

*Response to questions taken
on notice by ACOSS, received
14 September 2012.*

Response to questions on notice from Senate Education Employment and Workplace Relations Committee

Australian Council of Social Service, 14 September 2012

Senator Siewert has identified further questions that she would like to place on notice:

1. You comment that the NSA income test discourages part time and casual employment, can you explain this further?

Our main priority is to increase the maximum rate of payment for singles on Allowances. There are tensions between this goal and the liberalisation of income tests, notably the higher cost of increasing payments if they extend further up the income distribution and the possibility that part of the Allowance payment will become a general subsidy for minimum wages.

We advocate, in the short term, an increase in the allowance income test 'free area' offset in part by an increase in the taper rate from 50% to 60%. This is a simplification measure. A higher free area means that fewer people have their payments adjusted due to small earnings and a single taper rate is easier to understand. This would not increase the income level at which the payment cuts out, so that even with a \$50 increase in the single maximum rate, NSA would still not extend to minimum wage earners generally.

Keeping these policy trade-offs in mind, there is also a case for a more liberal income test to encourage those who are only required to seek part time employment to do so. This includes both single and partnered recipients of unemployment allowances, and people with partial work capacity. It is not reasonable to require these groups to seek part time employment and impose an income test that doesn't make it financially worthwhile for them to work part time. This was a major criticism of the 2006 Welfare to Work policy among recipients of income support payments. On these grounds, the Henry Report recommended a more liberal income test for these groups. This is now proposed by the Government for some parents on Allowance payments, but not for partnered parents or people with partial work capacity.

Of equal (or perhaps greater) importance for income support recipients seeking part time employment are the ancillary costs of employment, especially child care, the increase in rebated social housing rent payments, and the potential loss of concessions. It is noteworthy that some jurisdictions (including Queensland) still do not extend public transport concessions to allowance recipients despite their greater need for a subsidy due to job search requirements.

In our view there is a stronger case for changing the income test treatment of casual earnings. In the present labour market, casual employment is often the only option available to unemployed people with limited skills. There are three problems with the current income test for casual workers.

First, there is very little scope to 'average' earnings for income test purposes over periods longer than a fortnight. The 'working credit' which is supposed to alleviate this problem, only allows about week's employment at the minimum wage every 6 months, and it is so complex that few understand

it. We propose that people should be able to 'bank' their income test free area for up to 26 weeks, so that they could earn up a fortnight's minimum wages every 6 months without reduction in their payments.

Second, earnings must be declared as they accrue and before tax, but people are usually paid in arrears and in after tax dollars. This is probably the main cause of over and under-payments of income support for unemployed people. While there is logic to both these policies, practical solutions must be found to this problem. The United Kingdom, for example, is experimenting with automated reporting of earnings through the tax system to the social security administration. In Australia this is already done with Child Support payments so it should be technically feasible. There would be significant capital costs, but the ongoing administrative savings and greater peace of mind for clients would likely outweigh those costs.

Third, few people understand how the income test works, especially for casual earnings. People usually over-estimate the effect of income tests, which of course discourages employment. One option, also implemented in the United Kingdom, is the administration of a 'better off in work calculation' by job centre staff (their equivalent of Centrelink). This demonstrates to people considering casual employment how much better off they would be financially.

More detail is provided at pages 48 to 52 of our submission

- 2. You note that JSAs are underfunded to assist people who are long-term unemployed. What do you think JSA's would need to properly assist the long-term unemployed?**
- 3. You talk about JSA's working with a "growing proportion of people receiving income support who are long-term unemployed" Do you think stream-4 provides adequate support? What else do these people need to overcome barriers?**

Once people are unemployed for 12 months they enter the so-called 'Work Experience Phase' of JSA assistance. The main difference between this and assistance received in the first year of employment is not work experience. Rather, it is the reduction in the level of payments for providers to interview people regularly and invest in work experience and training. Most 'work experience phase' participants come from either Stream 3 or 4 since long term unemployment is associated with labour market disadvantage. For these clients, both service payments (for interviews) and Employment Pathway Fund credits (for investment) are lower during the Work Experience phase. Essentially, providers are funded to interview people every two months together with \$500 in the EPF. Importantly, this \$500 is not an annual amount, it is supposed to 'last' for the remaining duration of the person's unemployment spell, with the exception of an additional \$1,000 for the third year of unemployment (as discussed below).

The table below is a simplified version of the JSA fee structure. Since most work experience participants are Stream 3 clients, the fourth column in italics is of greatest relevance.

Job Services Australia fee structure 2012-13 (simplified)

	Stream 1 (least disadvantaged)	Stream 2	Stream 3	Stream 4 (most disadvantaged)
Initial phase of JSA assistance (first 12 months of unemployment)				
Typical service fees	\$781	\$885	<i>\$1,120</i>	\$1,919
Employment Pathway Fund credits	\$11	\$550	<i>\$1,100</i>	\$1,100
Typical outcome fees	\$440	\$440-\$2,456	<i>\$440-\$3,940</i>	\$440-\$3,940
'Work experience phase' after 12 months of unemployment				
Typical service fees	\$722 for first year of work experience, \$398 p.a. thereafter	\$722 for first year of work experience, \$398 p.a. thereafter	<i>\$722 for first year of work experience, \$398 p.a. thereafter</i>	\$722 for first year of work experience, \$398 p.a. thereafter
Employment Pathway Fund credits	\$500 in first year of work experience \$1,000 in second year	\$500 in first year of work experience \$1,000 in second year	<i>\$500 in first year of work experience \$1,000 in second year</i>	\$500 in first year of work experience \$1,000 in second year
Typical outcome fees	\$550-\$2,258	\$550-\$3,350	<i>\$550-\$5,550</i>	\$550-\$5,550

Source: DEEWR 2008, Request for tender for employment services 2009-12, updated after 2011-12 Budget.

In the 2011 Budget, the Government raised the EPF credits for people in their third year of unemployment ('very long term unemployed' people) and introduced a modest wage subsidy scheme (approx. 10,000 places a year). However, at the same time a new requirement was announced for 'very long term' people to participate in 11 months of activity during that year instead of the previous 6 months. This means that the average level of EPF 'funding' for work experience or training is still less than \$100 per month, which is clearly inadequate to purchase quality training or work experience.

Providers can 'redistribute' their EPF credits among jobseekers in order to invest more heavily where they believe it would make a greater difference to employment outcomes. However, the recently released EPF evaluation report indicates that providers are more likely to 'shift' EPF credits in favour of less disadvantaged Stream 2 clients rather than towards more disadvantaged clients. This suggests that the incentive structure is not working as it should, since it is well established that investment in work experience and training can make a substantial difference to employment

outcomes for long term and disadvantaged jobseekers and the system is supposed to encourage investment in those clients.

Although outcome payments increase with longer unemployment durations, they do not rise substantially until a person has been in the system for 5 years. Further, 'full' outcome payments are only paid in respect of a minority of long term unemployed clients (perhaps a quarter in any given year). It would be helpful to obtain a breakdown of the proportions of Work Experience phase clients in respect of whom various outcome payments are made as this is not available in the Labour Market Assistance Outcomes publication and there is no sound reason for withholding this information. Indeed, there is a clear public interest in it since the Government is spending money on JSA services to achieve employment outcomes.

We advocate increasing the level of service fees and EPF credits for all Work Experience Phase participants to the *annual* levels that apply to Stream 3 jobseekers in their first year of unemployment (typically around \$1,100 in each case, as indicated in the table). The cost is difficult to model in the absence of detailed data on the number and profile of Work Experience Phase participants, but we expect this would cost an average of between \$200 million and \$300 million per year over each of the next two years.

People with deep disadvantage in the labour market are not restricted to 'Stream 4' clients. We believe many Stream 3 clients face similar disadvantages. Proposals to detach Stream 4 from rest of the JSA system could be counterproductive in the sense that those disadvantaged people in Stream 3 might miss out on improved supports. The main problems with the support available for Stream 3 and 4 clients include the drop in support for both once they enter the Work Experience phase, and the purchasing model's lack of incentives and resources for providers to work closely with other services such as mental health, housing, family support or drug and alcohol services. The necessary collaboration on the ground between these services and JSA providers will not be achieved simply by directing providers to do so as a condition of funding. One barrier to collaboration which should not be underestimated is the division between Commonwealth and State/Territory responsibilities to assist people to overcome employment and other disadvantage.

The new wage subsidy scheme is very welcome since it gives people the opportunity of 6 months paid work experience in a regular job, which is widely recognised as an effective way to increase the employment prospects of long term unemployed people. For example, the EPF evaluation report indicates that wage subsidies are a relatively effective way to invest EPF funds.

In many cases (with previous wage subsidy schemes) the unemployed person is retained by the same employer. The employer uses the wage subsidy (which is typically equal to about half the minimum wage) to support what is in effect a 'work trial' and if the person performs satisfactorily they keep them on. Of course, wage subsidy schemes must be carefully targeted (to avoid 'deadweight costs') and well administered (to prevent 'gaming' by employers or providers). We advocate a doubling of the number of places in this scheme to 20,000 per year, which would cost around \$30 million per year.

Such wage subsidies do not work for all long term unemployed people. We have also advocated the introduction of a 100% wage subsidy for 6 to 12 months to give a minority of more deeply disadvantaged long term unemployed people direct experience of paid employment in a regular job. This could be provided in community organisations or social enterprises. Indeed, it is difficult for social enterprises to become self-financing while continuing to target the most disadvantaged (and presumably less productive) unemployed workers, without some form of ongoing wage subsidy. Such a scheme assisting 20,000 jobseekers might cost between \$200 and \$300 million per year, depending on the average duration of placements, 'drop out' rates, and the level of training wage that is paid.

Improving employment services is about much more than increasing the resources available to providers. It is vital to ensure that the funds are used effectively to offer the right help at the right time to people disadvantaged in the labour market. That requires better engagement with the people who use employment services: unemployed people and employers, and better incentives for providers to achieve lasting employment outcomes. More details are provided in our 'APESAA submission', a copy of which was forwarded to the Committee.

- 4. Can you go into a bit of detail about the reform underway in the UK. Do you think that is a good model to follow? Has enough been implemented to comment on its ability to: a) get long-term unemployed people into the workforce, b) support people who work intermittently c) provide enough to ensure an adequate standard of living for unemployed people.**

There are two major changes underway in the UK.

The first is the replacement of income support payments for people of working age with a single payment called 'universal credit'. This replaces basic income support payments for unemployed people, people with disability and sole parents. Various supplementary payments such as disability living allowances and housing benefits remain, though these are being cut back in some cases which has led to criticism.

An outline of the changes prepared by one of our equivalents in the UK, Child Poverty Action Group, is attached.

Our submission includes a figure describing the Universal Credit and payments it replaces, at page 70.

ACOSS does not have a view on the detail of the UK benefit reforms, which include changes to disability pensions initiated under the previous Government. However, we believe the new *payment structure* should be considered as an option for reform in Australia. The Universal Credit has many features in common with Australian income support payments: it has a flat maximum rate for all single people, higher payments for couples, and an income test with a similar taper rate. The key difference is that instead of dividing people into 'pension' and 'allowance' categories the Universal Credit is set at the same maximum rates for all.

We understand this reform had a number of objectives including to simplify the system, reduce administrative costs, remove the financial disincentives that result from differential payment rates, and to encourage part time employment for less than 16 hours a week (which was discouraged under the previous 'Working Credit' system), as a stepping stone to fulltime employment. We understand that distributional analysis of the impact of the Universal Credit indicates that it would increase the disposable incomes of some of the poorest households and reduce those of some households employed for just over 16 hours a week (who received the highest tax credits under the previous regime). Of course, the impact of a similar reform in Australia is likely to be different given our different starting points.

The Universal Credit is likely to improve support for unemployed people who work intermittently, if only because they only have to deal with a single Department instead of having to apply separately to Job Centres for social security and the Revenue Service for working credits. Arrangements are being made for the tax system to share earnings information with the social security system in real time. If this works it would reduce the need for unemployed people to regularly report their earnings to the social security system, and also reduce errors. We have not had the opportunity to assess these proposals in any detail.

Levels of income support payments for unemployed people in the UK are low by OECD standards (as are the equivalent Australian payments) but the UK Housing Benefit is very generous, paying most of people's rent if they are living on a low income. We understand that base rates of income support are being increased for some people and that housing benefits are being reduced in some cases, but have not assessed the overall impact on the incomes of households at risk of poverty in any detail. Our main interest in the Universal Credit is the structural reform. This is relevant to Australia because the UK has a similar income support system.

The second major reform is the 'Work Program' which replaces previous employment programs for long-term unemployed people. They will be referred to non-Government services providers who will be paid mainly according to outcomes achieved, and in many ways the new system is similar to Job Services Australia (JSA). Potential advantages of the Work Program compared with JSA include less detailed administrative monitoring and 'red tape' for services and official acknowledgement for budget purposes that more investment in employment services can save the Government money in future years. Potential disadvantages include the semi-monopoly status of 'prime' providers contracted to provide services in each region, incentives in the purchasing model to 'park' more disadvantaged unemployed people, a lack of oversight of the services provided on the ground (the so-called 'black box' approach) which reduces accountability, limited resources to invest in people who are more disadvantaged, and the fact that investment risk has not in reality been transferred from Government to providers (since large providers cannot be allowed to fail). It is too early to say whether the new services will be more responsive than the public job centres were to the needs of unemployed people and employers. We understand providers are struggling to achieve employment outcomes and remain financially viable in the tough labour market conditions that prevail in the UK, and expect that the model will be adjusted over time (to ensure provider viability and improve public accountability) as the Job Network was after it was introduced in the late 1990s in Australia.

5. Can you elaborate on the relationship between NSA and DSP? How does the current set-up of the system discourage people on DSP to engage in the workforce?

NSA is \$133 per week less than the DSP for single people. Yet this is more than a simple matter of people moving to higher payments in a mechanical response to financial incentives.

People with disability are vulnerable in the labour market. They are more likely to need income support to top up low earnings and as a safety net in case they lose a job. DSP offers greater income security as well as a higher income, but it is difficult to claim and is becoming more so.

Therefore, people with disability who already receive DSP are often fearful of trying their hand in the labour market in case they end up on NSA. Fear is often a stronger driver of behaviour than positive incentives and people who are fearful will often disadvantage themselves financially in order to 'buy' a little more security. A good example of this is the age pensioners who keep their incomes below the level at which they retain the maximum rate of pension or concessions, despite the financial disadvantage of doing so. Despite policies designed to ease these concerns, such as the two year period of grace in which a person can be employed and off DSP without triggering a job capacity review, and the separation of DSP and employment service assessments, this fear remains widespread.

On the other hand, the 100,000 or more people with disability already on NSA are likely to rely on that payment for longer periods of time, and find it impossible to live decently. This, together with the deterioration in people's health that often accompanies poverty and unemployment, leads to claims for DSP.

A further problem with the present division between NSA and DSP payments is that, despite recent changes in work capacity assessments intended to focus more on people's work capacity, people are still required to 'prove they can't work' to receive a higher pension payment.

A social security system with the same base rate of payment for people who are closer or further removed from the labour market would overcome these problems. Disability assessments would still be needed, but for the purposes of assessing what activity requirements and employment supports should apply (if any) and to assess whether they are likely to face higher costs due to their disability – not to assess whether they 'deserve a higher payment' because they 'can't work'. This would lead to a significant change in the 'culture' of the social security system, one that would strengthen employment participation. People would no longer be penalised financially as they set out on the path to paid employment and financial independence.

As indicated in page 68 of our submission, a 'costs of disability supplement' could be designed so that people retain that payment if they move into fulltime employment. This would be justified on the grounds that people with disability also face extra costs when they are employed. It would also strengthen work incentives, in much the same way that the extension of the maximum rate of Family Tax Benefit Part A to families in low paid full time employment does for working families.

When a person with disability moves from income support to fulltime employment they would retain the supplement, and they would no longer face the risk of dropping down to a lower payment if they lose the job. The proposed payment structure would reduce fear and increase positive incentives at the same time.

Over the last decade, employment participation policies have focussed on moving people from one category of payment to another to resolve the so called 'DSP problem' instead of focussing on how to improve transitions to employment for people with disability regardless of the payment they receive. The results are not encouraging. Few people with disabilities on income support have progressed into fulltime employment. The number of people with 'partial work capacity' on NSA or Youth Allowance has grown and now exceeds 100,000. The policy intention, to improve engagement with the labour market, is a good one that is supported by ACOSS and disability advocates. But that intention has become lost in the labyrinth of a dysfunctional payment structure.

We do not underestimate the difficulty in improving labour market outcomes for people with disability. Every OECD country is struggling with this. However improvements will only be achieved if policy is clearly focussed on the main barriers and opportunities. These include intensive work with employers to redesign jobs and make workplaces more accommodating for people with disabilities as well as skilling people for the jobs available, and helping people retain the jobs they have rather than waiting until they are unemployed before offering assistance. Benefit reform that encourages and eases transitions to employment has an important role to play, but it is likely to be a secondary role. If as much policy energy was devoted to improving employment assistance for people with disability as to reducing the number of people on the DSP payment, we would begin to make progress.

- 6. You say that people are "churning on a long-term basis between income support and casual employment" can you explain more about this? Why isn't the allowance system, or the JSA system supporting people into more secure employment? Are the jobs just not there?**
- 7. Do you think that the low rate of NSA is actually a barrier to finding employment? In your submission you talk about the costs of a job search. Can you provide the committee more information on that?**

We do not have much up to date data on the extent to which 'churning' occurs, either between benefits and employment or between different income support payments. Although much research was conducted into this problem in the mid 2000s, few independent researchers have since had access to the administrative data needed to properly assess the scope of this problem or which groups are affected. The Departments' submission indicates that around 15% of NSA recipients in 2007 left NSA and were back on that payment five years later. It is likely that if a shorter period of comparison was used, the proportion of people 'churning' in this way would be higher.

We do not have the resources to review the research in this area, so others would have a clearer view. Broadly speaking, we understand that most people who undertake part time or casual employment and remain in the paid labour force subsequently move (within a period of three to five

years) into more secure or fulltime jobs. However, a large minority either remains in casual or part time employment, or falls into unemployment. Also, those who have *previously* been unemployed and received income support are more likely fall back into unemployment after securing part time or casual jobs. This suggests that a period of unemployment has a scarring effect on future job prospects, and/or that many unemployed people have enduring labour market barriers (for example low skills or caring roles) that persist even though they find part time or casual employment.

We understand that those people on income support who are most likely to 'churn' on and off payments include sole parents with limited qualifications and young unemployed people. This reflects the elevated risk that women and young people with limited qualifications face of becoming stuck in the secondary labour market (less secure, low paid jobs).

Other people on income support who are more likely to miss out on job opportunities altogether (and are therefore less likely to 'churn') include people with disability and mature age unemployed people.

Those income support recipients who are the most likely to progress into fulltime ongoing employment include young and middle age unemployed people with post-school qualifications and recent fulltime employment experience.

Labour market conditions and low skills, rather than the social security system, are likely to be the main causes of involuntary 'churning' between benefits and casual jobs. The social security system could in theory contribute to the problem. This is most likely to occur where income support payments encourage part time employment but discourage subsequent transitions to fulltime jobs. If income tests were eased dramatically it is possible that the income support system would operate in this way.

However, the allowance income test currently discourages part time employment due to the low free area and 60% taper rate. As the Henry Report argued, this is not an appropriate income test for those people whom Governments expect to seek part time employment, including parents with school age children (single or partnered) and people with disability.

The main problem in this area which we identify in our submission is that those whom the labour market denies secure employment have a very tough time dealing with the social security system. These problems were discussed above.

8. Do you think that the low level of youth allowance payments acts as a barrier to study? We've heard that there is a disincentive for young people to engage in paid work experience, is this a problem?

In pages 38-41 of our submission we discuss student payments. The Bradley Report, which examined these issues in depth, found evidence that many post-secondary students faced financial hardship and that many others had working hours that interfered with their studies.

Paid work experience programs such as wage subsidies are effective in improving the employment prospects of long-term unemployed people, because they re-connect them with regular employment. One of the beneficial features of these programs from that point of view is that unemployed people are treated as regular employees and paid regular wages, rather than working on 'projects' for their unemployment payments.

Payment of normal or training wages also helps reduce poverty in the short term. We are not aware of disincentives for young or older unemployed people to participate in such programs. Provided they offer proper wages and work conditions and last for a reasonable time (at least 3 to 6 months), most would leap at the chance of boosting their incomes and job prospects in this way. The main problem is the shortage of places available.

9. Thank you for providing such a detailed and expansive review of the different ways of measuring disadvantage and poverty. Can you explain what these indicators mean in human terms? What are the physical and psychological impacts of allowance recipients? Does this impact their ability to look for work?

Between a third and one half of people receiving unemployment or sole parent payments suffer from anxiety or depression¹. It is well established that unemployment of itself erodes confidence and self-esteem as well as skills. Living in poverty, the stigma attached to unemployment payments, frequent knock-backs from employers, and the way in which the social security system treats unemployed people only add to these problems.

In addition, as indicated in our submission many people on these payments have disabilities or poor physical health. Many sole parents have experienced domestic violence (either from partners or from family members when they were children), which can permanently undermine self esteem and lead to sustained bouts of depression.

It is clear that these factors reduce people's capacity to search effectively for jobs and present themselves well to employers. As our submission argues, the profile of recipients of Newstart Allowance is now more disadvantaged than in the past. Our member agencies providing employment services indicate to us that factors such as disability, poor physical and mental health, and low self esteem have a greater impact on employability than the financial work incentives that attract greater attention in public policy debate. In our experience these problems are understood by the relevant policy Departments.

The quotes throughout our submission from the excellent book, 'Half a Citizen' which come directly from a series of interviews with people on income support payments, and the submissions to this Inquiry from benefit recipients, tell these stories more clearly than we can in submissions.

¹ Mental Health Problems, Disability and Income Support Receipt: A Replication and Extension Using the HILDA Survey Peter Butterworth, Australian Journal of Labour Economics ,No. 2, June 2004, pp 151 – 174.

- 10. I noted in your submission that you say "there is no consistent relationship internationally between low benefit rates and low unemployment" and that "evidence suggests that other factors mitigate against any unemployment-increasing effect on high benefit payments." Can you elaborate on this? Do you think the commonly held belief that low rates are an incentive to work is invalid? Can you outline the international evidence for this?**

The issue of incentives for fulltime employment is discussed at pages 44 to 48 of our submission. Two of the mitigating factors are activity requirements and investment in labour market programs. As the Andersen & Svarer article regarding unemployment in Denmark (at page 47 of the submission) indicates, both are important reasons for the low rate of unemployment in that country, despite unemployment insurance benefits of 90% of previous wages and safety net benefits of 60-80% of the unemployment insurance benefits (this does not include housing and other supplementary payments). The importance of activity requirements and supports has long been acknowledged by labour market economists (see page 47 of our submission).

In its 2006 Employment Outlook, the OECD presented the results of research that examined the impact of different labour market institutions (including rates of unemployment payments) on unemployment rates. One of its conclusions was as follows:

‘In the previous chapters it has been observed that careful integration of active and passive measures, combined with close monitoring of job search, can be effective in dampening disincentives effects brought about by generous unemployment benefits. This is confirmed by empirical analysis, which shows that the adverse impact of unemployment benefits is lower in countries that spend more on ALMPs. A rise in spending on ALMPs of the size corresponding to the “historically typical” reform, reduces the adverse impact of unemployment benefits by about 20%. In fact, in countries with a strong emphasis on activation policies, like Denmark and the Netherlands, unemployment benefits have a statistically insignificant effect on unemployment, (p217)’

Australian unemployment benefits are among the least generous in the OECD and our spending on labour market programs is among the lowest in the OECD.

The disadvantaged profile of NSA recipients (as indicated above and in our submission) also strongly suggests that the main barrier to employment for many is not financial incentives but a combination of limited employment capacity and limited employer demand for people with characteristics such as disability, mature age, or lack of recent work experience. This observation is often made to us by employment service providers.

- 11. You say "payment rates are based on people's distance from employment (and assumptions about 'deservingness') rather than their living costs. " Can you explain this more? What are the impacts of this?**
- 12. Your submission makes the point that the pension-allowance system makes life difficult for people as their circumstances change and they have to move from one payment to**

another. Can you tell us more about this? What are some examples? How can the allowance system change to make this easier?

- 13. You say that "income support payments should be set on the basis of financial need rather than employability. Employability is still important in determining which activity requirements and employment supports should apply, but should not determine levels of payment." What would this look like? How would the allowance system need to change? Would this help cope with changing labour market?**

These questions relate to our proposals to simplify the social security payment structure for people of working age, which are discussed at pages 61-69 of our submission.

The distinction between pensions and allowances for people of working age is based on the historical view that some people lack employment 'capacity' and are therefore more 'deserving' of income support than others who have employment capacity. A further assumption is that those lacking employment 'capacity' will need to rely on income support for much longer and therefore face greater hardship.

Those distinctions are neither objective nor immutable. It was always difficult to draw the line between eligibility for pensions and allowances. Employment participation policies and labour market change have blurred this historical distinction. Many people who were previously assumed to lack employment capacity (including women caring for children and many people with disability) are now encouraged or required to seek employment.

As long as the pension:allowance divide remains in place for 'working age' payments, employment participation policies will shift an increasing number of people from the pension category to the allowance one. One outcome of this is that many people experience sharp reductions in their level of payment despite the fact that their circumstances and income needs are not much different to those who retain pension status. The pension:allowance divide is in this sense a barrier to equitable employment participation policies.

At an individual level, the pension:allowance divide imposes severe financial penalties on people who are deemed to have to move closer to employment. Examples include:

- A \$59 per week reduction in payments for sole parents once their youngest child reaches their 8th birthday;
- A \$190 per week reduction in payments for Carers (after a brief period of grace) if the person they are caring for dies or transfers into nursing home care;
- A \$133 per week reduction in payments (compared with what they would have received on the DSP) for people with disability who secure a fulltime job for two years and subsequently lose that job.

None of these payment reductions reflect in a consistent way changes in the cost of living of those affected. Their living costs remain much the same but their income support is sharply reduced. A

carer who is no longer eligible for Carer Payment because their partner recently passed away is no less 'deserving' of decent income support to meet basic costs of living than they were while still classified as a 'carer' rather than 'unemployed'.

A fairer, simpler social security system would have the same set of base payment rates (for singles and couples respectively) for all people of working age, but different participation requirements. If the pension:allowance distinction were removed, this would make the transitions described above more seamless for people. Activity requirements (where appropriate) could be adjusted to better reflect individual circumstances, though categories such as 'disability' 'carer' and 'parenting' would still be needed to determine fairly and transparently the range of activity requirements that might apply to different people. Administrative effort would no longer be devoted to assessing people's employability to determine whether they should receive higher or lower payments. The system could be much simpler.

The proposed system is illustrated graphically on page 67 of the submission. We have not set out to detail the levels of payment that would apply (for example, all payments would not necessarily rise to current pension levels), or the income tests and activity requirements attached to future income support payments. These questions should be subject to detailed consultation as we propose in pages 58-60 of the submission.

Levels of payment should reflect basic financial needs rather than how 'close' or 'far' a person is from employment. This would include supplements to assist with rent, disability costs and the cost of caring.

For many people, little would change apart from higher 'base rate' payments for those currently on the lowest payment levels. But for the large number of people who occupy the policy 'grey areas' near the pension:allowance divide, and those undergoing transitions such the those described above, the system would be much simpler and fairer.

Universal credit

Updated July 2012

Universal credit is a new benefit that will be introduced from October 2013, replacing current means-tested benefits and tax credits for working-age people.

The basic provisions to implement universal credit are set out in the Welfare Reform Act 2012, which was passed on 8 March, and more detail has been provided in draft regulations issued in June 2012.

When will it be introduced?

October 2013 to April 2014	<p>New claims for universal credit, to be introduced over this period, possibly on a gradual basis by area.</p> <p>No new income-based jobseeker's allowance, income-related employment and support allowance, income support or housing benefit claims are accepted once universal credit has been introduced in an area.</p> <p>People moving from out-of-work benefits into work transfer onto universal credit.</p>
April 2014	No new claims for tax credits (except for people over pension credit qualifying age)
April 2014 to October 2017	Existing claimants transfer to universal credit.

Which benefits will go?

The following benefits will be abolished and replaced by universal credit:

- income support;
- income-based jobseeker's allowance;
- income-related employment and support allowance;
- housing benefit;
- child tax credit and working tax credit;
- budgeting loans and crisis loan alignment payments – to be replaced by payments on account (an advance of universal credit) in cases of need.

Council tax benefit, crisis loans for other needs and community care grants are also being abolished – responsibility for an equivalent will be passed to local authorities or devolved governments.

Disability living allowance for adults of working age is being abolished and replaced by personal independence payment (PIP) – see separate factsheet.

Which benefits will stay?

Benefits other than those listed above will remain. In particular, people will still be able to claim:

- contribution-based jobseeker's allowance. The earnings rules will be aligned with universal credit;
- contributory employment and support allowance. The earnings rules will be aligned with universal credit;
- child benefit;
- carer's allowance;
- bereavement allowance, bereavement payment and widowed parent's allowance (subject to separate reform proposals);
- maternity allowance;
- industrial injuries disablement benefit;
- statutory maternity/adoption/paternity pay;
- statutory sick pay;
- maternity grants, funeral payments and cold weather payments – to be extended to people on universal credit, according to the information available.

Who will be able to claim universal credit?

Universal credit will replace means-tested benefits and tax credits for working-age people up to pension credit age. It will be paid to people in or out of work. Details in the Act include the following basic conditions:

- Claims may be made by a single person, or members of a couple jointly.
- You must be at least 18 years old (regulations may prescribe a different minimum age in special cases).
- You must be under the qualifying age for pension credit (this will be 61 years and 10 months in October 2013 – rising to 65 by 2018). Where one member of a couple reaches the qualifying age for pension credit and the other is of working age, they must continue to claim universal credit until both have reached pension credit qualifying age.
- The capital rules will be the same as for income support, with lower and upper capital limits and tariff income assumed for capital between the limits. This will exclude people with savings over £16,000.
- Some income will be disregarded – eg, disability living allowance (and its replacement, personal independence payment), while other income will be taken into account in full – eg, occupational and personal pensions. Net earnings above the earnings disregard (see below) will be deducted from universal credit amounts at the proposed rate of 65 per cent – ie, 65p for every pound of extra earnings. Claimants will keep 35p for every pound earned above their disregard.
- A new minimum income will be assumed for self-employed claimants (see below).

How much will universal credit be?

Universal credit will be made up of:

- personal amounts for a single claimant or couple;
- additional amounts for:

- children (or qualifying young people), with additional amounts for disabled and severely disabled children;
- rent or a mortgage (support for mortgage interest will only be available to people who are not doing any paid work, and may include a waiting period and time limit);
- limited capability for work;
- limited capability for work-related activity;
- regular and substantial caring responsibilities for a severely disabled person.

The maximum award will be subject to the 'benefit cap' based on median net earnings – the government has projected this will be set at £500 a week for couples or lone parents in April 2013. The cap will include other benefits such as child benefit, but will be implemented by reducing the amount of universal credit someone gets.

There will be exceptions to the cap for:

- households where someone gets disability living allowance (or personal independence payment) or industrial injuries benefits;
- those with limited capability for work-related activity;
- war widows;
- working families (earning at least £430 per month); or
- unemployed after working for at least 12 months (exempt from cap for 9 months).

The universal credit amounts will be at a 'similar level of support than the current system', except the proposed amount for most disabled children is halved, and the amount for most disabled adults will be reduced due to the abolition of disability premiums.

What will be the earnings disregards?

It is intended that universal credit will allow most people to earn higher amounts than under the current benefits system before their payment is reduced.

Disregards will be set at different levels for each of the following groups:

- 1 • single people and couples without children;
- 1 • lone parents with one or more children;
- 1 • couples with one or more children; and
- 1 • disabled singles or couples.

Only one earnings disregard, whichever is highest, is to be available in each household.

It is proposed that there will be two levels of disregards for each group, depending on whether or not they are getting help with housing costs. There will be higher earnings disregards for households with no housing costs. The rates of the disregards will be set in line with Government spending commitments.

What about income from self-employment?

If you are self-employed and on a low income, you may be assumed to have a certain level of earnings. This will not apply during the first twelve months of starting a new business. It appears that self-employed people will have to report profits every month.

What will happen to existing claimants?

It is intended that existing claimants will not lose out at the point of change. There will be transitional protection in the form of additional payments.

How will you claim and get paid?

Universal credit will be administered by the DWP. Couples will make a joint claim. Claims will normally be made online with alternative access kept to a minimum. Subsequent contact will also be online, including claimants having access to an online account with details of their award and a facility for reporting changes of circumstances.

Universal credit will use HMRC's planned 'real-time' IT system to identify earnings when they are paid. Those paid through PAYE will have no need to report changes to their earnings.

Payments will change from the current fortnightly payments to monthly, paid directly by the DWP into a claimant's bank account, including amounts for rent. There will be provision to pay amounts differently if it appears necessary to protect the interests of the claimant, partner or child.

What about conditionality and sanctions?

There will be more conditionality and tougher sanctions for universal credit and for existing benefits. All claimants must accept a '**claimant commitment**' as a condition of receiving universal credit. They will then be placed into one of the four following groups:

A. Claimants subject to no work-related requirements:

- people with limited capability for work-related activity because of health or disability – ie, those in the support group for employment and support allowance;
- lone parents or the lead carer in a couple with a child under one;
- carers with regular and substantial caring responsibilities for a severely disabled person.

B. Claimants subject to the work-focused interview requirement only:

- lone parents or the lead carer in a couple with a child over one but below the age of five
- lone foster carers or the lead carer in a fostering couple, with a foster child under the age of 16

This group will be expected to attend periodic interviews to discuss their plans for returning to the labour market.

C. Claimants subject to the work preparation requirement:

- people with limited capability for work because of health or disability – ie, those

in the work-related activity group for ESA;

This group will be expected to take reasonable steps to prepare for work, such as attending a skills assessment, improving personal presentation, participating in training or an employment programme, and undertaking work experience or a work placement.

D. Claimants subject to all work-related requirements:

- everyone else - the default for claimants including lone parents and couples with children over the age of five.

This group will be subject to a work search requirement (including making applications and registering with employment agencies) and a work availability requirement (subject to limitations to be prescribed), as they would under jobseeker's allowance.

Other qualifying conditions for each group may be prescribed. Each adult in a household will be placed into her/his own conditionality group depending on her/his individual situation.

There will be a new concept of 'in-work conditionality' where working claimants are required to look for more work unless they are earning at least the minimum wage x 35 hours a week (or less if reduced availability for work has been agreed)

Sanctions

'Higher level sanctions' may be imposed on claimants subject to all work-related requirements. This includes failure for no good reason to comply with the requirement to prepare or apply for work, take up an offer of paid work; and ceasing work voluntarily or through misconduct. This may result in a reduction of the award, for a period up to a maximum of three years, depending on the number and regularity of such failures. The amount will be the value of the adult personal allowance, and will not include additional amounts, such as for children or housing.

Other sanctions may be imposed on claimants subject to work preparation requirements for failure to undertake work-related activity, or in the work-focused interview group for failure to attend an interview. These may be imposed for a period until a claimant meets the compliance condition, or for up to 26 weeks.

Hardship payments may be available for claimants who have been subject to sanctions and are, or will be in 'hardship'. Regulations will prescribe the circumstances and matters to be taken into account, the amount, duration and whether such payments are recoverable.

Is there a right of appeal?

It is expected that there will be a right of appeal to the First-tier Tribunal (Social Entitlement Chamber) against decisions concerning entitlement to universal credit, as with the current benefits and tax credits system. However, the Act includes a power to require consideration of a revision before an appeal, so that the right of appeal is only effective after the Secretary of State has reconsidered the issue.

Further information

CPAG information at: www.cpag.org.uk/universalcredit/.

Read the Welfare Reform Act 2012 and earlier documents on the DWP welfare reform webpage: <http://www.dwp.gov.uk/policy/welfare-reform/universal-credit>

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