

The Parent Trap: Childcare cuts under Universal Credit

Introduction

Universal Credit will form a crucial part of the government's plans to meet its statutory commitment to eradicate child poverty by 2020, by helping to make work pay for families. In order to succeed, sufficient support must be provided for families facing high childcare costs in work. Accordingly, The Children's Society welcomes the government's decision to extend help with childcare costs through the benefits system to those working under 16 hours per week, who are not currently entitled to receive this support.

However, the government's proposals for support with childcare costs under Universal Credit include a change that will substantially reduce the amount of support which some of Britain's lowest income working families receive. The loss of support with childcare costs through Housing Benefit and potentially Council Tax Benefit, which is addressed in this briefing, is set to cost 100,000 of the lowest income working families up to £4,000 per year in support with childcare.

This is not a simple cut in support, nor can the support simply be replaced. It is the result of restructuring of support, and specifically, the incorporation of Housing Benefit into Universal Credit. However, the impact of this change does need to be recognised, particularly as it disproportionately affects the lowest income working families, and the government needs to consider ways to offset the impact.

Summary

- Currently tax credits cover up to 70% of childcare costs for children in working families. However, many low-income working families can get up to 96% of their childcare costs covered through the benefits and tax credits system. The additional 26% is provided through Housing Benefit and Council Tax Benefit.
- Around 100,000 families (20% of those who receive help with childcare through the benefits and tax credits system) receive this additional support.
- Under Universal Credit, this additional support will be lost. All those entitled will receive 70% of their childcare costs.
- This will leave some of the lowest income working families having to pay up to **seven and a half** times as much towards their childcare costs from their own pocket than they do under the current system.
- Families could face a cut of up to £2,320 per year from their childcare support if they have one child or £3,980 per year if they have two or more children as a result of this change.
- The average loss of support is estimated to be around £23 per week or £1,200 per year.

- Working families living in poverty are **four times** more likely to be affected by this change than families not in poverty who are receiving help with childcare costs through the tax credit system.
- Low-income working families in areas where housing costs are high, such as in the South of England (London, South East, South West), are disproportionately likely to be affected by this change.

1. Current support with childcare costs through benefits and tax credits

Currently working families can get two forms of support with childcare costs through the benefits and tax credits system:

Firstly, they can get support through the childcare element of Working Tax Credit¹. This currently covers up to 70% of childcare costs up to a maximum of £175 for one child or £300 for two or more children.

Secondly, childcare costs are excluded from household income for the purposes of calculating entitlement to Housing Benefit and Council Tax Benefit. This means that a household with childcare costs may be entitled to a higher rate of Housing Benefit and Council Tax Benefit than a household with equivalent earnings but no childcare costs.

This additional disregard is worth up to an additional 26% of childcare costs on top of the 70% covered through tax credits (see Appendix A for the mechanics underlying how this operates). This means that in total, families can receive up to 96% of their childcare costs through the benefits and tax credits system.

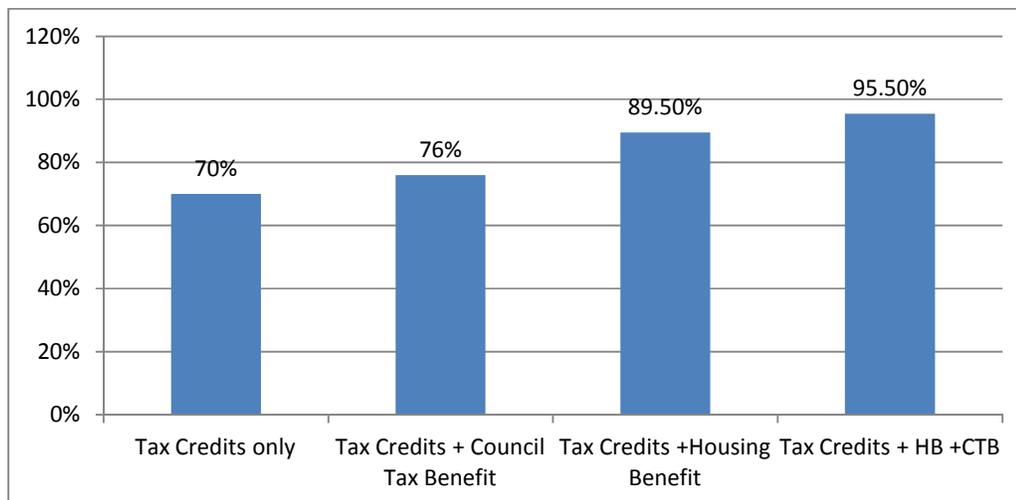
Figure 1 shows the different rates of support with childcare costs that households with varying combinations of benefits and tax credits receive.

As can be seen, for families receiving help with childcare costs through tax credits, of the additional 26% of childcare costs covered through Housing Benefit and Council Tax Benefit, 20% is covered by Housing Benefit and 6% through Council Tax Benefit.

¹ Families can receive the childcare element of Working Tax Credit if they are:

- A lone parent working at least 16 hours per week
- A couple and (a) both working at least 16 hours per week, or (b) one is working at least 16 hours per week and the other is incapacitated, in hospital or in prison.

Figure 1: Rates of support with childcare costs by types of benefit and tax credit received



There is currently no additional support with childcare costs for families with disabled children, and no variation in the level of support by the area of the country in which the family lives.

2. Support with childcare costs under Universal Credit

Under Universal Credit there will be substantial changes to the structure of support through the benefits and tax credits system for families with childcare costs.

Because tax credits and Housing Benefit are both being incorporated within Universal Credit, it will no longer be possible to offer a separate Housing Benefit disregard of childcare costs for Housing Benefit claimants.

Instead, a single 70% rate of support will be offered for childcare costs through Universal Credit, in line with the current rate of support offered through the tax credit system.

The maximum rates of childcare costs for which support can be received will remain the same as at present (£175 for one child, £300 for two or more children).

For the first time, families will be entitled to support with childcare costs through the benefits system when they are working under 16 hours per week.

Council Tax Benefit will not be integrated within Universal Credit. Instead, it is being "localised" with individual local authorities making them responsible for determining their own local schemes of assistance. It is unclear at this stage what these will look like and whether disregards of childcare costs will remain for the purposes of calculating entitlement. In cases where they do remain in place, Council Tax Benefit recipients receiving support with childcare costs through Universal Credit could receive support with up to 76% of their childcare costs (see figure 1).

However, local authorities are being expected to make substantial expenditure savings from Council Tax Benefit, so its future remains very unclear. In addition, claiming support with childcare costs through Council Tax Benefit means committing to regular reporting of childcare costs to the local authority. Given this, it is questionable whether parents will

consider it worth claiming such support where it only covers an additional 6% of their childcare costs.

4. What will this mean for families with childcare costs?

While it is a positive step that the government has extended support with childcare costs to those working under 16 hours per week, we are also concerned that the loss of a disregard of childcare costs for the purposes of Housing Benefit (and potentially Council Tax Benefit) under Universal Credit could leave some families considerably worse off than they are at present.

For example, the following case shows household income under the current system and Universal Credit for a lone parent with two one year old children, both in childcare, with total childcare costs of £250 per week (£125 for each child – around the national average for 30 hours of childcare²).

Case 1:

A lone parent with two children aged one, working 30 hours per week and earning £300, with £250 per week childcare costs, and rent £100 and Council Tax £20 (support included at same rate under Universal Credit as current system), and with 70% of childcare costs covered under Universal Credit:

(Out of work income for the family is £218 under both current system and Universal Credit)

Current System:

Tax Credits: £305
Housing Benefit: £69
Council Tax benefit: £11
Child Benefit: £34
Net earnings: £253

Rent/Council Tax: -£120
Childcare costs: -£250

Total: £301

Universal Credit:

Universal Credit: £332
Council Tax Benefit: £11
Child Benefit: £34
Net Earnings: £253

Rent/Council Tax: -£120
Childcare costs: -£250

Total: £260

In this case the family is £41 per week (£2,130 per year) better off under the current system than Universal Credit. The gain made from moving into work is reduced from £83 per week, to just £42 per week. Once travel and other work-related costs are taken into account, the family may see very little benefit from being in work.

As can be seen in Case 2, the impact is reduced where childcare costs are lower (in this case only required for one child rather than both). As can be seen, when childcare costs are £125

² The national average cost of 25 hours nursery care is £102 per week (Daycare Trust *Childcare Costs Survey 2012*) (equivalent to £122.40 for 30 hours) – lone parent working 30 hours is actually likely to require more than 30 hours of childcare to cover travel time etc.

rather than £250, household income increases by £30, and the difference to the current system reduces from £41 per week to £17 per week.

Case 2:

A lone parent with two children aged one and seven, working 30 hours per week and earning £300, with £125 per week childcare costs, and rent £100 and Council Tax £20 (support included at same rate under Universal Credit as current system), and with 70% of childcare costs covered under Universal Credit:

(Out of work income for the family is £218 under both the current system and Universal Credit)

Current System:

Tax Credits: £218
 Housing Benefit: £45
 Council Tax benefit: £3
 Child Benefit: £34
 Net earnings: £253

Rent/council Tax: -£120
 Childcare costs: -£125

Universal Credit:

Universal Credit: £245
 Council Tax Benefit: £3
 Child Benefit: £34
 Net Earnings: £253

Rent/Council Tax: -£120
 Childcare costs: -£125

Total: £307

Total: £290

Under both systems, families can receive support with weekly childcare costs of up to £175 for one child, or £300 for two or more children. This means that they can currently receive up to £167 per week in support for one child and £289 for two or more children. As shown below, under Universal Credit this drops to £123 per week for one child, or £210 for two or more children³.

This means that families with one child could lose up to £2,320 per year, families with two or more children in childcare could lose up to £3,980 per year.

Figure 2: Maximum support with childcare costs through benefits and tax credits system now and under Universal Credit

| | One child (£175) | Two children (£300) |
|--|--------------------|---------------------|
| Current System (WTC +Housing Benefit/Council Tax Benefit disregards) | £167.13 | £286.50 |
| Universal Credit | £122.50 | £210 |
| Difference | -£44.63 (£2320 pa) | -£76.50 (£3980 pa) |

³ If a Council Tax Benefit disregard remains in place and is claimed, this increases to £133 for one child and £228 for two or more children – the potential annual loss is then £1,775 per year for one child, or £3,042 per year for two or more children.

Based on average childcare costs of £90 for which help with childcare is received through Working Tax Credit⁴, the *average* loss of support would be around £23 per week -- or £1,200 per year.

The government estimates that there are 100,000 working families receiving help with childcare costs through both the childcare element of Working Tax Credit, and through Housing Benefit and/or Council Tax Benefit⁵. Since tax credit statistics suggest that around 455,000 families overall receive support through the childcare element of Working Tax Credit⁶, this means that around 22% of families receiving childcare costs through the tax credit system also receive help through Housing Benefit and/or Council Tax Benefit.

5. Variations in impact by family type

Using data from the *Family Resources Survey 2009/10*⁷ the impact of this additional cut in support with childcare costs was estimated for different family types. We analysed the impacts on families with disabled children, working families living in poverty and families in different regions across the UK.

i. Working families living in poverty

According to the analysis, working families who are living in poverty are around **four times more likely** to be affected by this change than families receiving help with childcare costs through tax credits who are not living in poverty⁸.

Out of 25 households living in poverty who receive support with their childcare costs through tax credits, 10 (or 40%) also receive Housing Benefit. In comparison, of the 334 households not living in poverty who receive support with their childcare costs through tax credits, 40 (or 11%) also receive Housing Benefit.

ii. Regional variations

We would expect areas with the highest housing costs to be most affected by the change, since local housing costs affect rates of entitlement to housing benefit. Analysis bears this out, suggesting that the South of England (where average rents and Housing Benefit awards are the highest⁹) is most affected by the change.

Figure 3 below shows the proportion of households affected in different regions of the UK¹⁰. It indicates that families in the **South (London, South East, South West) will be most**

⁴ <http://www.hmrc.gov.uk/stats/personal-tax-credits/cwtc-main-apr12.pdf>

⁵ <http://www.theyworkforyou.com/wrans/?id=2011-07-12b.63809.h&s=childcare+housing+benefit+section%3Awrans+section%3Awms#g63809.q0>

⁶ <http://www.hmrc.gov.uk/stats/personal-tax-credits/cwtc-main-apr12.pdf>

⁷ Households receiving support with their childcare costs through tax credits were identified using the CCTC variable in the Benefits dataset of the Family Resources Survey. Households in receipt of housing benefit were identified using the Housing Benefit ENHH variable in the Households Below Average Income dataset. In total 375 households were identified as having support with their childcare costs through tax credits, of which 50 (or 13%) also received housing benefit

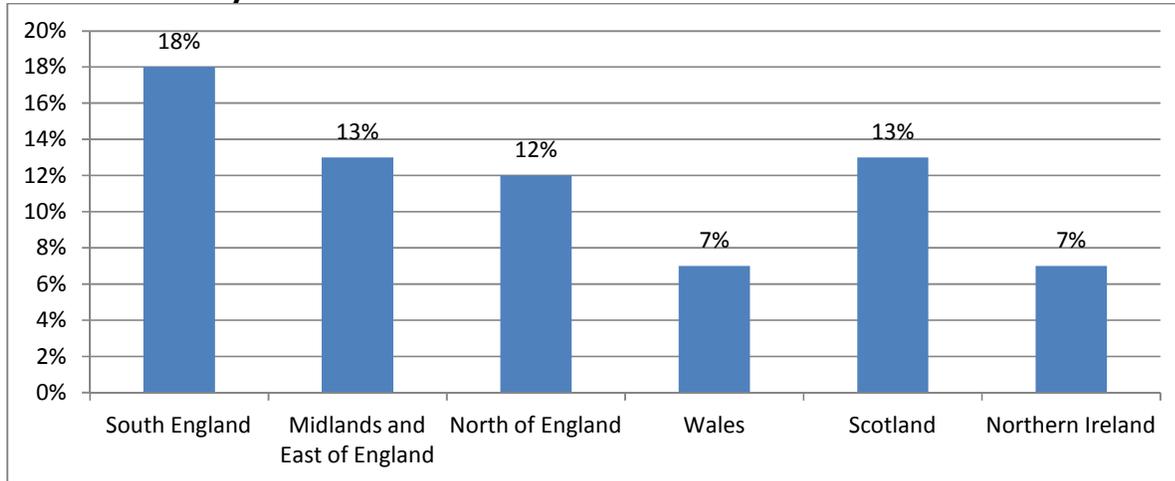
⁸ Households living in poverty were identified using the LOW60AHC variable in the Households Below Average Income dataset

⁹ DWP statistics indicate that highest average Housing Benefit awards in Britain are in London (£131 per week) followed by the South East (£96 per week), the British average is £86 per week. The South West has the fourth highest (after the East of England.) http://statistics.dwp.gov.uk/asd/asd1/adhoc_analysis/2012/hb_publication_march_2012.xls

¹⁰ A regional breakdown of households was identified using the GVTREGN variable in the Households Below Average Income dataset.

affected by this cut in support, with just under 20% of households receiving help with their childcare costs through tax credits affected. The analysis suggests that Wales and Northern Ireland will be least affected with, in both cases, only 7% of families affected.

Figure 3: Regional breakdown of those affected by the loss of the Housing Benefit childcare disregard as a proportion of households in receipt of assistance with childcare costs through the tax credits system



Additional regional breakdowns are given in Appendix B.

7. Conclusion and recommendations

This briefing raises concerns that 100,000 working families could see their support with childcare costs reduced by up to £4,000 per year under Universal Credit, with working families on the lowest incomes being affected the most.

The government should reconsider the structure of support with childcare costs under Universal Credit. While the structure of Universal Credit prevents support from being applied in the same way as the current system, it is critical that sufficient support with childcare costs is provided to enable work to always pay and be sustainable.

We recommend that the government consider two key policy changes to provide additional support with childcare costs.

i. Increase the level of support provided through the childcare element of Universal Credit

It is currently intended that the childcare element of Universal Credit will cover 70% of childcare costs. Increasing it to cover 80% of childcare costs would help ensure that work always paid under Universal Credit.

For example, if a parent took on an additional hour of work, which paid an extra £10, they would typically be able to keep £2.40 after tax and Universal Credit withdrawal. However, if they had to pay £8 in additional childcare costs in order to take on their extra work, then at 70% coverage of childcare costs, they would see no benefit in working the extra hour at all. If childcare costs were £9 for the extra hour, then the family would end up paying 30p to take on the additional work.

If Universal Credit covered 80% of childcare costs, the family would keep 80p from the additional hour of work when paying £8 per hour for childcare. Even at £9, they would still keep 60p from the extra hour's work.

While extending childcare cost coverage to 80% would not fully replace the reduction from 96% which may be faced by some families, it would help to ensure that work always pays for any work that a low income working family undertakes.

For example, given the same household circumstances as in case study 1, case study 3 below shows the impact of increasing childcare coverage under Universal Credit from 70 to 80%. In this case household income is increased from £260 to £285 per week, and while the household is still worse off than under the current system, the loss is more than halved. The overall financial benefit of moving into work for the family is increased from £42 to £67.

Case 3:

A lone parent with two children aged one, working 30 hours per week and earning £300, with £250 per week childcare costs, and rent £100 and Council Tax £20 (*support included at same rate under UC as current system*), and with 70% of childcare costs covered under universal credit:

(Out of work income in both cases is £218)

Current System:

Tax Credits: £305
 Housing Benefit: £69
 Council Tax benefit: £11
 Child Benefit: £34
 Net earnings: £253

Rent/council Tax: -£120
 Childcare costs: -£250

Total: £301

**Universal Credit
 (covering 80% child care costs)**

Universal Credit: £357
 Council Tax Benefit: £11
 Child Benefit: £34
 Net Earnings: £253

Rent/Council Tax: -£120
 Childcare costs: -£250

Total: £285

Based on average childcare costs of £83 per week for which support is received through the tax credit system, and 455,000 families receiving support, the cost of providing an additional 10% of childcare costs under Universal Credit would be about **£200 million per year**.¹¹

ii. A higher level of support for families living in areas of high childcare and housing costs

As shown on page six, the effect of losing the Housing Benefit childcare disregard varies regionally, with families in areas of high housing costs being particularly likely to be affected.

¹¹ This is calculated based on tax credit receipt. Changes to the structure of in-work support under Universal Credit may mean that the costs of additional provision under Universal Credit are different.

Analysis suggests that households in the South of England are most likely to be affected by losing support for their childcare costs through Housing Benefit. Covering an additional 10% of childcare costs for areas with high levels of housing costs would target additional support to those areas most likely to be affected by the change.

Of the 455,000 households receiving support with childcare costs through the tax credit system, 133,000 (29%) are in the South of England. Covering an additional 10% of childcare costs for households in these areas would therefore cost in the region of £58 million.

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About The Children's Society

The Children's Society supports nearly 50,000 children and young people every year through our specialist services and children's centres. We believe in achieving a better childhood for every child but have a particular focus on children who have nowhere else to turn, such as children in poverty, young refugees, children at risk on the streets, disabled children and children in trouble with the law. We seek to give a voice to children and young people and influence policy and practice so they have a better chance in life.

Appendix A: The mechanics of help with childcare costs through the benefits and tax credits system

On increasing childcare costs by £1 -

- Entitlement to childcare element of Working Tax Credit increases by **70p**
- Income for Housing Benefit and Council Tax Benefit purposes reduces by £1 as a result of additional childcare costs being disregarded
- Income for Housing Benefit/Council Tax Benefit increases by 70p as a result of increased tax credit entitlement – overall entitlement is reduced by 30p
- Housing Benefit/Council Tax Benefit withdrawn at a combined withdrawal rate of 85%, therefore 30p reduced income leads to an increase in Housing Benefit/Council Tax Benefit entitlement of **25.5p**
- Household pays out £1 in childcare costs, but receives 70p+25.5p in increased benefit entitlement – therefore overall childcare subsidy is worth **95.5p**

Appendix B: Additional regional breakdown

| Region | Proportion of households with childcare costs affected | Approximate number of households affected by region ¹² | Sample sizes (households receiving Housing Benefit as proportion of those receiving Childcare Tax Credits) |
|-------------------------------------|--|---|--|
| South England | 18% | 32,000 | 16 out of 89 |
| South West | 19% | 8,000 | 4 out of 21 |
| South East | 18% | 14,000 | 7 out of 39 |
| London | 17% | 10,000 | 5 out of 29 |
| | | | |
| Midlands and East of England | 13% | 22,000 | 11 out of 85 |
| West Midlands | 17% | 10,000 | 5 out of 29 |
| East Midlands | 14% | 8,000 | 4 out of 29 |
| Eastern | 7% | 4,000 | 2 out of 27 |
| | | | |
| North of England | 12% | 26,000 | 13 out of 105 |
| Yorkshire and Humberside | 19% | 14,000 | 7 out of 36 |
| North East | 6% | 2,000 | 1 out of 16 |
| North West | 9% | 10,000 | 5 out of 53 |
| | | | |
| Wales | 7% | 2,000 | 1 out of 14 |
| Scotland | 13% | 14,000 | 7 out of 55 |
| Northern Ireland | 7% | 4,000 | 2 out of 27 |

¹² Based on government estimate of 100,000 households affected