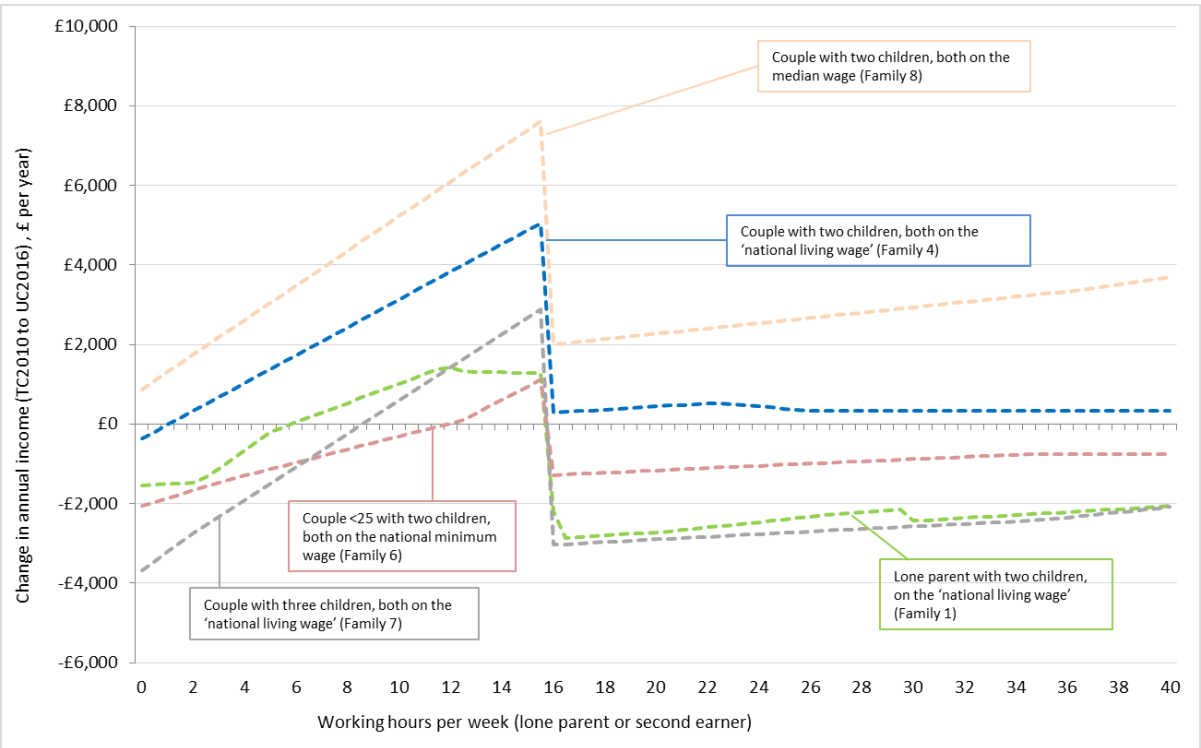
Family 1: lone parent, two children aged two and five, on the 'national living wage', average cost area
Family 2: lone parent, two children aged two and five, on the median wage, average cost area
Family 3: lone parent, one child aged two, on the 'national living wage', average cost area
Family 4: couple, two children aged two and five, both on the 'national living wage', average cost area
Family 5: couple, two children aged two and five, both on the 'national living wage', high cost area
Family 6: couples, two children aged two and five, both on the national minimum wage, average cost area
Family 7: couple, three children aged two, five and seven, both on the 'national living wage', average cost area
Family 8: couple, two children aged two and five, both on the median wage, high cost area

Figure 4.18 Changes in annual net income moving from the old tax credits system (TC2010) to today's universal credit (UC2016)

(a) Without childcare costs



(b) With childcare costs



Source: IPPR analysis using the Resolution Foundation micro-simulation model

4d. How adequate are family incomes under universal credit?

Family incomes compared with the poverty line

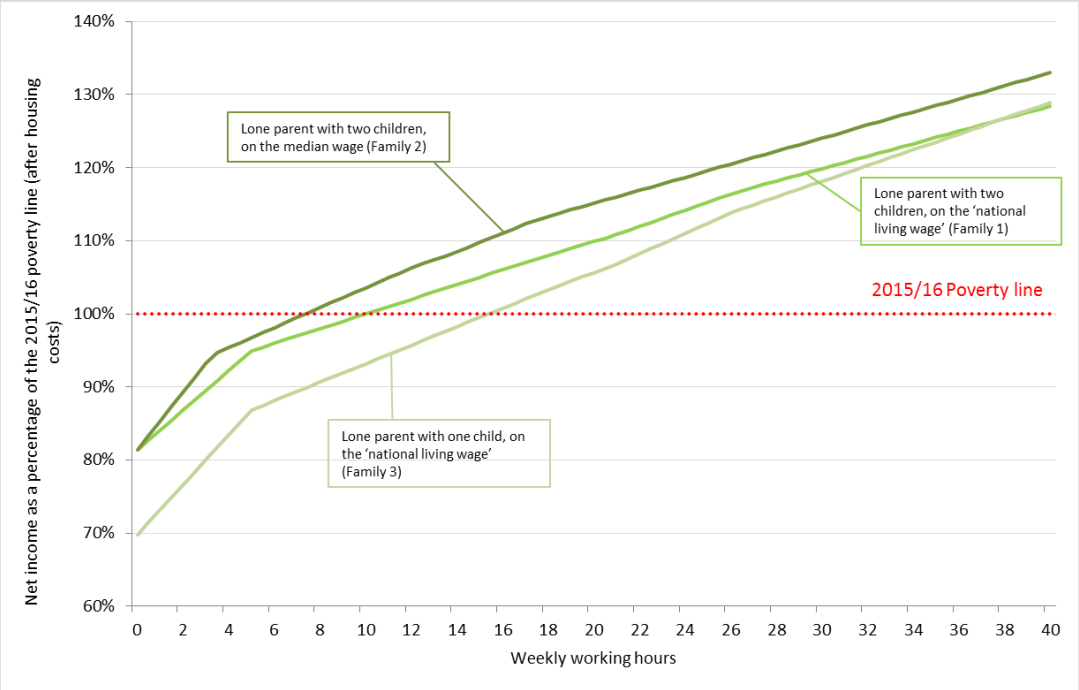
Figures 4.19 (lone parent families) and 4.20 (couple families) show the percentage of the 2015/16 poverty line (adjusted for each household type, and taken after housing costs) reached under UC2016 for our model families at different weekly working hours for lone parents and couples with one or two earners, with and without childcare costs.

These also show the approximate number of hours of work parents are required to keep their family out of poverty (although the poverty line may not be the same in 2020). All the lone parent families will be in poverty. A lone parent with one two-year-old would have to work 16 hours a week or more to escape poverty, or 18 if they require paid childcare.

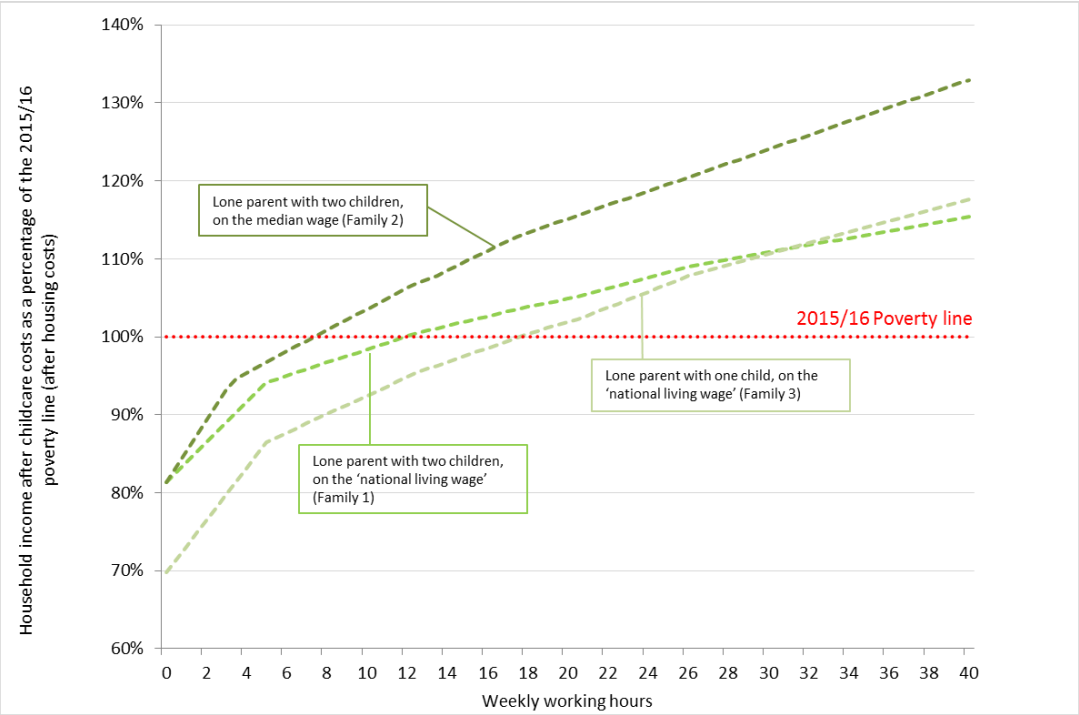
All the couples with children where the first earner earns the 'national living wage' or minimum wage would be in poverty if one parent stays at home. Couples with three children on the 'national living wage' would need a second earner working 15 hours to escape poverty (25 hours if they pay for childcare), while a couple aged under 25 with two children, on the minimum wage, would need a second earner working 17 hours a week (23 if they pay for childcare).

Figure 4.19 Income as a percentage of the poverty line under UC2016 (lone parent families)

(a) without childcare costs



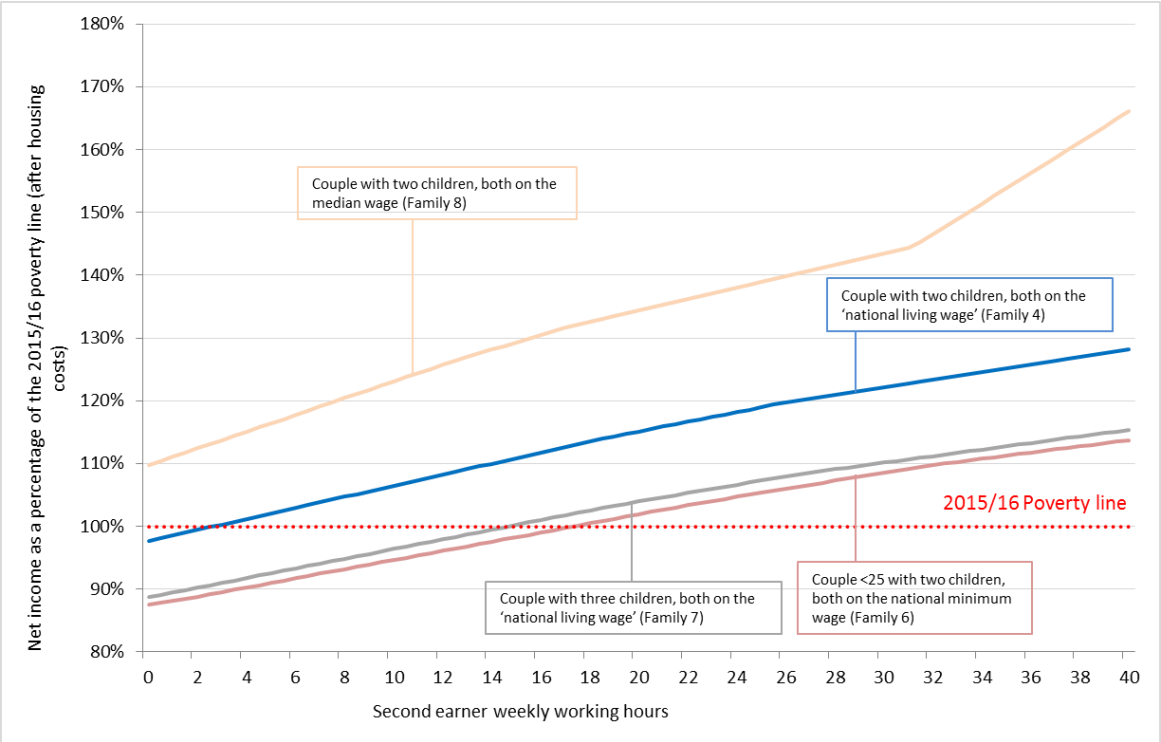
(b) with childcare costs



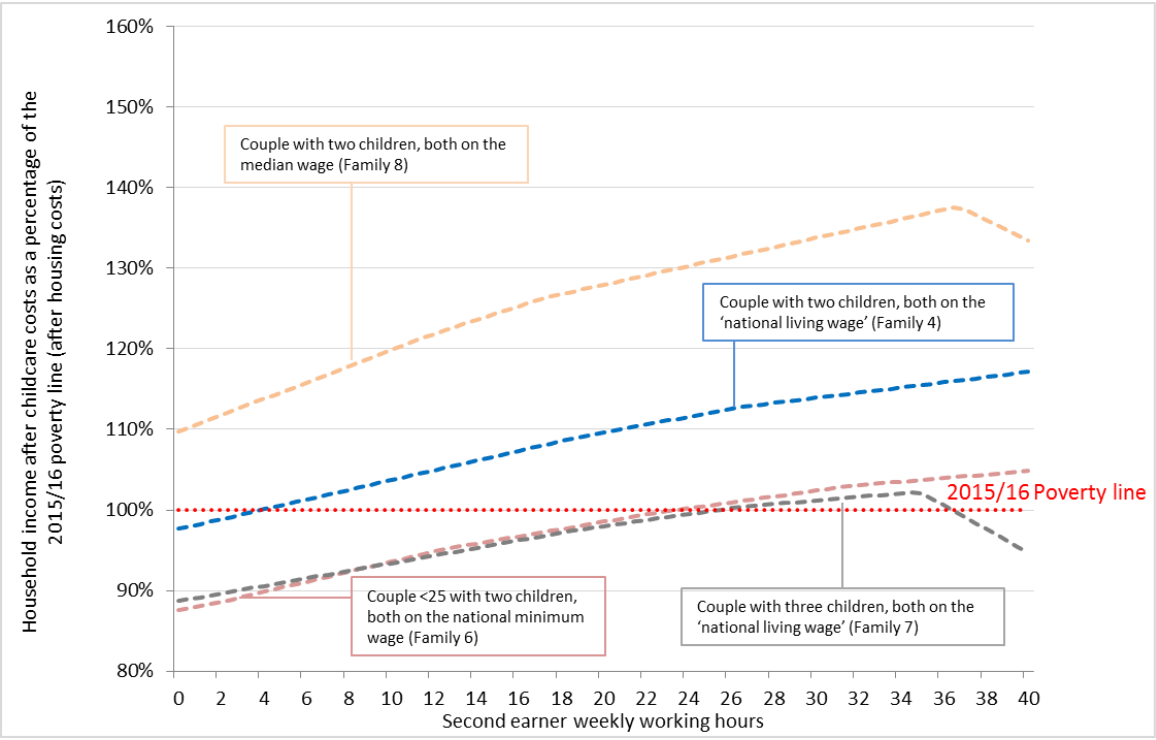
Source: CPAG analysis of IPPR modelling output

Figure 4.20 Percentage of the poverty line achieved under UC2016 by second earner working hours (couple families)

(a) without childcare costs



(b) with childcare costs



Source: CPAG analysis of IPPR modelling output

Comparisons with the minimum income standard

As well as comparing incomes under the different systems with the poverty line, it is useful to examine how they compare with the 'minimum income standard' (MIS) for each family. The MIS is an independently calculated measure of the income needed to provide a basic but decent standard of living. It is based on a basket of items agreed by members of the public to be essential for a socially acceptable standard of living in the UK today. For this analysis we have used the online 'MIS calculator'[78] to obtain the MIS for each of our family types in 2016/17 and adjusted this to 2015/16 prices using the CPI index[79] as shown in Box 4.3.

Box 4.3 Minimum Income Standards for our model families

Minimum Income Standards for 2017 (weekly, excluding rent and childcare):

Lone parent with 2yo and 5yo	£385.94
Lone parent with 2yo	£316.69
Couple with 2yo and 5yo	£474.57
Couple with 2yo, 5yo, 7yo	£553.96

Annualised, adjusted to 2015/16 prices and rounded to nearest £1:

Lone parent with 2yo and 5yo	£19,536
Lone parent with 2yo	£16,031
Couple with 2yo and 5yo	£24,023
Couple with 2yo, 5yo, 7yo	£28,042

None of our lone parent families meets the MIS under either TC2010 or UC2016, even if they work full time, although they would have come closer under TC2010. The cuts and the move to universal credit will leave our family 1 (a lone parent of two, on the 'national living wage') with a shortfall around ten per cent greater under UC2016 than they would have had under TC2010. If not working they will now take home just 53 per cent of the MIS compared with 61 per cent - barely more than half the income they need. If working 16 hours a week they will take home 69 per cent (or 67 per cent with childcare costs) rather than 78 per cent of the MIS. If working 30 hours a week they will take home 78 per cent (71 per cent with childcare costs) rather than 87 per cent (84 per cent with childcare costs).

Our couple parents under-25 (family 6) and our couple family with three children (Family 7) also would not have reached the MIS under either system, and will also face greater shortfalls under UC2016. With a single earner, both families would have had an income of around 75 per cent of the MIS under TC2010, but this falls to 66 per cent under UC2016. Under TC2010 they could have reached more than 90 per cent of the MIS with two full-time workers, but this is not possible under UC2016.

[78] The Minimum Income Calculator: http://www.minimumincome.org.uk/
[79] Office for National Statistics, *Consumer price inflation* dataset, October 2017

In contrast a couple with two children, both on the 'national living wage' (our Family 4), will attain a fairly similar proportion of MIS under both systems. They still cannot reach 100 per cent of the MIS under any system, though they approach this with two full time workers. With a single full-time earner their income will be around 75 per cent of the MIS under either TC2010 or TC2016.

A similar couple earning the median wage is the only family to reach 100 per cent of the MIS at any number of hours of work in either system. Under UC2016 they would need one full-time earner and a second earner working at least 18 hours a week (if no childcare costs) or 27 hours a week (with childcare costs), to reach the MIS. Under TC2010 they could only reach this point with a second earner working 26 hours a week without childcare costs, but if they pay for childcare then even two full-time earners could not attain the full MIS. These findings are summarised in Table 4.4.

Table 4.4 Percentage of the MIS achieved at different working hours under TC2010 and UC2016 for selected model families

Working hours (lone parent or second earner)	Income as a percentage of MIS (2010 tax credits system)	Income as a percentage of MIS (today's universal credit)
Lone parent with two children on the 'national living wage' (Family 1)		
0	61%	53%
16	78%	69%
	(78% after childcare costs)	(67% after childcare costs)
30	87%	78%
	(84%)	(72%)
Lone parent with two children on the median wage (Family 2)		
0	61%	53%
16	81%	74%
	(80%)	(72%)
30	91%	86%
	(88%)	(80%)
Couple under 25 with two children on the national minimum wage (Family 6)		
0	75%	66%
16	79%	75%
	(78%)	(73%)
30	86%	82%
	(81%)	(77%)
Couple with three children on the 'national living wage' (Family 7)		
0	79%	65%
16	83%	75%
	(82%)	(71%)
30	87%	81%
	(84%)	(75%)
Couple with two children on the 'national living wage' (Family 4)		
0	75%	74%
16	81%	84%
	(80%)	(81%)
30	93%	92%
	(85%)	(86%)
Couple with two children on the median wage (Family 8)		
0	79%	83%
16	88%	98%
	(86%)	(94%)
30	109%	108%
	(89%)	(101%)

Source: CPAG analysis of IPPR modelling output

4e. Childcare costs depress the rewards from work, so subsidies and disregards make a big difference

It is apparent from Figures 4.10 to 4.17 that, in any system, the costs of childcare bear down heavily on the rewards from work and push families closer to, or further below, the poverty line. Full supply-side subsidy for childcare, at times needed by parents and of good quality, would eliminate this problem and remove childcare costs from the calculations families have to make.

But under our current system of mixed demand- and supply-side provision there are considerable differences between social security systems in the net costs of childcare to households, illustrating the importance of policies to subsidise childcare costs through these systems. These mechanisms are both direct (through childcare elements in working tax credit and universal credit which pay a percentage of childcare costs) and indirect (through disregards for childcare costs in housing benefit and, formerly, council tax benefit).

In the tax credit system, no direct childcare subsidy is available if the main carer (lone parent or second earner in a couple) works less than 16 hours. However after this point, overall subsidy is relatively generous. In universal credit, childcare subsidy is available regardless of hours of work, which greatly improves the rewards from work for lone parents and second earners to work fewer than 16 hours per week. However once working more than 16 hours, support for some families can be less generous than through the old tax credits system. In some cases the overall percentage of childcare costs covered by universal credit, even with an 85 per cent subsidy, is lower than the percentage that would have been covered by the combination of working tax credit and disregards for childcare costs in housing benefit and council tax support childcare costs disregards, under the 2010 system.

Table 4.5 shows how childcare costs depress overall incomes and the rewards from work, for four of our model families, in the TC2010, TC2016, UC2013 and UC2016 systems. For each combination of family type, hours of work and childcare use, the system under which families would be (or would have been) best off financially is highlighted in pink.

Our lone parent family 1 would pay over £1,600 a year in childcare costs (after all available free provision and subsidies are taken into account) if working 12 hours a week under TC2010 or TC2016, worth 13 or 14 per cent of their income respectively. Under UC2016 they would pay just £242 a year under UC2016, or just 2 per cent of their income. However if working 30 hours a week they would pay just 3 per cent of their income (£533 a year) under TC2010 but 8 per cent (£1,142 a year) under UC2016.

Families with more children are, unsurprisingly, particularly affected by childcare costs. Our three-child Family 7 would face annual childcare costs (after all subsidies) of more than £1,100 (effectively reducing their income by 6 per cent) if the second earner works 18 hours per week. Under TC2010 the same family would pay just £519, effectively reducing their income by just 2 per cent.

It is not only pre-school children which bring significant childcare costs. A comparison of the childcare costs facing our lone parent Family 1 (with a two year old and a five year old child) and Family 3 (with a two year old only) shows that the addition of a primary school aged child creates substantial additional costs. Under UC2016 Family 1 will pay £232 more a year for childcare than Family 3 if the

parent works 18 hours a week (a 77 per cent higher spend) and almost £400 a year more if they work for 30 hours a week (a 50 per cent higher spend).

Table 4.5 Expenditure on childcare and effect on household incomes, for a range of families and working patterns

		TC2010				TC2016				UC2013				UC2016			
		Annual spending on childcare†		Annual income after rent and childcare		Annual spending on childcare		Annual income after rent and childcare		Annual spending on childcare		Annual income after rent and childcare		Annual spending on childcare		Annual income after rent and childcare	
Family	Weekly working hours*	£/year	% of income	With childcare costs	No childcare costs	£/year	% of income	With childcare costs	No childcare costs	£/year	% of income	With childcare costs	No childcare costs	£/year	% of income	With childcare costs	No childcare costs
1	12	£1,614	13%	£11,270	£12,884	£1,614	14%	£10,288	£11,902	£484	3%	£14,126	£14,610	£242	2%	£12,683	£12,925
	18	£106	1%	£15,962	£16,069	£160	1%	£14,780	£14,939	£1,064	7%	£14,316	£15,380	£532	4%	£13,157	£13,689
	30	£533	3%	£16,485	£17,018	£591	4%	£15,030	£15,621	£2,284	14%	£14,583	£16,867	£1,142	8%	£14,047	£15,189
3	12	£581	6%	£8,836	£9,417	£581	7%	£8,048	£8,630	£174	2%	£10,965	£11,140	£87	1%	£9,565	£9,652
	18	£60	0%	£11,994	£12,054	£90	1%	£11,014	£11,103	£599	5%	£11,310	£11,909	£300	3%	£10,117	£10,417
	30	£352	3%	£12,780	£13,132	£528	4%	£11,390	£11,918	£1,510	11%	£11,887	£13,397	£755	6%	£11,162	£11,916
4	12	£3,988	21%	£15,167	£19,155	£3,988	23%	£13,508	£17,496	£1,196	6%	£19,712	£20,909	£598	3%	£18,993	£19,591
	18	£771	4%	£19,288	£20,059	£628	3%	£17,401	£18,029	£1,795	8%	£20,018	£21,813	£897	4%	£19,649	£20,547
	30	£1,994	9%	£20,301	£22,295	£2,118	11%	£17,729	£19,847	£2,991	13%	£20,309	£23,300	£1,496	7%	£20,623	£22,119
5	12	£4,693	24%	£14,562	£19,255	£4,693	27%	£12,903	£17,596	£1,408	7%	£19,601	£21,009	£704	4%	£18,987	£19,691
	18	£493	2%	£19,314	£19,807	£739	4%	£17,390	£18,129	£2,112	10%	£19,801	£21,913	£1,056	5%	£19,590	£20,646
	30	£821	4%	£19,768	£20,589	£1,232	7%	£17,644	£18,876	£3,520	15%	£19,880	£23,400	£1,760	8%	£20,459	£22,219
7	12	£4,940	21%	£18,100	£23,041	£4,941	23%	£16,258	£21,199	£1,482	6%	£22,897	£24,379	£741	4%	£19,519	£20,260
	18	£519	2%	£23,074	£23,593	£447	2%	£20,954	£21,733	£2,223	9%	£23,060	£25,283	£1,112	6%	£19,909	£21,215
	30	£984	4%	£23,510	£24,494	£1,096	5%	£21,182	£22,479	£3,706	14%	£23,065	£26,770	£1,853	8%	£20,935	£22,788

Source: CPAG analysis of IPPR modelling output

* Lone parent or second earner † After childcare subsidies

Family 1: lone parent, two children aged two and five, earning the 'national living wage', average cost area
Family 3: lone parent, one child aged two, earning the 'national living wage', average cost area
Family 4: couple, two children aged two and five, both partners earning the 'national living wage', average cost area
Family 5: couple, two children aged two and five, both partners earning the 'national living wage', high cost area
Family 7: couple, three children aged two, five and seven, both partners earning the 'national living wage', average cost area

5. What next for universal credit?

In this section we consider a range of possibilities to improve universal credit and help restore its poverty-reducing potential.

Section 3 presented the effect of various cuts and changes on family incomes and poverty rates, which also equate to the gains to be made were these changes reversed.

In addition to the reversal of cuts we have modelled the effect a range of hypothetical changes to universal credit. Unless otherwise specified these are modifications to universal credit as it is currently legislated – our UC2016 system.

- Addition of a second earner work allowance (at 100% or 50% of the current work allowance)
- Reduction of the taper rate to 55 per cent (from 63 per cent)
- Raising the under-25 rate to the current 25+ rate
- Triple lock of the child element
- Triple lock of child benefit (in a universal credit system)
- All of the above changes (with the higher second earner work allowance hypothesised)

5a. Poverty reduction potential of changes to universal credit

Tables 5.1 and 5.2 illustrate the potential of each of these changes, including the reversal of cuts and hypothesised reforms, to reduce poverty, compared with the current system of universal credit. It also includes the cost of each measure, based on the difference in expenditure for a given scenario in 2020/21 compared with the baseline scenario (with all cuts in place) uprated to 2020/21.

Short of reversing all the cuts, it is clear that the single most effective intervention in terms of reducing child poverty would have been to maintain the child element at its original level and ensure uprating in line with inflation, or – even better – apply a triple lock in line with the state pension. To achieve comparable gains *now* by implementing a triple lock would also imply compensating for previous years of below-inflation uprating and the restoration of the first child premium.

In terms of the number of children who can be protected from poverty per pound spent, reversing the two child limit and benefit cap are obvious choices – both of which are pushing children into poverty while achieving limited savings - although they do not affect as many families as the freeze.

Other analysis for CPAG has suggested that raising child benefit to compensate for years of lost uprating (and going further to raise it by £5 a week for all children) would have a greater impact on child poverty than suggested by these findings.[80] The IPPR analysis models a smaller uplift in child benefit than £5 per child, and also finds that while the lower benefit cap remains in place this will limit the poverty impacts of investing in child benefit at a UK level. However there are many other reasons to prioritise investment in child benefit: take up is much higher than for means-tested benefits, and with most other benefits rolled into a single payment under universal credit families can find themselves left relying on their child benefit if anything goes wrong with their universal credit claim.

[80] A Keung and J Bradshaw, *Analysis of the impact of increases to child benefit and child tax credits on child poverty rates in the UK and Scotland*, University of York Social Policy Unit, 2016

Table 5.1 Effect of changes to universal credit on child poverty

	Cost (£millions / year)	Child poverty reduction potential								
		Children in poverty (AHC)			Children in poverty (BHC)			Children in severe poverty (BHC)		
		Total	Under-5s	Over-5s	Total	Under-5s	Over-5s	Total	Under-5s	Over-5s
Reversal of cuts since 2013/14										
All cuts	14,086	**1,000,000**	300,000	700,000	**1,000,000**	300,000	700,000	**900,000**	300,000	600,000
Uprating of UC and child benefit	9,179	**300,000**	100,000	200,000	**400,000**	100,000	200,000	**200,000**	100,000	100,000
Freeze of child benefit and child element	1,596	**200,000**	-	100,000	**100,000**	100,000	100,000	**100,000**	-	100,000
Freeze of child benefit	722	**-**	-	-	**-**	-	-	**-**	-	-
Freeze of child element	1,066	**100,000**	-	100,000	**100,000**	-	100,000	**100,000**	-	-
Removal of first child premium	1,758	**100,000**	-	100,000	**200,000**	100,000	100,000	**100,000**	-	100,000
Child element cuts (first child premium & freeze)	2,824	**200,000**	100,000	200,000	**300,000**	100,000	200,000	**200,000**	100,000	100,000
Work allowance cuts and freeze	4,158	**200,000**	100,000	200,000	**200,000**	100,000	200,000	**200,000**	-	100,000
Benefit cap	1,652	**100,000**	-	100,000	**100,000**	-	100,000	**200,000**	-	100,000
Two-child limit	751	**200,000**	100,000	100,000	**200,000**	100,000	100,000	**100,000**	-	100,000
Hypothesised changes (if applied since 2013/14)										
Second earner work allowance (100%)	1,292	**100,000**	-	100,000	**100,000**	-	100,000	**100,000**	-	100,000
Second earner work allowance (50%)	593	**-**	-	-	**100,000**	-	-	**-**	-	-
Increase in under-25 rate	1,022	**-**	-	-	**-**	-	-	**-**	-	-
55% taper rate	3,190	**200,000**	100,000	100,000	**200,000**	100,000	100,000	**100,000**	-	-
Triple lock of child benefit	1,737	**100,000**	-	-	**100,000**	-	100,000	**100,000**	-	-
Triple lock of child element	4,591	**400,000**	100,000	300,000	**500,000**	200,000	300,000	**300,000**	100,000	200,000
Triple lock child benefit & child element	6,294	**500,000**	100,000	300,000	**600,000**	200,000	400,000	**400,000**	100,000	200,000
Triple lock of child element*	2,833	**300,000**	100,000	200,000	**300,000**	100,000	200,000	**200,000**	100,000	100,000
Triple lock child benefit & child element-*	4,536	**400,000**	100,000	300,000	**400,000**	100,000	200,000	**300,000**	100,000	200,000
All changes (with higher second earner work allowance)	12,943	**900,000**	300,000	600,000	**700,000**	300,000	500,000	**500,000**	200,000	300,000

* With first child premium still removed.

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Table 5.2 Effect of changes to universal credit on working-age poverty

	Adults in poverty (AHC)	Adults in poverty (BHC)	Adults in severe poverty (BHC)
Reversal of cuts since 2013/14			
All cuts	900,000	800,000	800,000
Uprating of UC and child benefit	300,000	400,000	300,000
Freeze of child benefit and child element	100,000	100,000	100,000
Freeze of child benefit	-	-	-
Freeze of child element	100,000	100,000	100,000
Removal of first child premium	100,000	100,000	100,000
Child element cuts (first child premium & freeze)	200,000	300,000	100,000
Work allowance cuts and freeze	300,000	300,000	200,000
Benefit cap	-	100,000	100,000
Two-child limit	100,000	100,000	-
Hypothesised changes (if applied since 2013/14)			
Second earner work allowance (100%)	100,000	100,000	100,000
Second earner work allowance (50%)	-	-	-
Increase in under-25 rate	-	100,000	-
55% taper rate	200,000	200,000	100,000
Triple lock of child benefit	-	100,000	-
Triple lock of child element	300,000	400,000	200,000
Triple lock child benefit & child element	400,000	400,000	200,000
Triple lock of child element*	300,000	400,000	200,000
Triple lock child benefit & child element*	400,000	400,000	200,000
All changes	800,000	600,000	300,000

* With first child premium still removed.

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

However we are not only interested in national level poverty reduction potential but in how different decisions would affect different groups within the population. It might be desirable, for example, to target the poorest families or those at higher risk of poverty because of the age or number of children, or disability. We are also concerned about the effect on work incentives and whether these policies will help families avoid the unemployment trap and poverty trap, while also providing adequate support for those out of work. Below we explore how different policy options will affect different groups in the population and the most effective approaches to targeting various groups with higher risk of poverty. We then move on to considering the effect on work incentives for example model households.

5b. Effect of changes to universal credit on family incomes

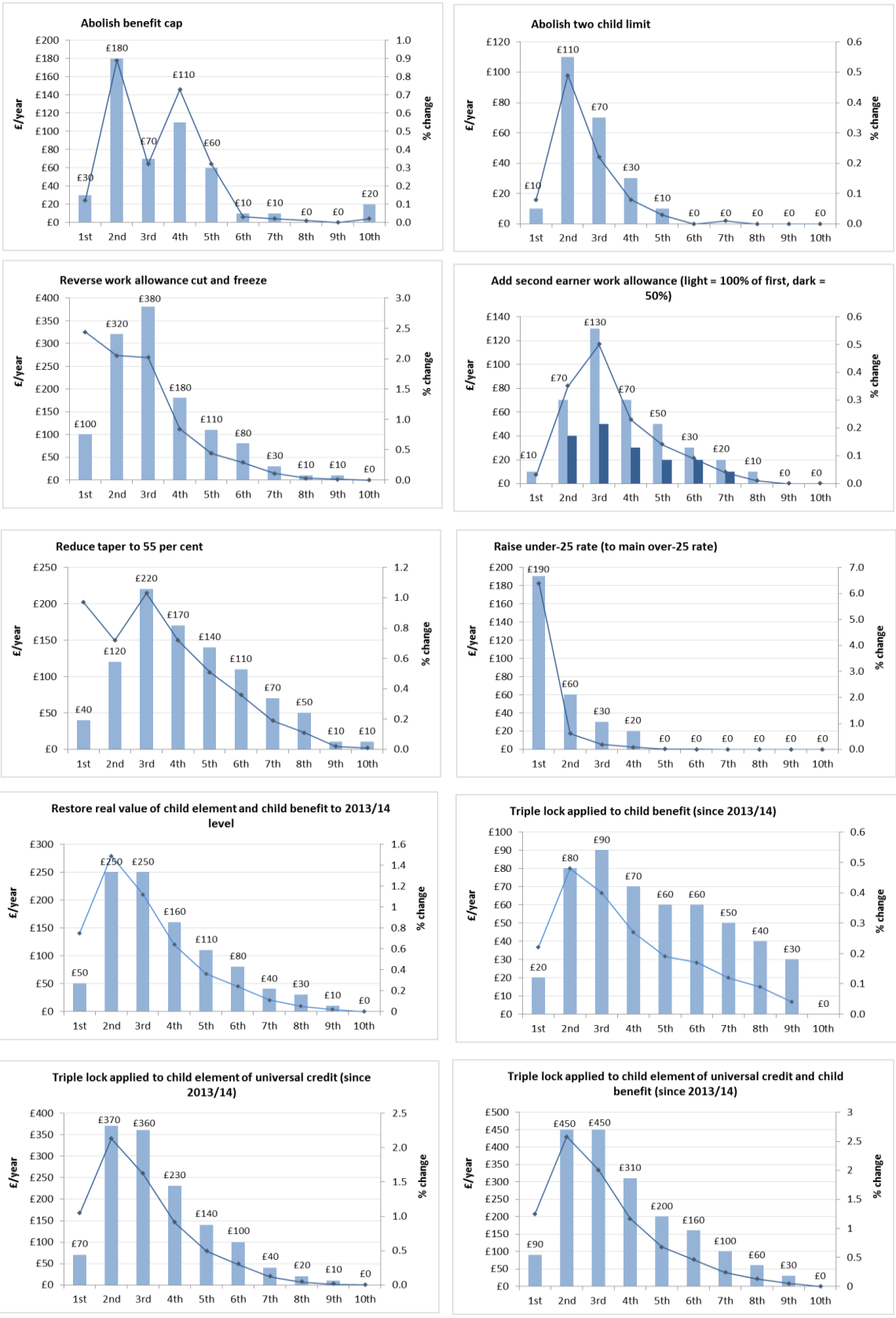
Lowest income families

Figure 5.1 compares the impacts of various hypothesised changes to a universal credit system by income decile. The single most beneficial change for the lowest (first) equivalised income decile would be to increase the under-25 rates in universal credit to match the over-25 rate. Unlike any of the other policy options considered, this would benefit the lowest decile far more than any other. This indicates the extent to which young adults are at risk of deep poverty, and makes a powerful case for raising the under-25 rate in spite of limited impacts on headline poverty rates at national level. Doing so would raise the income of the average family in the poorest ten percent of the population by £190 a year (a very significant 6.4 per cent increase).

Changes which particularly target families with children tend to have the greatest impacts in the second and third income deciles, probably because the very lowest income decile does not include so many families with children (partly because the adults in the lowest decile tend to be younger, and because receipt of children's benefits tends to boost incomes substantially in comparison with what is received by single people or couples without children, even after equivalisation). Thus reversing the two child limit or the benefit cap would have the greatest impact on families in the second income decile (increasing their income by an average of £110 or £180 a year respectively).

Applying a triple lock to the child element from 2013/14 would have seen incomes in the second decile increase by £370 a year (2.1 per cent) on average, and £360 a year (1.6 per cent) for the third decile. Applying a triple lock to child benefit also has the greatest impacts in the second decile, in cash and percentage terms. Its effects are fairly evenly spread in cash terms but in percentage terms this would still be a highly progressive investment.

Figure 5.1 Average effect of changes to universal credit and child benefit on family incomes by equivalised income decile



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Perhaps unsurprisingly, changes which benefit working families tend to have their greatest effects slightly higher up the income scale in the third or fourth deciles, at least in cash terms. Reversing the work allowance cuts made to date would benefit the second and third deciles most, probably because the greatest benefit would go to lone parent families who tend to have lower family incomes. In contrast, a second earner work allowance or a reduction in the taper rate provide greater average cash increases in the third and fourth deciles.

These might all be considered the 'just about managing', although it could be argued that many might feel that they are in fact struggling to manage. Families in the third decile would gain, on average, £380 a year (2 per cent) from the reversal of cuts to work allowances, £220 a year (1 per cent) from a reduction in the taper rate to 55%, or £130 a year (0.5 per cent) from a second earner work allowance equivalent to the current first earner allowance.

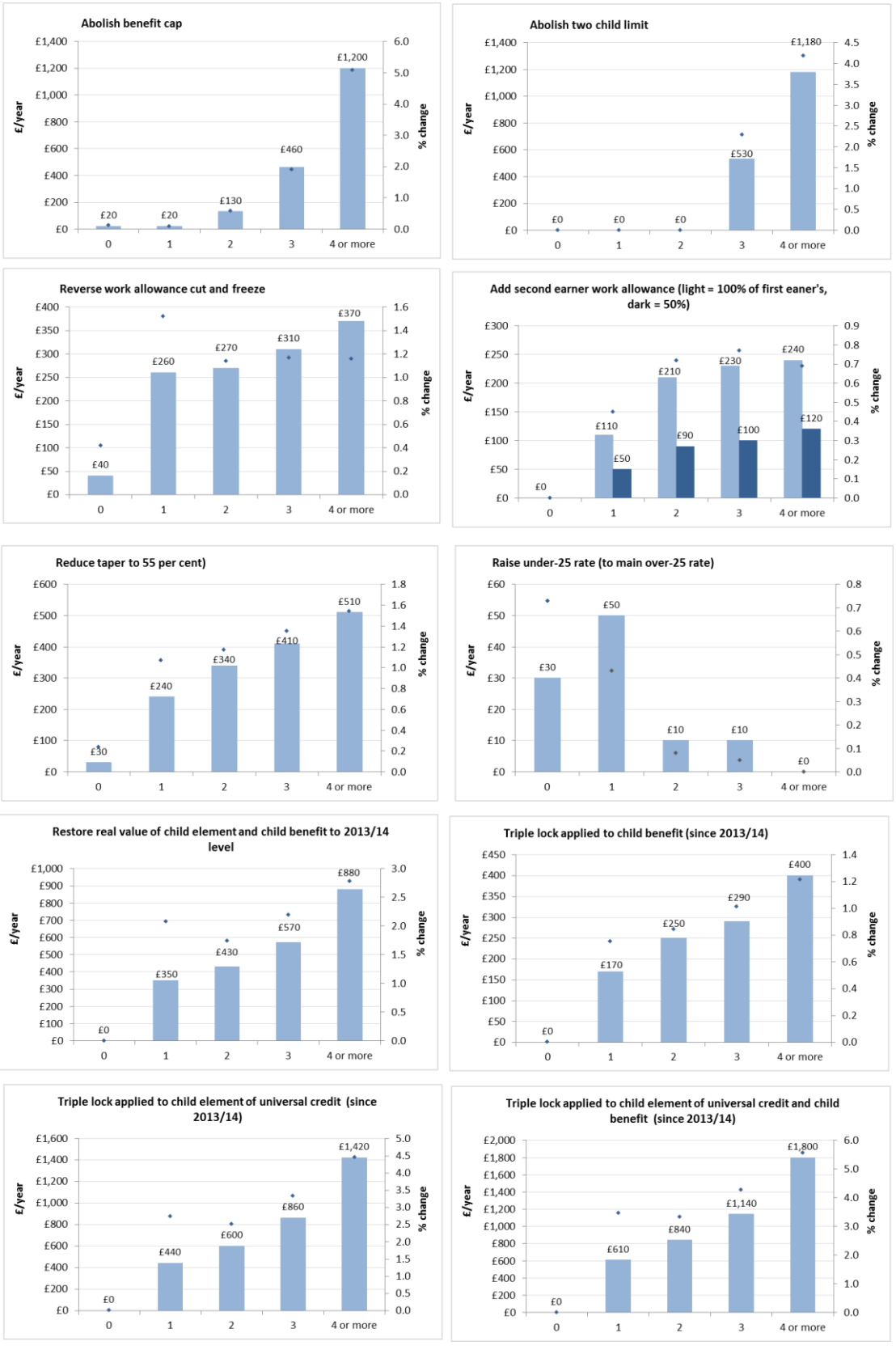
Larger families

Many of the possible changes have a progressively larger average effect for larger families, as shown in Figure 5.2. However the largest gains for families with three or more children would have come from maintaining the level of the child element and applying a triple lock (worth £860 a year to the average family with three children and £1,420 a year to the average family with four or more), abolishing the two child limit (worth £530 a year to the average three-child family and £1,180 on average to larger ones), or abolishing the benefit cap (worth £460 a year for families with three children and £1,200 a year for those with more). Abolishing the benefit cap would benefit fewer families than the other changes, but bring bigger gains for those affected. The only change for which a reverse pattern is seen is the raising of the under-25 rate, as younger adults are less likely to have children and likely to have fewer children.

Lone parents

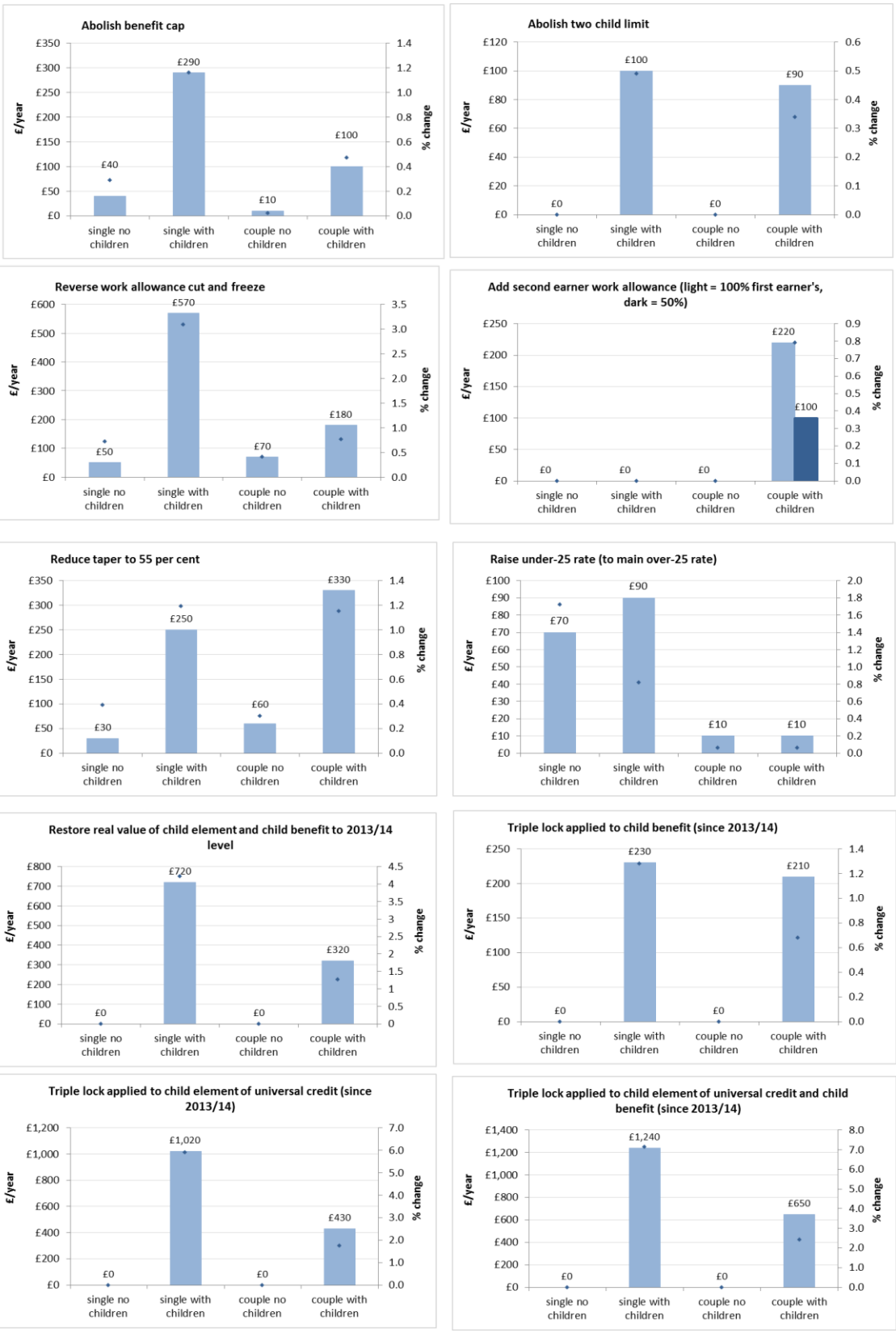
The greatest average benefit to lone parents would again have come from maintaining, and applying a triple lock to, the child element (worth £1,020 a year on average, an increase of almost 6 per cent). The next best option would have been to reverse cuts to work allowances, from which lone parents have lost the most, which would mean an income gain of £570 a year (just over 3 per cent) on average. Many of the other changes tend to benefit lone parents more than other family types on average, because lone parents are more likely to rely on universal credit/benefits. Exceptions are the second earner work allowance (which only benefits couples) and the reduced taper rate, which brings greater benefits to couples as they are more likely to have a parent in work and likely to have higher household earnings. See Figure 5.3.

Figure 5.2 Average effect of changes to universal credit and child benefit on family income, by number of children



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Figure 5.3 Average effect of changes to universal credit and child benefit on family income, by family type



Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Families with young children

The change which would most benefit any family with children under 16 would again have been to maintain and triple lock the child element (see Table 5.3). Families with a youngest child under five would have benefited most on average, standing to gain £630 a year or a 3 per cent increase in income. The next best change for this group, on average, would be a reduction in the taper rate to 55%, which would bring an additional £370 a year or a 1.3 per cent increase in income.

This outdoes the effect of restoring work allowances, at £280 a year, scrapping the two child limit or a triple lock on child benefit, which are both worth £220 a year on average for families with an under-five. Of course a child benefit triple lock would benefit more families than scrapping the two child limit, but the latter would have a much bigger effect for those affected. Increased support for childcare costs is also likely to benefit this group considerably (see section 5c below).

Table 5.3 Effect of changes to universal credit system on families with under-5s

	Average increase in annual income	
	£/year	Percentage increase
Reversing cuts		
Abolish benefit cap	£130	0.6
Abolish two child limit	£220	0.9
Restore work allowances	£280	1.3
Reverse all changes since 2013	£1,470	7.3
Hypothesised changes		
Second earner work allowance (equal to first earner)	£190	0.6
Second earner work allowance (50% of first earner's)	£90	0.3
Raising under-25 rate to 25+ rate	£70	0.5
55% taper rate	£370	1.3
Triple lock of child benefit since 2013/14	£220	0.9
Triple lock of child element since 2013/14	£630	3.0
All above changes (higher work allowance rate)	£1,610	6.8

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Families where someone has a disability

On average, families where someone has a disability benefit less from choices geared specifically towards working families, i.e. changing the taper rate or work allowances, and more from investment in children's benefits (Table 5.4). As our focus is on families with children in the round we have not modelled specific increases in support for disabled people or carers, or the reversal of cuts to disability benefits made before 2013 which would of course have a significant effect.

Table 5.4 Effect of changes to universal credit system by presence of disability in the family

	Average increase in annual income (£/year)		
	No disability	Disability	Severe disability
Reversing cuts			
Abolish benefit cap	£40	£20	£100
Abolish two child limit	£30	£20	£10
Restore work allowances	£100	£90	£90
Reverse all changes since 2013	£390	£300	£530
Hypothesised changes			
Second earner work allowance (equal to first earner)	£50	£30	£20
Second earner work allowance (50% of first earner's)	£20	£10	£10
Raising under-25 rate to 25+ rate	£30	£20	£30
55% taper rate	£110	£80	£70
Triple lock of child benefit since 2013/14	£60	£50	£30
Triple lock of child element since 2013/14	£150	£120	£110
All above changes (higher work allowance rate)	£440	£320	£270

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

Working families

It is also important to consider the effect of changes on the rewards from work and whether they help families to avoid the unemployment and poverty traps by increasing their income through work. Not surprisingly, reversing work allowance cuts, introducing a second earner work allowance and a lower taper rate perform well in this regard (Table 5.5).

Table 5.5 Effect of changes to universal credit system by working status of the family

	Average increase in annual income (£/year)	
	Working	Non-working
Reversing cuts		
Abolish benefit cap	£20	£110
Abolish two child limit	£30	£10
Restore work allowances	£150	-
Reverse all changes since 2013	£420	£400
Hypothesised changes		
Second earner work allowance (equal to first earner)	£60	-
Second earner work allowance (50% of first earner's)	£30	-
Raising under-25 rate to 25+ rate	£10	£60
55% taper rate	£150	-
Triple lock of child benefit since 2013/14	£70	£20
Triple lock of child element since 2013/14	£160	£90
All above changes (higher work allowance rate)	£510	£160

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

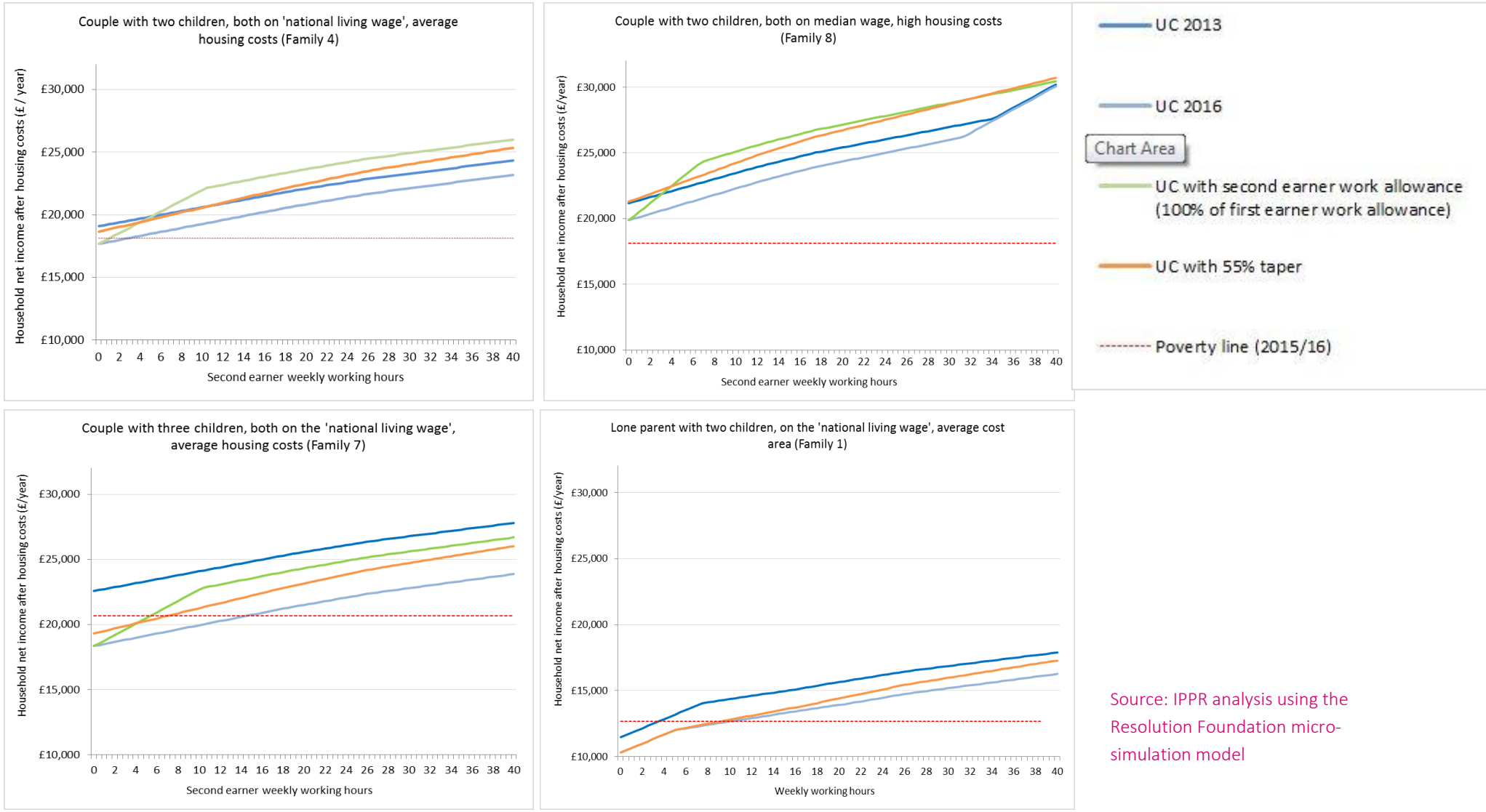
But there are choices to be made about which working families benefit, and our model families helps us to break down this broad category (see Figure 5.4 below). A second earner work allowance (equal to the current first earner work allowance) would raise incomes for a family with two earners more than a reduction in the taper rate, unless they have relatively high earnings (equivalent to two full time workers on the median wage). It would also have a very positive effect on the rewards from work for second earners. For families with two children and two earners, either of these changes would often be more helpful in terms of raising incomes even than reversing all the cuts and changes to universal credit since 2013. Families with three or more children would remain far worse off, however, than under UC2013.

A second earner work allowance, however, does not benefit lone parent families or single-earner couples at all. A reduction in the taper rate benefits them considerably but does not generally bring incomes up to the level that could have been expected under UC2013, particularly for those working part time and/or on lower incomes, or with larger numbers of children.

Others have also discussed the potential of higher work allowances to help ensure that families meet the MIS. It has been calculated that a couple with two children, one working full time and one part time on the 'national living wage', could achieve the MIS if the work allowance were increased by almost £2,000 a year (assuming that their wage rises to the planned 60 per cent of median earnings by 2020).[81] The author even notes that, in moving a family from a position of low pay (pre-'national living wage') to higher pay (the promised 60% of median), while raising the work allowance by £2000 a year, 'the state pays about the same amount in universal credit and takes more in taxation (so makes a net gain), while the higher wages allow the family to close the… weekly shortfall compared to the minimum income standard'.

[81] D Hirsch, *Not by pay alone,* 'Poverty' 156, February 2017

Figure 5.4 The effect of hypothesised changes to universal credit on incomes of four model families (without childcare costs)



Source: IPPR analysis using the Resolution Foundation micro-simulation model

5c. Help with childcare costs

Section 4e discussed the way in which childcare costs dampen the rewards from work for families with children, whether pre-school or school age.

We therefore modelled the effect of various policies to reduce childcare costs to families on our model families:

- An increase in the childcare subsidy under universal credit from 85 to 95 per cent
- A 50 per cent uplift in the childcare subsidy ceiling under universal credit
- Extension of free childcare to 30 hours a week for all two year olds
- Universal free extended schools, providing childcare from 8am-6pm for all school-age children

In all our model families, the 50 per cent uplift in the childcare cost ceiling had no effect. It might be beneficial for families with more or younger children, or those in the highest cost areas such as inner London. However it is excluded from the rest of this analysis for this reason.

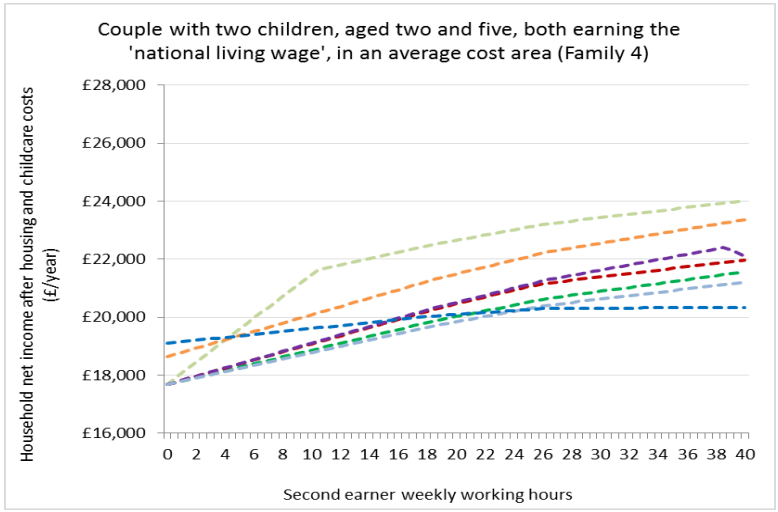
For all the couple families which we modelled, as long as the second earner works more than a few hours a week then a second earner work allowance (equal to the first earner allowance) is the most beneficial option in income terms. A reduction in the taper rate to 55 per cent tends to be the next most beneficial option, and is the best option for couple families with a single earner. See Figure 5.5.

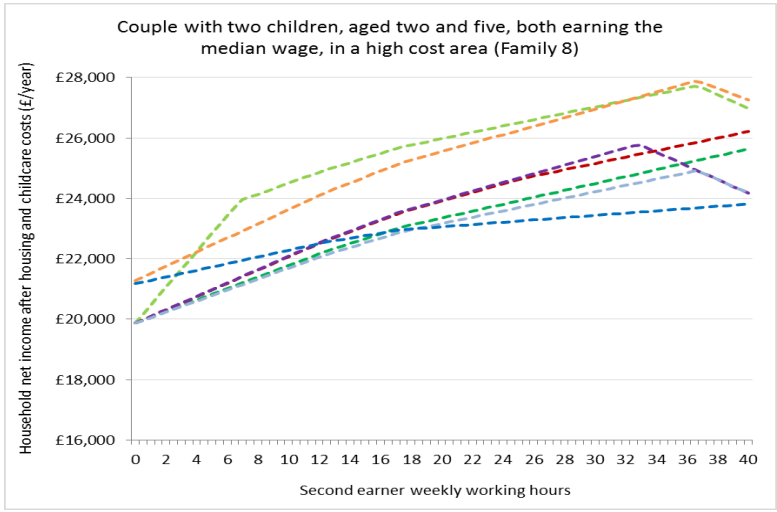
For the working lone parent families we modelled, a reduced taper performs best for a higher-earning parent with two children (on the median hourly wage rather than the 'national living wage') and for a lone parent on the 'national living wage' with just one two-year-old child. For a lower-earning lone parent with two children, the taper rate reduction and an increase in the childcare subsidy to 95 per cent offer very similar financial benefits at all hours of work. It seems likely that lone parent families on a lower hourly wage (e.g. those aged under 25) and/or with more or younger children might find an increase in the childcare subsidy more valuable than a reduction in the taper rate.

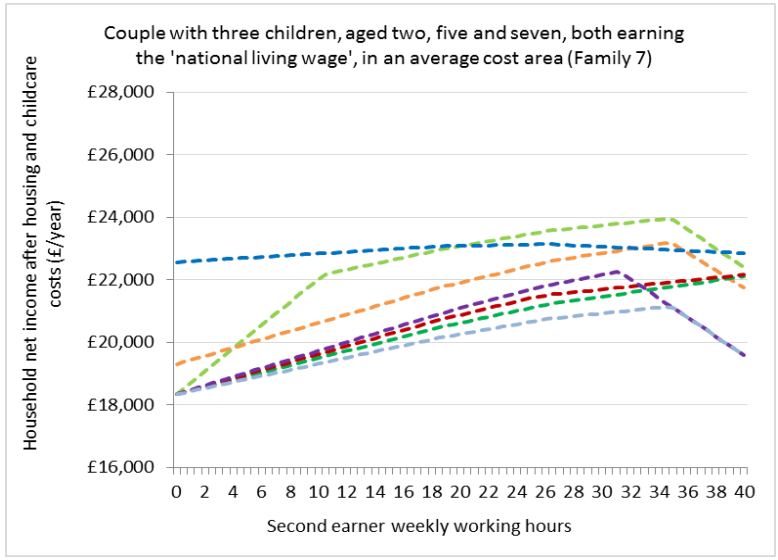
For our lone parent families 1 and 2, who each have a two-year-old and a five-year-old, the offer of 30 hours free provision for their two-year-old and extended school care for their five-year-old offer similar financial benefits, with extended school care slightly outdoing provision for two-year-olds for those working less than about 18 hours a week, and the reverse for those working more hours. For single parents working very low hours of up to 8 a week, the differences in income offered by all these policy options are marginal. See Figure 5.6.

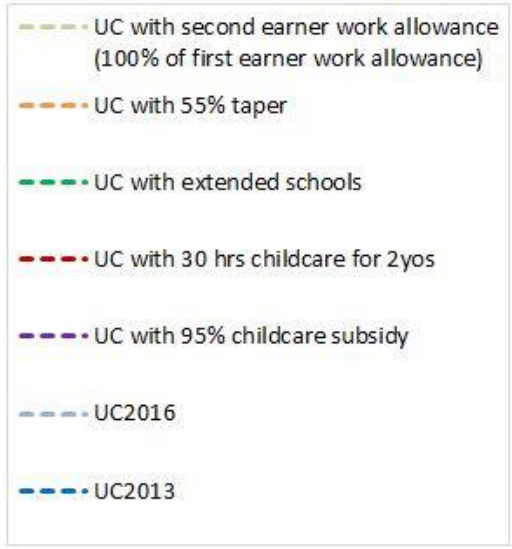
There are, however, strong arguments for a supply-side approach to childcare provision rather than focusing solely on demand-side subsidy, in spite of the apparent advantages for our families in terms of incomes after childcare costs, of an increased subsidy within universal credit. In practice it is likely that universal provision of extended schools and nursery hours would make childcare more readily available and accessible, avoid parents being deterred by apparently high costs (including upfront costs) or fear that their universal credit childcare element may not be paid or may be paid too late, allow the government to better ensure quality of provision, and bring down costs in the system as a whole. Extended schools could also provide for older children such as teenagers.

Figure 5.5 Effect of increased support for childcare, second earner work allowance and a reduced taper rate on selected couple families



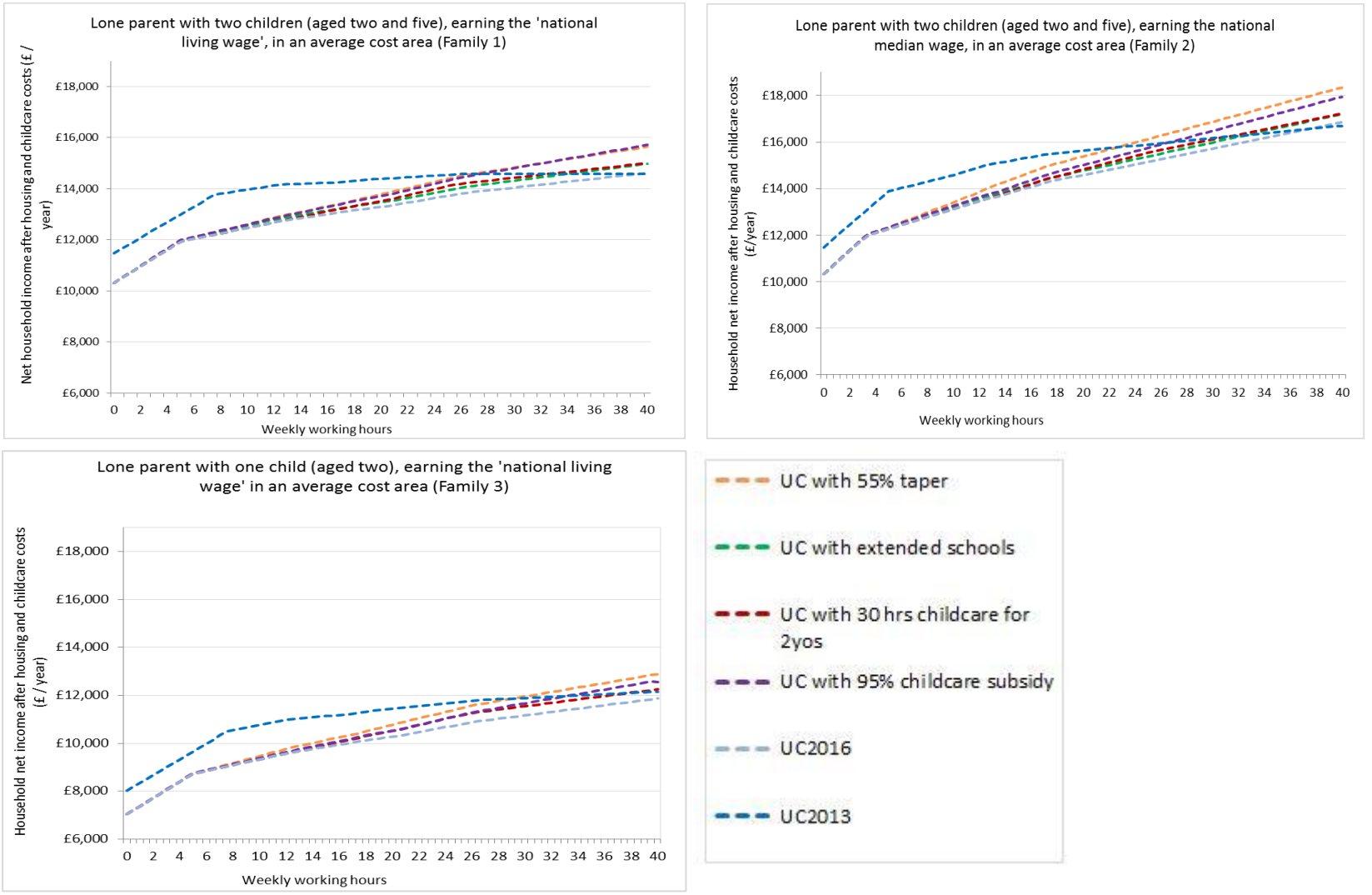






Source: IPPR analysis using the Resolution Foundation micro-simulation model

Figure 5.6 Effect of increased support for childcare and a reduced taper rate on lone parent families



Source: IPPR analysis using the Resolution Foundation micro-simulation model

5d. A 'full overhaul' of universal credit

We have also modelled what could be offered to low-income families with a 'full overhaul' of universal credit geared towards supporting families. This includes reversal of the cuts since 2013 (i.e. a return to UC2013), plus all the additional elements listed above with the higher second earner work allowance, additional funding for disabled children (by increasing the disabled child premium from £28 a week to £57 a week, matching its level in tax credits) and additional support for childcare costs (raising the childcare cost ceilings by 50% and increasing the subsidy to 95%).

This would require substantial investment but, in return, would lift 1,500,000 children out of poverty (after housing costs) compared with what we can expect under UC2013 (see Table 5.6).

The full overhaul would benefit families at greatest risk of poverty. Lone parent families would be better-off by an average £1,730 a year. Families with under-fives would gain on average £3,000 a year. Families with three children would be better-off by £4,620 a year and those with four or more children by £7,470 a year, on average. Working families would gain £930 a year on average.

Table 5.6 Poverty reduction potential of a 'full overhaul' of universal credit on poverty

Poverty measure	Poverty reduction under a full overhaul of universal credit
Children in poverty (AHC)	1,500,000
Children in poverty (BHC)	1,400,000
Children in severe poverty (BHC)	1,100,000
Adults in poverty (AHC)	1,400,000
Adults in poverty (BHC)	1,100,000
Adults in severe poverty (BHC)	900,000

Source: analysis of 2014/15 family resources survey using the IPPR tax-benefit model

6. Final remarks

A decade of cuts to social security are hitting families with children hard, and in particular are reducing the incomes of families already at greater risk of poverty: lone parents, families with very young children, larger families, those with a disability, and those in low-paid work. The same can be said of the transition to universal credit. Universal credit promised to lift children (and adults) out of poverty, and boost work incentives. The promise of poverty reduction has been broken, and for many families the promise of greater rewards from work has been too. Universal credit is receiving a great deal of attention this year as the roll out accelerates, and both claimants and frontline workers are reporting a host of problems associated with the implementation and functioning of the new systems. In the long run, however, what will matter most is the twin impact of austerity-driven cuts to social security and the roll-out of universal credit on living standards. This report tells us what this will mean for a generation of children growing up under austerity.