2015 Budget Representation to HM Treasury

Submission by the Joseph Rowntree Foundation

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Joseph Rowntree Foundation works for social change in the UK by researching the root causes of social problems and developing solutions. We use our evidence and our practical experience of developing housing and care services to influence policy, practice and public debate. We are politically independent, but we are not neutral about poverty.

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Summary of recommendations

**Low paid work**

- Change the remit of the Low Pay Commission to allow it to take into account a wider range of factors including changes to the cost of living.

- Devolve the majority of the skills budget to city regions in partnership with employers and skills providers so that supply can better match the demands of the labour market.

- Alongside this promote greater demand for skills by encouraging LEPs to experiment with new ways of working that pull together local skills strategies with economic development, innovation and business support strategies, focussing on low paid sectors;

- This work should be complemented by national, sector specific strategies for encouraging innovation within industries that have high proportions of low paid low skilled work, to connect with the support offers that LEPs’ make to local firms.

- Set out a timescale and implementation plan for including measures to tackle in-work poverty in all public procurement, including across local government, social care and the NHS.

**Welfare reform**

- Introduce a second earner disregard within Universal Credit so that people keep more of the money they earn before in-work benefits are withdrawn

- Target a greater proportion of the money set aside to support childcare costs on lower income families.

**Housing**

- Initiate a process of shifting housing subsidies away from a reliance on Housing Benefit towards increasing the supply of houses that are genuinely affordable to the lowest paid.
**Public services**

- Slow the pace of local government cuts to allow local authorities and their partners enough time to plan the next phase of reform.

- Lead a review of the public accounting systems necessary to allow local agencies to more effectively share the financial risks and rewards of preventative work.

- Declare the care sector a ‘sector of primary national strategic importance’, supported by a more sustainable funding settlement which shares responsibility equitably for the costs between the state and the citizen.
Introduction

Amidst the news of higher growth and lower unemployment the Chancellor used his 2014 Autumn Statement to highlight several unresolved economic problems. They were a still too high deficit; low productivity and skills levels; inadequate infrastructure; and a regional imbalance. Given the salience of these to household incomes (alongside changes to in and out work benefits) the UK’s mixed record in tackling poverty recently should not come as a surprise.

Whilst a sustained cross party consensus has delivered the lowest ever levels of pensioner and child poverty since 1981, poverty among working-age adults without children is at its highest point in more than four decades. In addition to restricting people’s chances to lead fulfilling, independent lives the labour and housing market problems that lend contemporary poverty its specific character generate substantial public finance pressures, making the deficit challenge harder.

However there are no quick or easy ways to solve the crisis. To make progress we must understand both the causes of poverty and its dynamic nature. A large percentage of the population will experience relative income poverty at some point in their lives. Their chances of escape will depend on personal decisions and circumstances as well as on policies enabling rather than constraining their ability to chart a course out.

The Government’s formula of labour activation through welfare reform, reduced income taxes for low earners and the triple lock for state pensions has yielded benefits for some households. Recent ministerial statements urging employers to pay the living wage where affordable are also welcome. Nevertheless, continuing complexity in the tax and benefits system, uneven economic growth, the decreasing value of working age benefits for people whether they are in employment or not; rising housing costs and the preponderance of low paid low skilled work from which only a minority escape are all substantial hindrances to poorer households.

To that point, JRF is currently working towards the development of the UK’s first evidenced anti-poverty strategy for all age groups. As part of this work we have commissioned several reviews of existing research and policy to assess
what works best to reduce poverty across areas such as employment, education, taxes and benefits, families and relationships, and the cost of living.

Some of these have helped to inform the following submission, which contains several ideas for how the Government – within the broad confines of its economic plan - could do more to help people carve a path out of poverty. Although the recommendations cover a range of policy areas, including the cities agenda, housing, and welfare reform they share a common theme of trying to tackle underlying causes rather than symptoms. Each proposal is supported by rigorous research with further detail on the findings briefly outlined here to be found in the reports listed in the bibliography.

Low paid work

Compared to other developed countries, the UK has a relatively large number of people working in low-paid, low-skilled jobs (see for example Whittaker and Hurrell 2013; Lanning and Lawton 2012). This is an important driver of the UK’s high levels of in-work poverty: half of all people living in poverty now live with an adult in work. Pay is the biggest factor predicting in work poverty, but other issues are also very important including hours of work, the number of adults in a household who work, security and opportunities for progression. Low-paid work may be acceptable as a transitional step into better work, but this is not the case for large numbers of people. Only a fifth of low-paid workers have escaped low pay ten years later (Hurrell 2013). This has implications for the country as a whole. The UK’s reliance on so much low-paid, low-skilled work holds back UK wide productivity, which compares poorly to other countries (OECD 2012).

Concern about in work poverty and the progression of low paid workers is a relatively new policy interest. One consequence of this is that it has not yet been fully integrated into many aspects of policy infrastructure, including the National Minimum Wage (NMW), itself is an important regulatory feature affecting the behaviour of firms. Between 2009 and 2012, the national NMW rate increased by only 7 per cent, at which point the numbers of low paid began to rise. This smaller uplift reflected concerns over the impact on employment levels of increasing rate. However as the Chancellor has noted, the labour market has been gaining strength recently, with both unemployment and the broader underemployment measures falling.
The slower rate of uplift from 2009 also coincides with an overall deterioration in living standards, with the proportion of people living in households below the JRF’s Minimum Income Standard increasing by a fifth between 2008/9 and 2011/12. Most of the increase came in the final year of this period. The most severe increase has been among single people of working age, where the percentage unable to afford this minimum acceptable standard of living rose from 29 per cent to 36 per cent (Hirsch 2013). The dramatic deterioration in single people’s circumstances is associated declining benefit levels and a sharp increase in private renting; where disposable income can be severely affected by high rent levels. Our research also suggests that the rate of inflation experienced by lower income households can be higher than the general rate due to a larger proportion of their budgets going towards essentials. **We therefore recommend that the remit of the Low Pay Commission should be changed to allow it to take into account a wider range of factors, including changes to the cost of living for low income households.**

In addition to regulatory pay structures, historically the main approaches taken to improve earnings among employees have been on the supply side of the economy, particularly training. It is certainly true that training and skills development will be important for some low paid employees. **We therefore support devolving the majority of the skills budget to city regions in partnership with employers and skills providers so that supply can better match the demands of the labour market.** However, analysis by Barnes and Lord (2013) also shows that a relatively large proportion of working age households living in poverty contains members that already hold medium to high level qualifications. In other words supply side interventions to up-skill employees and support progression will have limited impact in the absence of more demand for skilled workers, which is a problem in parts of the UK labour market.

The evidence suggests integrating local skills strategies with economic development, innovation and business support strategies can result in more opportunities to shape firms’ demand for skills (Sissons and Jones 2014; Henderson et al 2013) **Policy-makers and agencies should work with employers and business to create an environment where providing better conditions and opportunities becomes a logical (and desirable) choice for large numbers of employers. Much of the action to improve the quality of jobs and access to them needs to be taken at local authority and city region**
level and the Government’s work supporting agglomeration in the North and in other regions could act as an accelerant to this process.

However such potential is hampered by the remit and capacity of Local Enterprise Partnerships. Research for JRF demonstrates that they will need considerably more capacity to develop effective strategies to use employment and skills policies to tackle poverty. Many currently lack this capacity. There is also an underlying problem of their remit. Most LEPs focus almost exclusively on growth and have little interest in issues relating to poverty, despite their role being expanded to include administering European Social Fund spending. Local Enterprise Partnerships should be at the forefront of tackling in-work poverty; their goals, incentives and capacity need to support this. This would not only have positive benefits for people living in their area, it would also bring a net benefit to the Treasury as more people move into work and increase their hours and earnings.

To encourage greater local efforts to improve the quality of jobs on offer further national action is also required. First, we would urge the Treasury to work with the Department of Business, Innovation and Skills to develop a set of national, sector specific strategies to encourage innovation within industries with high proportions of low paid low skilled work, to connect with LEPs’ local business support offer.

Second, public sector procurement too has a part to play. For example, in the adult social care sector, local authorities are major purchasers of social care services, but pressure on their budgets combined with the availability of low skilled workers means companies providing care have little incentive to improve employee pay, conditions and working practices.

Procurement can additionally be used as a lever to secure employer engagement in career ladder or sectoral training programmes and increased coverage of the living wage. Recent JRF research (MacFarlane 2014) has shown that significant impacts on poverty could be achieved if the UK public sector pledged to generate a year’s work for a person from a target disadvantaged group for each £1million in contract value. The research suggests that requiring contractors to do this involves little or no extra cost, boosts the local economy and benefits contractors, who get a skilled and committed workforce.
Using procurement to engender greater uptake of the living wage may require longer timescales to enable contractors in some sectors to achieve this and to allow government commissioners to consider the cost implications and how far these can be mitigated by improving productivity and delivery mechanisms. To enable this we recommend the Government set out a timescale and implementation plan for including measures to tackle in-work poverty in all public procurement, including across local government, social care and the NHS.

Welfare reform

Important as pay is, it alone it does not offer a sufficient response to the problem of in-work poverty. Research for JRF has shown that 44 per cent of adults experiencing in-work poverty aren’t low paid themselves and don’t live with anyone who is. Only 12 per cent live in a family where everyone is low paid. In other words it is the amount of work that seems to matter to many households in working poverty. In nearly half of these households, one person works and one doesn’t (MacInnes et al, 2013 & 2014). Another quarter only have part-time workers. Yet despite wanting to encourage more people into work, and to work more hours the current welfare system continues to create disincentives for doing so.

The case of single earner families demonstrates well the way in which the labour market, tax and benefit systems interact to the detriment of some families. Financial incentives are particularly important for second earners in low-income households to move into work or work more hours. However the work incentives within the benefits system are already not strong for this group, and they are set to lose out in the transition to Universal Credit, as it has no earnings allowance for second earners, meaning the value of UC payments reduces as soon as the second earner enters work. Introducing an earning disregard for second earners, so they can keep more of their pay before benefits begin to be withdrawn, is likely to make paid work more worthwhile for this group, thus helping the Government to meet its employment targets. A second-earner disregard set at the same level as the existing disregard for a couple without children would cost around £700 million a year.
Other barriers also frequently prevent it paying to work. Chief among these is the cost of childcare and the challenge of balancing working and caring. Good quality and accessible childcare plays an important role in preventing poverty by enabling more parents to work and through its contribution to child development. This suggests that bringing down the cost of childcare will have a significant impact on low income households where childcare costs constitute a larger proportion of disposable income.

We therefore welcome the Government’s decision to raise the proportion of help with childcare costs that the parents of families in Universal Credit receive from 70 to 85 per cent. However we also think there are better ways to pay for it than by freezing the Universal Credit work allowances at their current level for an extra year. Cuts of this kind to in-work support are likely to lead to a further deterioration in living standards for households with and without children at the bottom of the income scale, even if they are able to secure additional hours of work.

A more progressive means of paying for the increased support would be to redirect some of the £750 million set aside for funding the tax free childcare aspect of the policy. As it currently stands the funds will benefit families earning as much as £150,000 in 2013/14. Targeting more of this resource at households in receipt of UC would support the government’s employment goals.

Housing

Despite the UK having one of the highest poverty rates in Western Europe key elements in the housing system including social rented housing, Housing Benefit, and mortgage-free retirement have helped to limit poverty rates. Indeed modelling for JRF suggests poverty levels in England can only continue to be contained if housing supply nearly doubles to 200,000 homes a year by 2040; social rents do not move closer to market rates and rises are limited to 1 per cent over inflation; Housing Benefit meets a similar proportion of rent as in 2008; and tenure patterns remain unchanged (Stephens at al, 2014).

The housing system is changing however, as private renting grows and social rents, at least in some parts of England, rise towards market levels. The ability
of Housing Benefit to protect tenants from higher rents has already been reduced in response to rising cost pressures, and this seems set to continue.

In the absence of reforms to the private rented sector social rented housing is likely to provide the most suitable option for households, especially those with children that seek long-term security but cannot access full or shared ownership safely. The National Affordable Homes Programme (NAHP) relies on stretching Government subsidy over more units by charging near (i.e. up to 80 per cent) market rents on new social lets and a proportion of re-lets, leveraging a much higher proportion of development costs in from the private sector and expecting housing associations to contribute by running down their balance sheets.

However it is uncertain whether the ‘affordable rent’ regime is viable beyond the current spending period. First, the differential between social housing and affordable housing rents varies considerably across England. In some areas social housing rents are at or even above market rents and thus there is little potential for creating an ‘affordable’ rental market. Elsewhere there are considerable differentials between social and market rents and this creates a space for ‘affordable’ rental products, with and without housing benefit subsidy but there are emerging concerns about the affordability of these higher rents to those prioritised for affordable housing, particularly since the welfare reforms came fully into effect in 2013. To avoid the relationship between housing and poverty becoming stronger over the medium term we recommend that the Treasury begin to develop a strategy ahead of the next spending round for shifting housing subsidies away from a reliance on Housing Benefit towards housing supply, as part of a new model for financing housing that is affordable to people on the lowest incomes.

Public services

Public services play an important role in the lives of people on low incomes. It is therefore a cause for concern that the cuts to local authority spending power are systematically greater in more deprived local authorities than in more affluent ones, with a difference of around £100 per head in both England and Scotland. Reductions have also generally been greater in the North and Midlands than in the south of England, and in the west rather than the east of Scotland. Having protected many services aimed at vulnerable groups local
authorities are now at a crossroads, leaner but not necessarily stronger (Hastings et al, forthcoming).

Nonetheless a new wave of retrenchment and reform is inevitable if resources are squeezed further during the next spending round. To avoid public discontent a new strategy is needed to give local authorities the requisite space to engage their communities and plot the next phase of reform. **We therefore recommend slowing the pace of local government cuts to allow local authorities and their partners enough time to plan the next phase of reform.** Central to any effective reform will be a greater focus on prevention. However the loss of organisational capacity and the urgency of the cuts conspire to make this difficult, as does the often long pay back periods and the risk of the gains going to other agencies. **We urge the government to consider how local agencies can be enabled to more effectively share the financial risks and rewards of preventative work, building on the work of CIPFA, the LGA and others.**

Finally, it is clear that the social care sector is in crisis. According to one estimate, cuts to local authority budgets have resulted in a 20% reduction in funding for adult social care since 2010, after adjustment for inflation and increased number of people with eligible care needs (Association of Directors of Adult Social Services 2013). Trying to deliver social care on the cheap is very expensive. The opportunity cost of low investment in our social care system is simply pushing higher cost onto the NHS. It is also inhibiting our national economic potential by failing to effectively support a modern labour force. **Ahead of the next spending round we believe the time is right to declare the care sector a ‘sector of primary national strategic importance’, supported by a more sustainable funding settlement which shares responsibility equitably for the costs between the state and the citizen.**

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