

Citizens Impact Assessment

Freeze to Working Age Benefits



Summary

The Government has set out plans for a two-year uprating freeze on most working-age benefits. It is vital that policymakers fully understand the potential impact of this change. Citizens Advice has been helping clients with the programme of welfare reform implemented over the last parliament. Our evidence therefore provides extensive insight into the challenges already presented, the issues affecting our clients now, and the likely impact of ongoing reform in the future.

- Benefits have been uprated below inflation since the start of 2013. This has placed significant financial pressure on millions of low income households. Over the last four years, there has been a sharp increase in Citizens Advice clients seeking advice on debt. The composition of debt is also changing, with a shift away from consumer credit issues towards problems in meeting basic household bills.
- The uprating freeze will therefore take effect at a point when many households are already financially vulnerable. A survey of 200 advisers at Citizens Advice found that two-thirds believed their clients were in a worse position to cope with the impacts of a freeze, in comparison to circumstances in 2012.
- With inflation projected to increase over the next two years, these risks should be considered against the savings intended; growth in problem debt entails very significant costs, both for those affected and the Exchequer, and affects work incentives, health outcomes and family life.
- The freeze will affect some of the most vulnerable in society. Of clients coming to Citizens Advice regarding benefits included in the freeze, nearly half are affected by a health condition or disability and over 40% have dependent children. These groups may also have fewer options to increase their incomes in the workplace.
- If the Government seeks to achieve its aims of cost savings, alongside protection of the vulnerable, it is vital that full consideration is given to meeting advice and support needs. In the case of an uprating freeze, this means reaching people early and providing help up-front; once people fall into debt, both addressing the problem and the costs it entails become much more difficult.

Context

In January 2014, the Chancellor announced that Treasury forecasts indicated a further £12 billion needed to be cut from the welfare bill in the next parliament. In justifying the decision to place the bulk of cuts on the welfare system, the contrast was drawn between the aim of a system that protected “the most vulnerable” with one that “offers up benefits as a lifestyle choice”.¹ The principle of ensuring fairness for both those in genuine need and to taxpayers was intended to guide decisions in this area.

This is one of a series of Citizens Impact Assessments, designed to clarify the detailed impacts of the policy proposals put forward so far. These are based on the extensive experience of Citizens Advice in working with many of the people likely to be affected by the reforms. It is vital that policymakers fully understand impacts before making decisions, that appropriate advice and support is provided to those affected by any change, and that the implementation process is safe and steady.

One of the decisions reached and announced in the 2015 Queen’s Speech was a two-year freeze on the majority of working-age benefits. Beginning in 2016, the main rates of working-age benefits, tax credits and Child Benefit will be frozen. Pensioners and benefits relating to disability costs will be protected, as well as statutory payments such as Maternity, Paternity and Adoption Pay.

The policy is intended to make large savings by spreading spending reductions over a broad spectrum of benefits. It follows similar measures brought in under the last parliament. The Coalition Government made significant savings by switching the indexing of benefit rates from RPI to the less generous CPI rate of inflation. From 2013, the increase of most working-age benefits was capped at 1% per year in nominal terms for three years. The IFS has calculated that together these changes made a very significant contribution to the £16.7bn worth of cuts made to the welfare system during the last parliament, amounting to £6bn by 2015-16.²

¹ G. Osborne (2014), *New Year Economy Speech by the Chancellor of the Exchequer*. At <https://www.gov.uk/government/speeches/new-year-economy-speech-by-the-chancellor-of-the-exchequer> (Accessed 30.06.15).

² A. Hood and D. Phillips (2015), *Benefit Spending and Reforms: The Coalition Government’s Record*, London: Institute for Fiscal Studies, p.9. At: <http://www.ifs.org.uk/uploads/publications/bns/BN160.pdf> (Accessed 30.06.15)

Policy rationale and objectives

Announcing the initial 1% cap on uprating in the Autumn Statement of 2012, the Chancellor presented the move as one which achieved the central aims of fairness, protection of the most vulnerable and cost saving. Given that wage growth during this period had failed to keep pace with inflation, the uprating cap would not only reduce welfare spending, but also bring benefits into line with wages. As the Chancellor stated, “we have to acknowledge that over the last five years those on out of work benefits have seen their incomes rise twice as fast as those in work...Those working in the public services, who have seen their basic pay frozen, will now see it rise by an average of 1%. A similar approach of a 1% rise should apply to those in receipt of benefits. That’s fair and it will ensure that we have a welfare system that Britain can afford.”³ The exclusion of disability and carers’ benefits from the move was designed to ‘support the vulnerable’.

The reforms in this area made under the last Government were certainly effective in realising savings, leading to a £6bn spending reduction. However, given the scale of the headline savings, it is vital to consider the cumulative impact the changes are having and how an extension of a policy which has already placed additional pressure on households with the lowest incomes will continue to affect their finances and prospects in the coming years.

Who will be affected?

Unlike cuts to specific benefits, this is a broad-based measure which affects much larger numbers of claimants. This means that the scale of reductions is rarely dramatic; the freeze to begin in 2016 is estimated to affect 11m families, calculated to effectively reduce their entitlements by an average of £100 each

³ G. Osborne (2012), *Autumn Statement 2012: Chancellor’s Statement*. At: <https://www.gov.uk/government/speeches/autumn-statement-2012-chancellors-statement> (Accessed 30.06.15)

year (although, as we go on to explain, some of the largest household costs, such as rent, are rising much faster than inflation).⁴ It also does not entail a direct cut to what families receive, acting instead to erode the value of their income.

Yet, despite its broad basis, this reform also entails significant distributional decisions. These may challenge its aims of combining spending reductions with fairness and protection of the vulnerable and - if consequences are not considered fully - may jeopardise the savings it sets out to achieve.

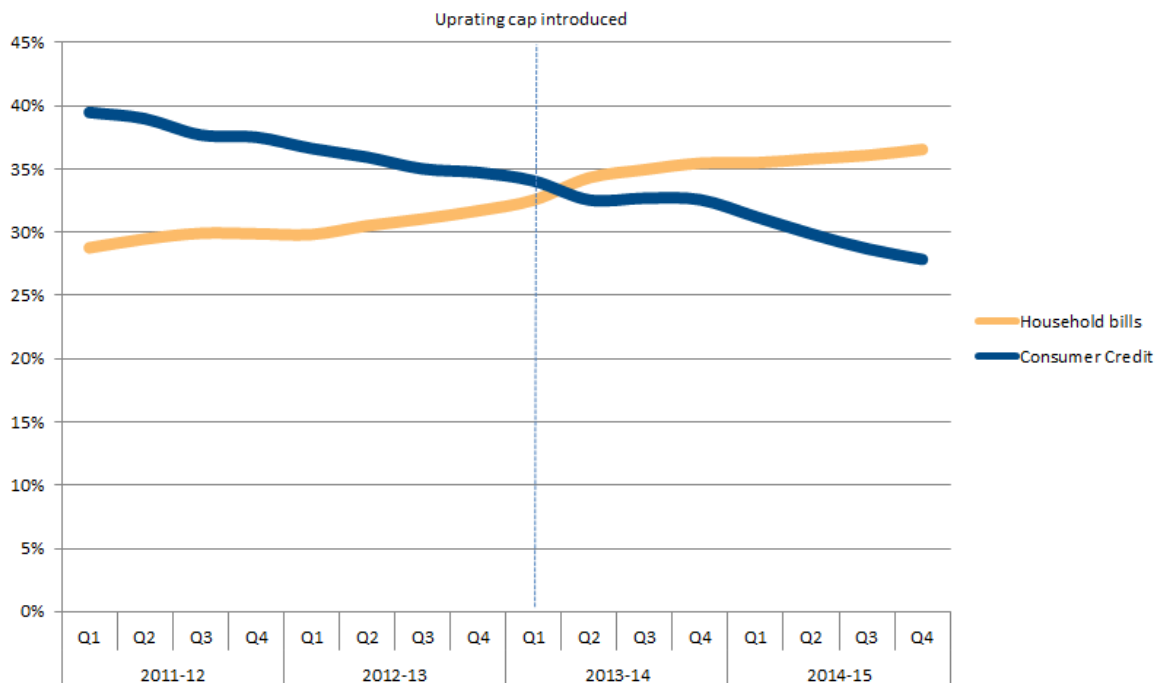
Impact on household finances and debt

The wide reach of the changes lead to risks of increased numbers of households struggling to meet the basic costs of living and falling into debt. This entails very significant costs, both for those affected and the Exchequer, and affects work incentives, health outcomes and family life.

Over the last four years, there has been a sharp increase in Citizens Advice clients seeking advice on debt. The composition of debt is also changing, with a shift away from consumer credit issues towards problems in meeting basic household bills. This reflects both reduced access to consumer credit, but also households dealing with smaller incomes, cutting consumer spending and struggling with essential costs, such as rent, water and fuel bills. The increase in council tax arrears has been especially marked.

⁴ R. Joyce (2014), *Benefit Cuts: Where might they come from?* London: Institute for Fiscal Studies. At <http://www.ifs.org.uk/publications/7762> (Accessed 30.06.15).

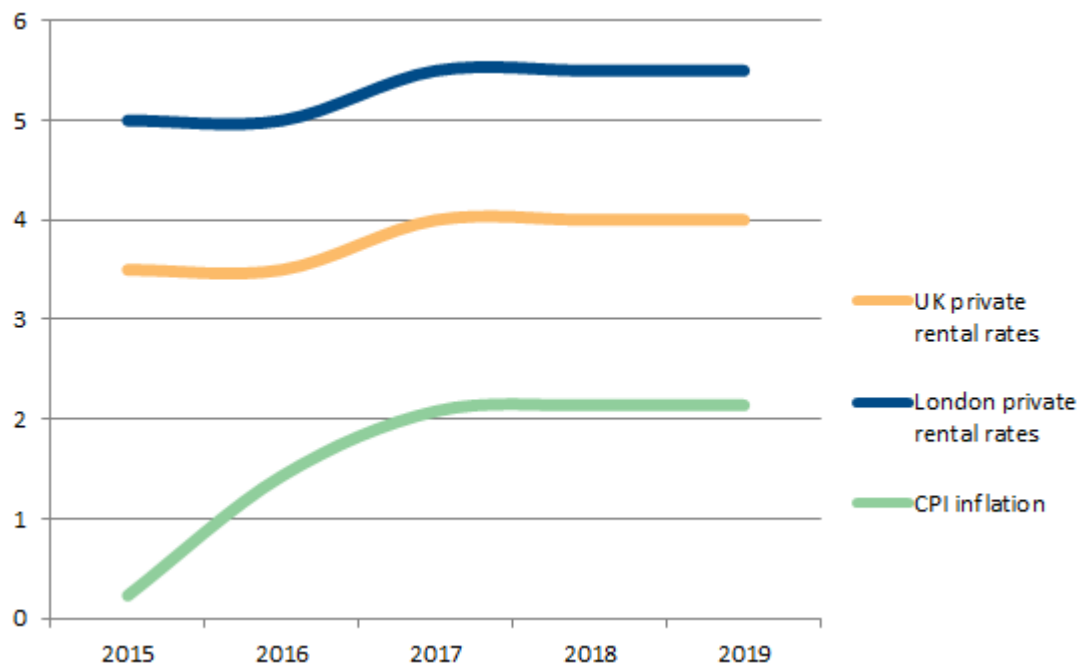
Proportion of Citizens Advice debt issues linked to consumer credit and household bills⁵



A freeze will increase these pressures and risks. What's more, forecasts for certain key items of household expenditure - particularly housing - suggest that simply looking at rates of inflation will mask the intensity of demands on household budgets in the future. For example, increases in rates of private rent are expected to be twice those of CPI inflation over the next four years.

⁵ Household bills include: Rent arrears (LAs or ALMOs, housing associations and private landlords), Mortgage & secured loan arrears, fuel debts, telephone and broadband debts, water supply and sewerage debts, council tax arrears. Consumer credit: Hire purchase arrears, Bank & building society overdrafts, Credit, store & charge card debts, Unsecured personal loan debts, Catalogue & mail order debts, payday loan debts, Logbook loan debts, debts to loan sharks/illegal lenders, guarantor loan debts, pawnbroker debts.

Projected increases (%) in rents, 2015-2019



Source: Savills; OBR

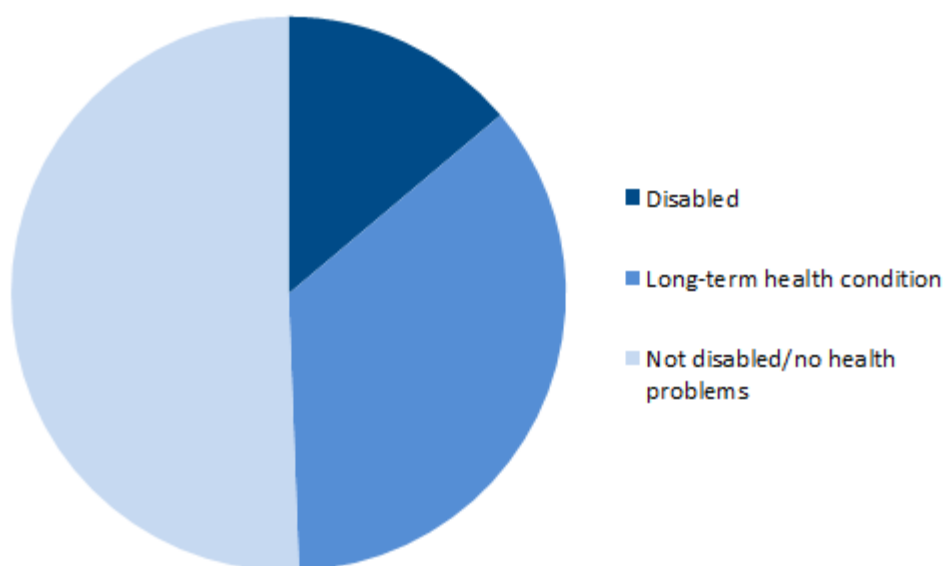
With Local Housing Allowance (the method for calculating Housing Benefit entitlements for low income private renters) also included in the freeze, meeting basic housing costs is likely to become ever more difficult for low-income families. For many of these households, rent accounts for the largest proportion of their expenditure and the risks of falling into arrears or facing eviction are severe.

Peter came to Llangefni Citizens Advice for help. He explained that he and his wife had recently seen their business fail and are now struggling to meet their everyday costs of living. His current rent is £500 pcm of which only £303 is covered by Local Housing Allowance. He has made efforts to find cheaper accommodation but worries that the costs of moving further away will be problematic for his business. However, after meeting their priority payments for utilities, the couple currently has no money to buy food.

Impact on those with health conditions or disabilities

Almost half of those coming to Citizens Advice with queries regarding benefits included in the freeze have a disability or long-term health condition. For those coping with poor health, support from the benefit system is essential.

Clients with issues related to benefits included in freeze, by health condition or disability



Mike approached Hayward's Heath Citizens Advice in financial difficulties. He lives with his 12 year-old son and is claiming ESA. However, he is struggling with various deductions from his income; he is paying back a Social Fund loan, arrears to Southern Water, and has been told he is now liable for Council Tax of £400 per year.

This problem has been recognised to some extent. The Government's commitment to ensure the most vulnerable people were not adversely affected

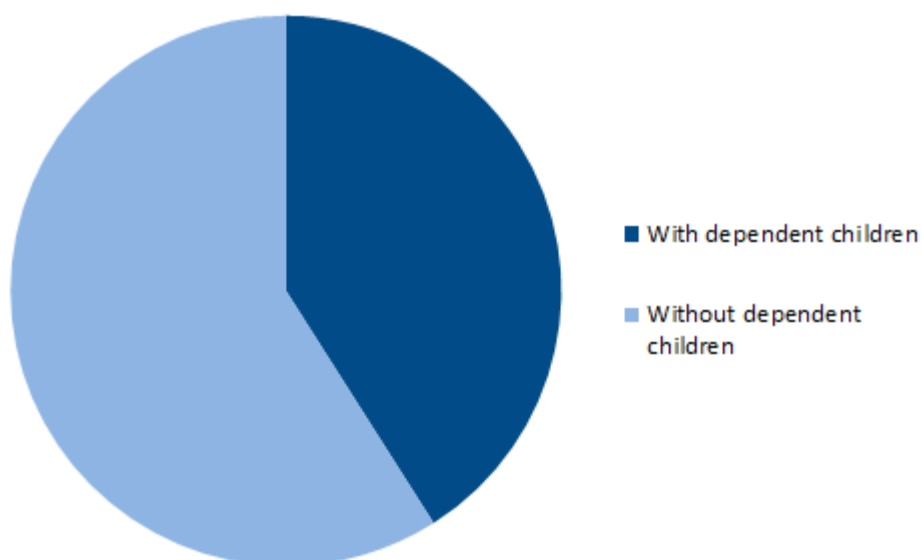
by the uprating changes led to the exemption of disability-related benefits from the reforms. This included PIP, DLA, Carer's Allowance, Attendance Allowance and those in the ESA support group.

However, all those receiving ESA will in fact be affected by the measure. This is because the majority of the benefit is formed by the 'basic rate' of ESA (currently £73.10 per week for those over 25), which is subject to the freeze. Those in the support group receive a top-up payment - the only part of their benefit which will be increased in line with inflation. This wider effect is significant, given all who receive the benefit have been assessed to have a disability or health condition that limits their ability to find and retain work. If those with work-limiting health conditions are classed as vulnerable, there is a failure to apply this principle consistently to those receiving ESA.

Impact on families with children

At Citizens Advice, 41% of clients we saw for issues related to working-age benefits included in the freeze had dependent children. Many such families are experiencing financial difficulties as living costs rise and this is often leading to stress, relationship difficulties and debt.

Clients with issues related to benefits included in freeze, by household type



Lorna came to Citizens Advice in Birmingham with mortgage arrears of £1200 and Council Tax arrears of £500. She is 36 years old and married, with three children aged 12, 8, and 19 weeks old. She lives with her husband in a mortgaged property. Her husband is a self-employed hairdresser working full-time. The family receives Child Benefit and Child Tax Credit. Her husband's business has been slow recently and the family are now in financial trouble - she mentioned rising fuel bills as a particular issue. This has been creating stress and affecting Lorna's relationship with her husband.

According to recent calculations, 7.7 million children have been affected by the below inflation rises to Child Benefit and Child Tax Credit under the last Government. Nearly two-thirds of the families affected had someone in work - families whose need for support from the welfare system was a result of low pay. One in five families supported by working-age benefits reported having cut back on food as their finances were squeezed - equivalent to one and a half million families with two and a half million children.⁶

Child poverty - particularly basic material deprivation - has well-documented impacts on attainment in school, health and wider prospects for adult life.⁷ A widening gap between families needing to rely on working-age benefits and those who do not will exacerbate the already significant gap in life chances between children in those households.

Equality considerations

While the freeze will apply across a wide spectrum of working-age benefits, there are two clear distributional impacts. The first is the potential for a growing gap between those working-age households who are in need of support from the

⁶ S. Royston (2015), *Short-Changed: The true cost of cuts to children's benefits* At: <http://endchildpoverty.org.uk/files/short-changed/Short-Changed-the-true-cost-of-cuts-to-childrens-benefits-FULL-REPORT.pdf> (Accessed 30.06.15)

⁷ D. Hirsch (2013), *An Estimate of the Cost of Child Poverty in 2013* At: [http://www.cpag.org.uk/sites/default/files/Cost%20of%20child%20poverty%20research%20update%20\(2013\).pdf](http://www.cpag.org.uk/sites/default/files/Cost%20of%20child%20poverty%20research%20update%20(2013).pdf) (Accessed 30.06.15).

welfare system and those who are not. As discussed, the original uprating reforms were designed to reflect the static wage growth of that period, bringing benefit-related income into line with wages. However, in May 2015 wage growth rose above 2%. With rising wages projected to continue, this means that the freeze on benefits is now likely to exacerbate income inequality between low-income or workless households and those on higher incomes. Of those who came to Citizens Advice about benefits included in the existing uprating cap, 74% had an income of less than £1000 per month - around the average salary for someone working full time on the minimum wage. The complete freeze of the coming two years will compound many of the existing pressures.

The second distributional implication is the decision that the burden of reducing welfare spending should be borne only by the working-age population. The state pension and pensioner benefits are not affected by the changes. Even more notable is the fact that the uprating system for the state pension has been adjusted to work in the opposite direction to the cap and freeze for working-age benefits. The 'triple lock', introduced by the Coalition Government in 2010, ensures that state pension rates increase each year by either the rate of inflation, average earnings or 2.5% - whichever is highest. Given the justification for changes at working-age was to ensure the burden was shared fairly and benefits remained in line with wages, the contrast between the principle applied to pensioners is stark. As the IFS has noted, "if the 'triple lock' for the state pension is retained in the long term, then the state pension will grow faster than prices and earnings, costing many billions of pounds a year. It will already be costing £4.6 billion a year in 2015-16 compared with earnings indexation".⁸

The combination of these two distributional choices means that, if overall welfare spending is to be reduced even while the rate of state pension is increased, then those on low incomes, managing a long term health condition or seeking employment will be required to absorb even greater cuts to their incomes. With real wages now rising, this means that this financially vulnerable group of households is likely to fall even further behind.

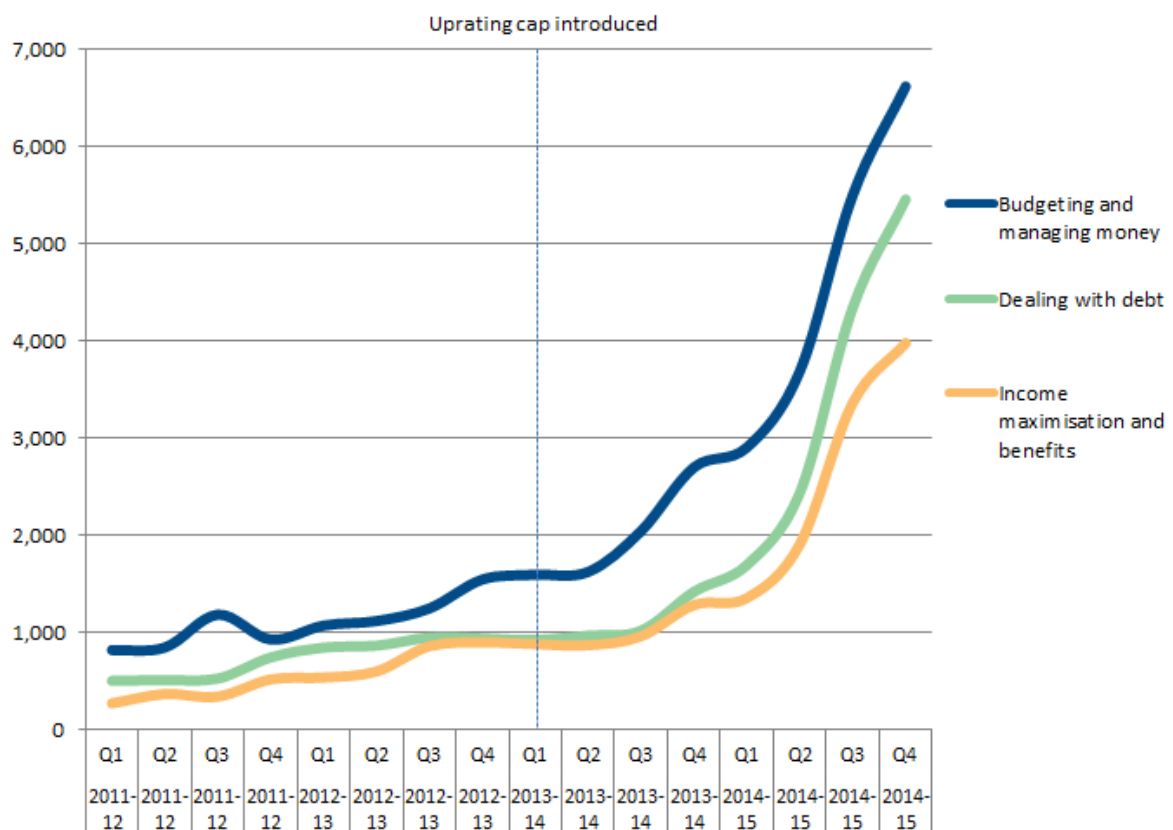
⁸ A. Hood and D. Phillips (2015), *Benefit Spending and Reforms: The Coalition Government's Record*, London: Institute for Fiscal Studies, p.2. At: <http://www.ifs.org.uk/uploads/publications/bns/BN160.pdf> (Accessed 30.06.15)

Impact on advice and support services

As discussed, while uprating changes rarely bring dramatic reductions in income, the fact that they are spread over millions of the lowest income households means advice and support needs are likely to be significant. For those on already tight household budgets, the changes may well require additional support around managing money. In worse cases, families may fall into debt.

At Citizens Advice, we have seen a notable increase in demand for advice in many of these areas since the uprating changes were introduced (although some of this may also be linked to delivery changes). Since the 1% cap took effect during the first quarter of 2013, this has been especially marked. Between Q4 2011-12 and Q4 2014-15, we saw over a 600% increase in clients with budgeting problems, those dealing with debt and those seeking advice on income maximisation and benefits.

Trends in demands for advice related to financial capability at Citizens Advice



These trends only reflect the uprating changes applied in the last four years. A total freeze over the next two years is likely to compound the problems we have already seen. A recent survey of 200 advisers at Citizens Advice found that two-thirds believed their clients were in a worse position to cope with the impacts of a freeze, in comparison to circumstances in 2012.⁹ If sufficient support is available in advance of reforms, this should be focused on budgeting advice and ensuring all families are aware of support to which they are entitled. If advance preparation is not offered, we can expect more households requiring debt-related services.

If the Government seeks to achieve its aims of cost savings, protection of the vulnerable and fairness, it is vital that full consideration is given to meeting these advice and support needs, particularly around budgeting help, clear information on entitlements to help and steps to take if problems occur. This needs to be available up-front; once people fall into debt, addressing the problem becomes harder and the costs associated with doing so much greater.

What are the main risks and assumptions?

With recent NAO research indicating that under the last parliament welfare reform “relied too heavily on uncertain and insufficiently challenged assumptions”¹⁰, it is imperative that the consequences of a reform such as the uprating freeze, affecting millions of low-income households already under pressure from three years of squeezed incomes, are given close attention. As set out these risks fall into two broad categories.

The first is that the changes - despite caveats made around certain disability benefits - provide insufficient protection for vulnerable groups. These include children and those with a work-limiting health condition. The Government has already acknowledged the huge costs to society posed by child poverty,

⁹ Citizens Advice Network Panel Survey, June 2015.

¹⁰ National Audit Office (2015), *Welfare reform - Lessons learned*, London: NAO, p.6. At: <http://www.nao.org.uk/wp-content/uploads/2015/05/10724-001Welfare-reform-Book.pdf> (Accessed 30.06.15)

particularly its long-term impacts on health, educational attainment and employment prospects. Those who have been assessed as having a work-limiting health condition will also be vulnerable, in that they have fewer options to increase their incomes. There are therefore current debates around exempting children's benefits and ESA from the changes.

The second is a broader risk that, after three years of below inflation uprating, a freeze will leave already financially-pressed households unable to keep up with the cost of living. At Citizens Advice, we have already seen a shift as clients cut back on consumer spending and begin to struggle with more basic essentials, such as household bills.

When people fall into debt their support needs - and the costs to the Exchequer - are greatly increased. Recent calculations suggest problem debt costs the UK £8.3bn through the damage it causes to mental and physical health, family life, productivity and employment prospects and costs to the welfare state, NHS, local government and other agencies.¹¹ Many become trapped in a cycle of debt from which it is difficult to escape. This has serious consequences for their ability to progress - into work, in employment or through education - and to reach a point at which they no longer require support from the welfare system. If sufficient advice and basic budgetary support are not available as these changes take effect, then such costs may well outweigh the headline savings.

Conclusions

The Government's changes to benefits uprating during the last parliament were associated with significant headline savings. The decision to continue with this policy has been set out in terms of balancing spending reduction with fairness and protections for the vulnerable. However, there are a number of reasons to be concerned that these aims will not be met.

There are obviously risks that the failure to exempt children or those with a work-limiting health condition will adversely affect these vulnerable groups. More widely, though, the families affected by these reforms are financially

¹¹ Step Change (2014), *The Social Cost of Problem Debt*. At: <http://www.stepchange.org/Mediacentre/Researchandreports/Socialcostofdebt.aspx> (Accessed 30.06.15)

vulnerable, predominantly on the lowest household incomes. The freeze proposed will compound the challenges of three years of below inflation uprating, which has already left many struggling to meet the costs of basic household bills and falling into debt. The decision to exempt pensioner benefits and increase state pension rates will leave this group of households to absorb ever greater reductions if overall welfare spending is to come down. It will also see them falling further behind other working-age households as wages begin to increase above inflation.

Such risks and the costs they entail suggest the best means of reducing welfare spending in a fair and sustainable way will be to address many of the structural problems faced by those on low incomes. Access to affordable housing, sustainable and reasonably paid work, and advice and support on finance and budgeting are likely to have far greater impact than simply reducing incomes. They also avoid the real costs associated with cycles of poverty and debt.

www.citizensadvice.org.uk

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