



DWP Department for
Work and Pensions

21st Century Welfare

Presented to Parliament by the Secretary of State
for Work and Pensions by Command of Her Majesty
July 2010

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Foreword by the Secretary of State

After less than three months of innovative Coalition Government, we want to begin real change to the benefits system by making it simpler and more efficient, with a view to fewer benefits, fewer layers of bureaucracy and with financial support firmly focused on making work pay. Less than one year ago, I said that unless politicians and civil servants acted to reform our complicated and inefficient benefits system, then further talk about work being the best route out of poverty would be more empty rhetoric.

Too often governments have tried to tackle poverty but ended up managing its symptoms. The changes outlined here are based on a recognition that poverty cannot be tackled through treating the symptoms alone.

The benefits system has shaped the decisions of the poorest in a way that has trapped generation after generation in a spiral of dependency and poverty. This has cost the country billions of pounds every year in cash payments and billions more in meeting the social costs of this failure.

The only way to make a sustainable difference is by tackling the root causes of poverty: family breakdown; educational failure; drug and alcohol addiction; severe personal indebtedness; and economic dependency.

These problems are interrelated and their solutions lie in society as a whole. However, we must recognise that the benefits system has an important role to play in supporting personal responsibility and helping to mend social ills.

We are going to end the culture of worklessness and dependency that has done so much harm to individuals, families and whole communities. Our aim is to change forever a system that has too often undermined work and the aspiration that goes with it.

By actively putting work at the centre of working-age support we want to create a new contract with the British people, which is why we are consulting them in this paper. We will help them to find work and make sure work pays when they do. They in return will be expected to seek work and take work when it is available. No longer will we leave people for years on long-term benefits without contact or support. This contract is about a responsible society working together to improve the quality of life for those who are worst off.



**The Rt Hon
Iain Duncan Smith MP**
Secretary of State for Work and Pensions

Executive summary

1. The benefits system as it stands often provides incentives to stay on benefits rather than take on a job. We want to support people to move into and progress in work, while still supporting those in greatest need.
2. The Budget outlined the first steps in achieving these goals. However, the scale of the Government's ambition in this area warrants the consideration of more fundamental structural reforms. This paper identifies the key failings of the benefits system and outlines the objectives we believe the system should attempt to achieve. We then focus on how we might seek to address these failings and outline some key issues we will need to work through to deliver a benefits system for the 21st Century.
3. The framework we are considering greatly improves on earlier reforms because it looks at the system of state support for the less well off as a whole and is designed to produce positive behavioural effects. We want to maximise work incentives while continuing to protect those most in need.
4. This discussion document outlines illustrative examples of structural reform, including options presented by external organisations.
5. Such structural reforms could enable us to deliver some fundamental changes to ensure that work always pays and is clearly seen to pay. We could achieve this through new rules on how much of their earnings people can keep without losing benefit and by withdrawing benefit as earnings rise at a single, reasonable, rate. This would mean that people taking the first steps into employment through a few hours of work each week would see substantial rewards for their efforts. It would also make the system much simpler.

6. We do not aim to reduce the levels of support for people in the most vulnerable circumstances but it is clearly important that we ensure support is well targeted, is fair to those on low pay and that the right money goes to the right people.
7. Finally, we are looking at how we could use smart automation to deliver support without the wasteful bureaucratic delays to payment that make the move into work more stressful than it needs to be. Similar technologies are already commonplace in the private sector and should make the benefits system quicker and more responsive for the customer and more efficient for the taxpayer whilst not increasing costs to business.
8. Our ideas would be consistent with possible steps to make aspects of the welfare system more localised. We will also be looking at individual measures for increasing work incentives and reducing the extent and costs of welfare dependency alongside consideration of reform of the structure of the system.
9. Subject to the outcome of this consultation, we hope to bring forward legislation early in the New Year to reform the benefits and Tax Credits system to make work pay. We would welcome views on how best to design such a system so as to meet our proposed principles and as part of our duties to have due regard to equality.

Introduction

1

1. We said at the outset of this Government that we would investigate how to simplify the benefits system in order to improve incentives to work. This commitment was restated in the Queen's Speech and the Budget. The Budget also set out the first steps in trying to achieve these aims. However, the Government wants to go further to improve incentives and reduce welfare dependency. This discussion document takes that work forward.
2. It is clear that, in common with other countries, we need to address the high and increasing costs of welfare dependency. There are now nearly five million working-age people receiving the main out-of-work benefits.¹ However, worklessness is not just the result of the recession – 1.4 million people have been receiving out-of-work benefits for nine or more of the last ten years.² Almost two million children are growing up in households where no-one is in work.
3. Successive governments have made well-intentioned but piecemeal reforms to the system. None have succeeded in tackling the fundamental structural problems that undermine personal responsibility and the effectiveness of welfare. They have left in place a hugely complex set of interdependent benefits and Tax Credits delivered by numerous different agencies.
4. Too many people believe they are better off on benefits than in work.³ Existing in-work support means that most should get more income when they work, but the gains for many are marginal and incentives are undermined by the need to navigate through the maze of in-work and out-of-work benefits and their interactions.

1 Latest Jobseeker's Allowance Claimant Count figures are available via the Office of National Statistics' Labour Market Statistics; Early estimates for Working Age Inactive Benefit Client Groups, and Benefit Caseload National Statistics are available via the Department for Work and Pensions' Tabulation Tool.

2 Department for Work and Pensions Longitudinal Study (the figure is for people claiming Income Support, incapacity benefits and Jobseeker's Allowance).

3 Examples of the concerns people have about managing financially when moving into a job can be found in Woodland S, Mandy W and Miller M, 2003, *Easing the transition into work (Part 2: client survey)*, Department for Work and Pensions Research Report No 186.

5. For example, in about 450,000 cases, Tax Credits awarded by HM Revenue & Customs are taken into account as income by the Local Authority in assessing Housing Benefit. The system gives with the one hand, only to take away with the other.
6. In short, the overly bureaucratic benefits system can act as a barrier to work, trapping people in poverty.

Affordability

7. Demographic changes mean that the cost of the welfare system is predicted to rise at a time when we can least afford it. We started to address this through the measures announced in the Budget, in particular the changes to the uprating of benefits, Disability Living Allowance and Housing Benefit. These reforms, along with reforms to obligations placed on out-of-work lone parents, build on a wealth of evidence that highlights the role of a strong system of conditionality in helping those dependent on benefits move into paid work.
8. The next step is to tackle the cost of the system by supporting many more people into work. Alongside the introduction of the Work Programme, we believe there is a strong case for reforming the system as a whole, addressing the root causes of the problems we face.

Rewarding work and personal responsibility

9. The experience from previous attempts at piecemeal reform suggest that it is unlikely that the full extent of the Government's ambition can be delivered without a more fundamental structural approach. By integrating and reforming the current income-related benefits and Tax Credits systems we could ensure that:
 - households and families see the gains from increasing the amount of paid work they do because they would keep more of their earnings;
 - a fair balance is struck between support and conditionality, making clear that we will not accept a culture of dependency nor will anyone be written off; and
 - positive behaviours, such as saving for retirement or buying your own home, are rewarded rather than penalised.

Reduced worklessness

10. We want to allow more people to do some paid work, and then to remain in work and increase their earnings. Getting the balance between these two elements will be crucially important. We also want to remove the fear that the system will punish them for doing so.
11. We would not propose to force people who are not able to work, or prepare for work, to do so. Support for people in the most vulnerable circumstances would remain unconditional.

A fair system that protects those in greatest need

12. Any reforms should also:
- establish a fairer relationship between the people who receive benefits and the people who pay for them and, as crucially, between the people on out-of-work benefits and the people who work in low-paid jobs;
 - target support more efficiently, supporting and protecting those in vulnerable circumstances;
 - help to divert people away from the pathways that lead to poverty and give people living in poverty a route out; and
 - support our wider goal of strengthening families, supporting carers and enabling disabled people to have an equal role in society.

A simpler system

13. The ideas for reform, discussed in this paper, would make it is easier for individuals to understand what they are entitled to, easier for people to make or change a claim and easier for them to understand how any changes in their circumstances will affect their claim.

Less delay, reduced error and fraud

14. The modern economy moves and changes quickly. Modern government should support people to be flexible in taking work, but the current benefits system is too cumbersome to do this effectively, creating delays to payments that discourage people from moving into work as and when the opportunities arise. Overpayments and subsequent repayments can also create serious cash-flow problems, making it even more difficult for them to manage their finances.
15. A simpler and fairer system could assess and pay benefits faster and could reduce the scope for error and fraud: claimants would more clearly understand what they are entitled to and would have less bureaucracy to deal with, while people who administer the system would be less likely to make errors.
16. A more modern automated payments system would bring public services into line with the standards we all expect of our banks. It would also allow people to be more flexible in taking on temporary work as they could be sure that support would be delivered as and when necessary without undue delay.

Conclusion

17. Work and personal responsibility must be at the heart of the new benefits system. This should provide support backed up by a strong system of conditionality that makes clear what is expected of claimants in return for the support they receive. In the next chapter, we consider in more depth the problems of the current system.

Problems with the current system

2

Summary

Our welfare system has failed to keep up with the pace of change in the economy and society. Successive governments have made piecemeal reforms without rationalising the overall landscape.

There are two key problems.

1. **Work incentives for some groups are poor:**

- interactions between benefits and Tax Credits make the transition to work risky and uncertain;
- the financial incentives to enter work at less than 16 hours are relatively low: this works against the successes of the strong conditionality regime; and
- the rate at which benefits and Tax Credits are withdrawn as earnings increase means that some people see no more than a few pence for every extra £1 earned – resulting in the perception that work does not pay.

2. **The system is too complex:**

- for claimants – arising from the interaction between different benefits and Tax Credits and layers of previous reforms, with many different benefits addressing the same underlying issue and entitlement to benefit paid by one agency affecting the benefit payable by another; and
- to administer – where people may need to provide the same information to different agencies, often through paper-based transactions.

As a result we have rising costs of state support – including waste through unproductive administration, error and fraud – accompanied by high rates of welfare dependency and poverty.

8 Chapter 2 Problems with the current system

1. The benefits system has evolved with good intentions but with flawed results. Successive governments have tinkered with bits of the system but have failed substantially to address:
 - rising costs of state support;
 - high rates of welfare dependency and poverty; and
 - a structure and set of rules that can drive negative rather than positive behaviours.
2. The situation stems from two key underlying problems:
 - work incentives can be poor; and
 - the system is too complex.

Rising costs of state support

3. The costs of maintaining a failing system are spiralling out of control; we cannot continue spending at such a rate on welfare that all too often has a negative rather than a positive impact. In the last decade, spending on working-age benefits and Tax Credits rose from £63 billion in 1996/97 to £87 billion in 2009/10 (in real terms, 2010/11 prices).⁴
4. Multiple agencies use valuable resources to gather and manage largely the same information in very similar ways. The Department for Work and Pensions and its agencies spend around £2 billion a year to administer and pay working-age benefits, Local Authorities spend a further £1 billion to administer Housing Benefit and Council Tax Benefit and HM Revenue & Customs spends more than £500 million a year.
5. Overpayments hit the poorest hardest, while error and fraud is estimated to cost the taxpayer around £5.2 billion a year: £2.1 billion in Tax Credits (around 8.9 per cent of entitlement in 2008/09)⁵ and £3.1 billion in Department for Work and Pensions benefits (around 2.1 per cent in 2009/10).⁶ Underpayments are also a problem, leaving customers without entitlements estimated at £1.3 billion a year in benefits and £260 million a year in Tax Credits.⁷

⁴ Department for Work and Pensions expenditure data.

⁵ HM Revenue & Customs, 2010, *Child and Working Tax Credits Error and Fraud Statistics 2008-09*: www.hmrc.gov.uk/stats/personal-tax-credits/cwtcredits-error0809.pdf

⁶ Department for Work and Pensions, *Fraud and Error in the Benefit System: October 2008 to September 2009*.

⁷ HM Revenue & Customs, 2010, *Child and Working Tax Credits Error and Fraud Statistics 2008-09*: www.hmrc.gov.uk/stats/personal-tax-credits/cwtcredits-error0809.pdf

6. As we noted in chapter 1, the cost of welfare is rising at a time when we can least afford it. The Budget announced a number of changes to existing benefits to curb rises in expenditure and to make the system fairer. Other countries are similarly considering their social security spending as public finances deteriorate. For example, the Irish government has reduced expenditure on social insurance and social assistance schemes through percentage reductions in benefit payments and tightening entitlement criteria for certain benefits. In Iceland, austerity measures include freezing welfare benefits for two years. In the UK we are considering further targeted reforms as part of the Spending Review.

High rates of welfare dependency and poverty

7. Welfare dependency has become a significant and growing problem in Britain, with huge social and economic cost for both claimants and wider society. The welfare state is now a vast, sprawling bureaucracy that can act to entrench, rather than solve, the problems of poverty and social exclusion.
8. 12 million working-age households receive benefits and Tax Credits costing more than £85 billion a year.⁸
- More than one in four working-age adults in the UK do not work and 2.6 million people have spent at least half of the last 10 years on some form of out-of-work benefit.⁹
 - Around a fifth of families with children are in poverty at any one time, and around two-fifths experience poverty at some time in a three year period.¹⁰
 - 35 per cent of families remain in poverty when a parent enters work¹¹ yet 2.4 million households now receive Working Tax Credit.¹²
9. The welfare system has failed to tackle intergenerational disadvantage and poverty. For example, a higher proportion of children grow up in a workless household in the UK than in almost any other EU country¹³ and the risk of poverty is higher for those who are poor as children or teenagers.¹⁴

Question 1

What steps should the Government consider to reduce the cost of the welfare system and reduce welfare dependency and poverty?

8 Cabinet Office, 2010, *State of the Nation report: Poverty, worklessness and welfare dependency in the UK*, HM Government ref 401172/0510.

9 Ibid.

10 Browne J and Paull G, 2010, *Parents' work entry, progression and retention and child poverty*, Department for Work and Pensions Research Report No. 626.

11 Ibid.

12 HM Revenue & Customs, April 2010, *Child and Working Tax Credits Statistics*, Office of National Statistics

13 Eurostat, 2008 data.

14 Blanden J and Gibbons S, 2006, *The persistence of poverty across generations: A view from two British cohorts*, Report for the Joseph Rowntree Foundation, Bristol: Policy Press.

Failure of the current system to generate positive behavioural effects

10. The current benefits system gives little consideration to the behaviours it generates. Complexity and poor financial incentives to work are a key factor in trapping people in worklessness. This is strongly linked with poverty and reduced well-being, poorer physical and mental health and an increased likelihood of becoming involved in the Criminal Justice System. Previous changes have failed to address the impact of benefits on these issues. Where parents have multiple disadvantages (such as low income, poor health, no qualifications), their children are also likely to experience disadvantage themselves.¹⁵

Work incentives can be poor

11. The current benefits and Tax Credits system influences financial work incentives through:
 - earnings disregards – the amount people can earn without it affecting their benefit;
 - additional payments for people working at least 16 or 30 hours through Tax Credits; and
 - tapered withdrawal – the rate at which earnings in excess of a disregard are deducted from benefit.
12. This system currently leaves some groups facing poor work incentives. These include lone parents who work less than 16 hours a week and young people for whom Working Tax Credit is not available.
13. People working fewer than 16 hours a week can continue to be eligible for out-of-work benefits but, for many claimants, there is little gain as every penny of earnings over a small disregard is lost. It is not surprising, therefore, that very few people on these benefits are doing any work at all.^{16,17}
14. Working Tax Credit provides support for people on low wages, but an individual or couple must satisfy the minimum-hours rules in order to qualify. The upshot is a system that can trap people into certain hours of work: they lose disproportionately if they work a few hours less and gain little by working more.

15 Cabinet Office, 2010, *State of the Nation report: Poverty, worklessness and welfare dependency in the UK*, HM Government ref 401172/0510.

16 Department for Work and Pensions Longitudinal Study.

17 This does not apply to Employment and Support Allowance claimants who can in some circumstances keep £93 a week in earnings and all of their benefit, including (since April 2010) Housing Benefit and Council Tax Benefit.

15. The introduction of Tax Credits improved work incentives for some groups but the picture is still patchy. The Institute for Fiscal Studies¹⁸ has long pointed to the problems with work incentives in the current system while evidence from the Citizens Advice service shows the negative impact the benefits system has on lone parents.¹⁹
16. It is estimated that in total, more than 600,000 people could face a Participation Tax Rate^{20,21} in excess of 90 per cent – that is more than 90 per cent of their gross earnings are lost through tax and withdrawn benefits. This measure does not take account of in-work costs such as travel, which can easily wipe out a meagre financial gain.
17. Table 1 below shows the number of people facing Marginal Deduction Rates²² of different degrees of severity – it shows for instance that 130,000 people face a Marginal Deduction Rate over 90 per cent who would gain 10p or less from a £1 increase in their pay because of the amounts lost through tax and withdrawal of benefits and Tax Credits.

Table 1	
Marginal Deduction Rates ²³	2011-12
Over 90 per cent	130,000
Over 80 per cent	330,000
Over 70 per cent	1,710,000
Over 60 per cent	1,935,000

Marginal Deduction Rate figures shown are for working heads of families in receipt of income-related benefits or Tax Credits where at least one person works 16 hours or more a week, and the head of the family is not receiving pensioner or disability premiums.

18. Figure 1 shows the complex way that benefits and Tax Credits interact with earnings to produce an overall household income. The way that benefits and tax credits are withdrawn as income rises combines with increased income tax and NI contributions to produce high Marginal Deduction Rates in some cases. In this example, based on current benefit and tax rates, a couple with a single earner and two children sees a Marginal Deduction Rate of 95.5 per cent²⁴ on earnings between £126 and £218. This means that someone at the National Minimum Wage would be less than £7 per week better off if they worked 16 extra hours and earned an extra £92 (an effective wage rate of 44p per hour). A system that produces this result cannot be right.

18 Adam, A. Brewer, M. and Shephard, A., 2006, *Financial Work Incentives in Britain: Comparisons over time and between Family Types*, IFS WP 06/20.

19 Citizens Advice, October 2008, *Citizens Advice Evidence Briefing: Barriers to work: Lone parents and the challenges of working*.

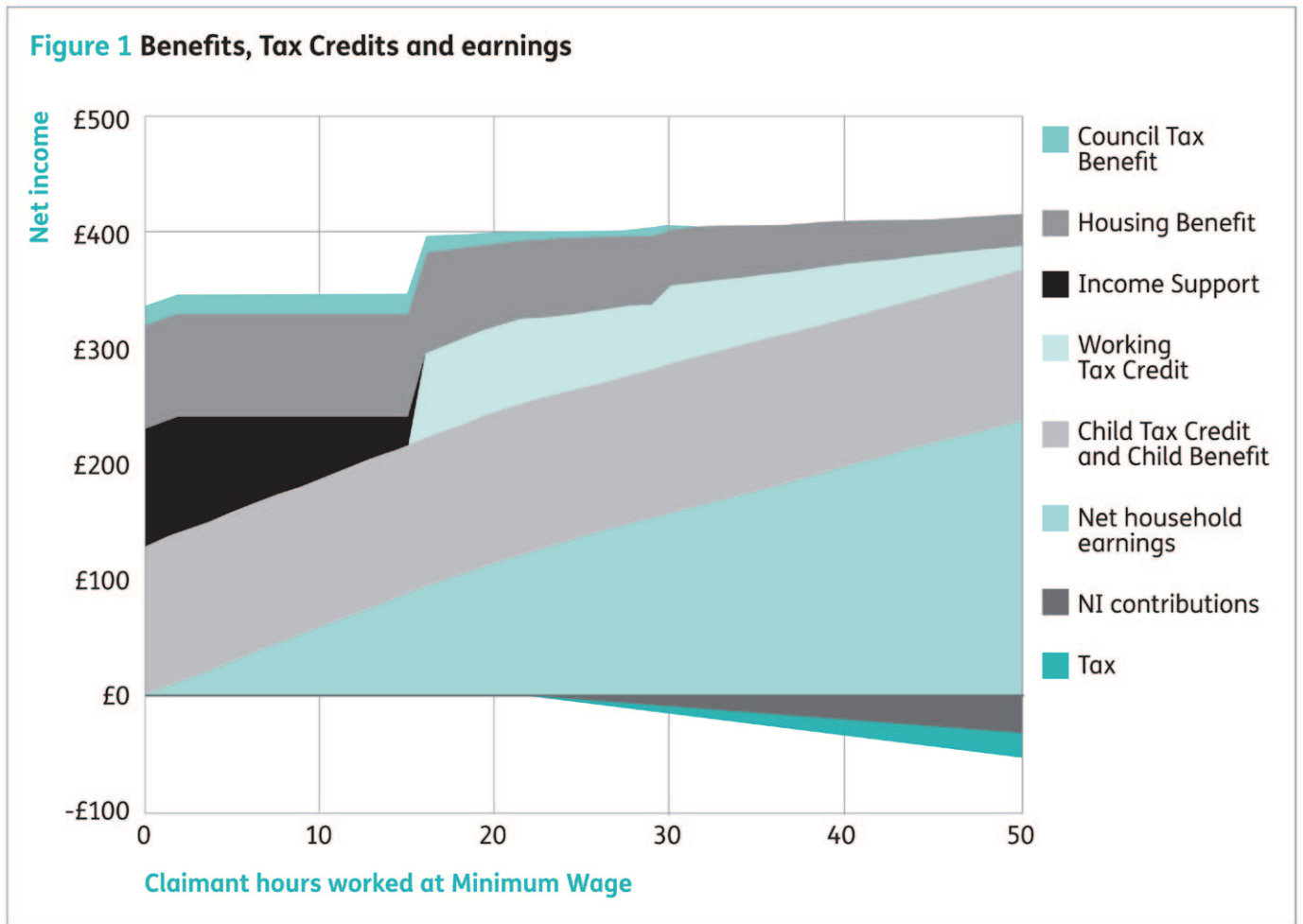
20 **Participation Tax Rate** – the proportion of gross earnings lost in tax and withdrawn benefits.

21 This figure was calculated using the Department's Policy Simulation Model, which is based on the 2007/08 Family Resources Survey and includes the tax and benefit policies announced in the June 2010 Budget. Those modelled as moving into work are assumed to do so at 25 hours at the minimum wage.

22 **Marginal Deduction Rate** – the proportion of an additional £1 in income lost in increased income tax and NI contributions and in reduced benefit and Tax Credit payments.

23 HM Treasury, June 2010, *Budget 2010*. The table shows people working over 16 hours a week and receiving income-related benefits or Tax Credits.

24 The changes in the June 2010 Budget will increase the maximum Marginal Deduction Rate to 95.95 per cent.



19. Leaving the security of the benefits system is made harder by uncertainty about how to get benefits reinstated quickly if the job does not work out. Distinct in-work benefits have failed to convince some people to make the transition to work. People often worry about the loss of Housing Benefit when they are thinking of returning to work, or are concerned that their Working Tax Credit may not be accurate or paid quickly enough.²⁵
20. People planning a move into work have understandable concerns about how they will support their families during the transition. They ask themselves: “Will the in-work benefits kick in quickly enough to fill the gap before my pay arrives?” and “How long will it take to get out-of-work benefits again if the job does not work out?”.

²⁵ Gloster, R et al, 2010, *Lone Parent Obligations: Early findings of implementation as well as experiences of the Income Support and Jobseeker's Allowance regimes*. Department for Work and Pensions Research Report No. 645.

21. The complexity of the system means that these legitimate questions can be difficult to answer. The fear and uncertainty that people experience when thinking about returning to work is real and understandable. For many, the world of work is an unknown that raises feelings of apprehension. Underpinning their fears is the perception that the rewards from working are small, leaving people feeling that they are being punished for working while their neighbours are rewarded for doing nothing.
22. As a result, working legitimately is not a rational choice for many poor people to make. Fraud is always wrong, but we must recognise that the benefits system is making matters worse by pushing valuable work, and the aspiration that this can engender, underground.²⁶

Box 1 Case study: weak work incentives in the current system

Ms A, a lone parent with three school-age children, earns £7.50 an hour as an office administrator. She is working 23 hours a week, which gives her a net weekly income (including benefits and Tax Credits) of £345 after paying rent and Council Tax. She has been offered the opportunity to work for 34 hours a week. However, this extra effort would only give her about £10 more, so she has very little incentive to take on the extra work.

Question 2

Which aspects of the current benefits and Tax Credits system in particular lead to the widely held view that work does not pay for benefit recipients?

The system is too complex

23. The complexity of the system is also a barrier in itself. Successive attempts to adapt the benefits system to meet immediate priorities have resulted in layer upon layer of ill-fitting changes, often with long periods of transitional protection, adding steadily to the complexity.
24. There are three basic income-maintenance benefits for people who are out of work: Jobseeker's Allowance, Employment and Support Allowance (replacing Incapacity Benefit) and Income Support, all paid by the Department for Work and Pensions and often providing the same level of financial support. These benefits combine with Housing Benefit, Council Tax Benefit, Child Tax Credit and – for people moving into work – Working Tax Credit to create an elaborate and confusing tangle of support. Added to this are contributory and universal benefits which create further benefit interactions.

²⁶ Barbour A, 2008, *Work Incentives in the benefits system: Increasing levels of Earnings Disregard*, Community links Evidence No. 12; SPARK Research, 2004, *A Review of the DWP Benefit Fraud Sanctions Regime*, Department for Work and Pensions In-house report.

14 Chapter 2 Problems with the current system

25. This complexity is inefficient, with customers having to go through multiple application processes with different thresholds, rules and payment periods. It also increases the risk of error, creates opportunities for fraud and puts decisions on benefit expenditure beyond effective democratic scrutiny.²⁷
26. The overlaps in what people can receive are significant. People can get support from different benefits and different benefits support the same needs. A lone parent with a young child, for example, might be receiving Income Support, Child Benefit, Child Tax Credit, Housing Benefit, Council Tax Benefit and a series of other 'passport' benefits, each with their own eligibility criteria and rules.
27. Many people have to deal with more than one agency. Nearly half of the six million people getting benefits from the Department for Work and Pensions also get Housing Benefit from a Local Authority. Around 1.6 million people receive a Department for Work and Pensions benefit and some Tax Credits from HM Revenue & Customs. About a third of Housing Benefit claimants also receive Tax Credits and have to deal with both HM Revenue & Customs and their Local Authority. This includes virtually all families with children on Housing Benefit.
28. Research shows that this complexity makes it difficult for people to know what benefits and Tax Credits they can get. Sometimes people are overpaid Tax Credits and have to return money later. Complexity undermines trust in the system and stops customers focusing on getting back to work.²⁸ People may fail to take up their entitlements. The transition between benefits and work can also cause severe financial hardship and emotional stress.²⁹ People from ethnic minority groups are more likely to have English as their second language and so may have particular difficulty with benefit complexity.³⁰

Box 2 Case study: transitions between benefits

Mr B is claiming Jobseeker's Allowance. After suffering an accident, he loses entitlement to Jobseeker's Allowance because his work capability is limited. He needs to claim the Employment and Support Allowance to continue to receive financial support. Any delay in making this claim could mean that he loses money and he could also lose support for his rent and Council Tax. It can take Jobcentre Plus a week or two to sort out Mr B's Employment and Support Allowance claim, during which time he may need to claim a Social Fund Crisis Loan to pay for food and other living expenses. After three months, Mr B has recovered enough to start looking for work again. His Employment and Support Allowance then ends and he has to claim Jobseeker's Allowance again.

Question 3

To what extent is the complexity of the system deterring some people from moving into work?

27 Martin, D, 2009, *Benefit simplification: How, and why, it must be done*, Centre for Policy Studies.

28 Community Links, Low Incomes Tax Reform Group, CPAG, 2007, *Interact: benefits, Tax Credits and moving into work*; (2010) Royston, S, 2007, *Benefit simplification and the customer*, Department for Work and Pensions paper www.dwp.gov.uk/docs/simplification-and-the-customer.pdf; Sainsbury R and Weston K, 2010, *Exploratory qualitative research on the 'Single Working Age Benefit'*.

29 Department for Work and Pensions Customer Insight evidence, 2010, *Single Working Age Benefit findings*, www.dwp.gov.uk/docs/customer-insight-single-working-age-benefit.pdf

30 Disability Alliance (2003), *Out of Sight – Race Inequality in the benefit system*.

Complexity in delivery

“The Department for Work and Pensions issues a total of 14 manuals, with a total of 8,690 pages, to its decision makers to help them to apply Department for Work and Pensions benefit rules correctly. A separate set of four volumes totalling over 1,200 pages covers Housing and Council Tax Benefits, which are primarily the responsibility of local authorities. The Tax Credits manual used by HM Revenue & Customs is a further 260 pages, even though it omits details for many relevant tax concepts which are found in other tax manuals. In addition to these encyclopaedic works is a cornucopia of circulars, news releases and guidance notes issued to professionals and claimants. The underlying legal statutes and statutory instruments make up a vast mass of further material.”
(from David Martin, *Benefit Simplification: How, and why, it must be done*³¹).

29. Given the range of benefits and agencies, it is hardly surprising that delivery is also fragmented and complex, requiring customers to make multiple contacts with different organisations. Applying for, varying or leaving benefits still requires too much paperwork from too many different government agencies and too much unproductive time dealing with officials either face-to-face or on the phone.
30. Customers may be required to communicate changes of circumstance separately to Jobcentre Plus, the Pension, Disability and Carers Service, the Local Authority and HM Revenue & Customs so that adjustments can be made to payments they receive. In many circumstances, the same information is requested several times over. This increases the number of unnecessary customer contacts, at a cost to both the customer and the taxpayer, and creates potential for error and fraud.
31. When people do move into work, delays in payment can occur as claims stop and start and entitlement is reassessed. This can affect crucial support, including in-work Housing Benefit and Council Tax Benefit. A significant number of people each year transfer between Jobseeker’s Allowance and incapacity benefits alone, even though the claim is with the same agency.
32. Delays in awarding or reassessing entitlement cause negative experiences of the general service.^{32,33} The resulting overpayments (and subsequent repayments) can affect those least able to cope with fluctuations in their relatively low levels of household income which can create stress and mistrust of the system.

Question 4

To what extent is structural reform needed to deliver customer service improvements, drive down administration costs and cut the levels of error, overpayments and fraud?

31 Martin, D, 2009, *Benefit Simplification: How, and why, it must be done*, Centre for Policy Studies.

32 Gloster, R et al, 2010, *Lone Parent Obligations: Early findings of implementation as well as experiences of the Income Support and Jobseeker’s Allowance regimes*. Department for Work and Pensions Research Report 645.

33 Department for Work and Pensions Customer Insight evidence, 2010, *Well enough to work findings*, www.dwp.gov.uk/docs/customer-insight-well-enough-to-work.pdf.

Conclusion

33. The Government has strong ambitions for the benefit system. The current problems and experience from previous reforms suggest that structural reform of the benefits and Tax Credits system as a whole may be needed to address the key problems of work incentives and complexity. In the next chapter we look at how we might do this and outline a set of principles to guide reform. In addition, there are complex interactions with other forms of welfare support for basic needs (for example, the financing of affordable housing provision and sub-market rents) and different options for delivery of a reformed system. Chapters 4 and 5 explore these.

Principles and options for reform

3

Summary

We have set out seven principles for reform which could guide the detailed design of the system.

This chapter outlines illustrative examples of how structural reform might look, including options presented by external organisations.

While they do it in different ways, these models all ensure that clearer gains are available as individuals move into and progress in work, and attempt to ensure that dependency is reduced in the longer term in order to improve the affordability of the system.

More work will also be needed to ensure that the specific design issues outlined are addressed, and that the relative costs and benefits of different reform options are assessed.

Principles for reform

1. We would propose to use a set of principles to guide reform. They could be to:
 - ensure that people can see that the clear rewards from taking all types of work outweigh the risks;
 - further incentivise and encourage households and families to move into work and to increase the amount of work they do, by improving the rewards from work at low earnings, and helping them keep more of their earnings as they work harder;
 - increase fairness between different groups of benefit recipients and between recipients and the taxpayer;
 - continue to support those most in need and reduce the numbers of workless households and children in poverty and ensure that interactions with other systems of support for basic needs are considered;
 - promote responsibility and positive behaviour, doing more to reward saving, strengthening the family and, in tandem with improving incentives, reinforcing conditionality;
 - automate processes and maximise self service, to reduce the scope for fraud, error and overpayments. This could include a responsive and immediate service that saves the taxpayer significant amounts of money and ensures compliance costs for employers, at worst, no worse than under the current system; and
 - ensure that the benefits and Tax Credits system is affordable in the short and longer term.

Question 5

Has the Government identified the right set of principles to use to guide reform?

A simpler system with improved work incentives

2. In order to put our principles into practice it is essential to improve work incentives. Different approaches could be designed to give greater emphasis to either increasing the incentive to take up work, or to increasing the incentive to increase earnings once in work. Striking a balance between these elements will be important.
3. With this in mind, there are two key areas where structural reform of the system could focus: firstly, the number and types of benefits and Tax Credits available should be considered; and secondly the way in which entitlements are withdrawn as individuals move into and progress in work could be adjusted.
4. The models outlined below consider these areas, and demonstrate the range of choices that structural reform would need to consider. Chapter 5 considers how reform of welfare delivery could also deliver improvements to the system.

A Universal Credit

5. A Universal Credit would be a new approach to supporting working-age households. It represents a move towards a system that brings together existing income-related out-of-work benefits and Tax Credits into a simpler, integrated system that supports people in and out of work. This builds on recommendations from a number of organisations from across the social policy field.³⁴ It would:
 - combine elements of the current income-related benefits and Tax Credits systems;
 - bring out-of-work and in-work support together in a single system; and
 - supplement household earnings through credit payments, reflecting circumstances (including children, housing and disability).
6. Such a structure would remove much of the complexity that burdens the system today. Crucially it would also create the platform for tackling the current problems of high Marginal Deduction Rates and low gains to work through reform of earnings disregards and tapers.

Box 3 How might a Universal Credit work?

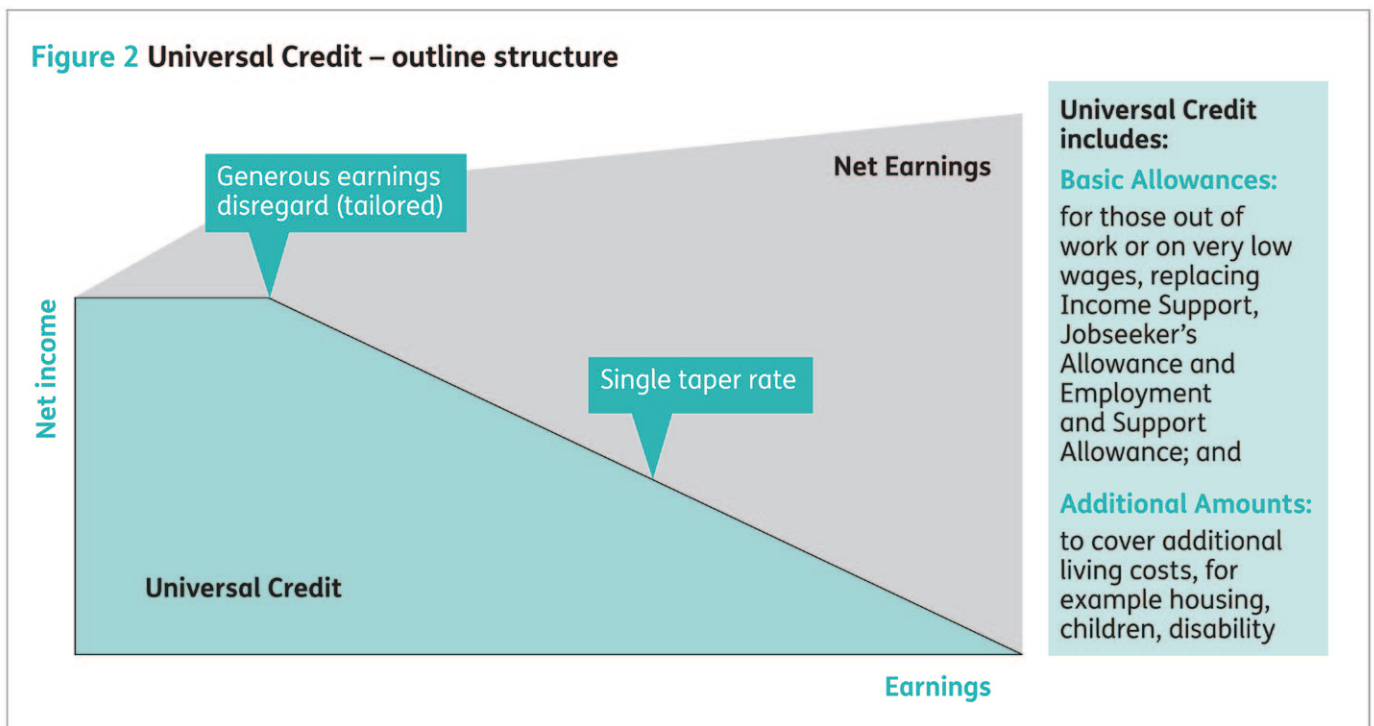
- **What would I get if I was out of work?** The family's gross entitlement would depend on their circumstances. Entitlements would be based on current benefit and Tax Credit rules, with amounts for individuals, couples, children, housing, disability or caring. The total would then be reduced for earnings and other income to produce the net amount payable. The credit would be payable to the household member making the application.
- **How would Universal Credit support me to move into and progress in work?** Household members would be incentivised to enter work by a consistent, reasonable, rate of withdrawal of the Universal Credit as earnings increase. The incentive would be reinforced through a system of disregards, which would leave Universal Credit payments unaffected by the first few hours of earnings.
- **What would happen to Tax Credits?** A Universal Credit would subsume Tax Credits as the form of income top-up for families on low earnings, including support for childcare.
- **How would this be delivered?** Universal Credit would be delivered through a new system which would use up-to-date earnings information from employers to calculate Universal Credit on a household basis – see chapter 5.
- **What would happen to the Work Capability Assessment?** This would still be needed to assess applications from customers unable to work through sickness or disability.

³⁴ Martin D, 2009, *Benefit Simplification: How and why it must be done*, Centre for Policy Studies; Centre for Social Justice, 2009, *Dynamic Benefits: Towards welfare that works*; Brewer M, Saez E and Shephard A, 2008, *Means Testing and Tax Rates on earnings*, Institute for Fiscal Studies.

Universal Credit – outline structure

7. Figure 2 below shows a possible outline structure for a Universal Credit system. For someone who is not working it would integrate a range of existing benefits and Tax Credits into a single payment. The amount received would depend on needs and circumstances. The Universal Credit could include the following elements of support, as appropriate:

- basic income replacement for single people and couples similar to the rates of Jobseeker's Allowance, Income Support and Employment and Support Allowance;
- help with mortgage interest and other housing costs currently available through those benefits;
- help with rent and council tax currently provided through Housing Benefit and Council Tax Benefit; and
- extra help for families in place of Child Tax Credit.



8. As we develop thinking on detailed rules, there might be scope to simplify and improve the focus of some of these elements of support relative to their current design. We would in any case separately consider the role of additional income-related payments for disability as we develop ideas on disability benefit reform. It would not, however, be our intention to use Universal Credit reform to reduce the levels of support for people in the most vulnerable circumstances. At the appropriate stage, we will assess the impact of our proposals on vulnerable groups.

9. The Universal Credit would gradually be reduced as post-tax household incomes rose. Entitlement to support would be available to people out of work and those with low earnings. There would continue to be some non-means-tested support, including contributory entitlements for people who have paid National Insurance contributions, but generally the amount of benefit payable would depend on the level of household income and savings. The impact of earnings on entitlement would be worked out using a system of disregards and a single Universal Credit withdrawal rate.
10. Alongside development of online services this could mean that people claiming Universal Credit would have access to a clear statement showing their earnings and entitlement to the Universal Credit in one place. This would be a huge improvement on the current system in which people have no access to a single statement of their entitlements.

Disregards and tapers

11. Chapter 2 highlighted the problem of poor financial work incentives and uncertainty, making people feel that it is not worth their while to take a job or to increase their hours.
12. To improve incentives to work (especially for low earners), people entering paid work would ideally see no reduction in their Universal Credit until they earn over a certain level (the earnings disregard). The level of this earnings disregard might depend on household circumstances. We would need to consider further, in the light of fiscal circumstances, how best to design the disregards. However, it may make sense to provide larger disregards for some groups, such as families bringing up children.
13. In order further to improve the incentive to earn more, the system might involve applying a single taper to reduce the Universal Credit where earnings (net of tax and National Insurance) exceed the level of the earnings disregard. This taper could apply to all earnings, regardless of the number of hours worked. It could also provide a single withdrawal rate in place of the current different withdrawal rates across out-of-work benefits, Tax Credits, Housing Benefit and Council Tax Benefit. Currently, these interact in complicated ways and produce very high overall Marginal Deduction Rates for many people.
14. A single withdrawal rate would make it clearer and simpler to calculate the financial gains from work and for people to be confident of being better off by taking a job and progressing to more hours and higher pay once in work.
15. In the current fiscal climate we need to strike a balance between incentives and affordability. This trade-off would, in particular, affect the rate of withdrawal that is feasible if a Universal Credit is introduced.

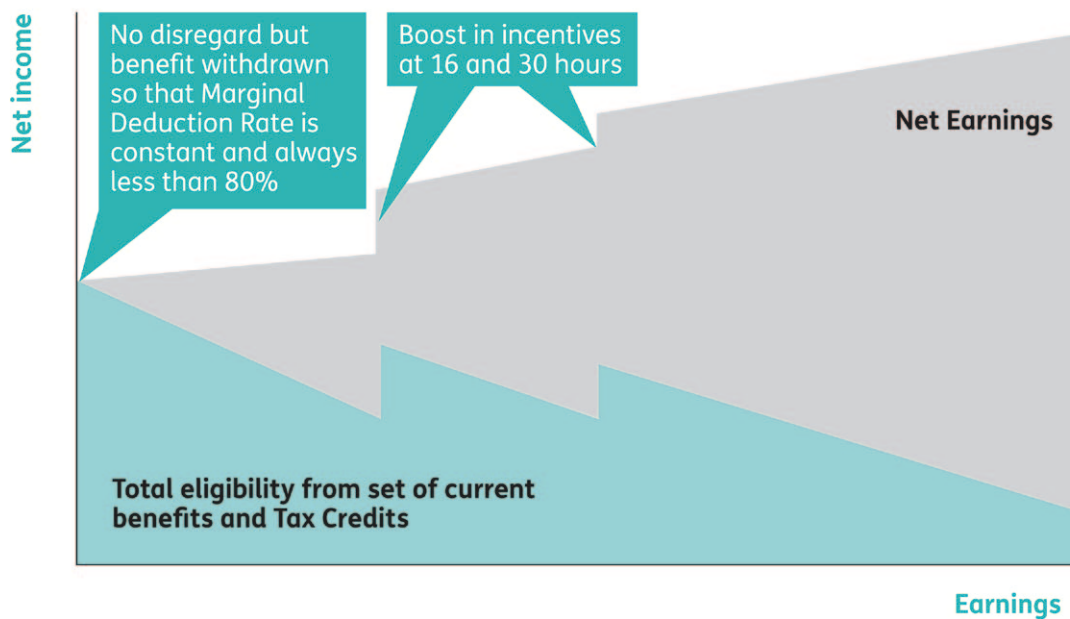
16. However, by way of illustration, for people paying Income Tax at 20p in the pound and National Insurance contributions at 12p in the pound, a withdrawal rate of 55 per cent would lead to an overall Marginal Deduction Rate of 69.4 per cent; a withdrawal rate of 70 per cent would lead to an overall Marginal Deduction Rate of 79.6 per cent. This compares with a current Marginal Deduction Rate of 73 per cent for people getting Working Tax Credit or Child Tax Credit only, 90.55 per cent for people getting Housing Benefit in addition to Tax Credits and 95.95 per cent for people getting Tax Credits, Housing Benefit and Council Tax Benefit.

A Single Unified Taper

17. A Single Unified Taper would retain a set of benefits reflecting that different families need support for different reasons. This means that both the major out-of-work benefits and the system of Tax Credits would be retained. However, we could also consider reform of certain benefits within or alongside a new structure. It would not be our intention to use reform to reduce the levels of support for people in the most vulnerable circumstances. Overall the total number of benefits available could be reduced and the system simplified.
18. It is hoped the model could then be delivered according to the principles of a reformed delivery system outlined in chapter 5. Once eligibility has been calculated, the system could work without earnings disregards and withdraw benefit entitlement in such a way that a person's Marginal Deduction Rate is constant until benefit receipt is exhausted.
19. As an individual increased their income, withdrawal would be through a taper that would be applied to their overall benefit eligibility, rather than the individual benefits as is currently the case. This would remove the complex interactions that currently cause high Marginal Deduction Rates. As an example, if the Single Unified Taper were set at 75 per cent:
- an out-of-work individual, or an individual with earnings below the threshold where they began to pay tax and National Insurance contributions, would face a taper rate of 75 per cent. This would be applied to their overall benefit receipt, not individual benefits, meaning that this would also be their Marginal Deduction Rate: they would increase their net income by £2.50 for every £10 they earned; and
 - an individual with earnings above the threshold for paying tax and National Insurance contributions would face a taper rate on their overall benefit receipt of 43 per cent as they increased their earnings. Combined with the tax they paid (32 per cent income tax and National Insurance) this would lead them to the same Marginal Deduction Rate of 75 per cent: they would increase their net income by £2.50 for every extra £10 they earned.

20. This would mean that individuals on benefits or Tax Credits keep the same amount of every pound they earn as they move into and progress in work. Thus, for every decision about entering or progressing in work, the claimant could know the exact amount they will keep after benefits and Tax Credits have been withdrawn.
21. As well as making current incentives more clear, such a system could also improve the incentive to enter work and to progress to higher incomes by reducing Marginal Deduction Rates and Participation Tax Rates. This is particularly true for those on low incomes and those on out-of-work benefits who currently have benefit withdrawn pound for pound with earnings. By retaining separate out-of-work benefits and Tax Credits, this approach also provides targeted incentives for people to increase their hours of work. Figure 3 shows how this could work. A balance between incentives and affordability would need to be struck when considering the rate at which the Single Unified Taper was set.

Figure 3 The Single Unified Taper



Box 4 How might a Single Unified Taper work?

- **What would I get if I was out of work?** The family's gross entitlement would depend on their circumstances and would be broadly similar to today's system as the majority of the current benefits and Tax Credits would be retained. The total would then be reduced for earnings and other income to produce the net amount payable. The credit would be payable to the household member making the application.
- **How would Single Unified Taper support me to move into and progress in work?** Household members would be incentivised to enter work by a consistent, reasonable, rate of withdrawal of benefits as earnings increase. This would be lower than the current 100 per cent withdrawal of benefits as claimants move into work.
- **What would happen to Tax Credits?** Tax Credits would be maintained to provide targeted support for families to enter and progress in work.
- **How would this be delivered?** The Single Unified Taper would be delivered through a new system which would use up-to-date earnings information from employers to calculate the Single Unified Taper on a household basis – see Chapter 5.
- **What would happen to the Work Capability Assessment?** This would still be needed to assess applications from customers unable to work through sickness or disability.

Single Working Age Benefit

22. The Institute for Public Policy Research have proposed a model for a Single Working Age Benefit.³⁵ This concept of a single benefit is a simple flat rate benefit that would give all working age claimants the same level of replacement income, regardless of whether they were jobseekers, lone parents, sick or disabled.
23. The other key features of this model would be:
 - no contributory entitlement (the paper argues that the contributory principle in working age benefits is misunderstood and of little real value);
 - a universal non-means-tested entitlement for the first 12 weeks out of work;
 - all benefit beyond 12 weeks to be means-tested; and
 - the option of individualised entitlement for couples.
24. The Institute for Public Policy Research envisage that the Single Working Age Benefit would replace existing out-of-work benefits. It assumes that there would continue to be separate provision for extra costs and that Tax Credits would remain as now.

³⁵ Sainsbury R and Stanley K, 2007, *One for all: active welfare and the single working age benefit*, Institute for Public Policy Research.

Mirrlees model

25. The Mirrlees model, proposed by the Institute for Fiscal Studies,³⁶ uses optimal tax theory to design an efficient system of household tax and transfer programmes. This model would replace Child Tax Credit, Working Tax Credit, Income Support/Jobseeker's Allowance, Housing Benefit, Council Tax Benefit and Child Benefit with an integrated 'family allowance' paid directly into bank accounts and withdrawn using the withholding system for Income Tax.
26. The allowance would be far less generous than current Income Support levels (£50 for a single person), but earnings up to £90 would have no impact on the allowance, and earnings above this subject to a 30 per cent withdrawal rate (with an additional 15 per cent on the housing element). Tax allowances would be adjusted so that tax and NI would be payable once the earnings disregard had been exhausted.
27. The model would replace all family benefits, housing support and Tax Credits and assumes that the family allowance would be tapered through the tax system. Support for families out of work would be substantially less than current benefits. The Mirrlees model represents a more complete integration of Income Tax and benefits than some other models.

Single benefit/negative income tax model

28. The TaxPayers' Alliance³⁷ recently published a report that recommends a reform that brings together a large number of the existing benefits. However, unlike other approaches that introduce a single benefit, it suggests the introduction of a negative income tax. This would replace current income-replacement benefits and tax credits. Alongside this, they suggest the maintenance of a number of the current benefits aimed at supporting those with a limited ability to work or who need extra support.
29. A household's eligibility for the negative income tax would be based on their characteristics, and set equal to a given proportion of (equivalised) median income. As household income increased from individuals moving into work or progressing in work, the level of the negative income tax would be reduced in such a way that the Marginal Deduction Rate (inclusive of Income Tax, NI contributions and the withdrawal of the negative income tax) was constant until all support was exhausted. This implies that the system does not have a system of earnings disregards.

36 J. Mirrlees, S. Adam, T. Besley, R. Blundell, S. Bond, R. Chote, M. Gammie, P. Johnson, G. Myles and J. Poterba (eds), April 2010, *Dimensions of Tax Design: the Mirrlees Review*, OUP.

37 Taylor C, Denham M, Baron R and Allum A, *Welfare Reform in Tough Fiscal Times: Creating a Better and Cheaper Benefit System* The TaxPayers' Alliance, July 2010.

Question 6

Would an approach along the lines of the models set out in chapter 3 improve work incentives and hence help the Government to reduce costs and tackle welfare dependency and poverty? Which elements would be most successful? What other approaches should the Government consider?

Conclusion

30. There are a number of different approaches to simplifying benefits and Tax Credits that could improve work incentives and make the available support easier to understand. This chapter has explored some of the different options available. We will also look at targeted measures for increasing work incentives and reducing the extent and costs of welfare dependency alongside consideration of structural reform.

Other areas of reform

4

Summary

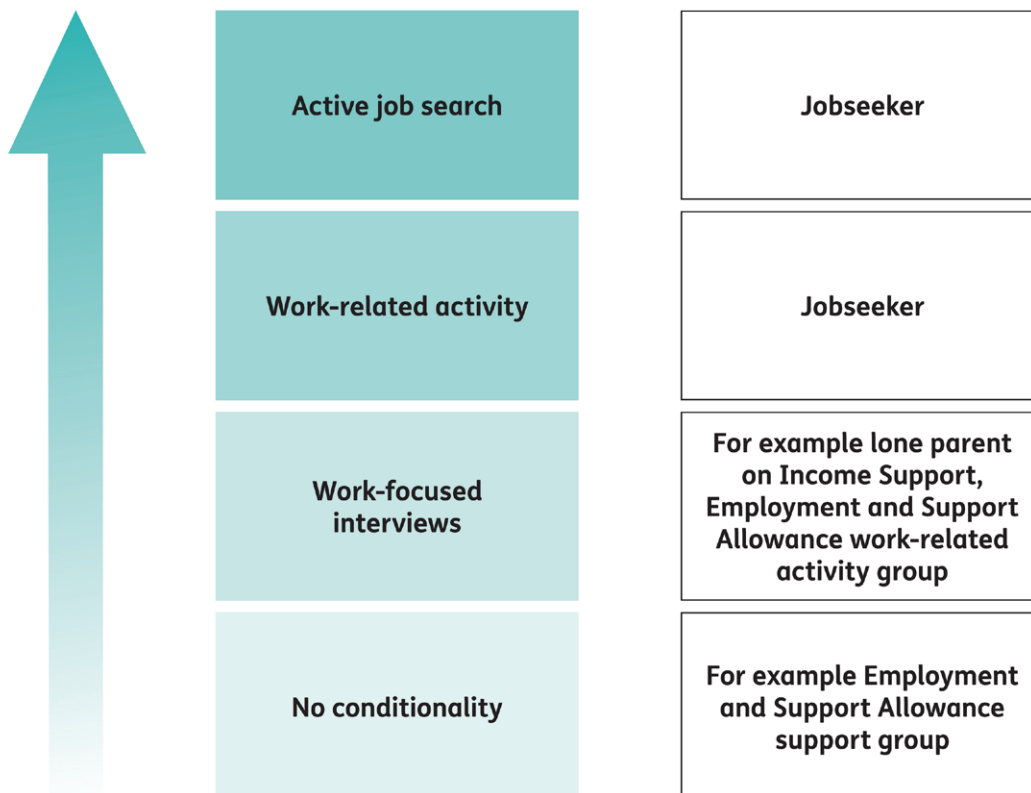
The potential for structural reform to the benefits and tax system brings with it the opportunity to consider other reforms of the system. External organisations have suggested that it is important to consider the role of conditionality and the contributory principle in reinforcing work incentives and providing support. There are also wider questions over the role of localism in the delivery of system welfare.

- Chapter 3 set out a number of options for structural reforms of the welfare system that could improve work incentives. Many of the reforms suggested by external organisations suggest that the role of the current system of conditionality and contributory benefits should be considered alongside potential structural reforms.

Conditionality

- Individuals who are able to look for work or prepare for work should be required to do so as a condition for receiving benefit and those who fail to meet their responsibilities should face a sanction such as a benefit reduction. This is known as conditionality. Evidence shows conditionality is effective in reducing unemployment. So it is essential that any changes to the structure of support are underpinned by clear expectations about what claimants need to do in return for the support they receive. In particular, any new arrangements should not water down the current conditionality for jobseekers.

Figure 4 Conditionality



3. In the current system the benefit claimed determines the level of conditionality. Generally Jobseeker's Allowance claimants must engage in active job search, with powers to extend conditions the longer a person is out of work. Evidence shows conditionality is effective in reducing unemployment. Any future reforms should seek to build on that success. Lone parents on Income Support and people in the Employment and Support Allowance work-related activity group must attend work-focused interviews. Figure 4 on the previous page illustrates the current system of conditionality for people on out-of-work benefits.
4. Some of the structural reforms could merge many of these benefits into a single payment. This creates the possibility that the level of conditionality would be determined, not by the benefit received, but by the reason for receiving benefit, creating a single progression to higher levels of conditionality. Structural reforms could also remove the distinction between in- and out-of-work benefits, enabling a new approach to conditionality that aimed to incentivise people to enter work and progress – increasing hours and earnings until they move off benefits altogether.
5. This would raise the issue of when a person is deemed to be doing enough work such that we would stop applying work-related conditions to their benefit. For example, it may not be sensible to cease applying conditions as soon as a person earns any income as that would increase the temptation for some people to remain working for just a few hours, thereby increasing welfare costs and fostering dependency rather than self sufficiency. We ought to look at applying conditionality in a way that pushes individuals to increase their work to levels that are appropriate to their own particular circumstances. For instance:

- **A single person working 17 hours a week at the National Minimum Wage.** Under the current system, no conditionality applies despite the fact that the individual may be claiming a range of benefits. Under a new system we could continue to apply conditionality to push that individual to extend their working hours and/or increase their earnings until they were working full time or until they were off benefits altogether.
- **Jobseekers.** Currently most Jobseeker's Allowance claimants are required to look for full-time work. In the future, for some individuals (for example, where the person had been away from the labour market for many years) conditionality could initially be used to move a person into work for a few hours. This work experience combined with ongoing conditionality could act as a stepping stone into sustained full-time work. The existing system may hamper the first step of this journey by requiring an immediate focus on full-time work, regardless of individual circumstances.
- **Benefit claimants who currently have no work search conditionality applied (for example because of ill health or caring responsibilities).** We could apply conditionality to match financial incentives for working even relatively short hours where appropriate – requiring some people to look for or prepare for work of a few hours a week in line with their capability and circumstances – and extend conditionality as an individual's circumstances change (for example, when their health improves).

6. Such an approach would require careful consideration to ensure that a personalised conditionality regime did not dilute or undermine the current success of conditionality in incentivising and promoting work. Our key aim is to make it much clearer that the commitment to work is the foundation of the benefits system for people of working age. This is at the heart of our thinking. We could ask everyone who is able to work, or to take steps to prepare for work, to sign a document setting out their obligations and the activity required to satisfy those obligations.
7. For those who fail to meet their obligations we may withdraw their benefit until they demonstrate that they have re-engaged with their personalised set of commitments. For those closest to the labour market this loss of benefit for the period of their non-compliance may be permanent. For others, some or all of their withheld benefit may be paid to them once they demonstrate re-engagement. We could explore the role that non-financial sanctions can play in encouraging compliance. We could also look again at the way the current safeguards against the risk of hardship operate and whether they need modernising to ensure that our wider reforms work effectively for everyone. However, financial support for people who are not able to work, or prepare for work, would remain unconditional.

Question 7

Do you think we should increase the obligations on benefit claimants who can work to take the steps necessary to seek and enter work?

Question 8

Do you think that we should have a system of conditionality which aims to maximise the amount of work a person does, consistent with their personal circumstances?

Localisation

8. The UK has a highly centralised system of benefit design and delivery. There are a number of advantages to this, not least in terms of economies of scale and ensuring national safety nets. However, a number of other countries, including Switzerland, the Netherlands and the United States, operate more devolved welfare systems, which can stimulate innovation and ensure that systems are more aligned to local circumstances.
9. There are a number of options for moving to a less centralised welfare system. In terms of incremental reform there could be more discretion to advisers at the local level – currently there are limited funding streams (the Adviser Discretionary Fund) and little wider autonomy at Jobcentre Plus district level.

Question 9

If you agree that there should be greater localism what local flexibility would be required to deliver this?

Linkages with other forms of labour market and welfare support

10. The benefits system is not the only way in which the Government seeks to support those in need. People out of work sometimes need to gain specific skills to enter and progress in employment and training. Any training offered needs to be flexible, responsive and relevant to the labour market and should facilitate the flexibility to continue training once in work. Another example is Government support for the provision of affordable housing and sub market rents. We recognise the imperative to increase the supply of new homes, including new affordable homes, and to ensure sustainable funding for the affordable homes that we already have.

Question 10

The Government is committed to delivering more affordable homes. How could reform best be implemented to ensure providers can continue to deliver the new homes we need and maintain the existing affordable homes?

Contributory Benefits

11. Contributory benefits play an important role in the system. However, reforms will need to consider the balance between contributory benefits and targeting support on those with the lowest incomes.

Northern Ireland

12. Social Security is a devolved matter in Northern Ireland. The Government will continue to work closely with the devolved administration in Northern Ireland to seek to maintain a single system across the United Kingdom.

Conclusion

13. The illustrative options for structural reform outlined in chapter 3 and suggestions from external organisations present us with the opportunity to consider a range of other issues in the current welfare system. As we continue to consider the case for reform, we will consider:
- the scope to strengthen the conditionality regime and ensure that it is aligned with any reforms to the system;
 - the scope for having a more tailored, personalised system in which the conditionality regime for people within certain groups could be extended;
 - the role of localism in delivering the welfare system; and
 - having a system which supports the Government's aim of moving everyone who can work into work and to maximise the percentage of a person's income that comes from their earnings.

Delivery of a reformed system

5

Summary

A 21st century welfare system requires a 21st century delivery solution.

More work would be needed to decide the most cost-effective approach to delivery, including how best to define the relationship between the Department for Work and Pensions' delivery agencies, HM Revenue & Customs and Local Authorities.

We envisage an integrated IT system to manage all claims, and a single payment system to apply a withdrawal rate and pay the correct entitlement. These would not be entirely new systems and could be built on our existing IT and capabilities.

HM Revenue & Customs is consulting employers and payroll providers on mechanisms that could support more frequent or real-time collection of Pay As You Earn data. Such a system could also enable the use of real-time earnings data to calculate net entitlement, removing the need for claimants to notify different agencies when their earnings change.

1. As described in chapter 2, the process of claiming benefits can be complex and confusing, with large numbers of different benefits available for similar or overlapping needs. Customers often have to deal with at least three different layers of national and local government, providing the same information multiple times. A simpler, fairer and less costly system which reduces these difficulties would be welcomed by customers, staff businesses and taxpayers alike.^{38,39}
2. A new delivery system could lessen bureaucracy and reduce the risk for people moving from benefits to work by making the system more responsive to fluctuations in earnings. People would be able to access support without endless form-filling and waiting.

Reforming delivery

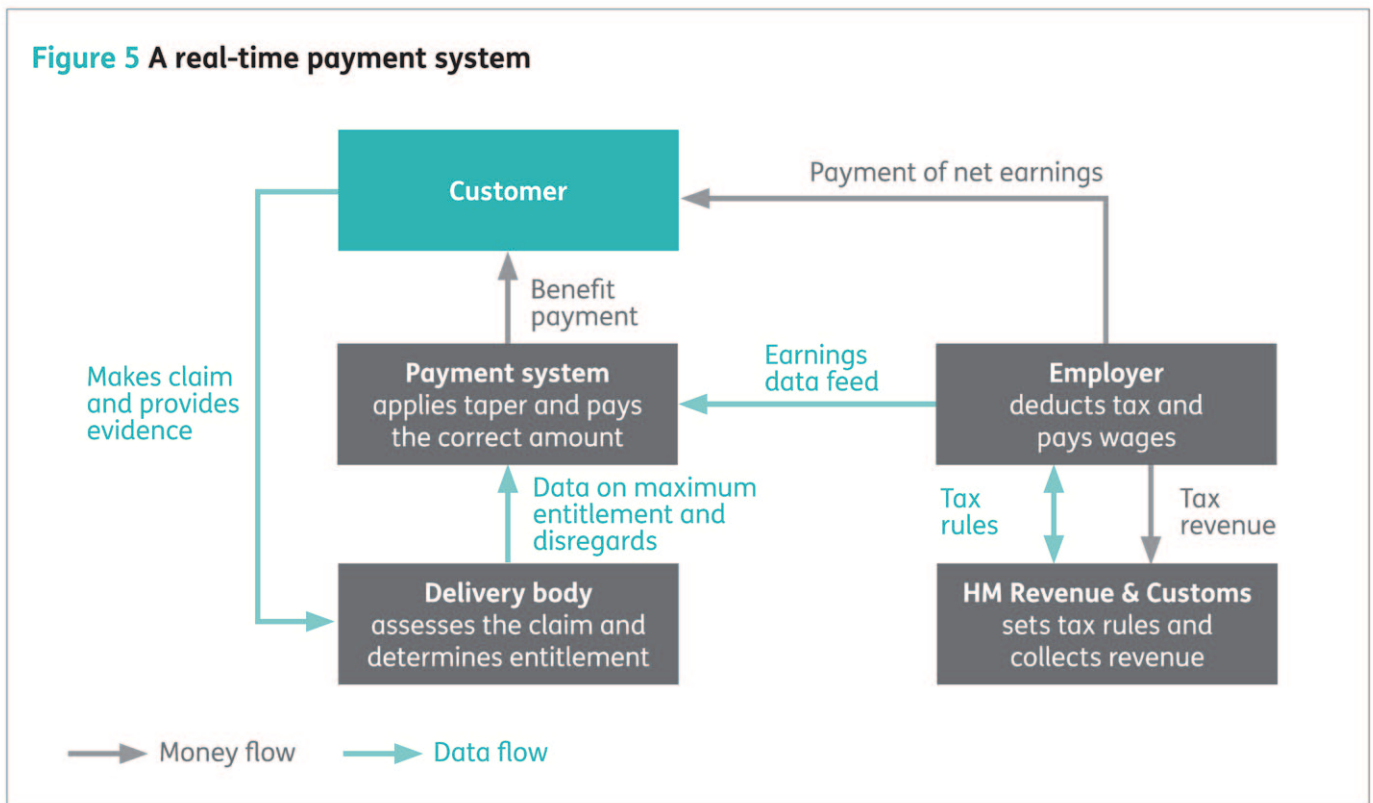
3. Our ideas for structural reform have significant implications for the way support is delivered and for how individuals interact with the system. We will ensure that our approach to delivery maximises the opportunity to increase efficiency, improve customer service and reduce the cost of administration. The goal is a delivery system fit for the 21st Century.
4. The ideas in this paper raise a number of choices about delivery routes. More work will be needed to identify the most cost-effective approach to delivery. Knowledge of our customers will be essential in ensuring that any new system is genuinely simpler and easier to use.
5. We envisage that customers would be able to make a single application for all major entitlements, ending the excessive form-filling of the current system. Within a household, one person would make the claim and receive the payment. The claims process would be as simple as possible and would build on existing plans within the Department for Work and Pensions to develop full online services.
6. We would also need to consider carefully the current organisation of work between the Department for Work and Pensions, HM Revenue & Customs and Local Authorities. We will work with all delivery agencies to establish how delivery can best be integrated and what this might mean in practice not only for all individuals but also for all types of business.

38 Hall, S, 2009, *Spending priorities in the benefits system: Deliberative research with the public*, Department for Work and Pensions Research Report 559.

39 Royston, S, 2007, *Benefit simplification and the customer*, Department for Work and Pensions paper. www.dwp.gov.uk/docs/simplification-and-the-customer.pdf.

Assessing entitlement and making payments

7. The IT changes that would be necessary to deliver a more integrated system would not constitute a major IT project, but two developments building on existing technologies.
8. A system to manage contact with customers, gather evidence and assess a household's entitlement to support could be built using existing technology in everyday use in both the public and private sector.
9. A second system would be required to bring together a household's total entitlement and information on their earnings. It would then use these pieces of information to apply the withdrawal rates and make the correct payment. This payment system could be built around the BACS system which is already used to pay benefits to 96 per cent of Department for Work and Pensions customers. Payments for self-employed people and others not covered by the PAYE system would need to be delivered differently but would be part of the system.
10. Alongside this paper, HM Revenue & Customs is seeking views from employers and payroll providers on mechanisms that could support more frequent or real-time collection of Pay As You Earn data. Under a new system that used real-time data, employers would report their employees' earnings to HM Revenue & Customs at the time those earnings are paid, rather than only at the end of the financial year.
11. Such a system could also present opportunities to use real-time earnings data in the calculation of entitlement. Access to real-time earnings data would remove the need for customers to notify changes of income, and make the system more responsive to fluctuating earnings and movements into or out of work. This could largely resolve the issue of overpayments and subsequent repayments, which hit the poorest hardest.

Figure 5 A real-time payment system

12. However, welfare reform could still be delivered if HM Revenue & Customs does not take forward changes to Pay As You Earn. This could entail a series of fixed period awards with customers required to notify any changes of income; a similar system to this was previously used in Australia.
13. More work will be needed over the coming months to decide on a preferred approach.

Tackling error, overpayments and fraud

14. The causes of error, overpayments and fraud in the current system fall into three categories.
 - The complex and fragmented nature of the system. This causes staff and customer errors and enables customers to represent themselves differently to different parts of the system.
 - Means-testing rules. We rely on customers letting us know about their earnings, savings and other sources of income, which introduces opportunities for error, overpayments and fraud.
 - Rules on non-financial circumstances. We similarly rely on customers letting us know accurately about personal circumstances such as where they live, whether they have a partner and whether they have children.

15. Significantly reducing complexity would allow a customer's details to be seen as a whole. Reducing system complexity should translate into less error and fewer overpayments through fewer mistakes made by staff and customers while navigating the system. Overpayments and subsequent recoveries often lead to hardship amongst those who can least afford those recoveries.
16. Having one main gateway for customers to access the system should make it impossible for customers to represent themselves differently to different parts of an organisation and so would further drive down levels of error, overpayments and fraud.
17. Access to real-time earnings data would allow for a significant reduction in the current levels of error and fraud due to unreported or inaccurately reported earnings, as well as the current high levels of overpayment. A single gateway would also enhance our ability to pick up on error and fraud associated with non-financial customer circumstances. By making intelligent use of data, it could be possible to obtain information on a number of customers who are illegitimately claiming while living with a partner or fraudulently claiming in more than one area.

Transition to a new system

18. A new delivery system would be more straightforward for customers to understand, remove the need for the same information to be collected and held several times over and speed up key parts of the process. This should be considerably more efficient to deliver than the existing system both for Government and for businesses. However, we would need to plan carefully to ensure that we can move customers smoothly and efficiently from the old system to the new. This would be a substantial project, potentially affecting millions of customers and businesses.
19. The introduction of a new system would also need to align with existing plans to better target support and simplify the system by closing previous incapacity benefits and moving people to more active and work-focused regimes (Employment and Support Allowance or Jobseeker's Allowance, depending on their circumstances). We are aiming to re-assess over 1.5 million people on incapacity benefits over a three-year period. We envisage that most people will have migrated onto their new benefit before a new system could be introduced.
20. In planning the transition to the new system, we would be guided by our principles of simplicity, fairness and affordability.

Conclusion

21. To deliver welfare reform we would need to work with all delivery agencies to consider carefully the most cost-effective and efficient delivery structure.
22. A new delivery system would not require a major IT project but two smaller developments to existing infrastructure. If HM Revenue & Customs takes forward reforms to the Pay As You Earn system, real-time earnings data could offer significant opportunities to streamline the payment process and respond more quickly to fluctuations in income.
23. The reduced complexity of the system and access to real-time earnings data could lead to reductions in error, overpayments and fraud.

Question 11

What would be the best way to organise delivery of a reformed system to achieve improvements in outcomes, customer service and efficiency?

Conclusion

6

1. The previous chapters outlined the kind of approach we are considering to address the failings of the current benefits system. These ideas are underpinned by the key aims outlined in chapter 1 of a system which improves work incentives, is fair, protects those most in need and is simpler.
2. Reforms could:
 - improve work incentives by reforming the way in which benefits are tapered as incomes rise and allow people to keep more of their earnings;
 - be fair and targeted to those most in need through tapers which focus payments on those on the lowest incomes, while maintaining levels of support for those out of work; and
 - provide simpler support paid to those in or out of work, by simplifying the complex array of overlapping in- and out-of-work means-tested benefits and Tax Credits.
3. Such changes could enable the Government to reduce worklessness, reduce error and fraud and contain welfare costs without increasing costs to business.
4. These ideas recognise that the rapid withdrawal of benefits and Tax Credits currently provide little incentive for many to enter work, particularly on low pay. Too often, there is little financial reward for greater effort. Benefits, Tax Credits and other support are withdrawn quickly at the same time as liability to Income Tax and National Insurance contributions increase.
5. A single withdrawal rate would make work pay by reducing Participation Tax Rates and Marginal Deduction Rates associated with a move into a job or increased hours of work. It would make gains to work much clearer to see, remove complex transitions between benefits and Tax Credits and would encourage more people to move into work.

6. Our ideas would contain spending on welfare more widely by focusing support to those most in need, building on announcements recently made to target support for Child Tax Credit and Housing Benefit on those with the lowest incomes. A reformed system would be based on the same structure of entitlement for people who are not working as now, including help with housing costs and extra support for families, disabled people and carers.
7. Such a system would reflect a balance between supporting those most in need and rewarding work and responsibility. We will help people to find work, and these reforms will make sure it pays when they do so. They in return will be expected to seek work and take work when it is available.
8. An impact assessment, including an equality impact assessment, will be produced as part of the policy development process for any proposals that follow.
9. By actively putting work at the centre of working-age support we want to create a new contract with the British people. This contract is about a responsible society working together to improve the quality of life for those who are worst off.
10. We would welcome views on the best way forward and in particular on the questions posed throughout this discussion document and repeated in chapter 7.

Questions

7

1. What steps should the Government consider to reduce the cost of the welfare system and reduce welfare dependency and poverty?
2. Which aspects of the current benefits and Tax Credits system in particular lead to the widely held view that work does not pay for benefit recipients?
3. To what extent is the complexity of the system deterring some people from moving into work?
4. To what extent is structural reform needed to deliver customer service improvements, drive down administration costs and cut the levels of error, overpayments and fraud?
5. Has the Government identified the right set of principles to use to guide reform?
6. Would an approach along the lines of the models set out in chapter 3 improve work incentives and hence help the Government to reduce costs and tackle welfare dependency and poverty? Which elements would be most successful? What other approaches should the Government consider?
7. Do you think we should increase the obligations on benefit claimants who can work to take the steps necessary to seek and enter work?
8. Do you think that we should have a system of conditionality which aims to maximise the amount of work a person does, consistent with their personal circumstances?

9. If you agree that there should be greater localism what local flexibility would be required to deliver this?
10. The Government is committed to delivering more affordable homes. How could reform best be implemented to ensure providers can continue to deliver the new homes we need and maintain the existing affordable homes?
11. What would be the best way to organise delivery of a reformed system to achieve improvements in outcomes, customer service and efficiency?
12. Is there anything else you would like to tell us about the proposals in this document?

Annex Seeking views

Purpose of the consultation

1. This discussion document seeks views to inform our thinking on reforms to the benefits and Tax Credits system. We would like to hear from all who are interested. Subject to the outcome of this consultation, we propose to bring forward legislation early in the New Year to reform the current system.

Duration of the consultation

2. The consultation period begins on 30 July 2010 and runs until 1 October 2010.

Consultation arrangements

3. Please send your consultation responses to:

Benefit Reform Division
Department for Work and Pensions
1st Floor
Caxton House
Tothill Street
London SW1H 9NA

Email: benefit.reform@dwp.gsi.gov.uk
Telephone: 020 7449 7688

4. Please ensure your response reaches us by 1 October 2010. We will acknowledge all responses. Please say whether you are responding as an individual, or on behalf of an organisation. If on behalf of an organisation, please make clear who the organisation represents, and how the views of members were obtained.

5. Copies of this publication can be made available in alternative formats if required. We will publish the responses to the consultation in a report on the consultations section of our website www.dwp.gov.uk/consultations. The report will summarise the responses and our next steps.

Freedom of information

6. The information you send us may need to be passed to colleagues within the Department for Work and Pensions, published in a summary of responses received and referred to in the published consultation report.
7. All information contained in your response may be subject to publication or disclosure if requested under the Freedom of Information Act 2000. By providing personal information for the purposes of the public consultation exercise, it is understood that you consent to its disclosure and publication. If this is not the case, you should limit any personal information provided, or remove it completely. If you want the information in your response to the consultation to be kept confidential, you should explain why as part of your response, although we cannot guarantee to do this.

The consultation criteria

8. The consultation is being conducted in line with the Government Code of Practice on Consultation www.berr.gov.uk/whatwedo/bre/consultation-guidance/page44420.html. The seven consultation criteria are:
 - **When to Consult.** Formal consultation should take place at a stage when there is scope to influence the outcome.
 - **Duration of consultation exercises.** The Government Code of Practice on Consultation recommends a minimum 12-week consultation period for public consultations, unless there are good reasons for a limited consultation period. In this case, we are consulting on general principles only. We intend to further consult on specific details as these are developed, and therefore our Minister has agreed that a limited consultation is appropriate.
 - **Clarity of scope and impact.** Consultation documents should be clear about the consultation process, what is being proposed, the scope to influence, and the expected costs and benefits of the proposals.
 - **Accessibility of consultation exercises.** Consultation exercises should be designed to be accessible to, and clearly targeted at, those people the exercise is designed to reach.
 - **The burden of consultation.** Keeping the burden of consultation to a minimum is essential if consultations are to be effective and if consultees' buy-in to the process is to be obtained.

- **Responsiveness of consultation exercises.** Consultation responses should be analysed carefully and clear feedback should be provided to participants following the consultation.
 - **Capacity to consult.** Officials running consultation exercises should seek guidance in how to run an effective consultation exercise, and share what they have learned from the experience.
9. An online version of this consultation will be available shortly after the publication. You can access this from the website:
www.dwp.gov.uk/21st-century-welfare.

Feedback on this consultation

10. We value your feedback on how well we consult. If you have any comments on the process of this consultation, for example, how it could be improved, but not about the issues raised, please contact our Consultation Coordinator:

Roger Pugh
DWP Consultation Coordinator
1st Floor
Crown House
2 Ferensway
Hull HU2 8NF
Email: roger.pugh@dwp.gsi.gov.uk

Impact assessment

11. The purpose of this discussion document is to inform the general direction of reform in the benefit and Tax Credits system. We are seeking views on the ideas covered by this document in order to inform the development of firm proposals. We will assess the impact of our more detailed proposals and we will produce a full Impact Assessment at the appropriate time. We will be considering equality impacts as the policy develops and we will produce an Equality Impact Assessment. During the consultation process we would welcome views on the impact of the ideas on the people covered by equality legislation to inform the Equality Impact Assessment.



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in alternative formats if required.

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