Coping and hoping

Navigating the ups and downs of monthly assessment in universal credit

Executive Summary

IPR Report

Dr Rita Griffiths, Dr Marsha Wood

April 2024

abrdn
Financial Fairness Trust

IPR Institute for Policy Research

Executive Summary

Knowing that the amounts you (and/or your partner) receive through earnings and/or benefits will cover your basic living expenses is one of the fundamental building blocks of income security and financial well-being.

For people in low-paid work and moving in and out of insecure forms of employment, earnings top-ups can be a lifeline, making the difference between having enough money to live on and having to borrow, between taking a job or remaining on benefits. Replacing six means-tested benefits and tax credits[1] with a single monthly household payment, Universal Credit (UC) is the UK's main, means-tested, working-age benefit for supplementing low household income for people both with and without earnings. It has been designed to respond swiftly to changes in income, earnings and circumstances, monthly, in real time, with the intention of helping claimants to budget, reducing errors and overpayments, and incentivising work and higher earnings.

As of December 2023, 6,352,771 people were claiming Universal Credit, approximately 39 per cent of whom were in paid work, or living with a partner who was working[2]. When the remaining three million or so claimants of legacy benefits and tax credits have all been moved onto UC, an estimated nine million adults, just under a quarter of the working-age population, will be claiming it, approaching half of whom are likely to be employed or self-employed.

To date, policy interest and research about Universal Credit has focussed on the impacts on and experiences of the poorest, mainly out-of-work, households. There has been much less focus on working households and no systematic research into how working claimants experience UC. In particular, little is known about how changes in monthly earnings affect the UC payment, how stable or volatile this makes household income, nor the effects on household budgeting. Based on the lived experience of 61 Universal Credit claimants in 42 households, this is what our research set out to discover. A particular focus was the monthly means test in which the benefit payment is automatically adjusted upwards or downwards based on a household's reported income and earnings in the previous month. We were also keen to explore whether and how the system of monthly assessment shapes work-related decisions.

1 Universal Credit is replacing Working Tax Credit, Child Tax Credit, Housing Benefit, Income Support, income-based Jobseeker's Allowance (JSA) and income-related Employment and Support Allowance (ESA).

2 DWP Stat-Xplore data release January 2024.

What makes Universal Credit different?

As a dynamic benefit intentionally designed to fluctuate in response to monthly changes in income, earnings and household circumstances, Universal Credit is a radical departure from the benefits and tax credits it is replacing. Unlike the legacy system, UC is assessed and paid monthly in arrears[3]. Tax credits, in contrast, were assessed annually, based on a self-completed return using the previous year's household income. Nor are earnings averaged out over the year, as was the case with tax credits. Rather, the UC payment reflects earnings in each claimant's monthly assessment period – which starts on the day they make their claim. Any earnings or other income received in the previous month, together with any changes of circumstance, are taken into account when calculating the monthly amount claimants[4] are entitled to. All PAYE (Pay As You Earn) earnings reported by employers via the HMRC's RTI (Real Time Information) feed and captured within a claimant's monthly assessment period, including any bonuses, backdated pay or wage advances, are counted. Self-employed claimants and those with earnings under the PAYE threshold must self-report their earnings each month. A single taper (currently 55 per cent) reduces entitlement gradually as earnings rise. Some working claimants with dependent children or limited capacity for work may be eligible for a 'work allowance' – allowing them to earn up to a specified amount each month before the taper is applied[5]. If monthly income, earnings and household circumstances remain the same, then the UC payment should stay the same, but if they change, the payment is intentionally designed to rise or fall in response. Tax credits, in comparison, generally remained fixed for a year.

A single household award that is assessed and paid monthly in arrears fits into an overarching policy narrative of benefit simplification and improved work incentives. A monthly payment designed to fluctuate each month, as earnings rise or fall, is intended to smooth and stabilise household incomes and make the financial impact of working additional hours more visible and immediate, thereby motivating claimants to earn more. Monthly assessment is furthermore intended to reduce the likelihood of overpayments, fraud and error. Annual assessment under tax credits meant that changes in income and circumstances were not generally taken into account until the end-year reconciliation, potentially giving rise to both under- and overpayments. Monthly assessment also fits into Universal Credit's wider remit of ensuring claimants meet their financial obligations in a timely way. Deductions – to repay a wide range of debts, including benefit and tax credit overpayments, loans and arrears of rent, council tax and utility bills – are taken at source from the UC award before the monthly payment is made.

3 Under 'Scottish Choices' claimants in Scotland can request to have their UC paid twice monthly and in Northern Ireland UC is normally paid twice a month. In England, payment of UC more frequently than monthly can only be arranged under exceptional circumstances with decisions made on a case by case basis.

4 A 'claimant' or 'benefit unit' can be an individual, a lone parent, or a couple, with or without dependent children.

5 In 2022/23 if a claimant received the housing element of UC, a lower work allowance of £344 per month applied. If they did not receive the housing element of UC, a higher work allowance of £573 per month applied. The rates for 2023/24 increased to £379 and £631 respectively.

Alongside Universal Credit's monthly assessment, debt recovery and payment regime is a digital platform for claimants' ongoing self-management of their claim through the use of an online account and journal. The account contains copies of the UC monthly statement and is used to notify the DWP of changes of circumstance and to raise queries and challenge decisions. A complementary programme of employment support, delivered by work coaches based in Jobcentres, is designed to encourage people into paid work and help those in employment to increase their earnings. A strict set of work conditionality requirements, overseen by work coaches and reinforced by sanctions, underpins the monthly assessment and payment regime.

Research aims

The aim of the research was to explore how the system of monthly assessment in Universal Credit – used for assessing entitlement, recovering debts and calculating payment – is affecting income security and financial well-being in working households. The specific research questions the study sought to answer were:

- How stable or volatile are monthly household incomes and what are the key drivers?
- To what extent does Universal Credit dampen or accentuate income insecurity and help with household budgeting?
- Is the adjustment to the UC payment in response to changes in earnings timely and smooth?
- Is household income sufficient to generate a buffer and cover reductions in the UC payment when earnings rise?
- What budgeting strategies do participants use to manage fluctuating payments and variations in household income?
- To what extent does monthly assessment incentivise employment, longer working hours and higher earnings?
- What conclusions and policy implications can be drawn from the findings and what policy recommendations can be made?

Research methods

Collecting both qualitative and quantitative data derived from regular, mainly monthly, interviews with 42 participants, the research recorded household income and essential household expenditure, month-to-month, in real time, for 13 months, between February 2022 and March 2023. All 42 participants took part in qualitative interviews, while 37 provided sufficient quantitative data (nine plus months) to allow month to month tracking of their income and earnings over time.

The main source used for accessing income and earnings data was the monthly Universal Credit statement, sent by participants to researchers via email and text as PDF attachments and screenshots. Interviews, conducted by telephone and face to face, gathered information about other household income and essential expenditure, budgeting strategies and work. In total, 256 interviews were conducted (55 face to face and 201 by telephone) and 491 Universal Credit monthly statements were collected.

Individual monthly household income profiles were created in Excel for 37 of the 42 households using data extracted from participants' UC statements, together with supplementary information gathered during interviews. Quantitative analysis was conducted using Excel and SPSS. Qualitative analysis was conducted using MAXQDA, a Computer Assisted Qualitative Data Analysis (CAQDAS) software package. All 256 interviews were transcribed verbatim, coded and analysed thematically.

The sample

The 42 participants – 36 women and six men – were living in a broad cross section of households in England, Scotland and Wales with a Universal Credit claim of at least six months duration. The youngest participant was 21 and the oldest 58. Thirty-three participants were White British, five were White Other, two were Black, one was Asian, and one was mixed. All the couples were female/male. Nineteen participants were claiming UC as a couple, 17 as a lone parent and six were single claimants. Because 19 participants had a partner, there were 61 UC claimants in total in the sample.

There were 33 families with dependent children, 16 of whom had at least one pre-school aged child. Eleven families had one dependent child, 14 had two, seven had three and one had four dependent children. In six households, there was an adult child living at home. Twenty-five households had someone with a serious health condition or disability, including seven families with at least one child with a disability. Three households had more than one child with a disability. Eighteen participants were living in social rented housing, 18 in private rented accommodation and six had a mortgage.

When the research started in the spring of 2022, the 61 claimants were either in paid employment or self-employment themselves and/or had a partner who was working. Including partners, 50 people were working when the first interview was conducted, three of whom had two jobs. Forty-two were employees and ten were self-employed, including two who were both employed and self-employed. Hourly pay ranged from £9.50 to £27. Of the 42 participants who were employed, 32 said their job was permanent, five were on temporary or fixed term contracts and five were not sure. Of the 50 claimants working at the start of the research, 34 were in the same job at the end.

Among couple households, 11 had a single earner and eight had two earners. In eight of the single-earner couple households, the male partner was the earner and in three it was the female partner. Eight families used paid childcare at some point during the study timeframe.

Twenty people were working 30 hours or more per week (including seven working 40 or more hours), 11 were working 20-29 hours, 16 were working 1-19 hours and three were unsure. Half of those with earnings had variable work hours. Half of those with earnings were paid monthly. The other half were paid weekly (9), four-weekly (7) or, fortnightly (2), or at different frequencies due to being self-employed (6) or on flexible pay (1).

Seven households experienced one or more change in their personal circumstances over the study timeframe which impacted on the UC claim including separating from a partner, children moving in or out of the family home, moving house, a close family bereavement and serious health issues involving time in hospital.

For the sample as a whole, earnings made up just under half of household income (49 per cent) and Universal Credit made up just over a third (34 per cent). Other benefits made up 10 per cent of household income, and other income, such as child maintenance payments, made up 4 per cent. The Government's cost of living payments – an additional £650 paid in two separate payments to eligible households in receipt of UC and other means-tested benefits during 2022 – made up the final 3 per cent.

This sample of working households provided us with a very detailed data-set, based on real-time and regular interviews and UC statements for a diversity of claimants, all with income from both earnings and UC, over a minimum period of nine months between February 2022 and March 2023.

Findings

How stable or volatile were monthly household incomes?

A large majority of households experienced significant monthly income variability during the course of the research. Nineteen households (51 per cent) had monthly incomes that were highly erratic or falling and a further seven households (19 per cent per cent) had incomes that were erratic. Only 11 households (30 per cent) had monthly incomes that were broadly stable or rising.

Variable earnings were the principal driver of changes in monthly income. These were surprisingly common and unexpectedly large:

- For 22 of 37 households, earnings varied month to month by an average of £200 or more.
- For 16 of 37 households, earnings varied month to month by an average of £300 or more.
- For 28 of 37 households, earnings varied by £500 or more from one month to the next at least once over the data collection period.
- For 16 of 37 households, earnings varied by £1000 or more from one month to the next at least once over the data collection period.

Monthly changes in earnings, in turn, drove changes in the Universal Credit payment. Monthly fluctuations in the UC payment were both frequent and sometimes very large:

- For 23 of the 37 households, UC payments varied month to month by an average or £100 or more.
- For 8 of the 37 households, UC payments varied month to month by an average of £200 or more.

These averages also conceal some very large single month UC payment fluctuations.

- For 20 of the 37 households, UC payments varied by £400 or more from one month to the next at least once in the year.
- For 10 of the 37 households, UC payments varied by £600 or more from one month the next at least once in the year.

The Government's cost of living payments had little overall effect on income variability. Other social security benefits, such as Child Benefit, Personal Independence Payment (PIP) and Disability Living Allowance (DLA), which are disregarded for the purposes of UC assessment, had a small stabilising effect for households that received them.

What were the key drivers of income volatility?

Earnings made up the largest proportion of income for most households in this research for most of the time. As such, variable earnings were the principal driver of variability in monthly income. However, it was the interaction over time between changing earnings and the UC payment that lay at the core of the income volatility experienced by most participants. Changes of circumstance were another reason for variability in the UC payment which, in turn, affected levels of monthly household income.

It is important to distinguish between variability in *actual* earnings – reflecting actual changes in wages earned and paid – and variability in *reported* earnings – that is, variability due to the way in which earnings data submitted by employers is captured by HMRC's RTI system, in which underlying earnings remain unchanged. Variability in *actual* earnings was due to a combination of factors including changeable working hours and shift patterns and periods of unemployment between jobs. Unpaid sick leave could also result in lower monthly earnings. Variable earnings as a result of variable and intermittent hours worked more commonly affected participants in less secure forms of work, including temporary and agency jobs and those with zero-hour contracts.

More unexpected was the extent of earnings variability among those paid monthly and in more secure forms of employment. Here, it was mainly due to higher in-month earnings as a result of non-consolidated pay awards, performance bonuses and backdated pay increases. When added to regular monthly earnings, these lump-sum payments could elevate monthly pay by hundreds, sometimes thousands, of pounds, causing UC to plunge or fall to zero in the following month or months. As a result, these participants often received less UC than they would otherwise have been entitled to if the equivalent amount had been paid monthly or spread more evenly throughout the year. Those affected by large spikes in pay would generally have preferred to have had these amounts paid over a longer period, stabilising UC payments, helping to smooth peaks and troughs in household income and minimising reductions in benefit entitlement. However, employers seemed mostly unaware of, or unable to mitigate, the detrimental financial effects on employees that could unwittingly be caused by payroll systems and remuneration policies.

As documented in other research, variability in *reported* earnings was generally due to pay frequency. Participants paid weekly, fortnightly or four-weekly could experience fluctuations in their UC payment for no reason other than that the date their earnings were reported as paid, and their UC assessment period – which had been arbitrarily assigned to them at the start of their claim – were poorly aligned. Had participants with weekly, fortnightly or four-weekly pay frequencies been paid the same earnings calendar monthly, they would not have been affected in these ways. Monthly-paid employees could be affected too if their regular pay date was close to the start or end of their monthly assessment period, or if they were paid early. Poor employer practices resulting in late and incorrect RTI earnings submissions, together with payroll and tax code errors, were another reason for variability in reported earnings. Under- or over-reporting of earnings meant an under- or overpayment of UC which would later need adjusting.

Alongside the budgeting difficulties that monthly income volatility could cause, a reduced UC payment could have serious knock-on effects in terms of the loss of entitlement for work allowances and other means-tested support these claimants might otherwise have been entitled to, including (but not limited to) help with council tax and prescription charges, potentially reducing household income by hundreds of pounds over the year. A nil UC award in the qualifying eligibility period for the Government's cost of living payments could also mean claimants losing out on this extra financial help.

People with fluctuating earnings (whether actual or reported) could find themselves eligible for help in one month but ineligible in the next, adding to income insecurity. A UC payment that frequently changed each month also made it hard to know whether the amount awarded was correct. Raising RTI disputes, correcting wage errors and challenging payment decisions was burdensome for working claimants. Financial losses caused by pay-related errors and benefit calculations they suspected were incorrect would often be absorbed through lack of time and attrition.

Was the adjustment to the UC payment in response to changes in earnings timely and smooth and did it help to dampen income fluctuations?

Intended to smooth and stabilise household income, UC is intentionally designed to adjust to monthly changes in income, earnings and circumstances. As earnings rise, the UC falls and when earnings fall, UC rises. The research found that while a higher UC payment in response to a fall in monthly earnings was a useful and timely income top-up, a reduction in the UC payment when earnings rose, was much less welcome. The reasons were not simply due to the loss of income, but that the amount of the reduction in UC was hard to predict and compensate for, particularly if it was large, which it frequently was. A significant reduction in or unexpected loss of UC was not easily absorbed by the lowest-earning participants who typically had no surplus income or savings to fall back on. Lump-sum bonuses and pay awards were often spent during or soon after the month of receipt, leaving little or nothing to set aside to cover the subsequent assessment period when the UC payment dropped or was nil.

Adjustment to the UC payment was also not necessarily as timely as the policy assumes. There could often be a time lag of two months between working more or fewer hours and receipt of a lower or higher UC award. This meant that higher earnings could sometimes coincide with an increased UC payment, while lower pay could correspond with a lower or even nil UC payment. People whose hours of work varied from month to month were obliged to continually juggle two sets of income uncertainty; earnings and the UC payment. For working parents required to pay childcare fees to pay in advance, but whose childcare costs were tapered with earnings and refunded in arrears, variability in the UC monthly payment sometimes became unmanageable. In these situations, contrary to the policy intent, the overall effect was to accentuate, rather than dampen, monthly income volatility.

Was household income sufficient to generate a buffer and cover reductions in the UC payment when earnings rose?

In and of itself, month to month variability in income is not necessarily problematic if overall household income is sufficient to enable people to manage monthly income dips. Indeed, the general expectation underlying the design of monthly assessment is that claimants should be able to both manage and absorb the financial highs and lows of variability in household income by careful planning and budgeting – saving and setting aside money in the months when earnings are higher and using any surplus to cover the periods when pay may fall or jobs end.

Few participants in this research were able to achieve this tricky balancing act, not because they lacked financial skills or because they were spendthrift, but because levels of earnings and benefit payments were simply too low to generate a surplus.

The Minimum Income Standard (MIS), developed by Loughborough University and used by the Joseph Rowntree Foundation and others, is the amount of money different types of households are considered to require to achieve a socially acceptable standard of living. Average monthly income after housing and childcare costs for the households in our sample was below the Minimum Income Standard (MIS) for all but five households.

Among the rest:

- 11 households had average monthly incomes that were 0-19 per cent below the MIS
- 16 households had average monthly incomes that were 20-39 per cent below the MIS
- 4 households had average monthly incomes that were 40-59 per cent below the MIS
- 1 household had average monthly income that was 60-79 per cent below the MIS

Overall, 32 of the 37 households had average incomes below the MIS despite 32 households having at least one earner throughout the study and 35 households having at least one earner for eight or more months of the study.

The five households with average monthly incomes above the MIS all contained at least one earner who was generally working full-time in a steady job, paid above the minimum wage, that they stayed in for the duration of the study. All five households were also in receipt of additional benefits due to one or more household members with a disability[6]. Though intended to cover the extra costs of disability, the additional income from benefits such as PIP, DLA and Carer's Allowance, allowed several of these households to get by, even to save. These families were also more likely to have the most stable incomes. Households with the lowest average monthly incomes, on the other hand, were more likely to have the most volatile incomes.

Some families also had access to additional income, or had more disposable income than their English counterparts, by virtue of living in the devolved nations. Claimants in Scotland and Wales do not pay prescription charges, nor do Scottish residents pay water rates. The Scottish Child Payment, a weekly means-tested benefit of £25 for each child aged 16 and under, also helped to top up the incomes of families with dependent children. Some participants living in Wales, who met the eligibility criteria, had also been able to access additional financial help including an unpaid carer's grant worth £500 and a winter fuel payment of £200.

The regular and sometimes large amounts taken from the UC award in deductions for loan repayments, benefit overpayments and third-party debts was an important reason why monthly disposable income was lower in many working households than it might otherwise have been. More than three-quarters of participants had deductions taken from the UC payment at some point during the timeframe of the research. For around a third, the deductions were continuous for the whole period of data collection.

The high rate of benefit withdrawal as earnings rose was another a significant factor in reducing monthly income in working households. Single claimants and second earners in two-earner couples with children (all of whom were women) who did not benefit from a work allowance, had their UC entitlement tapered from the first pound of earnings. Self-employed claimants who had been trading for more than 12 months, so subject to the minimum income floor (MIF)[7], were subject to further potential

6 It is important to note that the MIS does not include disability related costs. This means that monthly disposable income is over-estimated in these households because the costs of disability are not taken into account. If the extra costs of disability were included, it is likely that these households would fall below the MIS.

7 The MIF is broadly equivalent to the national minimum wage for each hour the claimant is expected to work as set out in their claimant commitment. If they earn more than the MIF, then their UC entitlement is calculated using their actual income. If they earn less than the MIF, then the MIF is used in place of their earnings, meaning that the UC payment will be lower than it would have been if based on their actual income.

reductions. Deductions for notional profits they had not actually earned could significantly reduce UC entitlement, sometimes by hundreds of pounds each month.

Monthly income was also sometimes unduly low as a result of UC errors and underpayments. Several participants were missing UC elements they should have been entitled to or had had their UC award incorrectly reduced. Whereas deductions for UC overpayments are automated, refunding underpayments for missing elements of UC are not. The onus is rather placed on the claimant to identify errors and have them corrected. Five families also had their household income reduced due to the imposition of the two-child limit and four were subject to the benefit cap at least once during the research. Two families with children had their UC payment reduced due to being sanctioned; in one case, four times.

The combination of low pay and reduced entitlement to UC due to multiple deductions taken at source from the monthly payment for earnings, loan repayments, overpayments and third-party debts, meant that few households in this research had levels of disposable income that stayed high enough for long enough to allow them to save or set aside funds. Indeed, some were left with household income below the level needed to cover basic living expenses. Two-thirds of participants said that they ran out of money before the end of the month. This seriously compromised their ability to bridge monthly income gaps when the UC payment fell. Though a welcome boost to the incomes of cash-strapped households, the Government's cost of living payments made little overall difference to participants' ability to manage month to month. As with one-off employer bonuses and backdated pay awards, these lump-sum payments were typically spent on pressing household needs soon after receipt.

The monthly income claimants had at their disposal, moreover, had a great deal of heavy lifting to do to. Having to bridge the often sizeable gap between the housing contribution they received and their monthly rent and council tax was a major factor contributing to low disposable monthly income. Debt repayments outside of the UC payment – to repay student loans, council tax and utility arrears for example – could also squeeze monthly income. For parents using paid childcare, making up the difference between the financial contribution they received and their childcare fees also chipped away at household budgets. Months in which both earnings and the UC payment dropped could sometimes lead to a deficit between monthly household income and essential outgoings, generating arrears and debt and little scope for saving.

What budgeting strategies do participants use to manage fluctuating payments and variations in household income?

In the main, participants in this research were highly resourceful, prioritising the payment of rent and essential bills and minimising borrowing and debts as far as possible. However, only a little over a quarter of households had any savings they could draw on when monthly earnings dipped or to cover the cost of replacing white goods, for example, without having to use credit cards, overdrafts or other forms of borrowing. Not unexpectedly, those better able to save and set aside income had higher and more stable earnings from jobs paying above the minimum hourly rate.

Nine participants had opened a government 'Help to Save'[8] savings account, which they found to be a very useful and generous scheme for incentivising and rewarding saving. However, levels of awareness were generally low and eligibility criteria restrictive. Many were unable to benefit because their net monthly earnings were less than the £722.45 needed to open an account. Some of those with the lowest incomes had insufficient disposable household income to allow them to save.

Interest free and easy to access, Budgeting and Change of Circumstances Advances could be a lifeline for those able to access them. However, most working participants in this research were ineligible for this help. Only claimants who have earned less than £2,600 (£3,600 jointly for couples) in the past six months are eligible for Budgeting Advances and Change of Circumstances Advances are only available to claimants whose UC payment has increased as a result of the change. In the main, working claimants appeared largely to be ineligible for local authority-administered discretionary funding schemes such as the Household Support Fund and discretionary housing payments because levels of household income were considered too high.

The cumulative and combined effect of low disposable household income and monthly income volatility was to reduce the ability of many participants to save or set aside money during the months when they had earnings, or when earnings rose. Having no monthly surplus or savings on which to draw, in turn, obliged many to borrow. Borrowing from family or friends, if they were able to, was the most common and preferred method used by participants for plugging monthly income gaps. If large amounts were needed – to replace a washing machine or pay for a car repair, for example – bank overdrafts or credit cards, if they had them, were sometimes used. However, though providing a short-term solution, this form of borrowing could be costly to service.

Participants with low earnings and insufficient household income to cover their regular monthly living expenses found it hard to pay bills and clear debts. Around half of the households had serious arrears of rent, council tax and/or utility bills. Having to bridge the often sizeable gap between the contribution they received towards housing costs and the amount they were obliged to pay in rent or mortgage payments and council tax each month, was a major factor contributing to arrears and debt. Only 17 of 42 households had their full rent included in their UC housing element.

If disposable income was particularly low one month, council tax and utility bills would often remain unpaid until sufficient funds – from earnings, UC or further borrowings – were available again. Some participants had been able to reduce the cost of household bills by accessing the help on offer from utility companies. However, levels of awareness about social tariffs and other similar help was low and eligibility criteria restrictive, in most cases debarring all but the poorest and most vulnerable households. Households with regular monthly income deficits found themselves in a perpetual cycle of 'robbing Peter to pay Paul' from which many were unable to extricate themselves. Borrowing to cover essential living expenses could, in turn, lead to chronic indebtedness with fewer opportunities still to save.

8 Help to Save is a government-backed savings account for low-income people with net monthly earnings of at least £7.

Did monthly assessment incentivise employment, longer working hours and higher earnings?

The aim of adjusting UC payments monthly through a single taper is to make the gains from working and from increasing hours of work starker and clearer. The underlying policy rationale is that claimants are motivated to work and increase their earnings because they can actually see and benefit from an immediate financial reward. However, for many in our research, the high rate of benefit withdrawal and visible loss of UC entitlement as earnings increased served mainly to discourage, rather than to incentivise, longer hours and higher earnings. Even at relatively low levels of earnings, entitlement for other means-tested help could be reduced or lost. Loss of entitlement for council tax and other means-tested support after tax, NI and the taper had already reduced earnings meant that for some claimants, work did not pay. Small increases in earnings actually made some participants financially worse off. Subject to marginal effective tax rates (METR)[9] often in excess of 75 per cent, many felt the level of the taper was unreasonably high.

Once they had fully grasped how UC worked, participants with no or few work conditionality requirements sometimes adjusted hours of work downwards to remain under the earnings threshold, while others declined offers of overtime. Having only one work allowance per household discouraged some non-earning partners in couples from entering work. Uncertainty over how much of their childcare costs would be refunded also discouraged some parents from working longer hours. Lone parents and 'second earners' in couples with children sometimes reduced their hours to avoid the need for paid childcare. Some mothers in couples, whose partners were working full time, questioned whether it was worth them working at all until their youngest child was old enough to start school. In situations such as these, contrary to the policy intent, UC's greater responsiveness and high rate of withdrawal appeared to have weakened, rather than strengthened, work incentives.

Policy recommendations

Increase the level of UC allowances and elements

While the 6.7 per cent uprating of benefits from April 2024 and one-off increase in the local housing allowance announced in the Chancellor's 2023 Autumn Statement are welcome, findings here support calls from the Joseph Rowntree Foundation (JRF) and the Trussell Trust for an 'essentials guarantee, based on a significant increase in UC standard allowance rates'[10]. Others have called for both in an increase and indexing of UC standard allowances and elements to reinstate their real cash value. To address the long-term, systematic erosion of value, we would support the call from the Resolution Foundation and others for working-age benefits to be annually uprated in line with earnings[11]. Restoring benefits to previous historical levels would help claimants to save and set aside money, allowing them to better manage dips in monthly household income.

9 The marginal effective tax rate (METR) measures how much a small increase in gross earnings is lost to tax, national insurance and reduced entitlement to means-tested benefits.
10 https://www.jrf.org.uk/report/guarantee-our-essentials
11 https://economy2030.resolutionfoundation.org/wp-content/uploads/2023/07/Sharing-the-benefits.pdf

Allow working claimants to keep more of their earnings

Alongside broader arguments in favour of increasing the adequacy and take up of benefits, a key priority arising from this research would be to ensure that claimants in paid work or self-employment are allowed to keep more of their earnings. The relative costs and benefits of reducing the taper rate, increasing the work allowance and extending it to single claimants and second earners in couples, including how far up the income distribution is it appropriate for UC eligibility to reach, should be assessed.

If the policy intent of UC to always make work pay is to be achieved, the potential loss of passported benefits and other means-tested help as earnings rise – including amongst other things, council tax support, free school meals and prescription charges – also needs reviewing. Cliff edges should be removed, earnings thresholds increased and greater standardisation introduced to reduce the inconsistency and unfairness that can arise from having a myriad of different, often discretionary, schemes operating at national and local levels. These issues are complex and further work is needed to explore them more fully. Such reforms would help both to increase incomes in working household and counter the disincentive effects of high marginal effective tax rates, while meeting one of the DWP's priority objectives set out in its 2023 strategic plan to 'maximise employment.'[12]

UC claimants with self-employed earnings raise a different but equally complex set of issues. Further research is needed into their experiences and the effects of current rules and regulations including the monthly calculation of profit and the minimum income floor (MIF).

Reform monthly assessment to increase income security for working claimants

Findings highlight the neglect of income security in the design of UC. Where claimants are usually paid on a monthly basis and receive more than one wage in the same assessment period, current regulations enable one of the wages to be treated as though paid in a different assessment period. The feasibility of extending the regulations to claimants paid weekly, fortnightly and four-weekly should be explored further. The case for adjusting monthly assessment to better accommodate claimants paid four-weekly is particularly strong.

Another possibility would be to provide claimants with longer-term fixed awards for three or even six months. This would provide greater predictability of income than the current system allows and could potentially encourage claimants to increase the number of hours worked as they would not face an immediate reduction in benefit.

Also in need of reform is the whole month approach to changes of circumstances. Changes in entitlement should take effect from the date of the change and awarded pro rata for the month, rather than assessed on the last day of a claimant's assessment period, as is the case currently.

12 https://committees.parliament.uk/publications/40123/documents/195656/default/

The rigidity of the monthly assessment period also needs challenging. More upfront information and advice should be communicated to UC applicants about the significance of the date a claim is made, giving them the option to defer the start date by a few days if their monthly assessment period does not align well with their pay dates. This is particularly important as the process of managed migration to move claimants of tax credits and legacy benefits across to UC begins to accelerate. Claimants already in work, or those who move to a job with a different pay frequency or pay date, should also be given the choice to change their assessment period.

Increase employer engagement

The research has shone a spotlight on the significance of employers to the financial well-being of working claimants. However, to date, their involvement in UC has been minimal. The DWP should make efforts to raise awareness among employers about the way in which pay systems, PAYE submissions and remuneration policies can affect benefit entitlement. At a more strategic level, their engagement should be sought as to the best way of mitigating the adverse financial effects and income uncertainty that can arise for employees who receive UC. Greater periods of notice for variations in hours and shifts and a reduction in the use of zero-hour contracts, should also be promoted.

Reform the childcare element of UC

To reduce the uncertainty and financial difficulties caused by upfront childcare payments and month to month variations in refunded fees, and to prevent the undermining of incentives to work or earn more (particularly among ‘second earners’ in couples), notwithstanding the changes to childcare policy announced by the Government in 2023, the treatment of childcare costs in UC also requires review. It would be simpler and more cost effective for working parents if childcare was funded directly, rather than through UC. Further work is needed to explore how to achieve this and other possible reforms.

Minimise deductions for debt and review other reductions in entitlement

The high level of deductions from many claimants’ UC awards was a key reason why monthly incomes often failed to cover essential outgoings. Both minimum and maximum amounts should be further reduced and historical overpayments and social fund loan debts older than seven years should also be written off. Higher and variable rates of deductions for households with earnings should also end.

Charities and civil society organisations have long campaigned for the two-child limit, benefit cap and spare room subsidy to be abolished, calls we would also endorse. Findings also support a review of the non-dependent adult deduction and the lower UC standard allowance paid to the under 25s.

Reform eligibility criteria for Budgeting and Change of Circumstance Advances and Help to Save

Eligibility criteria for budgeting loans should be revised to allow those with earnings above the current threshold (£2,600 for a single claimant and £3,600 for a couple) to apply. Eligibility criteria for change of circumstances advances should also be reviewed. The minimum net monthly earnings of £722.45 needed to open a 'Help to Save' account should be reduced to allow lower-earning claimants to benefit.

Ensure UC claimants receive all the elements and exceptions to which they are entitled

Our research suggests that Universal Credit's potential as a digitalised benefit is not being exploited as well as it might for the benefit of claimants. Data matching technologies which underpin UC's automated processes operate highly efficiently in the recovery of benefit overpayments and collection of third-party debts. A similar zeal should drive efforts to ensure that claimants receive all the financial support to which they are legally entitled; another DWP priority objective set out in their 2023 strategic plan.

Going forward

The next stage of work from this project will involve the production of a series of stand-alone policy briefs in 2024 to shine a more detailed light on three important policy areas that have emerged from this research as warranting further investigation: Universal Credit and childcare; Universal Credit and entitlement for other means-tested help; and Universal Credit and self-employed earnings. Further work which could usefully be undertaken include microsimulation analyses to explore the cost implications, differential impacts and distributional effects of the different policy recommendations (either singly or in combination) on working claimants in different sets of circumstances.

abrdn Financial Fairness Trust

abrdn Financial Fairness Trust has supported this project as part of its mission to contribute towards strategic change which improves financial well-being in the UK. The Trust funds research, policy work and campaigning activities to tackle financial problems and improve living standards for people on low-to-middle incomes in the UK. It is an independent charitable foundation registered in Scotland (SC040877).

Connect with us

Email us
ipr@bath.ac.uk

Find us online
www.bath.ac.uk/ipr

Read our blog
blogs.bath.ac.uk/iprblog

Follow us on Twitter
@UniofBathIPR

Like us on Facebook
www.facebook.com/instituteforpolicyresearch

Join our mailing list
https://bit.ly/2Ra9LOJ

Follow us on LinkedIn
linkedin.com/school/bath-ac-uk-ipr

abrdn
Financial Fairness Trust

IPR Institute for Policy Research