Welfare reform report

Impact on families with children

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Scottish Government
Riaghaltas na h-Alba
gov.scot

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Contents

1 Executive Summary

- Reversing key UK Government welfare reforms that have occurred since 2015 would bring an estimated 70,000 people out of poverty in Scotland, including 30,000 children, in 2023-24.

- Each of the following interventions, in isolation, would bring around 10,000 **children** out of poverty:
    - Re-instating the £20 uplift to Universal Credit
    - Reversing the benefit freeze
    - Reversing the two-child limit and the removal of the family element.

- Reversing all reforms would increase disposable income for households with children with the lowest 10% of incomes by around 11%, and for households in poverty with children by 10%.

- The total cost of reversing these reforms would be around £780 million per annum, including £50 million in increased expenditure on existing benefits provided by the Scottish Government such as the Scottish Child Payment (£20 million) and Discretionary Housing Payments (£30 million) as a result of increased eligibility for these benefits.

- Of these reforms, the most cost-effective way to reduce child poverty would be to reverse the two-child limit and the removal of the family element at a cost of £120 million. The least efficient way would be to re-instate the £20 uplift at a cost of £540 million.

- Re-instating the £20 uplift would move the most people out of poverty (30,000), followed by reversing the benefit freeze (20,000). The most cost-effective method would be to reinstate the £20 uplift while also reversing changes to the Universal Credit earnings taper rate and work allowances, at a cost of £320 million.

- Adjustments to Universal Credit work allowances and the earnings taper rate were a cost-effective way to lift working households out of poverty – reversing this change would push 10,000 people *into* poverty. However, these changes only affected households in employment, which tend to be closer to the poverty line.

- Work incentives for households with children are highly dependent on eligibility thresholds and earnings levels. Changes to the Universal Credit earnings taper rate and work allowances generally reduce the proportion of additional earnings which are lost to taxes and a reduction in benefit entitlements, but some reforms can lead to perverse outcomes as a result of the interaction between policies.

2 Introduction

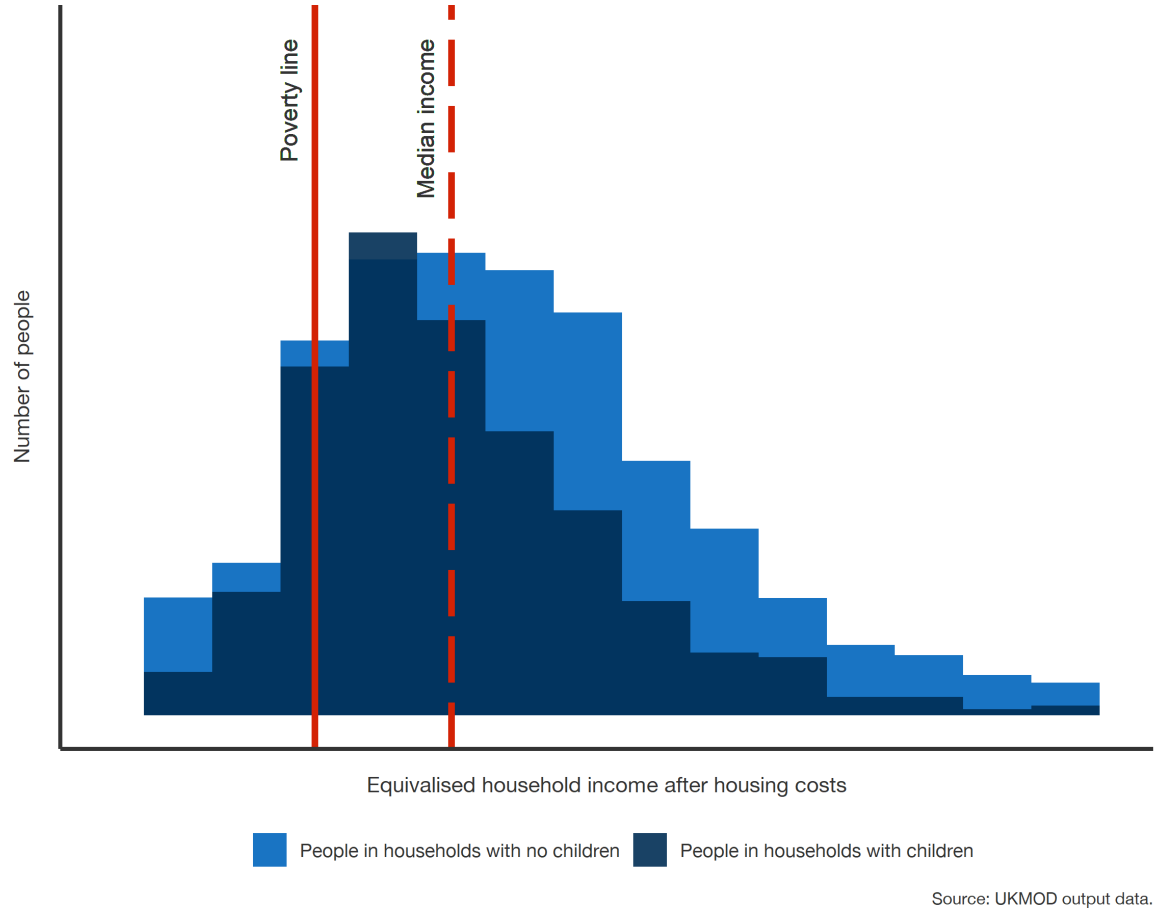
This report is part of the Scottish Government's Welfare Reform report series. We have used the microsimulation model 'UKMOD' to assess the impact of reversing a number of UK Government welfare reforms on households with children, and is the second such report to focus on this type of household.[1] We focus on the impact of reversing these reforms in the future, rather than the effect of the reforms themselves at the time they were implemented, to enable us to make a like-for-like assessment in the same period, namely 2023-24.

Of particular interest is child poverty. In 2017 the Scottish Parliament passed the Child Poverty (Scotland) Act which sets statutory targets for the reduction of child poverty by 2030, with interim targets to be met in 2023. This report sheds light on the impact of UK Government policy on poverty in Scotland, and what interventions might be most effective for reaching these targets. It therefore complements the Cumulative Impact Assessment which was published alongside the second Tackling Child Poverty Delivery Plan, setting out the impact of Scottish Government policies on child poverty and projecting the child poverty rate in 2023-24.[2]

As shown in the graph below (figure 2.1), people in households with children tend to have lower disposable incomes compared with people in households without children. The income distribution of such households is also more concentrated, which means more people in these households have incomes between the poverty line and the median income line.

[1] Welfare reform analysis - gov.scot (www.gov.scot)
[2] Tackling child poverty delivery plan 2022-2026 - annex 4: cumulative impact assessment - gov.scot (www.gov.scot)

2.1 Equivalised[3] household disposable income distribution, Scotland, 2023-24



Source: UKMOD output data.

As a result, the poverty rate for people in households with children can be sensitive to policy reform, with potentially many people being moved above or below the poverty line (indicated here with the solid vertical line) when changes are made. This is particularly the case if such policies do not have a large impact on the UK median income (dashed line), the base from which the poverty line is calculated.

We also know from OECD data that a key distinction between the United Kingdom and countries with lower child poverty rates is the rate of in work poverty, as show in figure 2.2. Despite rates of out of work poverty being significantly lower in the United Kingdom compared with Sweden or Norway, the large number of people who are in poverty while in work means the overall child poverty rate is higher than elsewhere.

[3] By adjusting for the composition of households we can make fair comparisons across them. A household with children has less disposable income per person, even if their earnings and housing costs are the same. See **Appendix C**.

2.2 Child poverty rate (50% median income)[4], 2016 or latest year[5]

	Out of work	In work	All
United Kingdom	39%	7%	12%
Sweden	77%	5%	9%
Norway	59%	4%	8%
Iceland	17%	5%	6%
Denmark	32%	2%	4%
Finland	35%	1%	3%

We also know that the proportion of households in poverty that are in work has increased in Scotland from 48% in 1996-99 to 59% in 2014-17. [6] As such, a particular focus of this report is the impact of welfare reform on working households with children.

There have been a number of welfare reforms over the past five years that have had an impact on households with children. To explore how these have affected the distribution described above, we have selected a number of key reforms and broken these down into three groups:

- Recent reforms, including the change to the Universal Credit earnings taper rate and work allowances, and the removal of the temporary £20 uplift to Universal Credit;
- Historical reforms, including the benefit freeze, the two-child limit, and the removal of the family element from Universal Credit and Tax Credits;
- A cumulative assessment of all these reforms.

We do not model the impacts of the benefit cap, which was introduced in 2013 and lowered in 2016. While this policy primarily affects households with children, the second Tackling Child Poverty Delivery Plan committed to mitigate the cap as fully as possible through Discretionary Housing Payments, beginning in 2022. This commitment is incorporated in the model. The impacts of some of the other policies modelled here are likely to be higher as a result of mitigating the benefit cap. This is because the benefit cap would have previously limited the impacts of policies for households which were subject to the cap.

In order to provide a full picture of the impact of each policy, and how that impact may differ for households with children, this report assesses changes to:

[4] This is distinct from the child poverty rates used in the rest of the report which are based on 60% of UK median income.
[5] OECD Family Database - OECD
[6] Working poverty analysis 2019 - gov.scot (www.gov.scot)

- Benefits expenditure (including Scottish Government social security spending)[7]
- Poverty
- Child poverty
- Income for people in priority groups for child poverty[8]
- Income for working and non-working households, with and without children
- Income for single and couple households, with and without children
- Income, broken down by income deciles, with and without children.

By comparing changes in benefits expenditure with indicators such as child poverty, we also estimate how efficient reversing each reform would be for reducing the number of people in poverty.

In addition to these short term impacts, this report also considers the behavioural impact of these changes on families by estimating the 'effective marginal tax rate' for households considering working an additional 10 hours a week. This measures the proportion of additional earnings which are lost to taxes and a reduction in benefit entitlements, which could affect the incentive to undertake paid work.

We have developed a set of hypothetical households that represent the characteristics of the child poverty priority groups to test the impact on work incentives using this measure. Further detail is set out in **Appendix D**.

[7] A number of devolved benefits, such as the Scottish Child Payment, are based on take up of reserved benefits.

[8] These are: households with a lone parent, households with someone who is disabled, households with three or more children, minority ethnic households, households with a child under one, households with a mother under 25.

3 The £20 uplift and changes to the Universal Credit earnings taper rate and work allowances

Background

We first assess the impact of reforms that have taken place during the COVID-19 pandemic.

The £20 uplift

At the outset of the COVID-19 pandemic, the UK Government temporarily increased Universal Credit standard allowances and the basic element of Working Tax Credits by £20 per week, increasing the disposable incomes of households on these benefits. This, alongside the 'furlough' scheme, was the primary way in which the government supported those who were unable to work, or saw reduced earnings, as a result of COVID-19. The uplift also helped those who were already claiming for these benefits before the pandemic, including those who are unable to work due to disability or caring responsibilities.

The UK Government removed this temporary measure in October 2021. A Scottish Government report found that withdrawing the uplift would have a particular impact on poorer households, including those with children.[9] Meanwhile, people on other legacy benefits, such as Employment and Support Allowance, did not receive the uplift in the first place.

We model the impacts of reinstating the uplift. However, the uplift was intended to be temporary, so this reinstatement would represent a permanent addition to the social security system, not just the reversal of a reform.

The earnings taper rate and work allowances

In the UK Government's Autumn 2021 budget, two significant changes were made to Universal Credit for households in employment.

The Universal Credit award that households are entitled to is partly determined by their earnings. Some households, including those with children, have their award partially protected by a work allowance. Above the work allowance, Universal Credit awards are gradually reduced at a fixed proportion of earnings, known as the taper rate. If there was no taper, there would be a 'cliff edge' where Universal Credit would be fully withdrawn once a household earned more than a certain amount.[10]

In the UK's Autumn budget of 2021, work allowances were increased by £500 per year (£42 per month) meaning that households could earn an additional £500 before their Universal Credit award began to reduce. At the same time the taper rate was

[9] Impact of withdrawing emergency benefit measures - gov.scot (www.gov.scot)
[10] Reducing the Universal Credit taper rate and the effect on incomes (parliament.uk)

reduced from 63% to 55%, meaning that each pound of earnings above the work allowance would reduce the Universal Credit award by 55p rather than 63p.

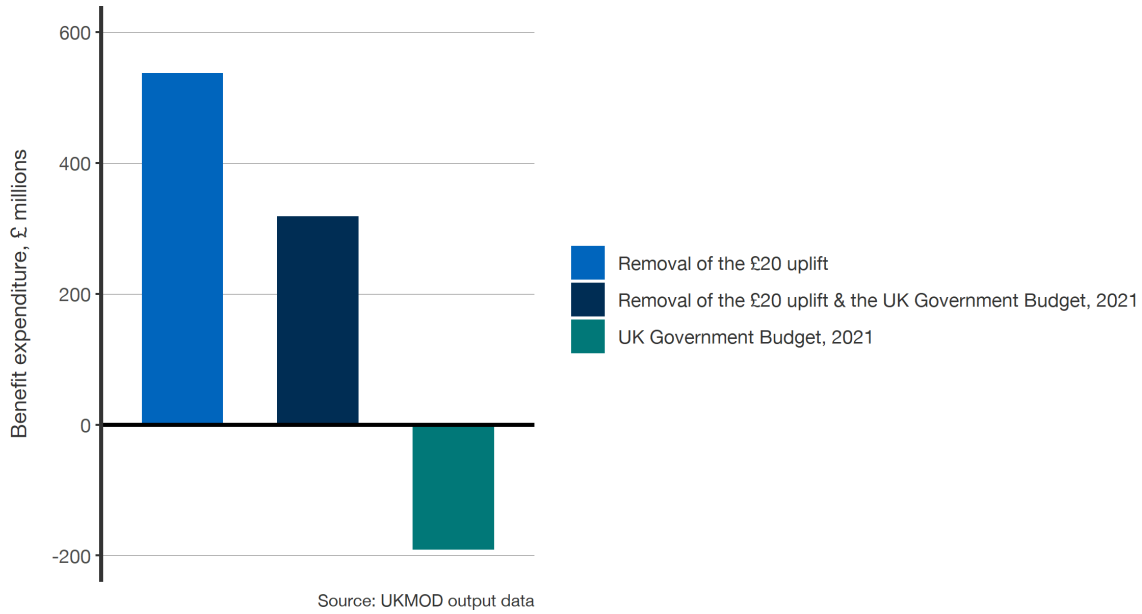
2023-24	Before	After
Earnings taper rate	63%	55%
Monthly work allowance[11]	£551/£313	£593/£355

Both of these reforms can be expected to boost income for Universal Credit claimants in work and to improve work incentives. However, these impacts are complex, particularly when interacting with the withdrawal of the £20 uplift, and the long-term behavioural effect is uncertain.

Despite this reform generally increasing household incomes, this report assesses the impact of reversing the reform rather than its implementation, in line with our treatment of the other policies considered. This means that it can be assessed on a like-for-like basis with other policies, and that the cumulative impact described later is a fair reflection of UK Government policy over the past six years.

Expenditure

3.1 Impact of reversing reforms on benefit expenditure, Scotland, 2023-24



12

[11] Value depends on whether a household receives support for housing costs
[12] Includes all benefit expenditure, including those devolved to Scotland.

As shown in the graph (figure 3.1), the total cost of reversing recent reforms to Universal Credit would be around £320 million per annum in 2023-24. This is a net figure, with the cost of reversing the removal of the uplift (£540 million) offset by the reduction of the taper rate (£190 million).

These figures include both expenditure made by the UK Government on reserved benefits such as Universal Credit and by the Scottish Government on devolved social security such as the Scottish Child Payment. Further detail is provided in **Appendix A**, where the implied reduction in expenditure made by the UK Government on households in Scotland is illustrated.[13]

The change in expenditure which would result from reversing both policies at once does not equal the sum of the figures for reversing each of the two policies in isolation. This is a result of the interactions between the two policies, as illustrated in the household example below.

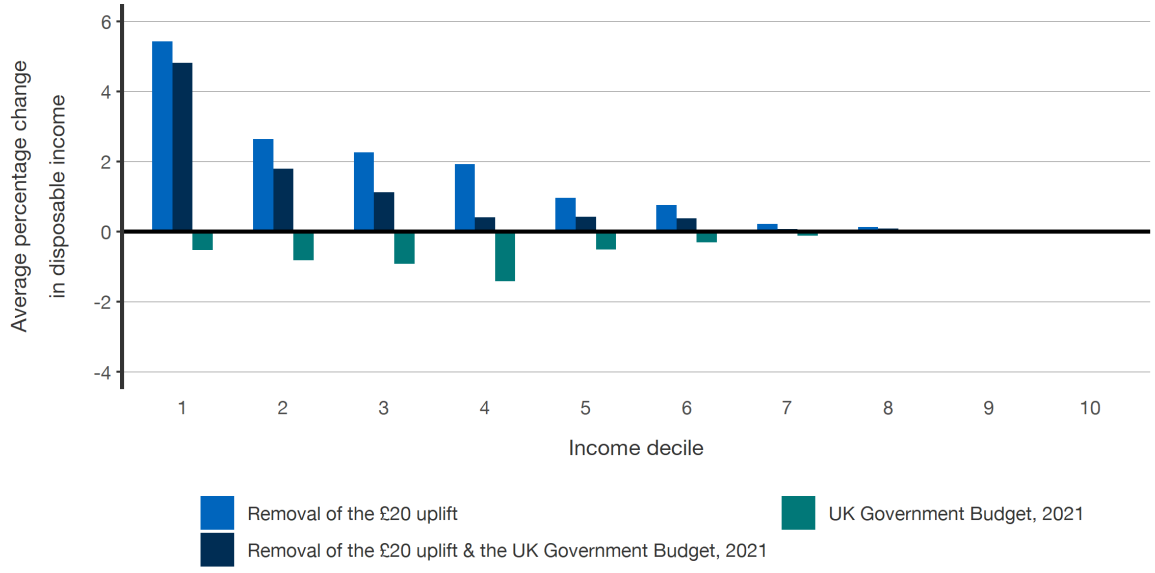
Household example: The Munro household has no Universal Credit award as their earnings have "tapered away" their entitlement to exactly £0. If the £20 uplift was reintroduced, the Munros would now have an award, but would only keep £9 of the uplift due to the 55% earnings taper rate. If the taper rate were higher, at 63%, this would drop further to only £7.40.

Had there only been an increase to the taper rate, there would have been no impact on the Munro household as their award was already £0. It only has an impact when introduced in tandem with the reintroduction of the £20 uplift.

[13] "Reduced benefit expenditure" analysis does not take account of the subsequent behavioural impacts of UK Government reform. If people are now more likely to work as a result of the reforms, we are likely to underestimate the size of the reduction in expenditure. No such caveat applies to "cost of reversal" analysis.

Disposable income

3.2 Percentage changes to disposable income after housing costs, by equivalised household disposable income decile, by reform reversed, Scotland, 2023-24



Source: UKMOD output data

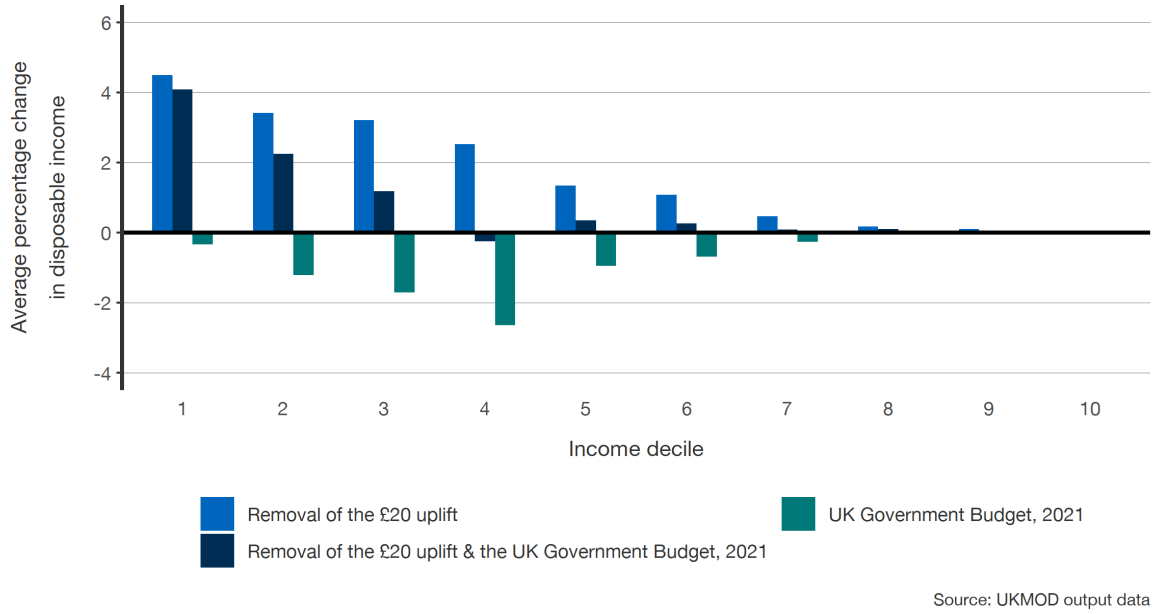
As shown in the graph (figure 3.2), reinstating the £20 uplift would have most impact on those in the lowest disposable income deciles, with the 10% of people in households with lowest incomes seeing increases of around 5% on average. [14]

However, reverting the earnings taper rate to 63% (from 55%) and reversing the increases in work allowances would primarily impact those with relatively higher incomes. As a result, the impact of reversing the £20 cut is significantly mitigated for those in deciles three and four should both reforms be reversed.

Depending on the median income in 2023-24, all households in income deciles one and two and most in decile three will be in poverty. The cumulative impact of reversing both reforms would have a significant positive impact for these households, on average, but some households may experience a negative impact if their household composition and earnings make them more sensitive to the budget measures than to the £20 uplift. Indeed, the poverty rate is highly sensitive to changes in the taper rate and work allowances as they primarily impact on people on or just above the poverty line.

[14] There is some evidence to suggest that data for people on very low incomes may not be reliable, with some under reporting of income possible (Brewer et al, 2017). This would mean that the actual percentage increases for people in this decile are over-stated.

3.3 Percentage changes to disposable income after housing costs, by equivalised household disposable income decile, by reform reversed, households with children, Scotland, 2023-24

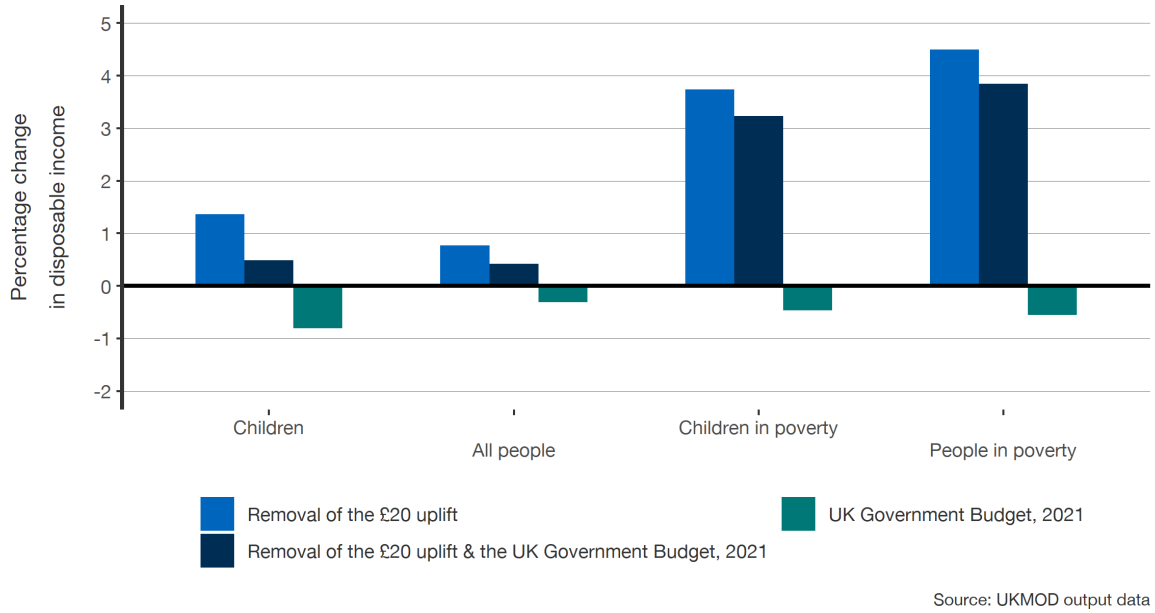


Source: UKMOD output data

Figure 3.3 demonstrates that reversing the removal of the £20 uplift would have a reduced impact on people in households with children in income decile 1 compared with people generally. However, in all other deciles the impact is greater, demonstrating that households with children in these deciles are more likely to receive Universal Credit or working tax credit.

Reversing the work allowance and taper rate changes in the UK Budget of 2021 would have a more significant impact on families compared with all households. This demonstrates that the incomes of people in lower income deciles and in households with children tend to be more sensitive to earnings-related reform, with people out-of-work more likely to have no children. For those households with children in decile four, the impacts of reversing both reforms would cancel out.

3.4 Average change in disposable income by household type after reversing reforms

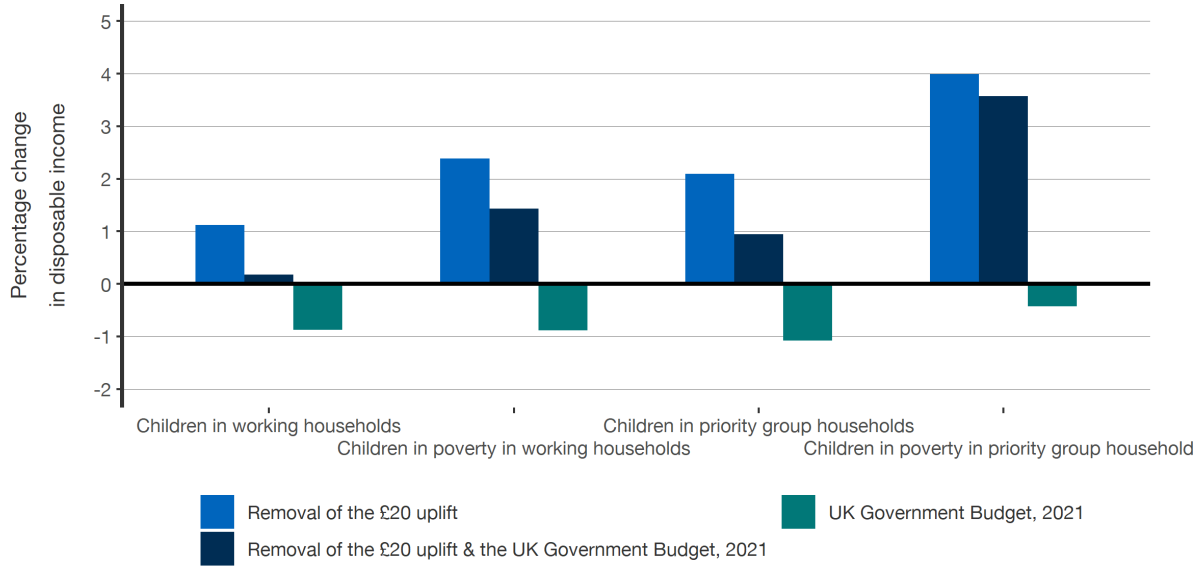


Source: UKMOD output data

Figure 3.4 shows how reversing either of these recent reforms will have a marginal impact on disposable income on average. However, there will be a significant change for people under the poverty line in 2023-24 if the £20 uplift were reversed.

Despite how sensitive poverty rates are to changes in the Universal Credit earnings taper rate, this graph shows that, on average, the taper rate change has little impact on disposable income. As shown in the graph below (figure 3.5), this is the case even for working households, with the £20 uplift more important. There is not necessarily a clear cut relationship between policies that are effective in helping people who in poverty and policies that are effective in moving people out of poverty, since the latter depends on the proximity of households to the poverty line.

3.5 Average change in disposable income by household type after reversing reforms



Source: UKMOD output data

Poverty

The cumulative impact of reversing recent welfare reforms would be to reduce poverty in 2023-24. The table below (figure 3.6) shows how the removal of the £20 uplift more than offsets the positive impact of the 2021 Budget reforms, which only had a minor impact on poverty rates.

3.6 Impact on poverty rates by reversal of reform, percentage point change, Scotland, 2023-24 [15]

	Removal of the £20 uplift	UK Government Budget, 2021	Both
All people	-1	*	-1
Children	-1	*	-1
People in working households	*	*	*
Children in working households	*	1	*
Children in single households	-2	*	-2
Children in couple households	*	*	*
Children in priority group households	-1	*	-1
People in absolute poverty	-1	*	-1
Children in absolute poverty	-2	*	-1

[15] * denotes that the result was suppressed due to a small sample size.

Reversing the removal of the £20 uplift would have a significant impact on the poverty rate for children in single adult households and on the absolute poverty rate for children. We also find that the absolute poverty rate for children is more sensitive than the relative poverty rate.

3.7 Number of people brought out of relative poverty by reversal of policy, Scotland, 2023-24[16]

	Removal of the £20 uplift	UK Government Budget, 2021	Both[17]
All people	30,000	-10,000	30,000
Children	10,000	*	10,000
People in working households	10,000	-20,000	10,000
Children in working households	*	*	*
Children in single households	10,000	*	*
Children in couple households	*	*	*
Children in priority group households	10,000	*	*

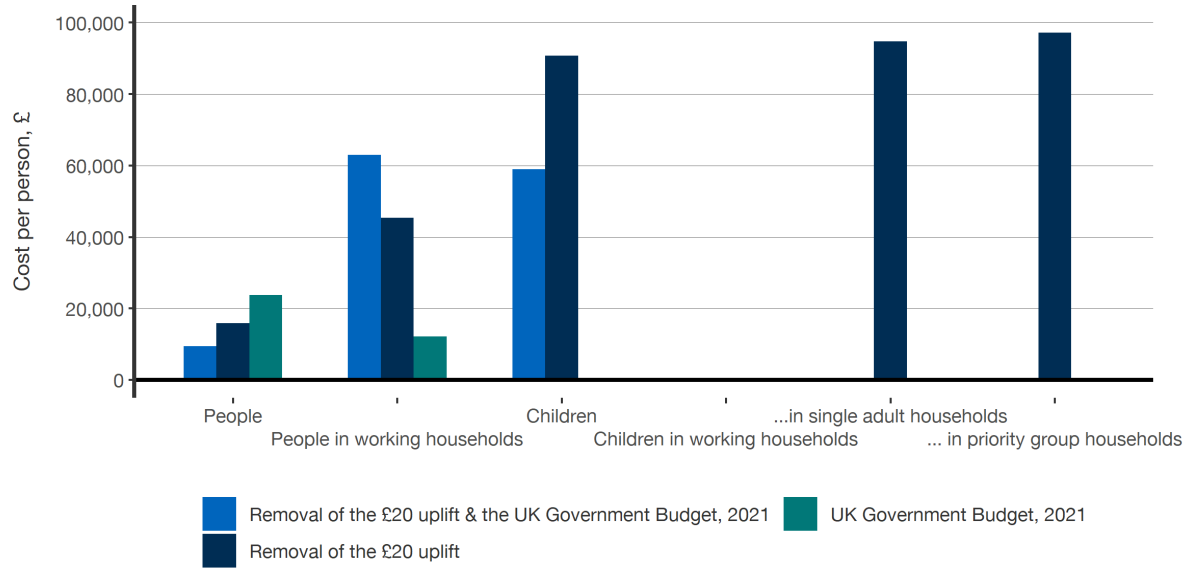
As mentioned above, the change to the earnings taper rate and work allowances has a large impact on those near to the poverty line. The table above (figure 3.7) shows that 10,000 people in working households would be moved into poverty should it be reversed in 2023-24.

Reinstating the £20 uplift to Universal Credit would move 30,000 people out of poverty, including 10,000 children. The change would particularly affect the number of children in single households in poverty.

We can combine our analysis of additional expenditure and poverty rates to find which policies are most cost-efficient for moving people above (or below) the poverty line. As shown in the graph (figure 3.8), reversing the removal of the £20 uplift and the 2021 budget measures would cost less than £10,000 per person taken out of poverty, with a cost-efficiency gain by reversing both policies together.

[16] Small changes of below 5,000 are suppressed (marked as *) due to sample size. All figures are rounded to the nearest 10,000.
[17] The impact of reversing both reforms may not be the sum of reversing each individually. Welfare reforms also change the value of the median income (and thus the poverty line) and, due to the shape of the income distribution curve, some reforms can outweigh the impact of others even when the individual impact is smaller. Rounding can exaggerate this effect.

3.8 Cost per person brought out of relative poverty by reversal of reform, Scotland, 2023-24[18]



Source: UKMOD output data

Given the lower number of people in working households and children, it generally costs more to bring them out of poverty. However, the graph does show that the budget was highly cost-effective for bringing people in working households out of poverty; for other groups, such as children in single adult households, reversing both reforms tends to be the most efficient way to reduce poverty.

Given the interactions between the policies and the non-linear income distribution of households in Scotland, no inference can be drawn about the cost-effectiveness of a partial reversal of the reforms (for example, a £10 uplift to Universal Credit).

There are a number of types of household, such as children in working households, where few people were brought in or out of poverty. These results have not been included in the chart, and demonstrate where reversing the reform would have no discernible impact on poverty rates for that group.

Household example: The Corbett household is a working household with children. They are among a small number of families for which the change to the work allowance and the earnings taper rate has lifted them out of poverty. A similar number of working families with children, including the Grahams, would also be lifted out of poverty if £20 uplift was reinstated.

If the uplift was reinstated but the earnings reforms reversed, there would be a small but similar number of working families with children moving above and below the poverty line, despite a significant increase in government expenditure.

[18] As explained in a previous footnote, we suppress results when the change in number of people moved in or out of poverty is less than 5,000

Work incentives

There are several mechanisms through which an increase in earnings does not translate one-for-one into an increase in disposable income, including income tax, National Insurance contributions, and the withdrawal of benefit payments.

The possible combined tax rate could be over 85%, depending on which income tax bands apply to working household members. At some earning increases, such as when they bring a household out of eligibility for Universal Credit and thus other benefits such as the Scottish Child Payment, the marginal tax rate could extend above 100%.

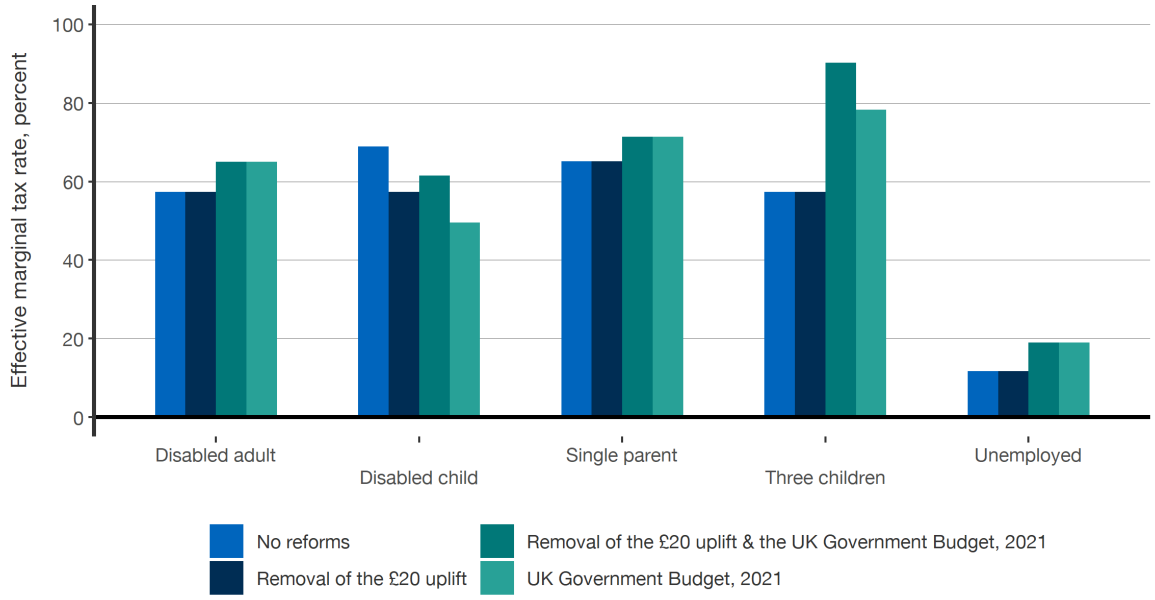
Household example: The Graham household has one child. Their earnings mean that their Universal Credit award is small, but they are still entitled to the Scottish Child Payment.

The household decides to change their working patterns to earn an extra £100 per week. They pay income tax of £21 and National Insurance of £13.25 on this additional earnings. Furthermore, what remains of their weekly Universal Credit award, £55 per week, is fully tapered away. Now ineligible for the Scottish Child Payment, they lose an additional £25 per week (in 2023-24).

On balance, the Graham household is worse off after increasing their earnings, with an effective tax rate of 109%. However, the effective tax rate for the next £100 of earnings is only 34%.

To explore this impact of policy reform on marginal tax rates, we have developed a number of illustrative households. These households are set out in detail in **Appendix D**.

3.9 Effective marginal tax rate after reversing reforms, 10 additional hours of work per week, illustrative households, Scotland, 2023-24



The graph above (figure 3.9) demonstrates that for some households the effective marginal tax rate is above 50%. It shows how reversing the change to the Universal Credit earnings taper rate from 63% to 55% and the work allowance would further increase the effective tax rate for most households.

However, for some households (disabled child, in this instance) the effective marginal tax rate will actually decrease as a result of reversing the change to the earnings taper rate. This is because they now have a larger Universal Credit award, and thus more of their earnings would be offset by the reduction of this award through the taper rate. This perverse outcome only affects households with smaller awards for which earnings reduces their award to zero.

For most working households with earnings over £10,000, changes to the taper rate represent only a small adjustment to the effective tax burden as at this threshold they also begin to pay income tax and National Insurance contributions.

For the unemployed household with children considering work, only compulsory workplace pension contributions and the earnings taper rate reduce disposable income. This is because their earnings would remain below the income tax and national insurance contribution allowances.

4 The two-child limit, the removal of the family element and the benefit freeze

Background

The benefit cap and the 'bedroom tax'.

The benefit cap and the 'bedroom tax' will both be mitigated by the Scottish Government by 2023-24 through Discretionary Housing Payments. This analysis therefore does not assess the impact of these interventions. Mitigation through Discretionary Housing Payments is incorporated into the model.

The two-child limit

The two child limit was introduced in 2017 and limits child tax credit and Universal Credit awards to two children per household. The policy affects those born from 6 April 2017. There are a number of exceptions to the rule.

We can expect the number of households affected by the two child limit to increase over time as more children have birthdays after April 2017. The number will continue to increase until April 2033, when all eligible children will have been born after April 2017.

The removal of the family element

In line with the two child limit, the family element of child tax credit and Universal Credit (also known as the 'first child premium') were removed in 2017. The family element is now only available to households with children born before 6 April 2017, and constitutes a cut of over £545 per annum for households with all children born after this date.

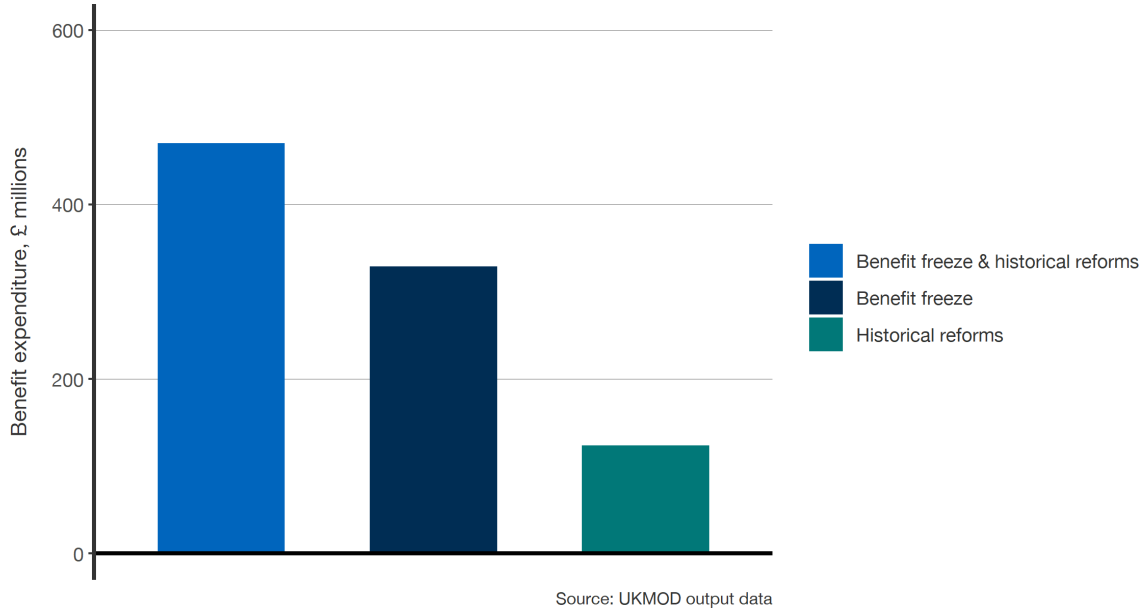
The benefit freeze

The benefit freeze was in place between 2015 and 2019 and affected a number of UK Government benefits such as Universal Credit, working tax credit and housing benefit. While these benefits have been uprated for inflation since 2019, the residual impact of the freeze is retained in the benefit rates available now and in 2023-24.

Universal Credit standard allowances would be 6% larger in 2023-24 had the allowances not been frozen between 2015 and 2019.

Expenditure

4.1 Impact on benefit expenditure by reversal of reform, Scotland, 2023-24



19

As shown in the graph (figure 4.1), the total cost of reversing the benefit freeze, the two-child limit and the removal of the family element would be around £470 million per annum in 2023-24. This is a cumulative figure, with the cost of reversing the benefit freeze (£330 million) complemented by the reversal of the two-child limit and the removal of the family element (£120 million). The figures include both expenditure made by the UK Government on reserved benefits such as Universal Credit and by the Scottish Government on devolved social security such as the Scottish Child Payment.

The expenditure figures for the two sets of policies do not add up to the cumulative total for reversing both together. This is a result of the interactions between the two sets of policies.

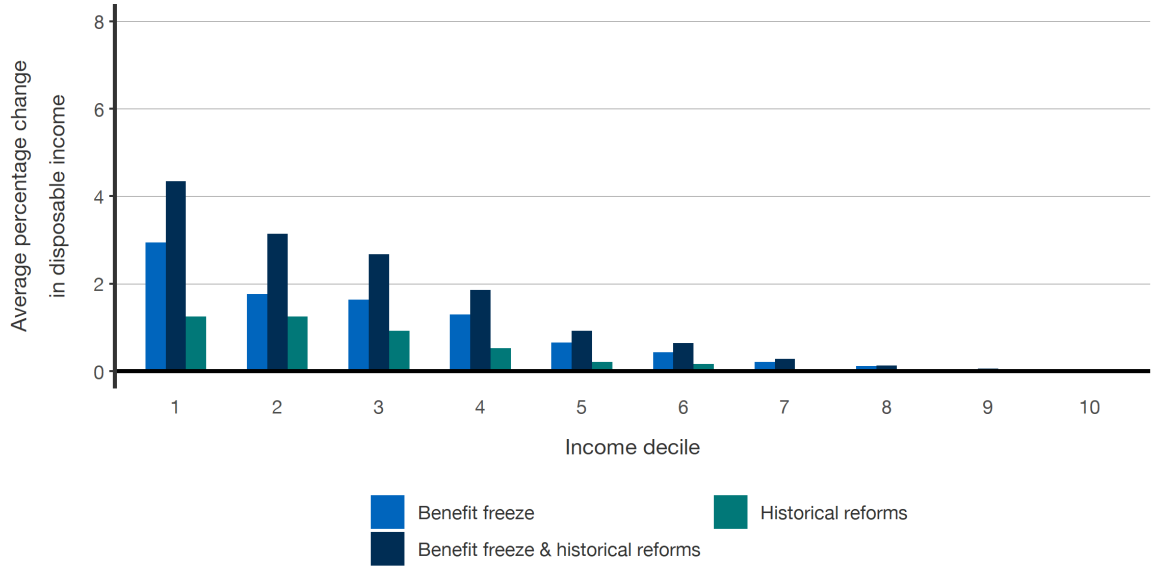
Household example: After the reversal of the two-child limit and the reintroduction of the family element, the Donald household now have additional benefit income allocated to them for their third child born after 2017 (£254), plus an additional payment for their first child (£49). – a total of £303 per month.

This income is further increased by the reversal of the benefit freeze, with their benefits – including those allocated for their third child – being uplifted in line with inflation between 2015 and 2019.

[19] Includes all benefit expenditure, including those devolved to Scotland.

Disposable income

4.2 Percentage changes to disposable income after housing costs, by equivalised household disposable income decile, by reform reversed, Scotland, 2023-24



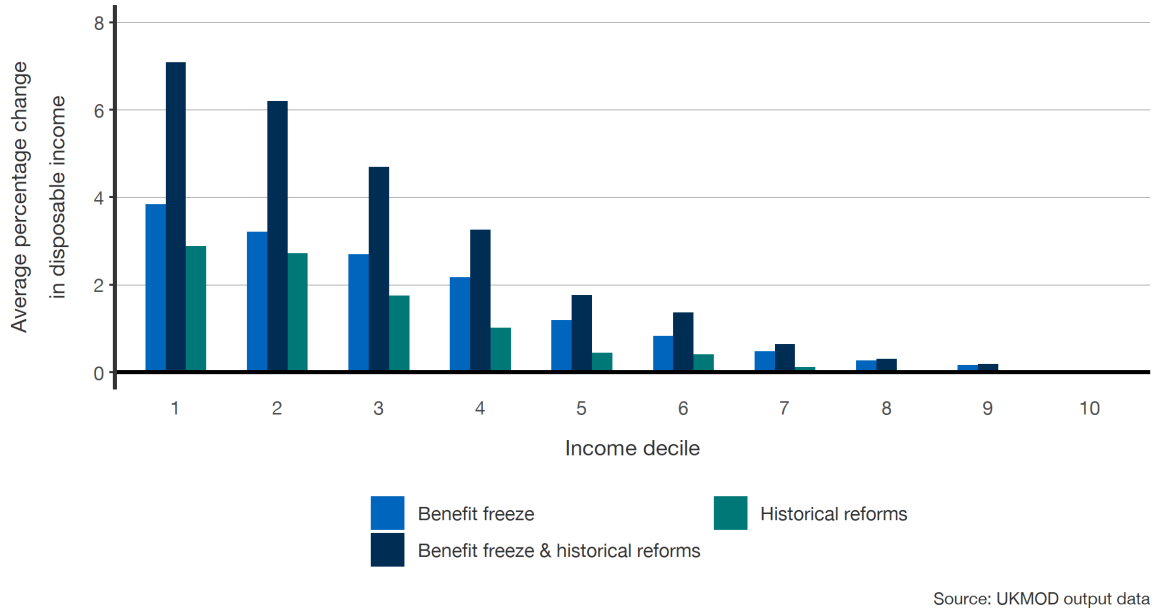
Source: UKMOD output data

As shown in the graph (figure 4.2), reversing both these reforms would have most impact on those in the lowest disposable income deciles, with the 10% of people in households with lowest incomes seeing increases of around 4% on average.

The impact of reversing the benefit freeze is less progressive than reversing the two-child limit and the removal of the family element, with a smaller proportional impact on people with lower incomes relative to those on higher incomes.

Depending on the median income in 2023-24, all households in income decile one and two and most in decile three will be in poverty. The cumulative impact of reversing both reforms would have a significant positive impact for these households.

4.3 Percentage changes to disposable income after housing costs, by equivalised household disposable income decile, by reform reversed, households with children, Scotland, 2023-24

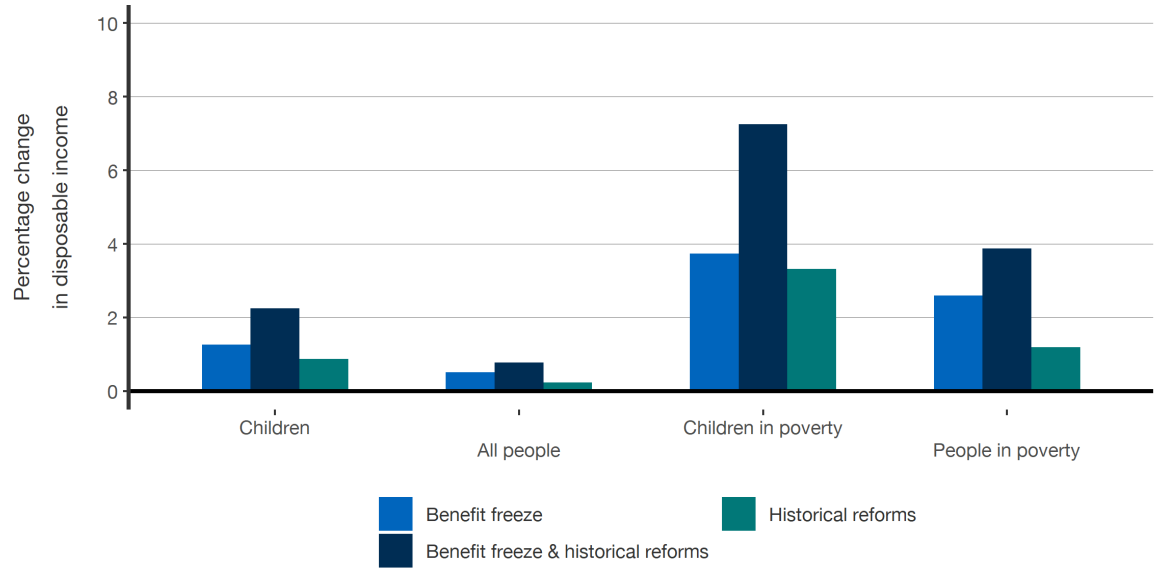


Source: UKMOD output data

Figure 4.3 demonstrates that, as expected, reversing the reforms would have a much larger impact on households with children, with significant increases in household income for those in the lowest income deciles.

In particular, the impact of reversing the benefit freeze is above 2% across deciles one to four, and is likely to influence the poverty rate for households with children. Reversing the two-child limit and the removal of the family element has a more significant influence on those with the very lowest incomes.

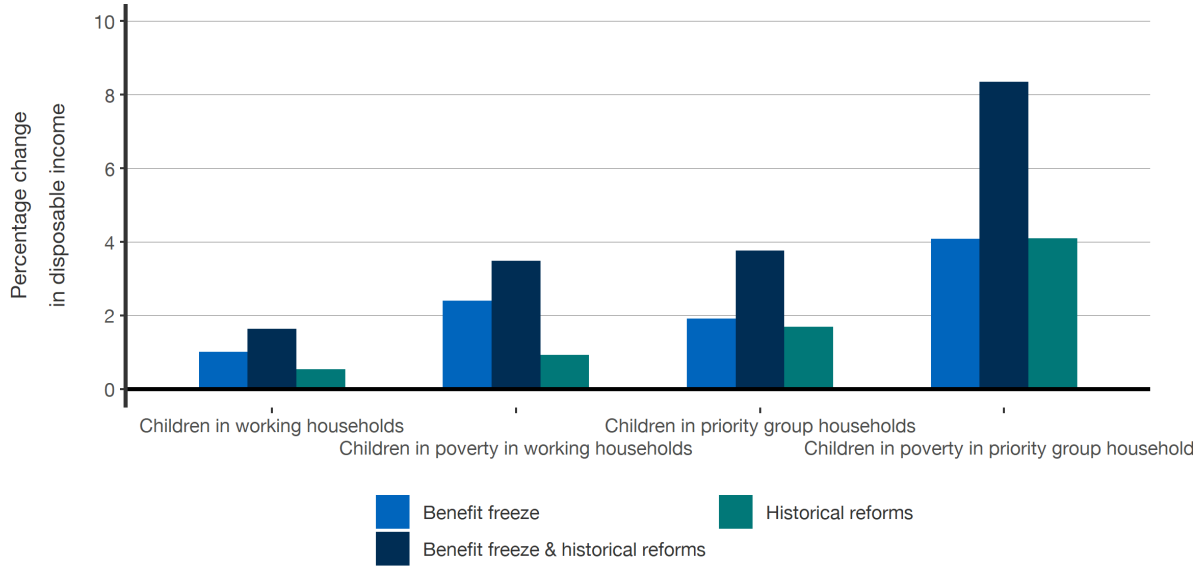
4.4 Average change in disposable income by household type after reversing reforms



Source: UKMOD output data

Figure 4.4 shows how reversing these reforms will have a marginal impact on disposable income on average. However, there will be a significant change, in aggregate, for people under the poverty line in 2023-24 if both sets of reforms are reversed. There is a particular impact on households in poverty with children, with reversing the two-child limit and the removal of the family element being a more important policy change relative to other households.

4.5 Average change in disposable income by household type after reversing reforms



Source: UKMOD output data

Figure 4.5 further demonstrates how important reversing the two-child limit and the removal of the family element would be for children in poverty, while reversing both reforms would lead to a significant increase of 8% for the average income of children in poverty in the priority groups.

Reversing the benefit freeze tends to have more impact on children in working households compared with other types of household.

Poverty

The cumulative impact of reversing the benefit freeze, the two-child limit and the removal of the family element would reduce poverty in 2023-24. The table below (figure 4.6) shows how both reforms would reduce child poverty. However, working households in poverty are less likely to be affected by the changes.

4.6 Impact on poverty rates by reversal of reform, percentage point change, Scotland, 2023-24[20]

	Benefit freeze	Two-child limit and the removal of the family element	Both
All people	*	*	-1
Children	-1	-1	-2
People in working households	*	*	*
Children in working households	*	*	-1
Children in single households	-3	-3	-5
Children in couple households	*	*	-1
Children in priority group households	-2	-2	-4
People in absolute poverty	-1	*	-1
Children in absolute poverty	-1	-1	-2

Figure 4.7 demonstrates that the poverty rate for single adult households with children would be particularly affected by the reversal of these reforms. The same is true for children in priority group households. However, the poverty rate for children in couple households is less sensitive to these changes.

The absolute poverty rate for both children is about as sensitive to reversing these reforms as the relative poverty rate, with both reforms having a similar impact.

4.7 Number of people brought out of relative poverty by reversal of policy, Scotland, 2023-24[21]

	Benefit freeze	Two-child limit and the removal of the family element	Both[22]
All people	20,000	10,000	30,000
Children	10,000	10,000	20,000
People in working households	*	*	10,000
Children in working households	*	*	*
Children in single households	10,000	10,000	20,000
Children in couple households	*	*	10,000
Children in priority group households	10,000	10,000	20,000

[20] * denotes that the result was suppressed due to a small sample size.

[21] Small changes of below 5,000 are suppressed (marked as *) due to sample size. All figures are rounded to the nearest 10,000.

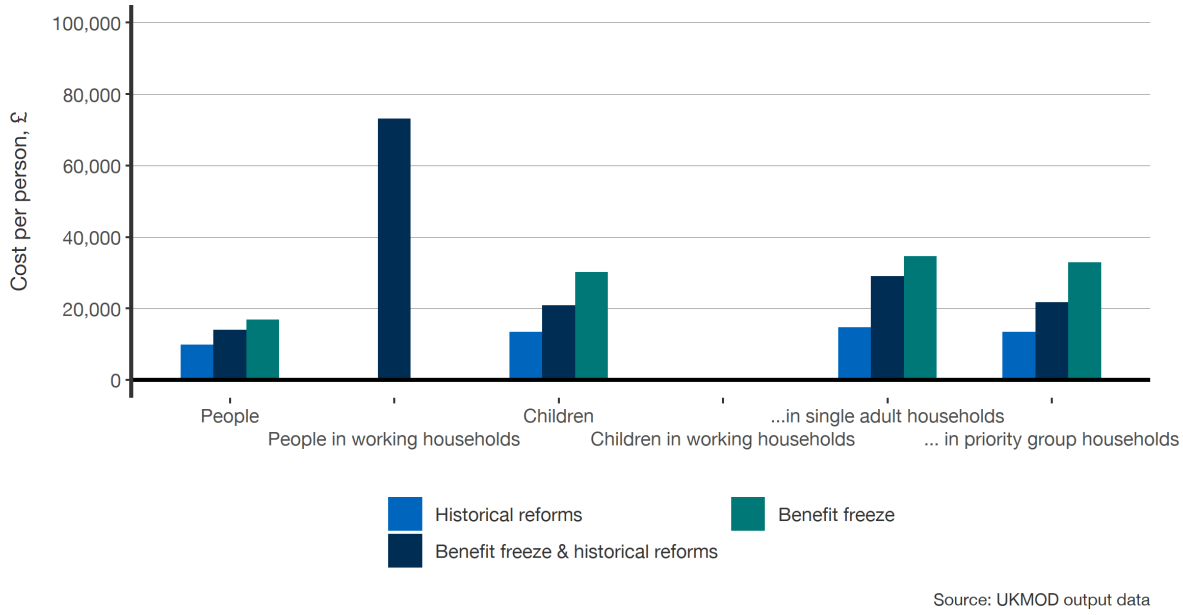
[22] The impact of reversing both reforms may not be the sum of reversing each individually. Welfare reforms also change the value of the median income (and thus the poverty line) and, due to the shape of the income distribution curve, some reforms can outweigh the impact of others even when the individual impact is smaller. Rounding can exaggerate this effect.

Reversing historical reforms and the benefit freeze has a large impact on those on or around the poverty line. The table above (figure 4.7) shows that 20,000 people would be moved out of poverty in 2023-24, including 10,000 children.

This would not have a significant impact on in-work poverty, but does have a particular impact on children in priority group households. The majority of children affected are in single adult households.

We can combine our analysis of additional expenditure and poverty rates to find which policies are most cost-efficient for moving people above (or below) the poverty line.

4.8 Cost per person brought of poverty by reversal of reform, Scotland, 2023-24



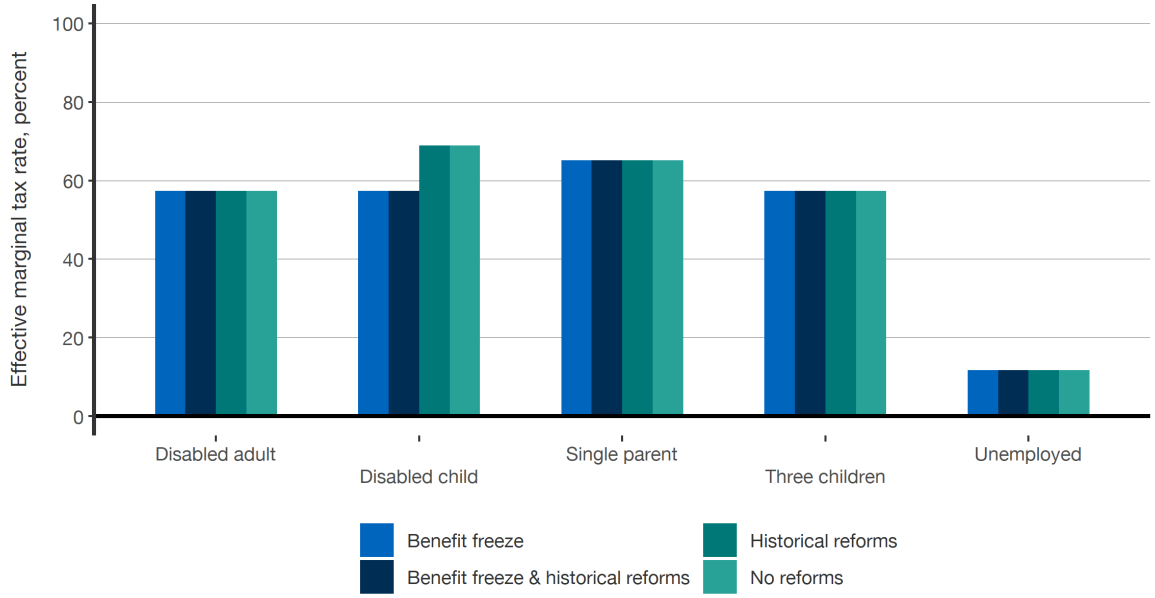
As shown in the graph (figure 4.8), reversing the two-child limit and the removal of the family element would cost less than £10,000 per person taken out of poverty.

There are no cases where reversing both reforms leads to efficiencies, with reversing the two-child limit and the removal of the family element usually the most cost-effective option, particularly for children. This is despite the benefit freeze having a larger overall impact on poverty rates.

There are a number of types of household, such as children in working households, where few people were brought in or out of poverty. These results have not been included in the chart, and demonstrate where reversing the reform would have no discernible impact on poverty rates for that group.

Work incentives

4.9 Effective marginal tax rate after reversing reforms, 10 additional hours of work per week, illustrative households, Scotland, 2023-24



The graph above (figure 4.9) demonstrates that compared with changes to the Universal Credit taper rate and work allowances, the reforms detailed in this section only have an impact on work incentives if households are close to the threshold for eligibility for benefits.

For most households the marginal effective rate is unchanged as a result of reversing these policies. For a household with a disabled child, reversing the benefit freeze reduces the effective tax rate because the increased benefit award keeps them above the eligibility income threshold for other benefits.

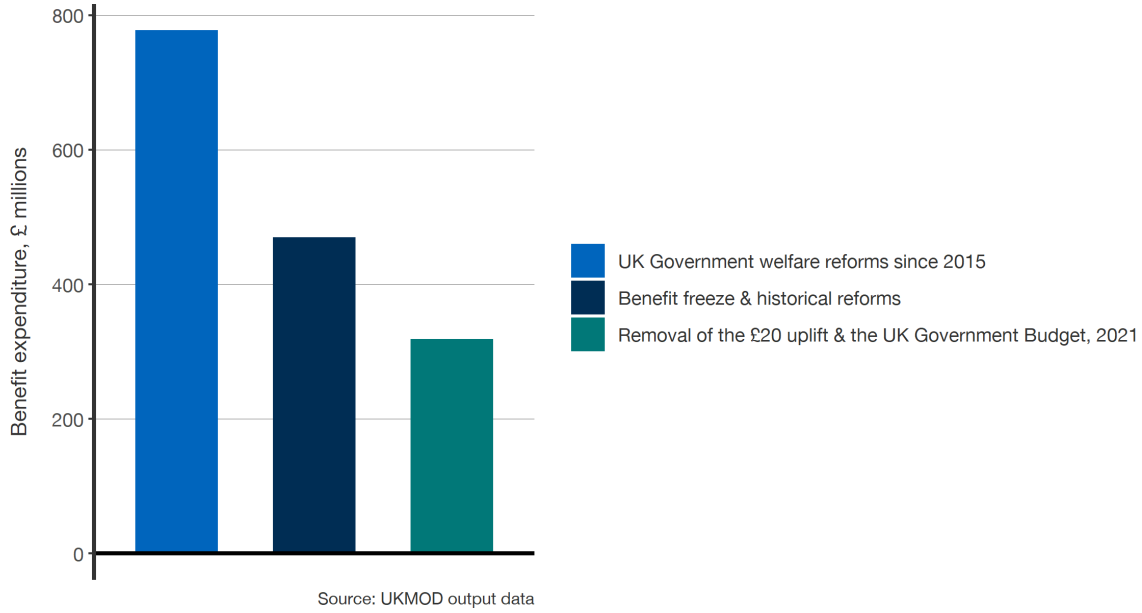
5 Cumulative impacts

Background

When new policies are introduced, they interact with those which are already in place. Considering the cumulative impacts of reversing both recent reforms and historical reforms therefore allows us to consider how welfare policies combine to impact the living standards of families.

Expenditure

5.1 Impact on benefit expenditure by reversal of reform, Scotland, 2023-24



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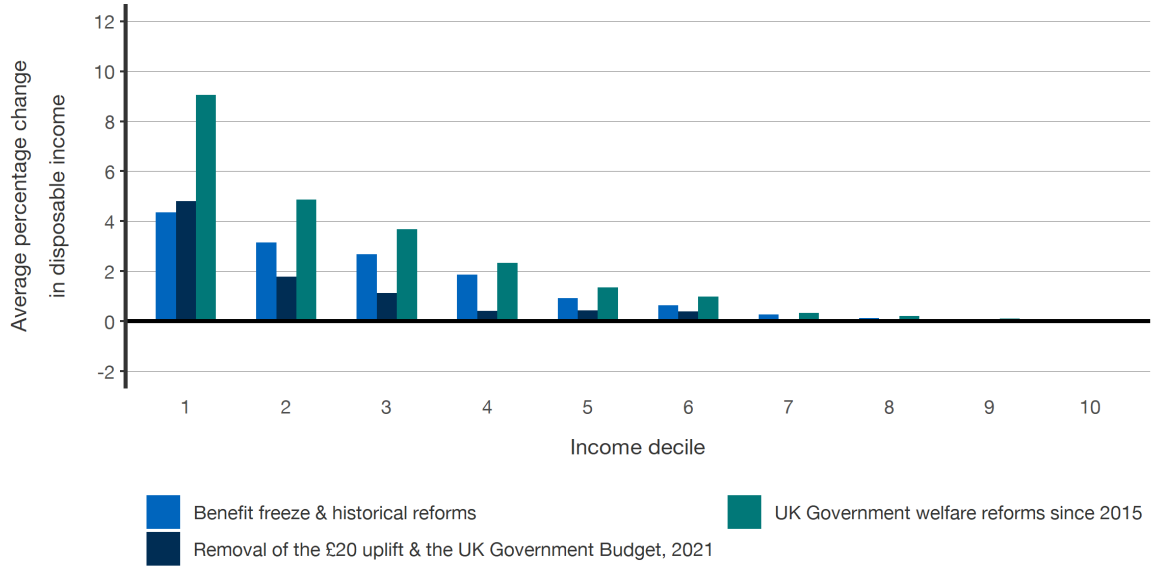
As shown in the graph (figure 5.1), the total cost of reversing UK Government reforms since 2015 would be around £780 million in 2023-24. This is a cumulative figure, with the cost of reversing the benefit freeze, the two-child limit and the removal of the family element (£470 million) and the reversal of recent reforms (£320 million) contributing to the total, including the offsetting effect of reversing the 2021 budget measures. These figures include both expenditure made by the UK Government (£730 million) on reserved benefits such as Universal Credit and by the

[23] Includes all benefit expenditure, including those devolved to Scotland.
[24] Expenditure would have been £14 million higher in the Benefit freeze reversal scenario had the benefit cap not been in place.

Scottish Government on devolved social security (£50 million) such as the Scottish Child Payment.

Disposable income

5.2 Percentage changes to disposable income after housing costs, by equivalised household disposable income decile, by reform reversed, Scotland, 2023-24



Source: UKMOD output data

As shown in the graph (figure 5.2), reversing both sets of reforms would have most impact on those in the lowest disposable income deciles, with the 10% of people in households with lowest incomes seeing increases of around 9% on average. The impact on incomes reduces as incomes increase, with recent welfare reforms contributing to this effect.

Depending on the median income in 2023-24, all households in income decile one and two and most in decile three will be in poverty. The cumulative impact of reversing all UK government reforms on people near the poverty line could be less than half that in the lowest income decile.

5.3 Percentage changes to disposable income after housing costs, by equivalised household disposable income decile, by reform reversed, households with children, Scotland, 2023-24

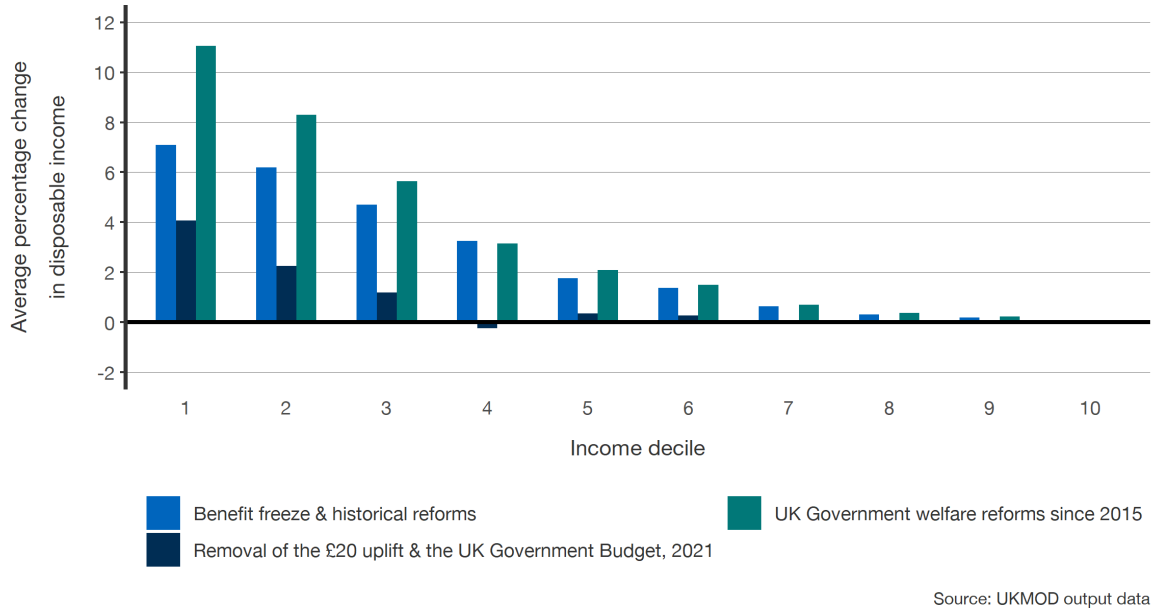
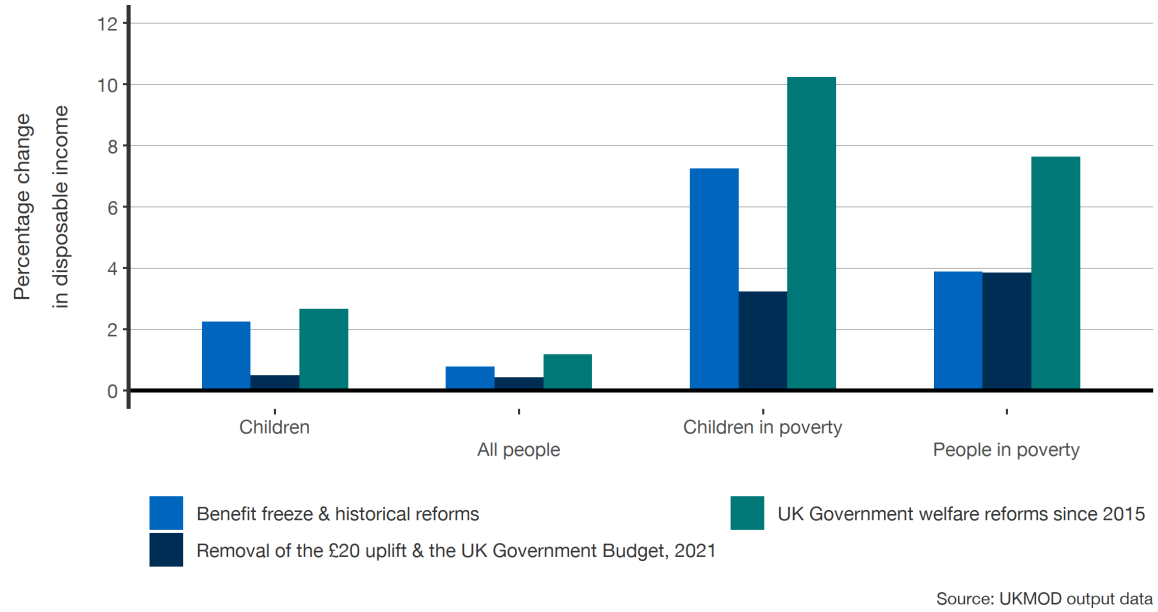


Figure 5.3 demonstrates that reversing all reforms would have a much larger impact on households with children, with significant increases in household income for those in the lowest income deciles (around 11%).

Recent welfare reforms are less important for children in these lower income deciles, and have negligible impact on those in decile 4 and above. Reversing the benefit freeze, the two-child limit and the removal of the family element would have a much more significant impact.

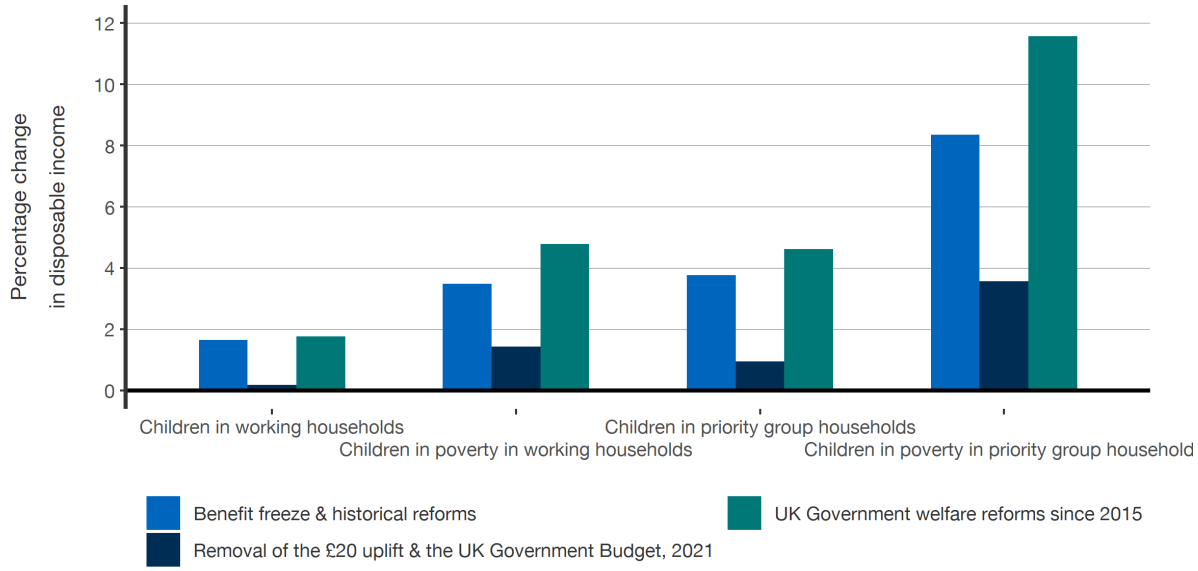
5.4 Average change in disposable income by household type after reversing reforms



Source: UKMOD output data

Figure 5.4 shows how reversing UK Government welfare reforms will have a marginal impact on incomes on average (around 1%). However, there will be a significant change for people under the poverty line in 2023-24 if all reforms are reversed. There is a particular impact on households in poverty with children (around 10% increase, on average), with reversing the two-child limit, the removal of the family element and the benefit freeze a more important policy change compared with the impact on other households.

5.5 Average change in disposable income by household type after reversing reforms



Source: UKMOD output data

Figure 5.5 further demonstrates how important reversing the two-child limit and the removal of the family element would be for children in poverty, while reversing all reforms would lead to a very significant increase of nearly 12% for the average income of children in poverty in the child poverty priority groups.

Household example: In 2023-24, the Hewitt household has earnings of £2,600 per month, with one adult working full time on the minimum wage and another working three days per week. They have three children. They live in Stirling and receive support for their housing costs with an Universal Credit award of £790 per month and Child Benefit of £52 per month. They pay income taxes of £180 per month.

- Reinstating the £20 uplift would increase their household income by £93 per month in 2023-24.
- Reversing the change to the Universal Credit earnings taper rate and work allowances would **reduce** their new, higher award by £203 per month, with their earnings eating into their benefit award at a higher rate of 63%.
- Abolishing the two-child limit and reinstating the family element would increase their award by an additional £303 per month, with their third child now recognised in their benefit award.
- Reversing the residual impact of the benefit freeze would impact on every non-housing element of their Universal Credit award (including the reinstated family element) along with child benefit. This would further increase their award by £91 per month, taking into account of the period when benefits were frozen between 2015 and 2019.

The cumulative impact of reversing all these reforms would increase their benefit award by £283 per month (34%). It would increase their disposable income (after housing costs) by 12%.

Poverty

The cumulative impact of reversing all UK Government reforms would reduce poverty in 2023-24. The graph above (figure 5.6) shows this would have a particular impact on child poverty, reducing the poverty rate by 3 percentage points. However, working households in poverty are less likely to be affected by the changes.

5.6 Impact on relative poverty rates by reversal of reform, percentage point change, Scotland, 2023-24[25]

	Benefit freeze, the two-child limit and the removal of the family element	Removal of the £20 uplift & the UK Government Budget, 2021	UK Government welfare reforms since 2015
All people	-1	-1	-1
Children	-2	-1	-3
People in working households	*	*	-1
Children in working households	-1	*	-1
Children in single households	-5	-2	-7
Children in couple households	-1	*	-1
Children in priority group households	-4	-1	-5
People in absolute poverty	-1	-1	-2
Children in absolute poverty	-2	-1	-3

Figure 5.6 demonstrates that the poverty rate for children in single adult households would be particularly affected by the reversal of these reforms, reducing it by around 7 percentage points. There is also a significant impact for children in priority group households (5 percentage points). The cumulative impact of reversing the benefit freeze, the two-child limit and the removal of the family element contributes more to these changes than more recent welfare reforms. The poverty rate for children in couple households is less sensitive to these changes.

The table also demonstrates that the absolute poverty rate for both children is about as sensitive to reversing all UK Government reforms as the relative poverty rate, while it is higher for people in general. The child poverty rate is more responsive to reversing the benefit freeze, the two-child limit and the removal of the family element relative to more recent reforms.

[25] * denotes that the result was suppressed due to a small sample size.

5.7 Number of people brought out of relative poverty by reversal of policy, Scotland, 2023-24[26]

	Benefit freeze, the two-child limit and the removal of the family element	Removal of the £20 uplift & the UK Government Budget, 2021	UK Government welfare reforms since 2015[27]
All people	30,000	30,000	70,000
Children	20,000	10,000	30,000
People in working households	10,000	10,000	20,000
Children in working households	*	*	10,000
Children in single households	20,000	*	20,000
Children in couple households	10,000	*	10,000
Children in priority group households	20,000	*	30,000

Reversing UK Government welfare reforms since 2015 would have a significant impact on poverty rates in Scotland. The table above (figure 5.7) shows that 70,000 people would be moved out of poverty in 2023-24, including 30,000 children.

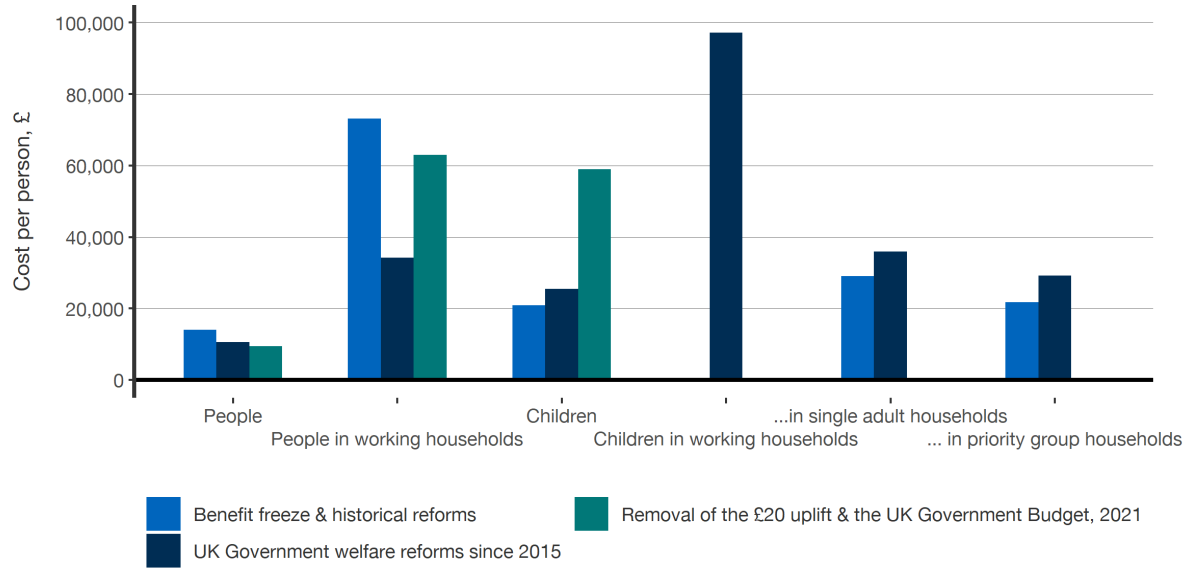
10,000 of these children would be in working households, and 20,000 would be in single adult households. 30,000 are in priority groups for child poverty.

We can combine our analysis of additional expenditure and poverty rates to find which policies are most cost-efficient for moving people above (or below) the poverty line.

[26] Small changes of below 5,000 are suppressed (marked as *) due to sample size. All figures are rounded to the nearest 10,000.

[27] The impact of reversing both reforms may not be the sum of reversing each individually. Welfare reforms also change the value of the median income (and thus the poverty line) and, due to the shape of the income distribution curve, some reforms can outweigh the impact of others even when the individual impact is smaller. Rounding can exaggerate this effect.

5.8 Cost per person brought out of relative poverty by reversal of reform, Scotland, 2023-24



Source: UKMOD output data

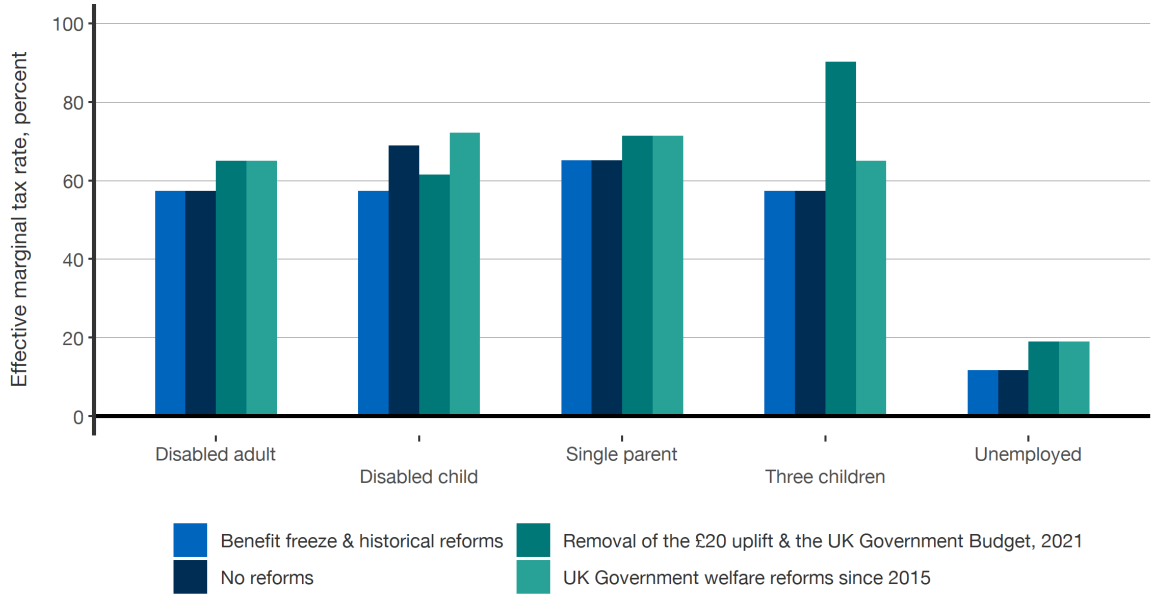
As shown in the graph (figure 5.8), reversing all welfare reforms since 2015 would cost less than £10,000 per person taken out of poverty.

Given the lower number of people in working households and children, it generally costs more to bring them out of poverty. However, the graph does show that reversing older reforms is more effective for targeting children, generally, while for working households reversing all UK Government reforms is most cost-effective (even though this increases the earnings taper rate and work allowance). Only for working households is there an efficiency gain by reversing all reforms.

There are a number of types of household, such as children in working households, where few people were brought in or out of poverty; the only discernible impact on poverty rates would come from reversing all reforms.

Work incentives

5.9 Effective marginal tax rate after reversing reforms, 10 additional hours of work per week, illustrative households, Scotland, 2023-24

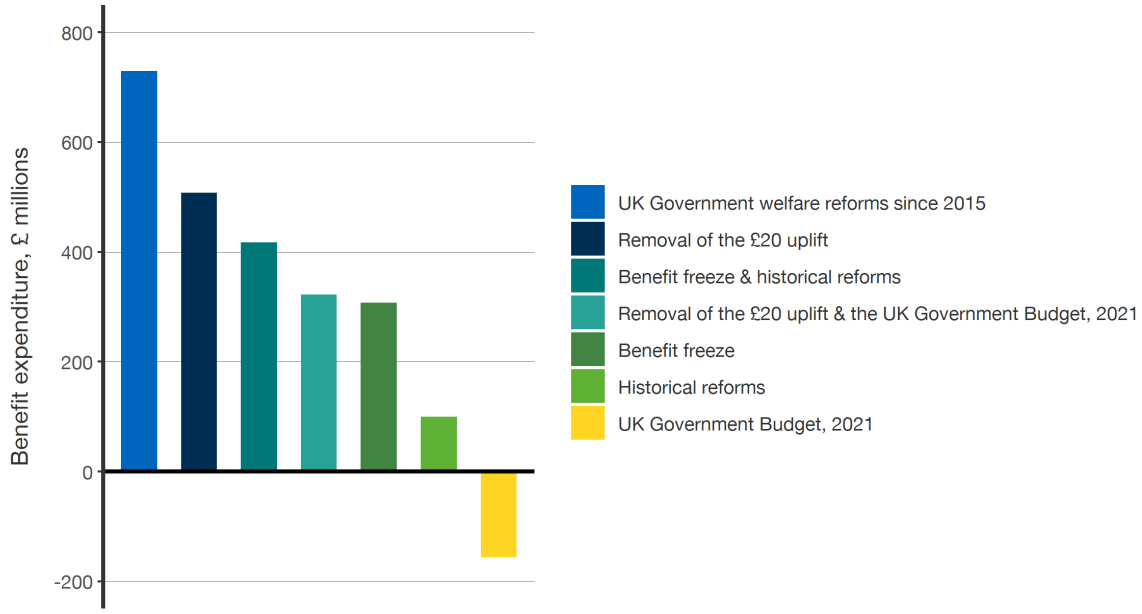


The graph above (figure 5.9) demonstrates that reversing all UK Government welfare reforms since 2015 increase the 'tax rate' for these example households, as increases in benefit award interact with changes in the Universal Credit earnings taper rate.

The graph also demonstrates the interactions between the policy reforms; for families with a large number of children, reversing the change to the taper rate would have a significant impact on the 'tax rate', but this impact would be largely offset by reversing other reforms.

Appendix A: Additional graphs

A.1: Impact on expenditure on reserved benefits by reversal of reform, Scotland, 2023-24



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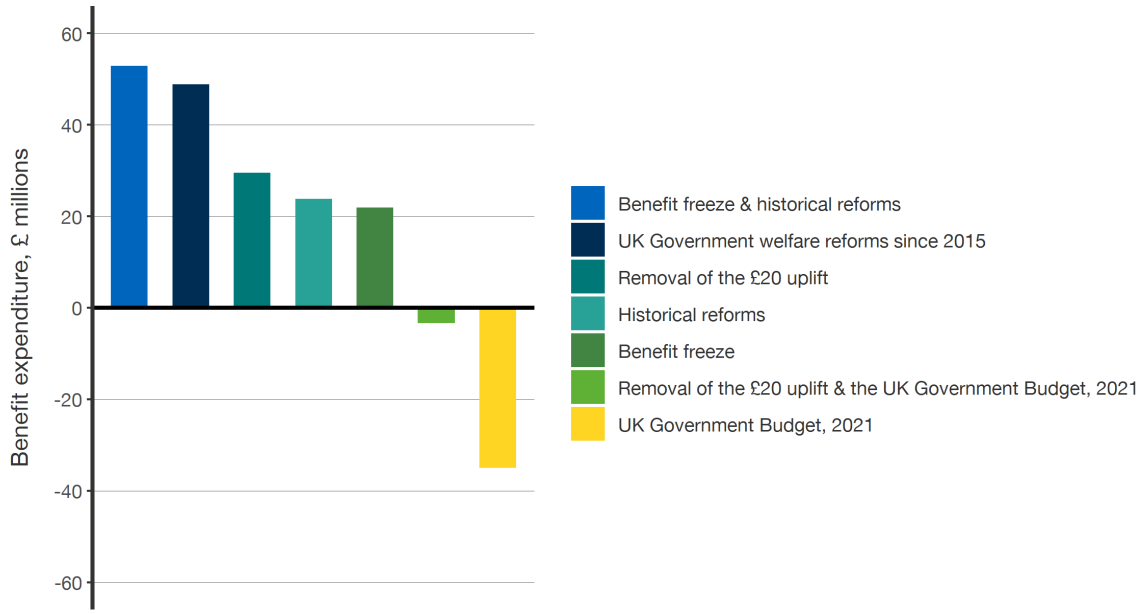
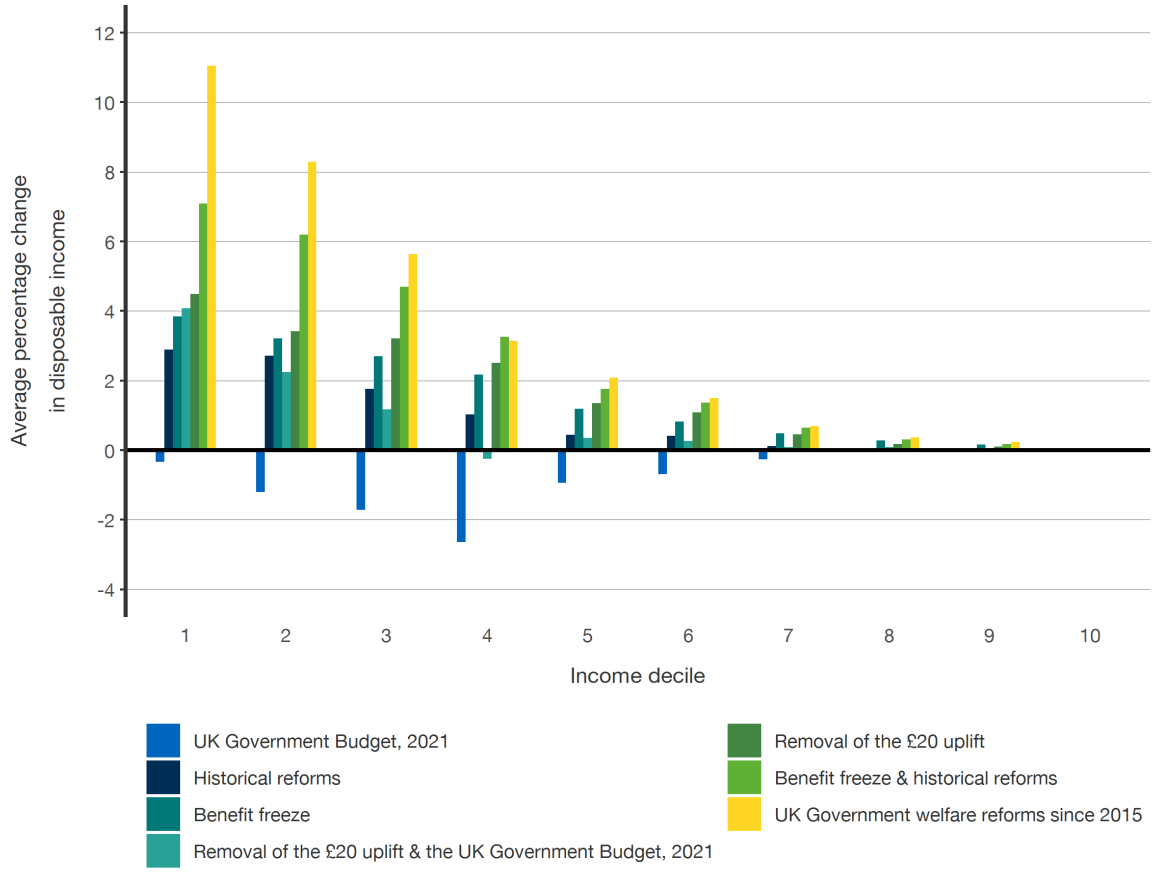
A.2 Impact on expenditure on devolved benefits by reversal of reform, Scotland, 2023-24[29]



[28] Excludes the benefit cap
[29] This is primarily expenditure on the Scottish Child Payment and Discretionary Housing Payments

A.3 Percentage changes to disposable income after housing costs, by equivalised household disposable income decile, by reform reversed, Scotland, 2023-24 (Households with children only)



Source: UKMOD output data

Appendix B: Additional tables

B.1 Most cost-effective way to reduce poverty in each group, Scotland, 2023-24[30]

Type	Best option	Second best option
Children	Two-child limit and the removal of the family element	Benefit freeze & two-child limit and the removal of the family element
People	Removal of the £20 uplift & the UK Government Budget, 2021	Two-child limit and the removal of the family element
Children in working households	All reforms	*
People in working households	UK Government Budget, 2021	All reforms
Children in single adult households	Two-child limit and the removal of the family element	Benefit freeze & two-child limit and the removal of the family element
Children in priority group households	Two-child limit and the removal of the family element	Benefit freeze & two-child limit and the removal of the family element

B.2 Number of people out of poverty by reversal of reform, Scotland, 2023-24

	Children	People
UK Government Budget, 2021	*	(10,000)
Removal of the £20 uplift	10,000	30,000
Removal of the £20 uplift & the UK Government Budget, 2021	10,000	30,000
Benefit freeze	10,000	20,000
Historical reforms	10,000	10,000
Benefit freeze & historical reforms	20,000	30,000
UK Government welfare reforms since 2015	30,000	70,000

[30] Excludes scenarios where fewer than 5,000 people are moved out of poverty, even if more cost – effective.

B.3 Average change in disposable income by reversal of reform, Scotland, 2023-24

	Children	People	Children in poverty	People in poverty	Children in working households	People in working households	Children in priority group households[31]
UK Government Budget, 2021	-1%	0%	0%	-1%	-1%	0%	0%
Removal of the £20 uplift & the UK Government Budget, 2021	0%	0%	3%	4%	0%	0%	4%
Two-child limit and the removal of the family element	1%	0%	3%	1%	1%	0%	4%
Benefit freeze	1%	1%	4%	3%	1%	0%	4%
Removal of the £20 uplift	1%	1%	3%	4%	1%	1%	4%
Benefit freeze & two-child limit and the removal of the family element	2%	1%	7%	4%	2%	1%	8%
UK Government welfare reforms since 2015	3%	1%	10%	8%	2%	1%	12%

[31] Only those in poverty

B.4 Number of people out of poverty by reversal of reform, Scotland, 2023-24, fixed versus floating poverty line

Differences highlighted in blue.	Floating poverty line		Fixed poverty line	
	People	Children	People	Children
Removal of the £20 uplift	30,000	10,000	50,000	10,000
UK Government Budget, 2021	- 10,000	*	- 20,000	- 10,000
Benefit freeze	20,000	10,000	30,000	10,000
Historical reforms	10,000	10,000	10,000	10,000
Removal of the £20 uplift & the UK Government Budget, 2021	30,000	10,000	40,000	10,000
Benefit freeze & historical reforms	30,000	20,000	50,000	20,000
UK Government welfare reforms since 2015	70,000	30,000	100,000	40,000

Note: Discussed below in **Appendix C**.

Appendix C: Methodology

In order to assess the impact of reversing each reform, we have used UKMOD, an open-access microsimulation model developed by the Institute for Social and Economic Research (ISER) at the University of Essex. The model applies tax and benefit rules to a set of individual and household-level data, allowing the user to simulate and compare alternative scenarios.

The input data in UKMOD is derived from DWP's Family Resources Survey (FRS). The analysis in this report uses FRS data from 2017-18, 2018-19, and 2019-20. To pool the data, the grossing weights used to scale the FRS sample to the whole population are divided by the number of data years, in this case three, and a set of adjustments are applied in order to uprate them to 2023-24.

The baseline in the model is equivalent to 2023/24 'policy' scenario in the Cumulative Impact Assessment which was published alongside the 2022 Tackling Child Poverty Delivery Plan.[32] All impacts outlined in this report are relative to that projection.

Behavioural response

A significant caveat is that UKMOD is a static model; that is, it does not model changes in behaviour resulting from changes in policy. Previous analysis by the Scottish Government has found that increases in tax are likely to have behavioural effects, so we can assume that changes to the Universal Credit earnings taper rate, for example, could have a similar impact.

By modelling the reversal of these reforms in the future (2023-24), the behavioural response to their implication has been captured in the underlying input data. Therefore our results illustrate only the short-run impact of any change.

The implications of any *future* behavioural effect on the reversal of these reforms is uncertain. We found that changes to the earnings taper rate are marginal for working families who pay Income tax and National Insurance, but more significant for those whose earnings are above the Universal Credit work allowance but below the income tax or national insurance thresholds.

Universal Credit roll out

Some of the reforms detailed in this report only impact on Universal Credit. UKMOD assumes that only 68% of households to have migrated across to Universal Credit from legacy benefits by 2023-24, and thus the impact of such reforms will be limited to these households.

Disposable income

Income is defined as equivalised disposable household income after housing costs. This comprises total income from all sources across the household, minus income

[32] Tackling child poverty delivery plan 2022-2026 - annex 4: cumulative impact assessment - gov.scot (www.gov.scot)

tax, national insurance contributions, pension contributions, and some others transfers such as child maintenance payments. Housing costs are also subtracted from income; these include rent, water rates, mortgage interest payments, structural insurance premiums, ground rent, and service charges. Income is then adjusted to take into account variations in the size and age composition of different household in a process known as equivalisation.

This equivalisation process does not take place for the illustrative households detailed in the report; the disposable incomes presented there are not adjusted for household composition.

Floating UK relative poverty line

The relative poverty line is calculated as 60% of median UK equivalised household disposable income after housing costs. Previous welfare reform reports held the poverty line constant when comparing scenarios.

However, the welfare reforms described here impacted households across the UK and reversing them will, in some cases, have a material impact on UK median incomes, particularly when they relate to earnings. This has a subsequent impact on the UK poverty line and thus poverty rates in Scotland.

We therefore recalculate the UK poverty line in each scenario and apply this line to our calculations. The difference this change in methodology has on poverty rates is detailed Appendix B, table 4., which illustrates how the number of people brought out of poverty is smaller compared with an analysis that uses a fixed poverty line.

Household example: The Ladder household is not on benefits and their income is not affected by any of the welfare reforms detailed in this report. Their household income is just above the poverty line.

Following the reversal of a reform, the median UK income has increased, and the **floating** UK poverty line shifts upwards. Despite seeing no change in their income, the Ladder household is now in relative poverty having dropped below the poverty line.

The Cromdale household, however, was affected by the reform and lifted out of poverty. The net impact on poverty across these households is zero.

Fixed UK absolute poverty line

This line is based on the 2010-11 relative poverty line and adjusts for inflation only.

Appendix D: Illustrative households

The illustrative households set out below are based on the following broad assumptions, designed to provide a reasonable illustration of how the reforms might impact on typical households in Scotland. They do not provide a comprehensive view, and few (if any) households in Scotland will have the precise characteristics set out below.

- Working single mothers work 19 hours per week, on average[33]
- The minimum wage will be uprated at the same rate as other wages by 2023 (3.9%). This wage is used for the lone parent and unemployed households only[34]
- The median salary in Scotland will have increased by 9% by 2023 compared with 2021. [35]
- Rent is based on Local Housing Allowance rates for Stirling[36]
- Other household characteristics have been chosen for simplicity or analytical purposes

		Baseline				
		Lone parent	Three children	Unemployed	Disabled adult	Disabled child
Equivalised household income, AHC, baseline		12,000	10,000	6,500	14,400	13,200
Rent		500	940	650	650	650
Salary basis		Minimum wage	Average salary	-	Average salary	Average salary
Adult 1	Age	24	45	45	45	45
	Hours worked per week	19	37.5	0	37.5	37.5
	Earnings per month	810	2880	0	2880	2880
	Work history	6	27	0	27	27
Adult 2	Age		45	45	45	45
	Hours worked per week		0	0	0	0

[33] Income from employment - Tackling child poverty: second year progress report - annex C - gov.scot (www.gov.scot)
[34] Economic and fiscal outlook - October 2021 - Office for Budget Responsibility (obr.uk)

[35] Annual Survey of Hours and Earnings (ASHE) – Estimates of full-time employee, full-time male and full-time female annual earnings by occupation and region, 2020 and 2021 - Office for National Statistics (ons.gov.uk)
[36] Local Housing Allowance Rates: 2021-2022 - gov.scot (www.gov.scot)

	Earnings per month		0	0	0	0
	Work history		0	0	15	0
Child 1	Age	1	16	16	16	16
Child 2	Age		12	12	12	12
Child 3	Age		8			
Manual benefits					£388 per month DLA /PIP	£388 per month DLA /PIP

		Baseline + 10 hours work				
		Lone parent	Three children	Unemployed	Disabled adult	Disabled child
Equivalised household income, AHC, baseline		13,400	11,600	8,700	15,300	14,500
Rent		500	940	650	650	650
Salary basis		Minimum wage	Average salary	Average salary	Average salary	Average salary
Adult 1	Age	24	45	45	45	45
	Hours worked per week	29	37.5	10	37.5	37.5
	Earnings per month	1240	2880	430	2880	2880
	Work history	6	27	27	27	27
Adult 2	Age		45	45	45	45
	Hours worked per week		10	0	10	10
	Earnings per month		780	0	430	780
	Work history		27	0	15	27
Child 1	Age	1	16	16	16	16
Child 2	Age		12	12	12	12
Child 3	Age		8			
Manual benefits					£388 per month DLA /PIP	£388 per month DLA /PIP

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Any enquiries regarding this publication should be sent to us at

The Scottish Government
St Andrew's House
Edinburgh
EH1 3DG

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