Low Incomes Tax Reform Group.

A voice for the unrepresented.

Public Accounts Committee: Progress in Implementing Universal Credit
Response from the Low Incomes Tax Reform Group (LITRG)

1 Executive Summary

1.1 We welcome this opportunity to provide written evidence to the Committee's inquiry. Our response focuses mainly on the transition of tax credit claimants to universal credit (UC), as we feel this is where we can add the most value to the inquiry.

1.2 The Government made a commitment that anyone moving from legacy benefits to UC, without a change of circumstances, will not lose out in cash terms. Transitional protection is the mechanism used to give effect to this. In reality, the transitional protection rules do not guarantee this in all cases which means that some people may get less in UC than they were getting on legacy benefits but they will not get transitional protection. As a result, the commitment made does not apply to all migrating claimants.

1.3 Since 2018, we have urged DWP to do a full assessment of transitional protection to get a better understanding of: how many people will not get transitional protection, even though their UC award will be lower than their legacy benefits; and how many people will get a transitional element in their UC award even though it is higher than their legacy benefit award. We suggest that DWP should do this urgently before they further increase the number of migration notices. In addition, DWP should clarify their guidance to:

- make it clear that some people may not fully benefit from the commitment that there will be no cash losers at the point of transition and it is possible that their actual UC award will be less than their legacy benefits,
- provide examples of the most common situations where this is likely to occur, and
- explain that the transitional element is calculated based on an indicative UC amount and not the actual UC award.

1.4 The information provided by DWP about transitional protection is currently misleading by suggesting that the comparison is between the amount the claimant was receiving on legacy benefits and the amount they will get under universal credit. This is incorrect – when assessing whether someone is entitled to transitional protection, the comparison is between their legacy benefit amount and an 'indicative' UC amount. This indicative UC amount may differ from their first actual UC award for a number of reasons. This guidance should be updated urgently.

1.5 We are aware of some cases where transitional protection has been calculated and added after the first UC award has been calculated. This appears to be contrary to the legislation and confusing for claimants.

1.6 There is a lack of transparency around transitional protection both for claimants and advisers. For claimants, DWP do not provide information about how transitional protection is calculated as a matter of course. Claimants must know to ask for this and then challenge it by way of a mandatory reconsideration. We urge DWP to improve transparency and include transitional protection calculations on award notices as a matter of course.

1.7 Up to March 2023, nearly 27% of tax credit claimants who were sent a migration notice did not claim UC and missed out on an average of £300 a month. DWP do not appear to have done any detailed research with that specific group to understand why they did not claim and look at whether any mitigations can be put in place to encourage people to claim the support they are entitled to. More work should be done to understand why so many tax credit claimants do not go on to claim UC.

2 About us/introduction

2.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998, LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low-income workers, pensioners, migrants, students, disabled people and carers.

2.2 LITRG works extensively with HM Revenue & Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.

2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

2.4 We welcome this opportunity to provide evidence to the Committee's inquiry into progress in implementing UC. Our primary focus is on the tax and tax credits system, but we are interested in those elements of UC that affect tax credit claimants and that interact with tax. We have therefore limited our evidence to those areas where we feel we can add value and expertise. There are many other welfare rights organisations who will be able to provide evidence about the wider issues people experience when moving to and claiming UC.

3 Transitional protection issues

3.1 *No cash losers at the point of transition*

3.1.1 In November 2010, the Government published a white paper stating their intention to replace legacy benefits with UC. The paper stated:

'No-one will experience a reduction in the benefit they are receiving as a result of the introduction of Universal Credit. At the point of transition onto the new system, those households whose circumstances remain unchanged and who would otherwise experience a reduction in income will receive cash protection.'[1]

This commitment, that anyone moving from legacy benefits to UC without a change of circumstances will not lose out in cash terms, has since been repeated many times[2].

3.1.2 To give effect to this commitment, the Government introduced transitional protection for those migrating from legacy benefits to UC. Transitional protection is made up of a transitional element, and for tax credit claimants a transitional capital disregard and protection for claimants who are full-time students. It is the transitional element which seeks to give effect to the Government's commitment that there will be no cash losers upon migration to UC.

3.1.3 Transitional protection does not apply where people move to UC outside of the formal migration exercise.[3] The legislation[4] requires DWP to determine whether the transitional capital disregard and/or the transitional element is to be included in a UC award before they make a decision on the qualifying UC claim.

3.1.4 In 2018, the Social Security Advisory Committee (SSAC) consulted on the draft migration regulations. Those regulations introduced the migration process and set out how the transitional capital disregard and transition element were to be calculated. We made a number of points in our response to SSAC[5] about the suggested migration process but one of the most important points was in relation to the principle behind transitional protection - to avoid cash losers at the point of migration from legacy benefits to UC. This was, and still is, one of the most important parts of migration from a claimant perspective. Based on the repeated commitments given, that no-one would be worse of at the point of migration, claimants enter the process expecting the monthly payments they will get from UC will broadly equal payments they were getting under legacy benefits.

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[1] Page 53, Universal Credit – Welfare that Works White Paper, November 2010 https://assets.publishing.service.gov.uk/media/5a79581640f0b63d72fc4fd9/universal-credit-full-document.pdf

[2] See for example this statement from the Secretary of State for Work and Pensions in 2018 https://hansard.parliament.uk/commons/2018-06-07/debates/18060727000016/UniversalCredit which says 'The Government have already made a commitment that anyone who is moved to universal credit without a change of circumstance will not lose out in cash terms. Transitional protection will be provided to eligible claimants to safeguard their existing benefit entitlement until their circumstances change.'

[3] There is an exception for those who have a severe disability premium in legacy benefit who may qualify for a transitional SDP element if they claim UC.

[4] SI 2014/1230 Regulation 50: https://www.legislation.gov.uk/uksi/2014/1230/regulation/50

[5] https://www.litrg.org.uk/submissions/moving-claimants-universal-credit-other-working-age-benefits

3.1.5 However, in our 2018 submission to SSAC, we pointed out that the method chosen to calculate transitional protection in the draft regulations was likely to lead to situations where that commitment is not met – meaning some people end up with more money or less money than they had under the legacy benefit system. That situation remains the case now that migration is underway – some people are given a transitional element even though their actual UC award is higher than their legacy benefits and others don't get any transitional protection even though their actual UC award is lower than their legacy benefits.

3.1.6 In 2018, we suggested that a full analysis should be undertaken and published to ensure that the DWP understood where these variations might occur and consider whether any mitigations were possible. Some assessment of the numbers involved should have been undertaken. To date, as far as we are aware, nothing has been published that shows any such assessments were undertaken and no significant changes were made to the migration regulations to mitigate any potential issues. We suggest that DWP publish something as soon as possible showing their assessment in regard to the headline commitment. This should specifically quantify how many people may receive an actual UC award that is less than their legacy benefits (where they either have a transitional element but the award is still less, or no transitional element is included).

3.1.7 Our second suggestion was that, at the very least, it was important that communications managed people's expectations in this regard. It is disappointing that guidance from DWP still refers to the headline commitment without any qualification. For example, the current GOV.UK transitional protection page[1] says:

'*Transitional protection payments are an additional amount to help with your move to Universal Credit. The payment will make up the difference if your Universal Credit entitlement is less than your previous tax credits or benefits*'.

This is not the case for some claimants and, as we explain below, it is misleading about how transitional protection actually works. DWP must improve their guidance and communications to:

- make it clear that some people may not fully benefit from the commitment that there will be no cash losers at the point of transition and it is possible their actual UC award will be less than their legacy benefits,
- provide examples of the most common situations where this is likely to occur, and
- explain that the transitional element is calculated based on an indicative UC amount and not the actual UC award.

3.2 ***Transitional element – indicative UC amount***

3.2.1 We have stated above that in some cases, claimants migrated from legacy benefits to UC will be worse off, despite the Government's commitment that there will be no cash losers at the point of transition. This is because either: they are not entitled to the transitional element; or the amount of

[1] https://www.gov.uk/guidance/transitional-protection-if-you-receive-a-migration-notice-letter

transitional element they get does not bring their actual UC award up to the same level of their legacy benefits. The remainder of this submission focuses on tax credit only claimants who are transitioning to UC, although we understand similar issues apply to all legacy benefit claimants.

3.2.2 Creating transitional protection to smooth the move from an annual based system (tax credits) with rules and definitions aligned to the tax system to a monthly based system (UC) that has different definitions of income was always going to be challenging.

3.2.3 The biggest misunderstanding about transitional protection is that most claimants expect the comparison to be between the amount they were getting from legacy benefits with their actual UC award. Where the UC award is lower, they expect the difference to be made up by the addition of a transitional element. This misunderstanding is reinforced by DWP's explanation on GOV.UK[1]:

> **'Example**
>
> Jane is entitled to £800 on her existing tax credits or benefits.
>
> Her Universal Credit entitlement is £600.
>
> This means Jane's transitional protection amount will be £200.
>
> Her total Universal Credit entitlement is now £800.'

3.2.4 This example is incorrect because it compares Jane's UC entitlement with her previous legacy benefit entitlement. In fact, the migration regulations[2] state that the transitional element is to be calculated by comparing an 'indicative UC amount' to the legacy benefit entitlement. This indicative UC amount is calculated by following a set of assumptions set out in legislation – some of which are based on tax credit rules and not UC rules. This means that an individual's indicative UC amount may be different from the actual UC award they get in their first assessment period.

3.2.5 It is this potential difference, between the indicative UC amount and the actual first UC award amount, that leads to the possibility that some people will receive a lower UC award than their legacy benefits yet they will not receive any transitional protection. The DWP example above (paragraph 3.2.3) does not mention the UC indicative amount. If the UC indicative amount is £800 in Jane's case, then she will get no transitional protection, even though her actual UC award will be £200 a month less than her legacy benefit award.

3.2.6 The actual UC award amount is therefore irrelevant in calculating transitional protection – a crucial fact that does not seem to be mentioned in any DWP guidance or communications aimed at claimants.

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[1] https://www.gov.uk/guidance/transitional-protection-if-you-receive-a-migration-notice-letter#transitional-protection-payments

[2] SI 2014/1230 Regulation 54: https://www.legislation.gov.uk/uksi/2014/1230/regulation/54

3.2.7 There are numerous reasons why the indicative UC award amount may be different to the actual UC award amount. The indicative UC amount is the amount the claimant would be entitled to if a claim for UC were made by reference to their circumstances on migration day, applying certain assumptions. These assumptions mean that childcare costs are calculated under tax credit rules rather than UC rules and that earned income is based on tax credit rules rather than UC rules. The number of children included in the indicative UC calculation is based on those on the tax credit award (which may not be the same as on the actual UC award).

3.2.8 Some other reasons for differences between the indicative UC amount and the actual UC award amount include:

- Tax credits are, in many cases, calculated based on previous year income. This means that a claimant's 2024/25 tax credit award is likely based on their 2023/24 income. The indicative UC award will use that same 2023/24 income (calculated as a monthly figure) whereas the actual first UC award will use their current income. This current income figure may be substantially higher or lower than the figure used in their indicative UC calculation.
- Tax credits take into account the value of benefits in kind as income, for example company cars. This will be included in the income used in the indicative UC amount but when the actual UC award is calculated, those benefits in kind will not be taken into account.
- Tax credits allow self-employed claimants who make a loss to offset that loss against their other income as well as income of their partner. They can also carry forward losses against future self-employed income from the same trade. However, for the actual UC award, previous year losses would not be taken into account.
- Tax credit claimants who are directors have any salary from the company treated as employment income and dividends as investment income. Our understanding is that the indicative UC amount will only take into account employment income (not dividends). However, once they claim UC, if they are in a position analogous to a sole trader, they will be treated as if they are self-employed for UC. Whilst any salary they pay themselves will still be treated as their employed earnings, the company's profit each assessment period will be treated as their individual self-employed earnings (or share thereof if others are involved in the business).
- Childcare support in the tax credits system is based on average childcare costs, sometimes over a 52-week period, whereas UC looks at the actual costs in an assessment period. The indicative UC amount will be based on the tax credit childcare figure, which may be different to the childcare figure used in calculating the actual UC award.
- Tax credits are based on annual income. If a tax credit claimant starts employment mid-way through the year, their annual figure will only contain say 6 months of employment income. However, that figure will be divided by 12 to convert into a monthly income figure in calculating the indicative UC amount. The actual UC award will use the full monthly amount. Therefore, whilst the transitional element calculation will be based on the same figure for earnings which may lead to no transitional element, the actual UC award will use a different, real-time earnings figure in the assessment period, highlighting the disconnect between the legacy benefits amount and the actual UC award.

3.2.9 As explained above, we think it is crucial for DWP to publish an assessment that indicates to what extent the Government's commitment regarding no cash losers at transition is met in reality. This should include an assessment of: the number of people migrating who have an actual UC award that is less than their legacy benefits; and the number of people who receive a transitional element even though their actual UC award is higher than their legacy benefits. It is also crucial that DWP look to refine their guidance to explain how transitional protection works by reference to an indicative UC amount rather than the actual UC award, with some examples of why people may get a lower UC award without a top-up of transitional protection.

3.2.10 We are also aware, anecdotally, of some cases where there has been a delay in calculating the transitional element and it has been added after the first award has already been calculated. It is not clear how widespread this is, but it is confusing and disconcerting for claimants and it is contrary to legislation which requires DWP to calculate transitional protection before making a decision on the qualifying UC claim.

3.3 ***DWP transitional protection process/guidance***

3.3.1 The calculation and application of transitional protection has been shrouded in some mystery since migrations started. It has been incredibly difficult for advisers to get concrete information about how exactly DWP are calculating transitional protection and what information they are using to do those calculations. It also remains the case that claimants are not automatically provided with information about how their transitional protection has been calculated.

3.3.2 As a result, we are aware that some advice organisations were telling claimants they could not provide any help regarding transitional protection calculations because they lacked the information needed to do so with confidence. Recently, DWP have shared directly with organisations some guidance specifically for advisers, but it would have been far more helpful had that been done much earlier in the process. We would urge DWP to provide claimants with a breakdown of their transitional protection calculation as a matter of course.

4 Tax credit claimants moving to UC

4.1 ***Take-up concerns***

4.1.1 Around 27% of tax credit claimants who were sent a migration notice between November 2022 and March 2023 did not make a claim for UC – the average lost being around £300 per month.[1] More recent figures suggest this figure is still around 20%.[2] DWP have stated there are three themes showing why this is the case[3]:

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[1] https://cpag.org.uk/news/limits-test-and-learn

[2] https://www.gov.uk/government/statistics/move-to-universal-credit-statistics-july-2022-to-december-2023/completing-the-move-to-universal-credit-statistics-related-to-the-move-of-households-claiming-tax-credits-and-dwp-benefits-to-universal-credit-data#introduction

[3] https://www.gov.uk/government/publications/completing-the-move-to-universal-credit-learning-from-initial-tax-credit-migrations/completing-the-move-to-universal-credit-learning-from-initial-tax-credit-migrations

- Some claimants made a conscious decision not to claim as the amount they would receive was particularly small and they perceived it was not worth fulfilling associated claims requirements
- Some claimants believed they were not eligible for UC, as their circumstances had recently changed and their tax credits had already stopped
- Some claimants felt a stigma attached to claiming UC, or that they felt they had sufficient income and that they believed benefits should only be for those who really need them

4.1.2 As CPAG noted in their November 2023 blog post[1], these reasons are hard to align with a Freedom of Information (FOI) answer that shows the average loss was £300 per month. A further FOI shows that DWP has not done any detailed research into why those tax credit claimants did not make a claim for UC. We agree with CPAG's conclusion that it is concerning that there is no proper understanding of why so many people with a strong financial incentive to move to UC are not doing so and yet DWP are continuing to increase the number of migration notices issued. DWP should prioritise more detailed research with this specific group of tax credit claimants before increasing the number of migration notices.

4.1.3 Anecdotally, we have seen some self-employed tax credit claimants who have particular concerns about the move to UC and the way UC treats self-employed claimants compared to tax credits – especially in relation to the minimum income floor. In addition, some people say they are concerned about the amount of conditionality and interaction required with DWP compared to tax credits. There are likely many other reasons that need further exploration and, where possible, appropriate mitigations put in place so that claimants don't needlessly opt out of support they are entitled to.

LITRG
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[1] https://cpag.org.uk/news/limits-test-and-learn