On Target

Protecting vulnerable households from the inflation crisis

September 2022

The Centre for Social Justice

www.centreforsocialjustice.org.uk

Table of Contents

About the Centre for Social Justice

Established in 2004, the Centre for Social Justice is an independent think-tank that studies the root causes of Britain's social problems and addresses them by recommending practical, workable policy interventions. The CSJ's vision is to give people in the UK who are experiencing the worst multiple disadvantages and injustice every possible opportunity to reach their full potential.

The majority of the CSJ's work is organised around five "pathways to poverty", first identified in our ground-breaking 2007 report, Breakthrough Britain. These are: educational failure; family breakdown; economic dependency and worklessness; addiction to drugs and alcohol; and severe personal debt.

Since its inception, the CSJ has changed the landscape of our political discourse by putting social justice at the heart of British politics. This has led to a transformation in government thinking and policy. For instance, in March 2013, the CSJ report It Happens Here shone a light on the horrific reality of human trafficking and modern slavery in the UK. As a direct result of this report, the Government passed the Modern Slavery Act 2015, one of the first pieces of legislation in the world to address slavery and trafficking in the 21st century.

Our research is informed by experts including prominent academics, practitioners and policy-makers. We also draw upon our CSJ Alliance, a unique group of charities, social enterprises and other grass-roots organisations that have a proven track-record of reversing social breakdown across the UK.

The social challenges facing Britain remain serious. In 2022 and beyond, we will continue to advance the cause of social justice so that more people can continue to fulfil their potential.

Acknowledgements

With thanks to Deven Ghelani, Alex Clegg, Tylor-Maria Johnson and the Policy in Practice team for the analysis which is included in this report. We are indebted to many charities who gave up time to talk to the CSJ about the ongoing impact of the cost of living crisis on their clients.

> *We are finding that many more people are now coming to us in crisis and finding that crisis point is coming much quicker than it previously did. We have come straight out of a pandemic and hit people with a cost of living crisis. When the headlines in the papers say 'heat or eat' this is not an exaggeration, this is happening.*

CSJ Alliance charity, Bridlington, Yorkshire

> *The current cost of living has had a significant impact on the families we support. It has had both a negative impact on pupil's education but also their mental health as they see parents struggling with costs. One pupil was missing a Thursday and Friday of school; we found out later it was because their mum had only enough money for fuel to fill the car up Monday-Wednesday.*

CSJ Alliance charity, Craigavon, Northern Ireland

> *The more families are under pressure, the more children will suffer and not only in terms of their emotional and cognitive development but also nutrition and health. The rising stresses in life will take over*

CSJ Alliance charity, Wallasey, Merseyside

Executive Summary

It has become increasingly obvious that the cost of living crisis is going to get worse before it gets better. With energy bills to hit £3,549 in October and forecast to exceed £5,380 in January,[1] we are now faced with the prospect of a devastating autumn and winter period for several million people.

In this paper we propose a new package of cost of living support, combining effective 'tax cuts' for the poorest working households with a highly targeted welfare boost for households on Universal Credit (UC), legacy benefits and pension credit.

The package would see low-income households receive an additional £262 between October and January 2023 on average, rising to £288 for lone parents and £462 for couples with children, to help protect the worst off from spiking inflation.[2] On top of this, we recommend restoring UC Work Allowances to their pre-2016 levels, which would see 1.87 million of the poorest working households keep more of their earnings to battle the rising cost of living – boosting incomes annually by an average of £449.

The 13.3 per cent benefit uprating and effective 'tax cut' package can be implemented immediately this autumn following a special fiscal event. We estimate that this would cost £3.8 billion and help over 8.5 million household over an initial three-month period.

New analysis by Policy in Practice of granular income and expenditure data from over 114,000 low-income households suggests that this package would help to significantly counteract the fall in average real income levels among poorer households now expected this autumn (which sadly persist even when factoring in the welcome £15 billion support package that Government is already providing).

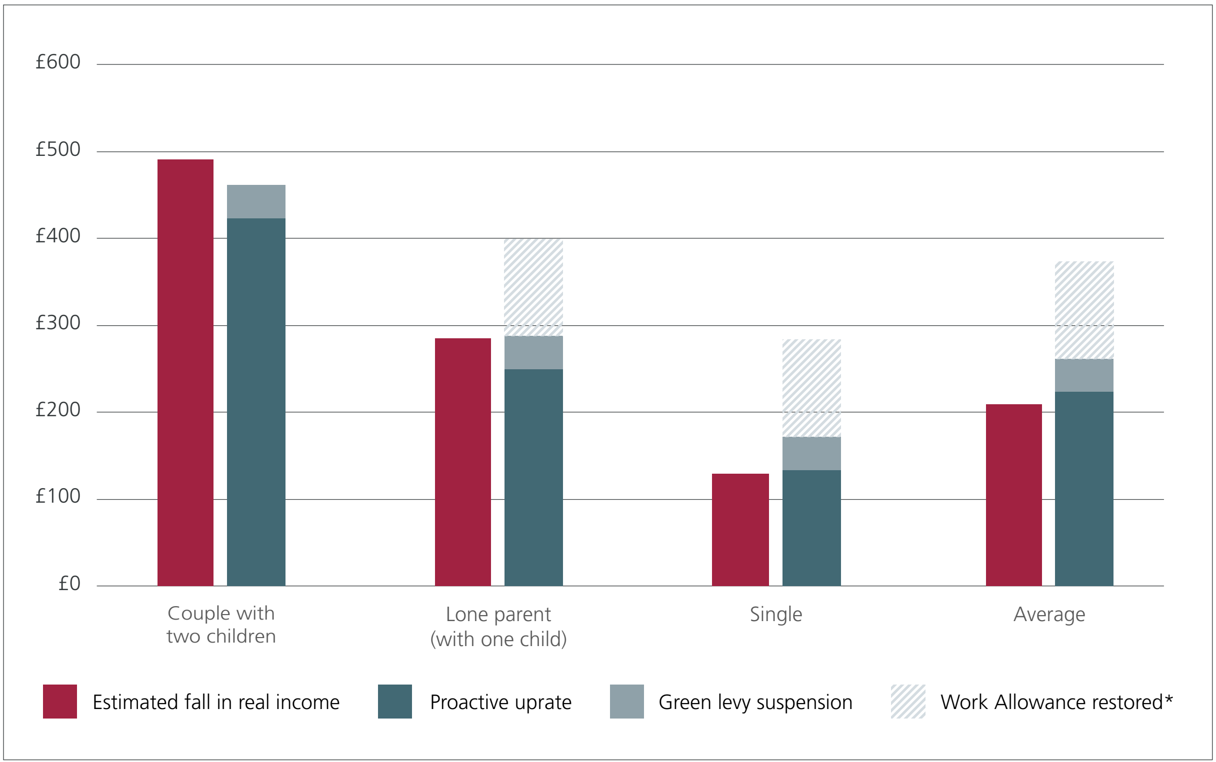
The Government should use more up to date data to inform a further tranche of support, which we recommend should be rolled out in January 2023 when prices are set to rise even more astronomically. If current inflationary forecasts are unchanged, the cost of the intervention would rise to around £8.2 billion if extended by another three months to April 2023.[3]

1 Cornwall Insight, 'Cornwall Insight comments on the announcement of the October price cap', August 2022

2 These estimates factor in the suspension of so-called green levies (see below, ch 10) but exclude other measures affecting a significant minority of recipients such as the suspension of government debt deductions in Universal Credit.

3 The figure uses a January energy price cap forecast of £5,380 (Cornwall Insights, August 2022) and CPI inflation of 13.3 in October and 15 per cent in January (Bank of England, August 2022)

Figure 1. The impact of the proposed welfare and effective 'tax cut' package for households on means-tested benefits (October 2022 – January 2023)



*Source: Policy in Practice analysis of local authority administrative data on 114,000 low-income households on council tax support and/or housing benefit across six local authority areas in July 2022; ONS Family Spending Workbook; Ofgem; Cornwall Insights; DWP Stat X-plore; authors calculations. *The Work Allowance element is averaged by household type and only applies to UC claimants.*

We recognise it is not just the worst off facing extremely difficult choices this autumn/winter. Our targeted proposal leaves fiscal headroom for the new Prime Minister to direct additional support to middle-income households (for example through the tax system) and small businesses, many of whom will also struggle to absorb spiralling energy costs.

By using the welfare system, our recommendations avoid the issues associated with proposals made by others to distribute further 'flat-rate' payments or rebates universally, which do not account for varying bill sizes across household types, as well as attempts to 'freeze' the global energy market, which would see wealthier households receive the same support as those on the lowest incomes.

The Government must rise to face the unprecedented cost of living challenge before the leaves begin to fall this autumn. We believe this to be the most deliverable, cost-effective and targeted package available to the incoming Prime Minister, who we urge to put social justice at the heart of their cost of living policy response.

Summary of recommendations

- **Recommendation**: The Government should take the earliest opportunity to hold another special fiscal event, laying the appropriate legislation required to direct additional financial assistance to individuals and families who are facing even higher inflationary pressures than previously forecast.
- **Recommendation:** The Government should introduce a 'proactive uprating' of benefits in October 2022 to reflect forecast inflation of 13.3 per cent. This would see the average household on Universal Credit receive an additional £224 over the autumn period rising to £423 for families with children.
- **Recommendation:** The Government should commit now to a further fiscal intervention in January, in order to provide additional support to maintain real income levels among the most vulnerable households, informed by up-to-date analysis of the changing inflationary picture.

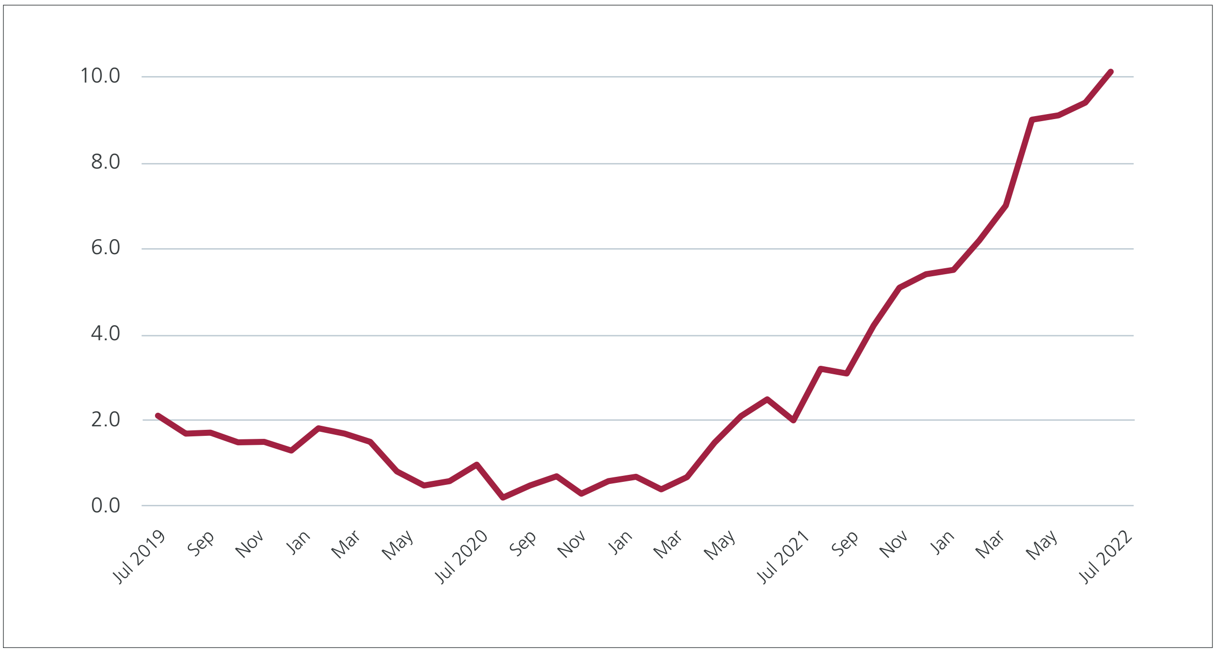
- Recommendation: Work Allowances should be restored to their pre-2016 levels. This would represent an effective ‘tax cut’ for 1.87 million of the poorest working households worth £842 million, boosting incomes by £449 on average and helping more people move further off welfare into work.
- Recommendation: The Government should mirror the ‘proactive uprating’ with an additional payment to people on mean-tested benefits including legacy benefits and pension credit. This would average £224 more support between October and January, and could be distributed using local administrative data in order to target support proportionally by household type.
- Recommendation: Environmental and renewables levies should, where legally possible, be paused for the duration of the current energy crisis (and at least between the October-March period), boosting household incomes by an estimated £153 annually and bringing the autumn package of additional support for households on low incomes up to around £262 on average (excluding the additional income working households on UC would receive from the restoration of Work Allowances).
- Recommendation: Debt repayment to government bodies within UC should be suspended for six months, as it was at the beginning of the Covid pandemic, to allow households to adjust to turbulent energy prices.
- Recommendation: The maximum level at which debts and benefit overpayments can be recovered through UC should be reduced to 10 per cent of the standard allowance.
- Recommendation: The Illegal Money Lending Team should be allocated additional funding to scale up its operation in light of the cost-of-living crisis.
- Recommendation: The Government should overhaul the Credit Union Act 1979 to address the key challenges preventing credit union growth.
- Recommendation: The Government should initiate the rollout of Universal Support, jointly administered by the Department for Work & Pensions and Department for Levelling Up, Housing & Communities, to help those furthest from the labour market take advantage of rising job vacancies.

1. Cost of living crisis: the changing picture

The UK is in the grip of a cost of living crisis.

The economic fallout of the pandemic and the ongoing war in Ukraine have driven a global inflationary surge that is continuing to hit British households and businesses. By July 2022 prices measured by the Consumer Price Index (CPI) were 10.1 per cent higher than a year earlier, reaching 12.3 per cent when measured by the Retail Price Index – the highest reading since 1991.[4]

Figure 2. Consumer Price Index (percentage change over twelve months)



Source: Office for National Statistics

In August the Office for National Statistics reported that nine in ten (89 per cent) adults in Britain said their cost of living had increased, having risen from six in ten in November 2021.[5] More than a third reported cutting back spending on "food and essentials", while an estimated six million increased their use of credit.[6] Meanwhile the cost of living has risen to occupy the number one issue of public concern.[7]

Yet the inflationary squeeze is getting tighter still.

In its August *Monetary Policy Report* the Bank of England upwardly revised expected CPI inflation to peak at 13.3 per cent in October 2022, remaining at "very elevated levels" through much of 2023. Correspondingly the Bank Rate of interest jumped to 1.75 per cent (the fastest rate rise in 27 years). Goldman Sachs and EY have said they expect an inflation rate of at least 15 per cent around the start of next year.[8] The investment bank Citi put this at 18.6 per cent.[9]

At the centre of the inflationary surge has been the spike in energy prices, which shows little sign of easing with Russia continuing to curb gas supplies to Europe, and droughts denying power stations shipments of coal and other commodities across the continent.

4 Office for National Statistics (ONS), Consumer Price Inflation tables, August 2022

5 ONS, Opinions and Lifestyle Survey, August 2022

6 Ibid

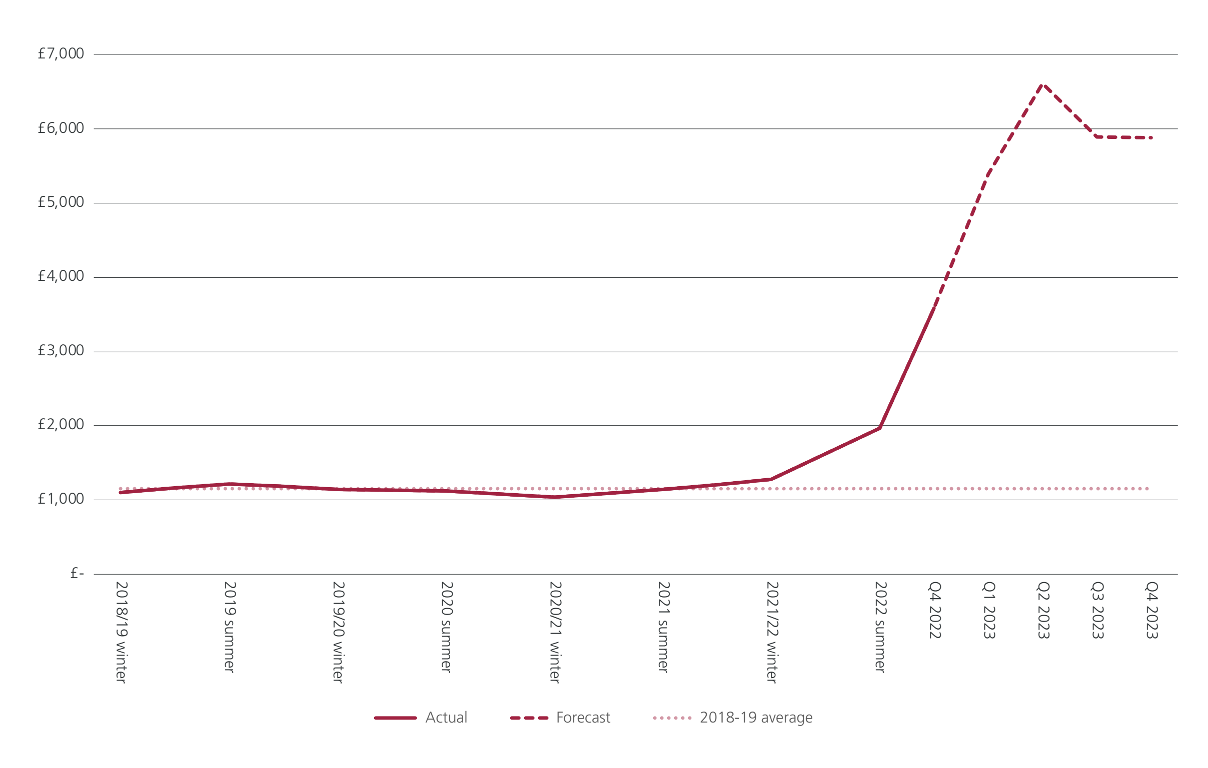
7 More in Common, 'Britons and the rising cost of living', April 2022

8 Financial Times, 'UK inflation to hit 18.6% next year according to Citi', August 2022

9 Ibid

On the contrary, the price of gas almost doubled in the three months since May.[10] Both Bank of England and industry analysts are now predicting yet more unprecedented increases to the Ofgem price cap this winter (which is linked to the rates suppliers can charge consumers for their electricity and gas standing charges and unit rates).

Figure 3. Default tariff price cap (£ per annum, Direct Debit, national average)



Source: Ofgem, Cornwall Insight

By January the average annual energy bill is now set to reach £3,549 following Ofgem's announcement in August 2022. By April, forecasters expected average annual bills to rise even further, meaning a typical household is now predicted to pay the equivalent of £5,382 a year over the three months to March 2023.[11] This compares to £1,156 in Winter 2021-21.

Ofgem has also announced a £1,591 increase to the cap for more than four million households on prepay tariffs – to £3,608 per year for a typical household.

Although estimates are highly volatile month-by-month, most forecasters now expect energy costs to remain at highly elevated levels throughout 2023. Some expect bills exceeding £6,000 by January 2023. Ofgem, meanwhile, continues to urge caution over price cap forecasts given the volatility in the market.[12]

Although central, it is not only energy prices driving the inflationary pressure households are experiencing. Analysis by Kantar in July 2022 found that the average family faces a £454 increase in annual grocery bills, while inflation in housing costs jumped up to 3.8 per cent in June 2022, according to the Office for National Statistics (compared to an average of one per cent in 2019).[13]

10 Bank of England, Monetary Policy Report, August 2022

11 Cornwall Insights, 'Cornwall Insight release final predictions for October's Price Cap', August 2022

12 Financial Times, 'British energy bills forecast to soar above £5,000 next year', August 2022

13 ONS, Consumer Price Inflation tables, August 2022

2. The inflationary surge will continue to hit the poorest the hardest

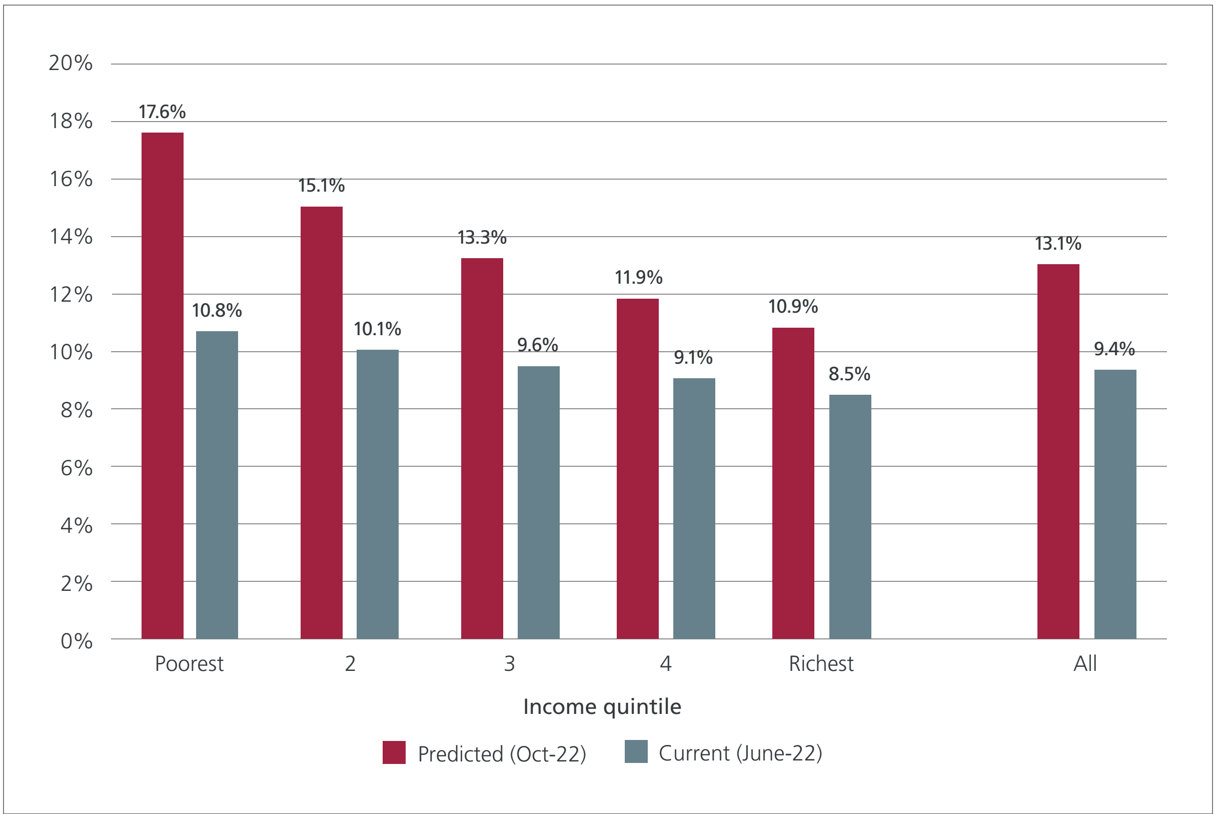
While almost everyone is tightening their belts in response to inflation, it is the least well off who are at the sharpest edge of the cost of living crisis.

Given that the lowest-income households pay a disproportionate share of their income towards the cost of energy, they are the least able to absorb a rapid increase in electricity and gas prices of the kind we have seen since the beginning of 2022 and which are projected to continue to rise steeply.

Based on the latest forecast for the energy price cap change, low-income households will have to reduce their spending by three times as much as high-income households in January-March 2023.[14] The poorest, in the lowest income quintile of the distribution, will have to cut their non-essential spendings by 24 per cent, compared to a cut of eight per cent for the richest tenth of households.

The distributional impact of the changing inflationary picture has been modelled by the Institute for Fiscal Studies (IFS). As the primary driver of Autumn 2022's forecast escalation in prices is energy costs, they argue that "the pattern of inflation is even more unfavourable towards poorer households . . . who tend to spend more of their budgets on energy." By October 2022 the IFS expect CPI inflation to hit an eye-watering 17.6 per cent for the poorest quintile, compared to 10.9 per cent for the wealthiest.

Figure 4. Expected inflation by income quintile in October 2022



Source: Institute for Fiscal Studies

14 Resolution Foundation, Low-income households will have to cut back on spending by three times as much as high-income households this winter, August 2022

3. The Government's policy response and its impact

The current Conservative leadership contest has been marked by the debate over how to respond to escalating cost of living crisis, a debate to which we will return shortly. In this context it is perhaps easy to overlook the scale of the Government's policy response pre-dating Boris Johnson's announcement in July 2022 that he would step down as Prime Minister. But understanding the impact of recent policy – both its strengths and weaknesses – is an important way of illuminating what we do next.

In the face of considerable pressure – including calls by the Centre for Social Justice in May 2022 to respond urgently to the crisis with targeted financial assistance via the welfare system – the Chancellor announced a £15 billion package to support households with the rising cost of living.

This was on top of £9.1 billion announced in February 2022 (carrying forward a £150 council tax rebate for the roughly 80 per cent who live in band A-D homes, and converting an earlier energy bill loan scheme into a grant), including a:

- £400 energy rebate for all households (paid over six months from October 2022)
- £300 payment to pensioners
- £150 payment for people with disabilities
- £650 support payment to low-income households (on means-tested benefits) paid in two instalments

Contrasting March's Spring Statement, which was dominated by the rise in National Insurance contributions (and the accompanying threshold change to offset rise this for most workers), the intervention was widely praised – including by the CSJ – for the renewed focus on protecting those with the least.

In earlier interventions an estimated £6 in £10 went to the top half of the income distribution.[15] However, analysis by the Resolution Foundation found that the combined impact of earlier cost of living packages, tax rises and the May package delivered much more progressive outcomes, leading to "an average cash gain to households in the bottom quintile of £1,195, compared to £799 for households in the middle quintile, while households in the top quintile are set for an average cash loss of £456."[16]

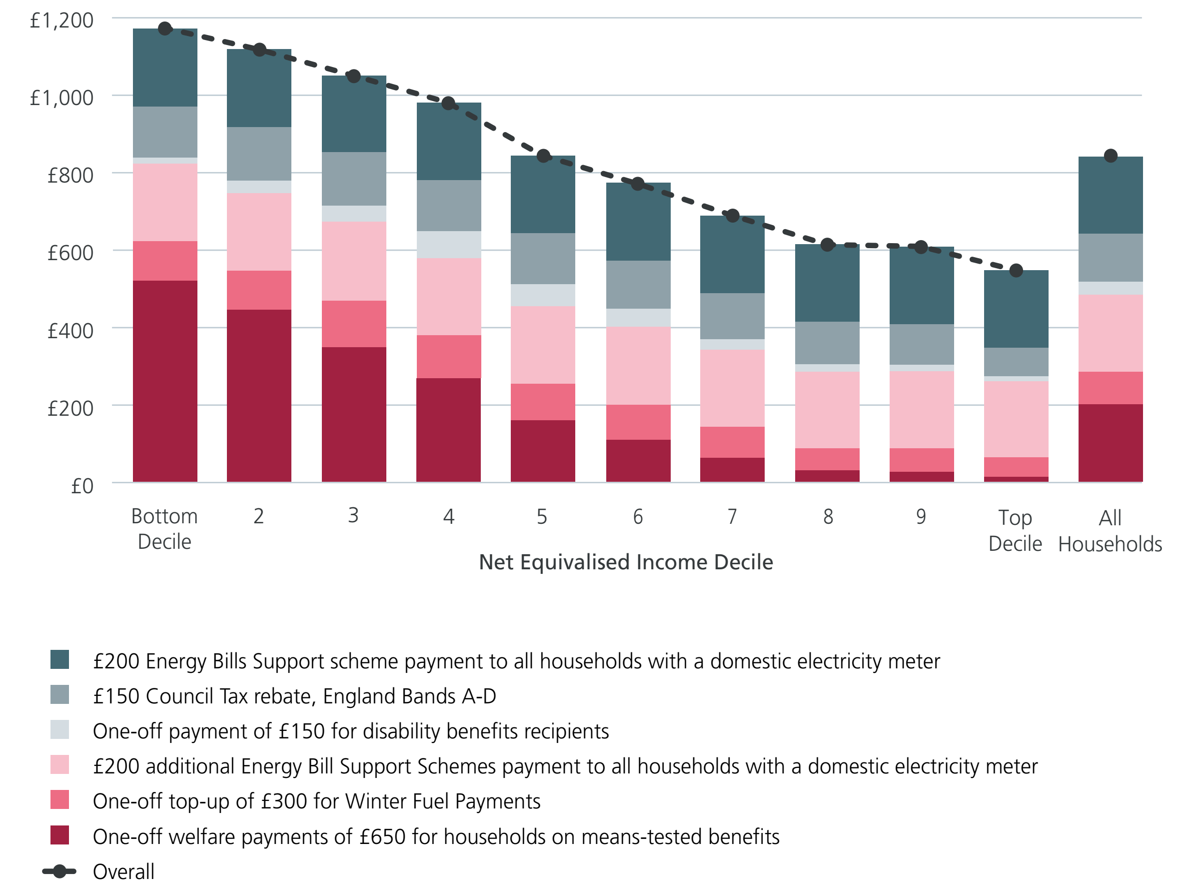
Distributional analysis later published by HM Treasury showed that households with the lowest incomes benefit from support worth on average £1,170.[17]

15 Resolution Foundation, 'Chancellor almost doubles cost-of-living support with two-thirds of fresh cash going to the poorest half of households', May 2022

16 Ibid.

17 HM Treasury, 'Illustrative analysis of the impact of the May 2022 Cost of Living Support package and February 2022 Energy Support package on households', May 2022

Figure 5. Impact of measures announced in February and May 2022 on English households in 2022-23 (percentage of income by income decile)



Source: HM Treasury

Still, as cash instalments and rebates on bills have begun to appear, the support package has come under criticism for its relative 'scattergun' approach, which (for reasons explored below) opted for flat-rate payments rather than bringing forward the uprating of benefits.[18]

When challenged as to why wealthier households were also due to receive the universal £400 energy rebate, the then Chancellor said he would give the value of his own rebate to charity, explaining that "[t]his being universal means that we avoid all of those problems and really do get help to everyone who needs it".[19] We estimate that around £2.3 billion will be spent on the wealthiest fifth of households in energy bill rebates.

However, the biggest relative 'losers' from the lump sum approach are families. As the Resolution Foundation has argued:

> The biggest group to lose out from the approach of lump sum payments versus benefits uprating are families with children, with large families facing the greatest risks of severe fuel stress this winter. Households on benefits with three children would have, on average, received £968 from 9.5 per cent benefits uprating in October, compared to £720 from the support announced today.[20]

18 In May 2022 the Centre for Social Justice argued for benefits to be uprated in line with inflation more dynamically for the period of inflationary turbulence. See: CSJ, Cost of Living: Alleviating the Crisis, May 2022

19 Evening Standard, 'Rishi Sunak: I'll give £400 energy rebate to charity and other wealthy families should too', 27 May 2022

20 Resolution Foundation, 'Chancellor almost doubles cost-of-living support with two-thirds of fresh cash going to the poorest half of households', May 2022

A likely reason that the lump sum approach was adopted is the delivery challenges associated with more targeted support. Many dismissed the 'technical problems', highlighted by the Chancellor in early May as stopping him raising benefits in line with inflation earlier than April 2023, as an excuse not to increase spending. But this falls over in light of the larger package announced later that month.

The former Chancellor's claim that it is only possible to uprate benefits once per year does reflect a genuine technical barrier in respect of legacy benefits. UC can be uprated dynamically, as demonstrated by the speed of implementing the £20 uplift in March 2020 and the cut to the UC taper after the Autumn 2021 Budget. This is not, however, as easy with legacy benefits, some of which rely on old IT and even paper-based infrastructure.

The timescale under which the May support package was developed no doubt also shaped the Treasury's decision to pursue a more universalist policy response, deploying blunter policy levers in the form of direct payments.

The CSJ also understands the Government's concerns regarding risk of legal challenge due to UC and legacy benefit claimants being treated differently. Litigation over the original £20 uplift, which was not administered to legacy benefit claimants in the same way, is still ongoing. However, the fact that a work-around in the form of a substitute one-off payment was found proves that solutions are possible. Moreover, it is far from clear that the legal challenges to the Government over UC/legacy disparities will succeed.

It is a social injustice that larger families with greater need did not receive more proportional support in the May package, which could have been achieved through a dynamic uprating of benefits. The lump sum payments administered to all benefit claimants regardless of need was a blunt instrument; the CSJ calls upon the Government to use the administrative power of the welfare infrastructure to deliver targeted support in the most efficient and effective way.

Recommendation: *Any further fiscal injection of cost of living support should deploy the welfare system more effectively to target support more proportionally to need – for example, due to household size. (See below, 'Our proposal')*

4. The need for another special fiscal event

As we now know, the cost of living crisis is going to get worse before it is going to get better.

This should prompt a difficult but honest conversation about the scale of the economic challenge before us. We are a poorer country than we thought we were. However, this must also include commitments to shield those who have the least to defend themselves from the sharpest edges of inflation.

This changing picture means that, while the support package initiated in May was immensely welcome, we need to respond to changing nature of the challenge.

Without further cost of living support, the IFS estimates that the poorest households, illustrated by the case of out-of-work single parents, could be over £1,000 worse off over the year.[21] More specifically, working-age families out-of-work and on benefits are set to see a fall in their real benefit income of about £620 from 2021-22 to 2022-23, while pensioners on means-tested benefits will see a £140 decline.

New analysis of over 114,000 low-income households presented in this report suggests that, even taking into account the £1,200 summer support package, families with children will experience an estimated £491 fall in real income in the three months from October 2022 alone.[22] The combined impact of rising everyday costs and soaring energy bills leaves households who were already struggling faced with a £209 fall in real income on average this autumn.

Table 1. Estimated fall in real income among low-income households (taking into account the existing cost of living package)

Low-income household type (claiming housing benefit/council tax support)	Estimated fall in real income (Oct 22 – Jan 23)
Couple with two children	-£490.77
Lone parent	-£284.59
Single adult	-£129.72
All (households on HB/CST)	**-£209.18**

Source: Policy in Practice analysis of July 2022 'administrative data' on 114,000 low-income households on council tax support and/or housing benefit in six local authority areas across the UK; ONS Family Spending Workbook; Bank of England; Ofgem

This size of additional costs, the analysis finds, could double the proportion of low-income households falling into negative budgets – that is, that is, where a household cannot meet all expected costs, such as water, food, or clothing. Not acting on this situation given what we now know would represent a both moral and political failure.

It is becoming increasingly clear that the Government may also need to adopt additional supply-side policies in response to the energy crisis (and looming recession). But at the very least, the welfare system must perform its duty in ensuring that the support given to the poorest and most vulnerable is 'uprated' in line with rising fixed costs.

21 Institute for Fiscal Studies (IFS), 'The long squeeze: rising inflation and the current government support package', August 2022

22 Methodology: the CSJ commissioned Policy in Practice to produce an illustrative analysis of the expected fall in real incomes affecting low-income households with a sample of 114,000 low-income households on HB and/or Council Tax Support in six local authorities across different regions of the UK in July 2022. The 'administrative data' used in the analysis provides detailed information on low-income household demographics covering a large population size. In order to calculate the average fall in real incomes across different household types, analysts used data from the ONS Family Spending Workbook to uprate third decile household expenditure (equivalised based on household size and characteristics) in line with October and January inflationary forecasts from the Bank of England and Cornwall Insights, factoring in the £400 energy rebate announced in May.

Given the urgency of the situation, the Chancellor of the Exchequer – or his successor – should commit to a special fiscal event focused on the cost of living to be brought before Parliament as a matter of urgency and, if necessary, before wider economic and fiscal policy is prepared for the Autumn Budget.

Recommendation: *The Government should take the earliest opportunity to hold another special fiscal event, laying the appropriate legislation required to direct additional financial assistance to individuals and families who are facing even higher inflationary pressures than previously forecast.*

5. How do existing proposals compare?

While the early stages of the leadership contest revolved squarely around tax cuts, the inflationary forecasts highlighted above have brought the true scale of the energy crisis, and calls for a much fuller fiscal support response, crashing to the forefront of the debate.

Liz Truss

Liz Truss has committed to an emergency budget in September focused on tax cuts, specifically pledging to reverse the rise in National Insurance contributions and remove the Green Levies on household energy bills. She has also pledged to halt the rise to corporation tax scheduled for April.

The dire inflationary picture has led to a clarification of earlier commitments to avoid 'handouts', with Truss's supporters insisting that 'all options are on the table' to get additional financial support to households 'whether that's a targeted way or a general way'.[23]

Recent reports suggest the Truss team are contemplating increasing support through the welfare system, using tax cuts to support households on middle incomes rather than further increasing or extending the £400 universal energy bill rebate announced in May.[24] This comes after analysts found proposals to reverse the rise in National Insurance contributions would help the poorest decile of the population by just 76p per month compared on average, compared to £93 per month for the wealthiest households.[25] Suspending Green Levies would cost an estimated £4.2 billion, while reversing the national rise would cost around £13 billion.

Rishi Sunak

Rishi Sunak initially pledged to remove the five per cent VAT on household energy bills for 12 months from October. This would provide an average reduction of about £154 on all domestic energy bills, applying to every household, according to the IFS.[26] In August, the former Chancellor also committed to give households more money through emergency support payments by expanding the existing schemes in place by up to £10 billion. This is expected to maintain the 'lump sum' approach adopted during May's package and examined above.

Labour

Meanwhile, Labour has proposed a scheme to 'freeze' energy bills at the current Ofgem cap at its current level of £1,971, preventing it from increasing to £3,549 in October. To pay for the scheme, the universal £400 rebate set to for Autumn would be cancelled (facilitating the redirection of £14 billion), while the windfall tax on energy companies would be extended and backdated (raising £8 billion). Labour has argued, optimistically, that this would reduce inflation by four per cent (saving £7 billion in interest payments on government debt).

Overall, across six months the policy is costed at £29 billion, although doubt has been cast on the programme's likelihood of lasting less than twelve months, which would bring the total cost to nearly that of the furlough scheme introduced during the pandemic. The proposal has faced criticism for overly optimistic assumptions about its expected reduction of government debt expenditure, and for being much less targeted than either the earlier May package or other proposals for direct support via the welfare system.

23 Sky News, Liz Truss and Rishi Sunak supporters on handouts for the vulnerable, 12th August 2022

24 The Times, Liz Truss's energy plans will leave pensioners more than £2,000 worse off, claims Rishi Sunak, 16th August 2022

25 Huffpost, This Liz Truss Policy Would Save Poorest 76p A Month – And Richest £93 – Think Tank Finds, 12th August 2022

26 Institute for Fiscal Studies (IFS), Rishi Sunak's proposal to temporarily remove VAT on energy bills, 27th July 2022

6. Our proposal: a cost of living support package for those who need it the most

There are merits to each of the proposals examined above. And it is clear that the social and economic consequences of the energy crisis, the war in Ukraine and the long shadow of the pandemic will continue to be felt in the years ahead. This will require bold thinking and perhaps even economic policy interventions on the scale seen during the pandemic, as the energy crisis rips through businesses and significantly reduces discretionary spending in the economy.

Still, we believe the most pressing and baseline need to be protections for the poorest households from the worst of inflation. The annual cycles of inflationary uprating have been exposed as unfit for the current period of inflationary pressure. We must harness the dynamism in the welfare system where it exists to bring forward April 2023's planned uprating to October 2022 – ensuring that larger households including families with children receive support more proportional to their needs.

Equally it is important that we recognise the international economic reality, which is that energy is a more precious commodity than prior to the Ukraine war. Attempting to 'freeze' this market for everyone, with an estimated £30-60 billion bill attached, does not, in our view, represent the fairest response to this changing landscape. This should prioritise helping those who have the least while incentivising those who are most able to reduce their energy usage for the period of turbulence.

And so we are calling for a combined package of a targeted welfare boost and effective 'tax cuts' for the poorest workers. This includes uprating Universal Credit by 13.3 per cent in October 2022 for an initial three-month period, in order to provide more help to larger households facing higher bills (such as families with children) than earlier packages.

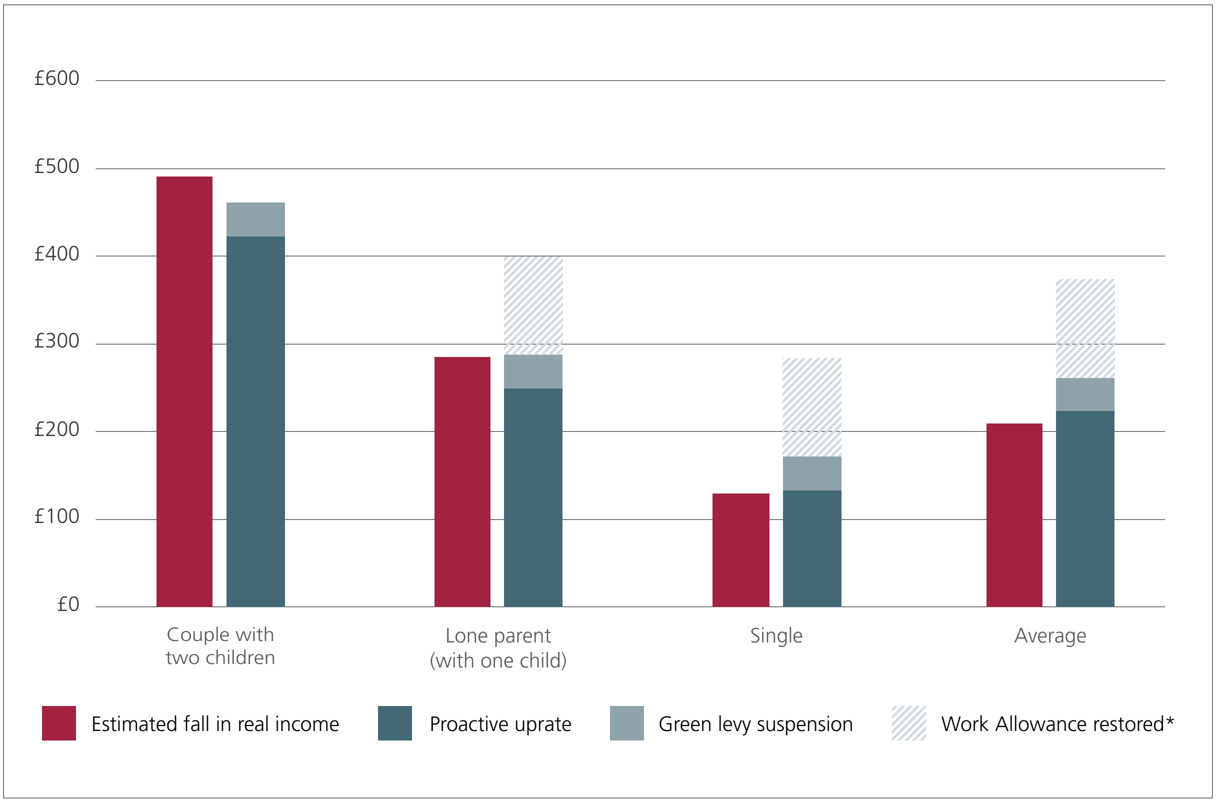
This would be the most targeted way to shield low-income households from the worst of inflation – and the uprating alone would see 4.7 million households receive an additional £224 on average in the three months from October, rising to £249 for lone parents and £423 for families with children. This should be mirrored by a payment for the 3.8 million in receipt of legacy benefits or pension credit, including an additional disability payment. This could be distributed as a one-off £224 payment or in a more targeted way by using local authority administrative data, and bringing the total number of benefitting households to 8.5 million.

But we must also better equip people to defend themselves against inflation. And so we are also recommending an effective 'tax cut' for the poorest workers worth £842 million, by restoring Universal Credit Work Allowances to their pre-2016 levels. This would see around 1.87 million low-income working households keep more of their own money before seeing their Universal Credit tapered off, boosting incomes annually by an average of £449.

The combined welfare support package and effective 'tax cut' elements would cost £2.75 billion to cover the October to January period, leaving the next Prime Minister considerable fiscal headroom to deploy additional financial assistance to higher earners, tax cuts or other measures such as the suspension of Green Levies or VAT on energy bills. Indeed, suspending Green Levies on energy bills would bring the total average increase to those on the lowest incomes to around £262 for the three months between October and January 2023 (rising to £461 for couples with children) – bringing the total proposed package of targeted support, effective 'tax cuts' and suspended levies to 3.82 billion.[27]

27 Note this figure includes the annual cost of restoring Work Allowances, assuming this to be implemented as a permanent effective 'tax cut'.

Figure 6. The impact of the proposed welfare and effective 'tax cut' package for households on means-tested benefits (October 2022 – January 2023)



*Source: Policy in Practice analysis of local authority administrative data on 114,000 low-income households on council tax support and/or housing benefit across six local authority areas in July 2022; ONS Family Spending Workbook; Ofgem; Cornwall Insights; DWP Stat X-plore; authors calculations. *The Work Allowance element is averaged by household type and only applies to UC claimants.*

Finally, we propose that ministers ditch 'annual uprating' in favour of a more dynamic approach responding to the fast-moving inflationary picture.

A further fiscal intervention will need to take place in January, where prices are expected to rise even more astronomically. This should be informed by the latest inflationary data including the announcement of the next energy price cap. CSJ calculations using existing forecasts suggest that a further uprating of 8.5 per cent could be needed to maintain real incomes among low-income households between October 2022 and April 2023. This could bring the total effective tax cut, welfare boost and Green Levies suspension to £8.2 billion over the six-month period.

This combined impact of this package would, according to Policy in Practice, significantly counteract the additional inflationary pressures now forecast to hit low-income households, while targeting support more effectively to families than previous packages.

Recommendation: *The Government should introduce a 'proactive uprating' of benefits in October 2022 to reflect forecast inflation of 13.3 per cent. This would see the average household on Universal Credit receive an additional £224 over the autumn period rising to £423 for families with children.*

Recommendation: *The Government should commit now to a further fiscal intervention in January, in order to provide additional support to maintain real income levels among the most vulnerable households, informed by up-to-date analysis of the changing inflationary picture.*

Recommendation: *Work Allowances should be restored to their pre-2016 levels. This would represent an effective 'tax cut' for 1.87 million of the poorest working households worth £842 million, boosting incomes by £449 on average annually.*

Recommendation: *The Government should mirror the 'proactive uprating' with an additional payment to people on mean-tested benefits including legacy benefits and pension credit. This would average £224 more support between October and January, and could be distributed using local administrative data in order to target support proportionally by household type.*

Recommendation: *Environmental and renewables levies should, where legally possible, be paused for the duration of the current energy crisis (and at least between the October-March period), boosting household incomes by an estimated £153 annually and bringing the autumn package of additional support for households on low incomes up to around £262 on average (excluding the additional income working households on UC would receive from the restoration of Work Allowances).*

7. An ongoing squeeze: the cost of debt recovery within Universal Credit

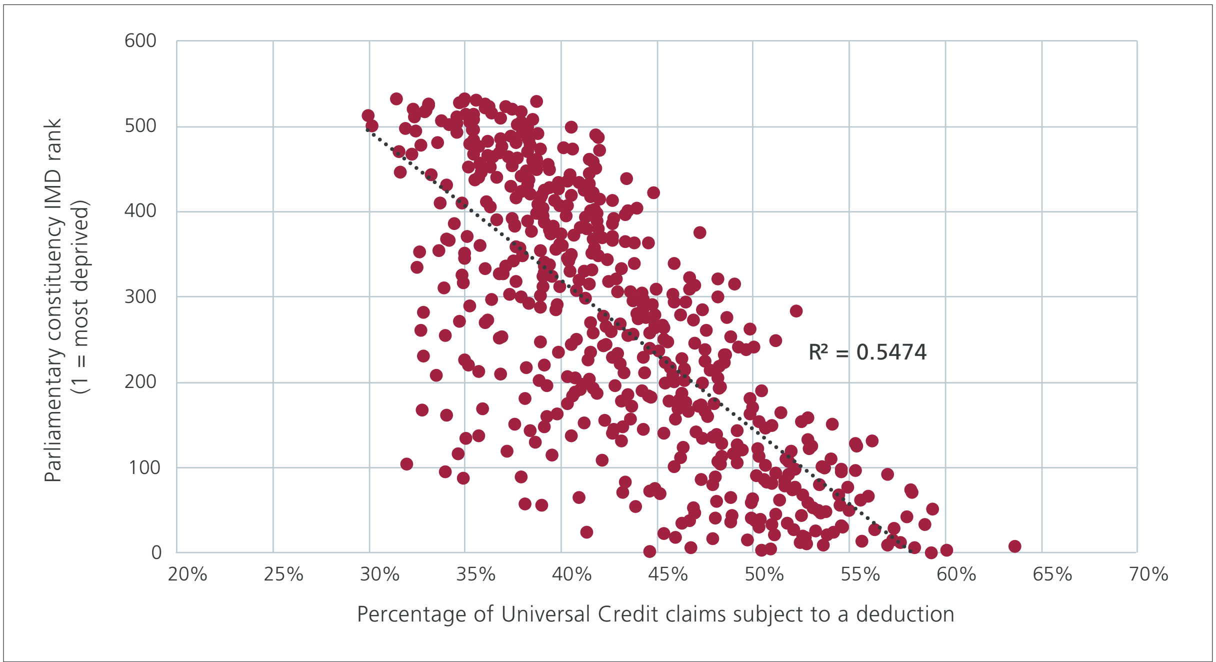
Yet there is more that the Government can do to protect the poorest. For example, the levels of Universal Credit awards are only meaningfully understood taking into account the deductions many claimants face for debts.

Prior to the Covid-19 pandemic or current cost of living increase, many households in receipt of Universal Credit were receiving deductions from their awards of up to 25 per cent as part of the debt recovery process within UC. Figures from 2021 show that 45 per cent of Universal Credit claims – over two million claimants – were subject to a deduction from their welfare payment totalling over £176 million across the UK.[28]

Indeed, more recent figures show that deductions can often be taken from those in particularly vulnerable circumstances. Data from February 2022 shows that 646,000 households with children – equivalent to 31 per cent of households with children on UC - were losing over a fifth of their income to deductions compared to 13 per cent of households without children and 21 per cent of all households.[29]

As Figure 7 below shows, UC deductions are correlated with deprivation. More deprived places in England are likely to have a greater percentage of their claimants facing deductions, and this means they will face a disproportionately greater challenge in the face of the cost of living crisis. Some of the most deprived places in England, including parts of Liverpool, Blackpool, Knowsley, and Middlesborough all rank in the top ten most deprived places in England as well as the top ten areas that have the greatest percentage of UC deductions.

Figure 7. Percentage of Universal Credit claimants subject to deductions by parliamentary constituency 2019 IMD rank



Source: CSJ Analysis of Department of Work and Pensions and Index of Multiple Deprivation 2019

28 Will Quince, Question for Department of Work and Pensions, UIN 16144; Index of Multiple Deprivation 2019

29 UK Parliament, Written questions, answers and statements - Universal Credit, June 2022

While much of this repayment is to return UC advances – a key smoothing mechanism to avoid the overpayments which blighted the legacy system – a significant number of people continue to repay historic tax credit overpayments. Data from the Department of Work and Pensions shows that some 10 per cent of Universal Credit claimants were repaying £55 on average to repay tax credit overpayments in December 2020. These repayments are the result of design flaws in the legacy benefit system that have been transferred to the DWP and into the UC system and estimated to be worth approximately £5.4 billion in debt.[30]

While there is need to increase the responsiveness of uprating to the contend with current economic turbulence, we must also pay attention to the large amounts being removed from claimants' awards by deductions.

As we argued in our 2020 report, *Collecting Dust*,[31] it is unfair that historical debts born of design issues in the legacy benefits system should be recovered via Universal Credit. It is particularly unfair when it is recovered through large deductions to the standard allowance, and much of the debt (one estimate put this at 61 per cent) is over three years old.

During the early stages of the pandemic, the Government suspending debt deductions in UC to support incomes. While a long-term suspension of debt repayments is not the preferable course of action, and it is an important matter of social justice that debt is repaid, the Government could reduce maximum benefit deductions for private debts and overpayments to help people on the lowest incomes cope. The case for this is particularly strong for historical tax credit overpayments.

Recommendation: *Debt repayment to government bodies within UC should be suspended for six months, as it was at the beginning of the Covid pandemic, to allow households to adjust to turbulent energy prices.*

Recommendation: *The maximum level at which debts and benefit overpayments can be recovered through UC should be reduced to 10 per cent of the standard allowance.*

30 Lloyds Banking Foundation, Deductions: Drivers of Poverty, May 2022

31 Centre for Social Justice, Collecting Dust: A path forward for government debt collection, April 2020

8. Being in work remains the best defence against inflation

For some periods wages will outstrip inflation (i.e. real wages will rise) and for other periods (such as the present) they will not. Currently, inflation has overtaken nominal wage growth, damaging workers' real incomes. However, there has nevertheless been a degree of nominal wage growth in the labour market over the last year. Average growth in nominal pay in the 12 months to July 2022 was 6.2 per cent.[32]

At the time of writing, the CPI rate of inflation for the 12 months to July 2022 was 10.1 per cent.[33] This means that an average full-time worker will be 3.9 per cent worse off in real terms. This is a steep cut in real pay, but is a significantly less dramatic loss of income than that facing benefit claimants this year, had the previous Chancellor not intervened with his cost of living support package. Those dependent entirely on means-tested benefits would have been facing a real-terms cut of 7 per cent.

Real pay has indeed fallen at the fastest rate in 20 years.[34] Nevertheless, it remains clear that being in full-time work is still a much better defence against inflation than relying on the fiscal power of the state to provide the necessary financial support. More generally, someone in work is likely to have a higher income than someone not in work, rendering the impact of a real-terms pay cut more manageable.

Given this, it should remain a key aim of Government to help more UC claimants (who are able) into work, and for those who are working to progress within work. A person in employment will stand a much better chance of weathering the impact of inflation than someone who is reliant on the uprating of benefits.

Reducing the number of claimants of Universal Credit, which stood at over 5.6 million people in July 2022 (an increase of 3.3 million from February 2020),[35] and increasing the supply of workers at a time when demand for labour is high, would serve the twin goals of loosening the labour market and increasing the economic resilience of those who have moved into work.

Rolling out Universal Support (see below) would help to move those on UC with work expectations into work, meaning fewer households depending on UC to shield them from inflation. It would also help to decrease the caseload of UC claimants, generating more fiscal headroom for HM Treasury.

32 ONS, Average Weekly Earnings in July 2022, July 2022

33 ONS, Consumer Price Inflation, UK: July 2022, August 2022

34 Financial Times, Record wage drop signals more financial pain for UK households, August 2022

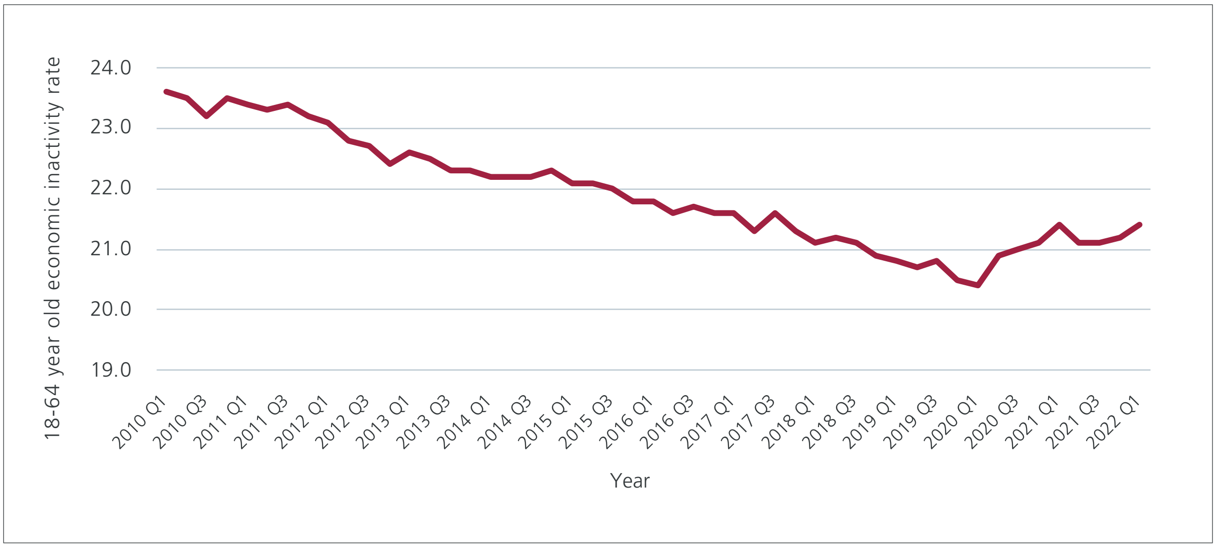
35 DWP, Stat-Xplore, August 2022. NB some of the increase in the numbers of people on UC is accounted for by migration from legacy benefits, but adjusting for this there has still been a net increase in the caseload of people on means-tested benefits.

9. Rolling out Universal Support

With the overhauled welfare system now set up to help claimants into work, investing more in Universal Credit as we propose is both more transformative for claimants and more fiscally responsible than discretionary support schemes (such as in the form of the Household Support Fund) or emergency hand-outs. Still, many claimants face complex and overlapping needs which have kept them at distance from the labour market.

While employment figures have improved since the start of the pandemic, we have also seen rising rates of economic inactivity among working age adults, reversing the pre-pandemic trend. In the early stages of the pandemic, it was driven by 16-24 year olds becoming inactive. But since May 2021, 50-64 year olds have made up an increasing share of the total exiting the labour market. In November 2021 the Resolution Foundation estimated that 600,000 people had stopped working due to worsened mental health.

Figure 8: Percentage of 18-64 year olds who are economically inactive



Source: Labour Force Survey

It is a long-standing position of the CSJ that individuals with complex and overlapping needs, which provide significant barriers to employment, need interventions that go further than increasing the level of financial support provided through Universal Credit. These complex social obstacles include, but are not limited to:

- Poor physical or mental health
- Substance or gambling addiction
- Problem debt
- Abusive relationships and / or family breakdown
- Poor educational prospects or outcomes, including poor literacy (including digital literacy)
- Long-term worklessness and benefit dependency
- Social isolation
- Caring responsibilities
- Language barriers
- Unstable housing or homelessness

The CSJ therefore recommends that the HM Government should roll out Universal Support, an intervention successfully piloted in 2014 by Lord Freud and 'sister' to Universal Credit designed to help those furthest from the labour market into work. The unique nature of UC is that it identifies those who have significant ancillary issues, while Universal Support enables them to receive support and sustain employment (retaining the associated financial, social and health benefits).

The purpose of Universal Support (US) is to:

- Identify individuals in need of support with multiple barriers to work.
- Refer them to a Local Authority assigned Key Worker who is independent of the DWP.
- Provide a bespoke "wrap-around" support plan for the vulnerable individual, including triage and sign-posting and triage to the organisations and groups best able to help them overcome complex and overlapping barriers.

Initial points of referral to Universal Support can include the DWP / Job Centre Plus, GP surgery, Citizens' Advice, third sector organisations such as Step Change Debt Charity, mental health and addiction support groups, local housing associations.

The CSJ estimates that implementing Universal Support would cost £460 million, but with an expected return on investment of 1.5-2, matching the funding for the Work & Health Programme & Intensive Personalised Employment Support (IPES) programme for people with disabilities. Helping people reap the financial, social and health benefits of employment should be part of the Government's action plan to shield the most vulnerable from the worst of inflation.

Recommendation: *The Government should initiate the rollout of Universal Support, jointly administered by the Department for Work & Pensions and Department for Levelling Up, Housing & Communities, to help those furthest from the labour market take advantage of rising job vacancies*

10. Impact of 'Green Levies' on household energy bills

Prior to the Covid-19 pandemic, the wholesale prices of oil, gas and coal had fallen for a number of years. Professor Dieter Helm's Cost of Energy Review (2017) noted:

> *"Productivity increases should have been putting further downward pressure on the cost of transmission, distribution and supply. New technologies should mean lower, not higher, costs and a much greater scope for energy efficiency. Margins should be falling as competition is increasing. Yet in this period, households and industry have seen limited benefits from these cost reductions. Prices have gone up, not down, for many customers."*[36]

He notes that typical electricity bills have been estimated by the Climate Chance Committee (CCC) to be 20 per cent higher due to the passing on of the costs of decarbonisation.[37]

By 2022, costs associated with renewables subsidies were estimated at approximately £150–£200 per household.[38] These estimates reflect Climate Change Committee figures.[39] Conservative leadership contender Liz Truss recently pledged a 'temporary moratorium' on the green energy levy to cut '£153' from household energy bills.

Helm notes that prior to the current period of severe energy price inflation, the cost of renewables was going through a period of sustained decrease, yet at the same time the price of renewables subsidies to consumers was actually rising.

Some of these levies are environmental and social obligations with a legal grounding which have been written into contracts that have already been signed, but others are straightforward taxes which could be alleviated if the Government was minded to do so.[40]

The levies include:

- The Climate Change Levy
- The Green Gas Levy
- The Carbon Price Floor
- The Renewables Obligation
- The Carbon Reduction Commitment
- The Domestic Renewable Heat Incentive
- The Warm Homes Discount
- The emissions trading scheme[41]

Functionally, levies are charged on businesses, including electricity and gas suppliers, on a per kWh basis, and then passed on to consumers via their bills.

The funding of renewables projects and "environmental and social obligations" through household energy bills rather than through taxation has been a policy choice of successive governments, and a way of keeping the costs of subsidising carbon reduction away from the Treasury.

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36 Professor Dieter Helm, Cost of Energy Review, p. 18, October 2017

37 Ibid.

38 Professor Dieter Helm, Luck is not an energy policy – the cost of energy, the price cap and what to do about it, January 2022 - It should be noted that Ofgem claims that 15.3 per cent of average duel household bills (gas and electricity) is made up of "environmental and social obligation": Ofgem Data portal, though the Government has not contested the higher 25 per cent figure estimated by Helm.

39 The Climate Change Committee, Energy Prices and Bills - impacts of meeting carbon budgets, March 2017

40 Daily Mail, So what DOES the green tax on your energy bill actually pay for?, January 2022

41 Office for Budget Responsibility, Public finances databank, 2021-22

However, this has an inherently regressive effect, making lower income households pay disproportionately towards the costs of decarbonisation and renewables development. Given the burgeoning cost of living crisis, which will hit the poorest most severely, this is a poor way of funding environmental projects, and a needless addition to household costs.

As a point of principle, while the government cannot control global wholesale energy prices, and the Ofgem price cap must to an extent reflect the wholesale market, the government should seek to remit that portion of household monthly energy bills for which it is itself responsible.

Helm argues that renewables "are public goods and should not be parcelled out onto customers' bills in relation to the volume of their demands."[42] If indeed the Government has determined that investment in renewables is a public good, it should distribute the costs thereof in a fair and progressive way, avoiding placing a disproportionate burden on the poorest households.

It should also be noted that the UK's statutory commitment to attaining Net Zero by 2050 was written into law[43] prior to the global Covid-19 pandemic and subsequent worldwide inflationary surge, and prior to the outbreak of the Russia-Ukraine conflict. Failing to reassess the timetable for Net Zero represents a conscious choice to prioritise environmental objectives over the current economic crisis. As such, if the Net Zero timetable is to remain unchanged, then the costs associated with the renewables transition should be socialised progressively.

The Warm Homes Discount scheme stands out among the various levies, since its purpose is to provide an energy bill rebate to older bill payers. The costs are passed on to all bill payers. It is not suggested that the Warm Homes Discount scheme should be suspended, though the government should review whether energy bills are the best mechanism for subsidising older people's energy costs. However, there is a strong case that, in the present circumstances, the other so-called 'Green Levies' should be suspended and placed under urgent review.

Recommendation: *environmental and renewables levies should, where legally possible, be suspended for the duration of the current energy crisis (at least the October-March period) and placed under review, with the aim of bringing levies out of household bills and absorbing them into general taxation.*

Recommendation: *The Warm Homes Discount should be retained, and the government should review how it is funded with a view towards removing it from household energy bills*

42 Professor Dieter Helm, Luck is not an energy policy – the cost of energy, the price cap and what to do about it, December 2021

43 Climate Change Act 2008, amended 2019

11. Renewing the fight against illegal money lending

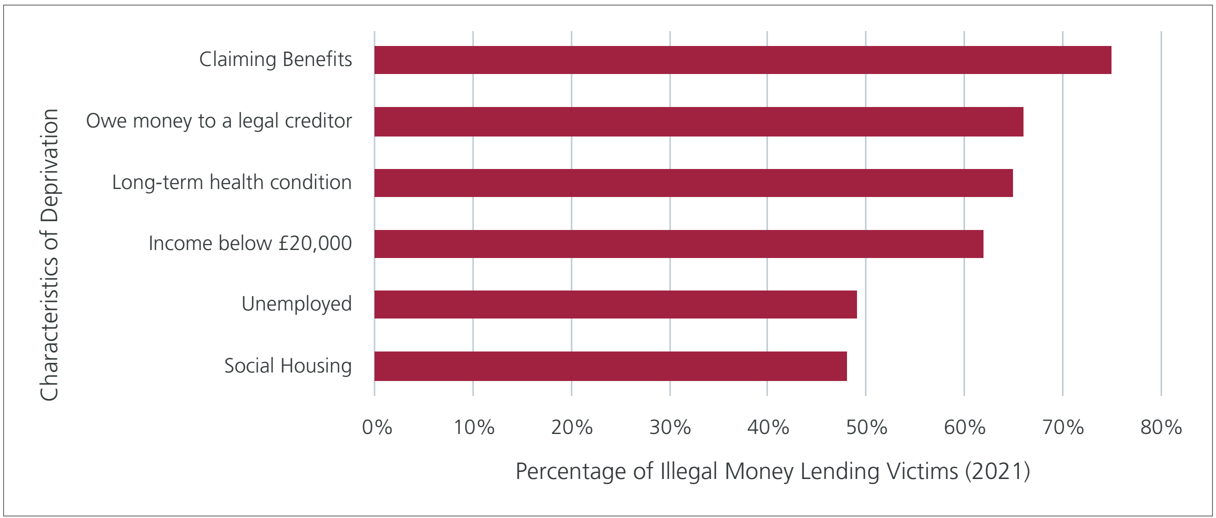
In response to the inflationary pressures explored above, families are adopting new strategies to manage their finances. Indeed, over half of Brits (51 per cent) say they have already taken steps to change their spending in response to the increases in the cost of living.[44]

In addition to this, more people will begin to rely on credit to smooth their income, while others will fall into arrears. Polling for the CSJ found that one in ten people earning under £20,000 said that they would increase their borrowing levels due to the cost-of-living crisis.[45]

Figures from the ONS's Lifestyle and Opinions survey place this even higher, with 23 per cent of those in the most deprived areas of England saying that they had borrowed more money or used more credit than usual.[46]

The heightened demand for credit is being exploited by unregulated lenders who encourage vulnerable borrowers to take on 'hidden debt'. In our *Swimming with Sharks* report we estimated that up to a million people in England could be borrowing from an illegal money lender in England.

Figure 3: Percentage of illegal money lending victims (2021) by deprivation characteristic



Source: CSJ analysis of illegal money lending team England data

Illegal money lenders exist for multiple complex social and economic reasons. Both their proximity and close social ties many often to a local community facilitate their role as an illegal creditor, but so too does the unfulfilled need for credit.

We found that almost two in five (38 per cent of) illegal money lending victims attempt to borrow from legitimate sources of credit, but 80 per cent of those who try are rejected.[47] This speaks a number of issues, including both the tightness of the credit market, but also the lack of knowledge what an illegal lender is and the other options available to borrowers.

While increasing household borrowing is not a remotely sustainable answer to the cost of living crisis, we cannot not ignore the real pressures families are facing and the raised incentives to borrow; it must be that there are safe and regulated providers are available, and that illegal lenders are not given the space to exploit those in need.

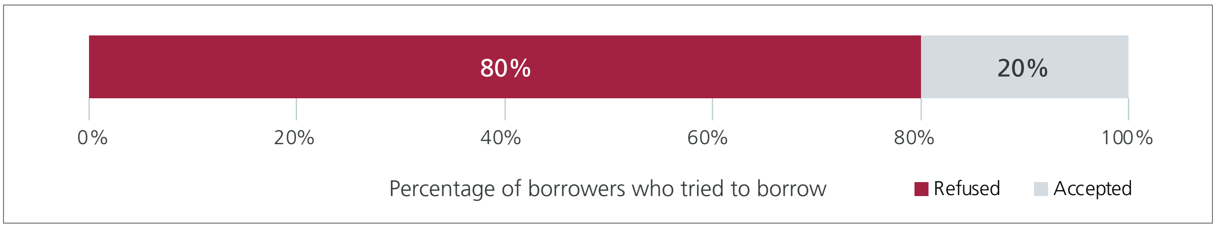
44 YouGov, Finance survey, May 2022

45 Polling by Opinium for the Centre for Social Justice, field dates: 25th February – 1st March 2022.

46 ONS, The rising cost of living and its impact on individuals in Great Britain, November 2021 to March 2022

47 Centre for Social Justice, Swimming with Sharks: Tackling illegal money lending in England, March 2022

Figure 4: Percentage outcome for illegal victims who attempt to borrow from a legitimate source of credit first.



Source: CSJ analysis of illegal money lending team England data (n = 289)

Providing the alternative to illegal lenders

We found that when borrowers do attempt to use a legitimate source, they often cite trying a bank (45 per cent) who are not likely to lend in the small sums they require or a high-cost short-term credit provider (29 per cent), who hold an increasingly diminished market position. Just 8 per cent attempt to use a credit union, a low-cost, community provider.[48]

Credit unions are co-operative societies who provide financial services – primarily savings and loan facilities – to their member-owners. They are registered as Co-operative Societies under the Co-operatives and Community Benefit Societies Act 2014 and the Credit Unions Act 1979. Credit unions are non-profit making, and each union is separate and autonomous.[49]

Each credit union has a common bond which determines who can join it. The common bond may be for people living or working in the same area, people working for the same employer or people who belong to the same association, such as a church or trade union. A common bond cannot exceed a maximum potential membership of 3 million.

Despite their ability to offer low-cost, alternative credit to those who need it, credit union growth has been stifled by out-dated, overly prescriptive legislation dating back to 1979. These take the form of six key challenges. The CSJ explores these in our report, *Swimming with Sharks*.[50] The restrictive common bond limits the geographical spread and reduces the competitiveness of credit unions. The lack of clarity over which services credit unions can offer also stifles growth.[51] But this can be easily tweaked in the upcoming Financial Services and Markets Bill.

Clamping down on illegal lending

Illegal money lending is a crime, and the tactics illegal lenders use to lure, capture, and extort their vulnerable victims for further repayment range from coercive and manipulation behaviour to intimidation, threats of violence, and physical assault. The damage caused by an illegal lender and their activities is therefore not just financial, but psychological and sometimes physical.

We believe that more must be done to protect the most vulnerable from illegal money lenders. As the cost-of-living crisis deepens, we can expect more people to borrow from illegal lenders. Vigilance is therefore necessary. We recommend:

Recommendation: *The Illegal Money Lending Team should be allocated additional funding to scale up its operation in light of the cost-of-living crisis.*

Recommendation: *The Government should overhaul the Credit Union Act 1979 to address the key challenges preventing credit union growth.*

48 Ibid

49 House of Commons library, Briefing paper-Credit Unions, January 2015

50 Centre for Social Justice, Swimming with Sharks: Tackling illegal money lending in England, March 2022

51 Ibid

On Target

Protecting vulnerable households from the inflation crisis

September 2022

The Centre for Social Justice
Kings Buildings
16 Smith Square
Westminster, SW1P 3HQ

t: +44 (0) 20 3150 2326

Twitter: @csjthinktank

www.centreforsocialjustice.org.uk

CSJ The Centre for Social Justice