UNIVERSITY OF BATH

Timing it right or timing it wrong: How should income-tested benefits deal with changing circumstances?

Peter Whiteford, Crawford School of Public Policy, Australian National University and Visiting Fellow, University of Bath, peter.whiteford@anu.edu.au
Jane Millar, Institute for Policy Research, University of Bath, j.i.millar@bath.ac.uk

September 2019

IPR Institute for Policy Research

Overview

1. Background and introduction
2. Australian experience
3. The United Kingdom
4. Some reflections

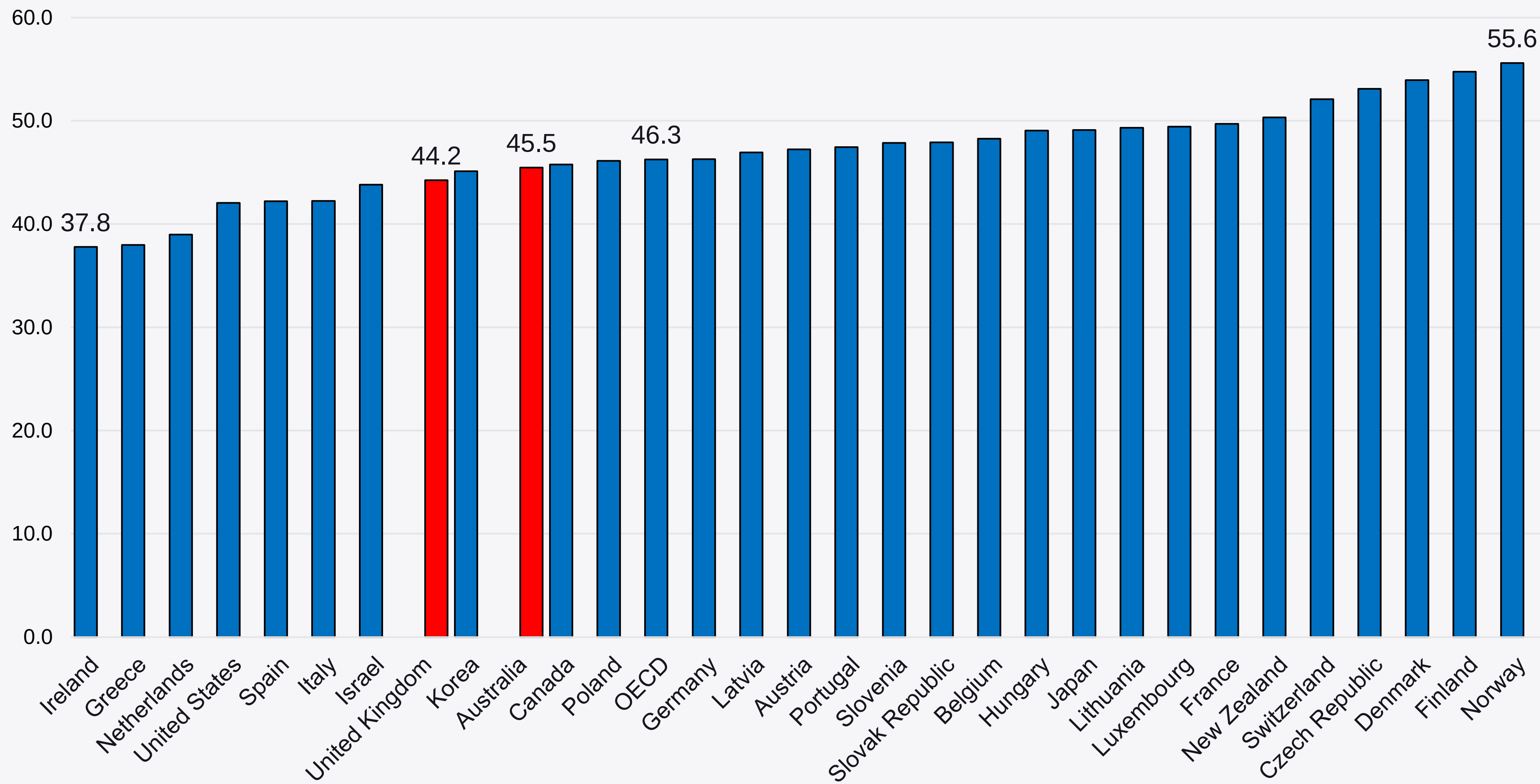
Timing issues and income tests

- “designing a system which, on the one hand, provides families with the help they need at the time when they need it, while, on the other hand, minimising the need for intrusive, complex, costly and administratively burdensome procedures. In short, the system must balance responsiveness and simplicity”. (Whiteford, Mendelson and Millar, 2005)
- “…In order to ease access barriers to social protection, policy makers should consider: … making means tests more responsive to people’s needs by shortening the reference periods for needs assessments and by putting appropriate weight on recent or current incomes of all family members” (OECD, 2019)
- “More volatile career patterns or a growing diversity of employment forms pose specific challenges for social protection provisions that link support entitlements or financing burdens to past or present employment … tax-benefit provisions, which create sudden income drops or gains as people vary earnings or working hours, are more likely to affect working time and earnings when choices are no longer constrained to, say, 40, 30 or 20 hours per week ” (OECD, 2019)

Labour market change

- The decline in “standard employment”, where the standard employment contract was assumed to be full-time employment for a full-working career – a pattern that applied primarily to men.
- Growth in non-standard work, including more volatile employment such as ‘zero-hours’ contracts and casual work
- Job losses through automation and digital economy.

Share of population of working age in full-time jobs earning more than two-thirds of median income, 2015



Income volatility in UK …..

- More evidence emerging
  - Hills et al, 2006: 93 families, over one year. Seven with stable weekly incomes, 21 broadly stable, 26 erratic, including 8 highly erratic.
  - Resolution Foundation, 7 million Lloyds accounts. Monthly pay fluctuations the norm for the majority of employees. Lower earnings most volatile: 80 per cent plus of those with a steady job on take-home pay of around £10,000 per year had volatile pay, compared to two-thirds of those with take-home pay of around £35,000 a year.
  - Living Wage Foundation, around 5 million workers, are in low paid, insecure forms of work, including short-term contracts, and contracts with unpredictable pay and hours
  - Qualitative research, change & budgeting over short periods, e.g. Kyprianou, 2015; David Finch, Kate Summers.

…. and Australia

- 2018 ABS Survey: 24% of all employees in Australia have earnings that vary from one period to the next (excluding overtime) – about half of all casuals and 15% of permanent employees. Also 73% of self-employed (unincorporated, without employees). Overall, nearly one-third of workforce.
- HILDA tracks people from year to year: more than half of all working age individuals have a spell on an income-tested benefit, and 70% of working-age households include someone who received an income support payment in the period
- Brotherhood of St Laurence and RMIT University survey of 70 low- and moderate-income households in suburban Melbourne found that over half of the participants experienced highly erratic variations (greater than 25 per cent) in their fortnightly incomes. 9 households had variations greater than 60 per cent.
- All - UK and Australia - find that income volatility greater for low-income households, precipitating financial hardship and sometimes debt, including social security debt.

Issues for social security

1. Coverage and inclusion – are atypical workers covered?
2. Funding – enough from contributions to meet costs?
3. In-work poverty – how to ensure adequate incomes in work, or as people make transitions in and out of work, between jobs?
4. Overpayments and debt – introducing further instability into family life?

Our focus in on how to match income and needs in income-tested benefits

Australian experiences: family debts,“robo-debts” and real-time reporting

- New Family Tax Benefit from July 2000 required claimants to estimate income for the next financial year to determine fortnightly entitlement for that year, with an end-of financial-year reconciliation.
  - After the introduction of new arrangements, 670,000 families were overpaid – more than 12 times as many as the previous year – about 1/3 of those receiving payments.
  - Addressed by lump sum, end of year payments
- Data-matching by Centrelink with the Tax Office started in 1991. The automation of the system was increased in 2011. The current “robo-debt” controversy arose from changes introduced in the 2016 Omnibus Budget Bill. New computer system and “real-time” wage reporting. Shifted administrative burden onto recipients.
  - 2016 changes automated matching and raising an overpayment. Number of “interventions” rose from 20,000 in 2015-16 to nearly 800,000 in 2016-17.
  - Algorithm assuming stable earnings almost certainly wrong for people leaving benefits before the end of the tax year e.g. all completing students.
  - New system used to justify proposed abolition of lump sum family payments.

Australian experiences: income bank and smoothing fluctuating earnings

- Assessment and payment period is fortnightly for income support payments.
- The Income Bank is calculated automatically and accumulates when total income is less than $48 per fortnight. It is possible to build up to a total "bank" of $1,000 for those receiving most working-age payments, and $3,500 for those receiving Youth Allowance as a job seeker (the payment for unemployed people less than 22 years of age). For students, the Income Bank arrangement is similar, but much more generous ($10,900).
- The Income Bank allows people to earn more before their payment is reduced. Available credits offset excess earnings until the bank is zero, and then the income support payment starts to reduce. Thus, fluctuations in earnings are smoothed. Those returning to benefits within 13 weeks have no ordinary waiting period or liquid asset test waiting period.
- The treatment of couples in the income test provides a form of 'partial individualisation'. Each member in a couple has their own entitlement, and they also have their own individual work allowance and the income test is sequentially applied. This means that the earnings of one partner in a couple does not reduce the partner's payment until the other earner's component is fully extinguished.

The UK: brief outline of past approaches

- ‘Out of work’ income-tested benefits: typically based on current income, seven day waiting period, paid fortnightly usually, but can be weekly, monthly. Housing Benefit usually paid at same frequency as rent due.
- ‘In work’ benefits: the early 1970s to late 1990s, assessed over 5 weeks, paid weekly, for 52 weeks regardless of changes in circumstances, later reduced to 26 weeks regardless of changes.
- Currently: two systems in parallel
  - ‘legacy’ benefits – 4 income-related benefits plus 2 tax credits
  - Universal Credit – combines these into one system

UK: Tax Credits, annual

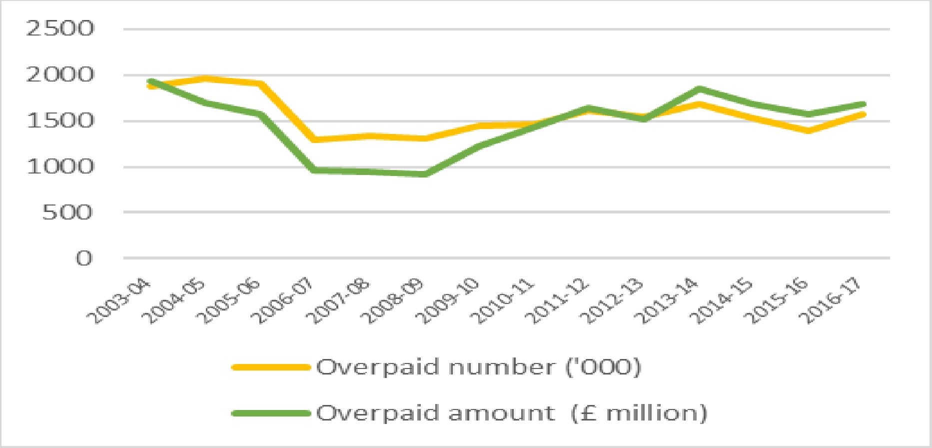
Working Families Tax Credit/Child Tax Credit

- Assess on previous year's earnings
- Report some changes in year or wait to end
- Reconcile at year end
- Result: under and overpayments

Disregards to reduce impact of overpayments

2003 – 2006: £2,500
2006 – 2011: £25,000
2011 - 2013: £10,000
2013 – 2016: £5,000
2016 - date: £2,500

Extent of overpayments



A problem then… not a problem now

"… as Tax Credits are being replaced by Universal Credit, they "are not a permanent feature of the landscape" and therefore the appetite within government to change existing systems and processes is very low' (Public Accounts Committee, 2019, page 9).

UK Universal Credit, monthly

Key features

- Monthly assessment period - set by date of claim
- Monthly payment in arrears
- Real-time-information (RTI) from employers for changes in earnings
- Self-report for all other changes that have to be reported - mostly online

UK Universal Credit, monthly

Monthly assessment

- 5 week wait at start → debts
- Wages may not line up with UC (weekly paid)
- 2 earners – different pay dates and cycles
- RTI – possible errors & how to challenge these
- ‘Whole month’ – ‘arbitrary shortfalls’

Monthly payment

- Budgeting
- Deductions from benefits
- Upfront childcare

- Uncertainty about how much people will get
- Visible ‘poverty trap’
- Risk that for many the relationship between needs and payments adrift and opaque

Issues for income-testing design

1. Debts by design

2. IT, automation and administration

3. Are benefit packages with different timing desirable?

4. How responsive *should* benefits be?