StepChange Debt Charity

Problem debt and the social security system

How the safety net is driving and exacerbating problem debt among those with low incomes

2020

Summary

National polling commissioned by StepChange Debt Charity shows that over half (54%) of those in problem debt receive support through the social security system.[1]

Given the link between the social safety net and problem debt, it is crucial that the social security system works well for those experiencing financial difficulty. Our findings demonstrate that this is currently not the case and the system is falling short:[2]

Inadequate support is causing hardship.
Half (52%) of those who responded to our survey of debt advice clients in receipt of support meet the definition of destitution developed by the Joseph Rowntree Foundation. This means that in the last month they have gone without two or more basic essentials, such as sufficient food, heating or toiletries, because they cannot afford them. 27% of respondents had recently used a food bank.

Those receiving social security support are often forced to use credit to pay for essentials.
Nationally, 43% of those receiving social security support have used credit to pay for essentials in the last year – a key risk factor in developing debt problems. Alarmingly, of the clients we surveyed 10% told us that they had used an illegal loan shark as a result of a problem linked to social security (we sometimes found that this includes online scams as well as very high cost legal credit).

Delays and errors in the social security system are causing serious financial difficulty.
Four in ten clients had recently been affected by delays (excluding the five week wait for Universal Credit) or errors; over half of those affected had experienced difficulties, such as falling behind on rent payments, as a result.

Excessive deductions from social security payments to repay debt are compounding debt problems.
Over half (54%) of clients who receive Universal Credit have one or more deductions in place. This compares to 36% of those receiving legacy payments. The process of obtaining information and raising concerns about deductions is fragmented and confusing, and the majority of those who seek to negotiate affordable repayments are unhappy with the outcome.

Key design features of Universal Credit are driving hardship and problem debt.
The five-week wait for the first payment led almost all clients affected (92%) to experience some form of hardship or financial difficulty. Clients also told us other characteristics of Universal Credit, such as unpredictable monthly payments, are causing problems. Two-thirds felt that Universal Credit had made it harder for them to budget and manage their financial situation.

The social security system should support financial resilience and recovery from problem debt. The present system too often undermines, rather than supports these aims. Universal Credit is central to these issues: our polling indicates that 25% of those receiving Universal Credit are in problem debt, three times the rate among the general population (8%), and 11% more than those receiving legacy benefits (14%).

This report sets out recommendations organised around three principles:

01
Standard payments should be adequate and sufficiently stable to allow people to meet living costs without experiencing financial difficulty and problem debt.

02
The social security system should support sustainable recovery from problem debt.

03
The social safety net should support people to safely meet unpredictable peaks in essential costs.

[1] Polling commissioned from YouGov (further details in methodology section). Figures for those receiving working age social security payments.
[2] StepChange (2019) Personal Debt in the UK: 2019 Statistics Mid-Year Update. London: StepChange Debt Charity.

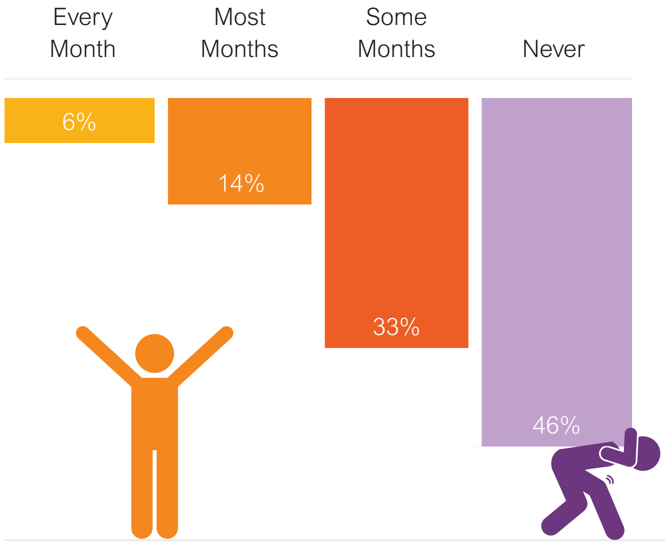
01 Making ends meet

"The money does not last me a whole month to the next payment. ...I have learnt to eat one meal a day most of the time."

"It's a mentally draining mission to budget every month."

27% of clients receiving working age social security have used a foodbank within the last two years

How often are you able to make ends meet?[4]



The majority of debt advice clients who rely on social security are struggling to make ends meet, with only six per cent reporting that they are able to make ends meet every month, and almost half (46%) reporting that they can never make ends meet.

To better understand the impact of poverty on the ability of clients to meet essentials, we asked whether they had gone without specific items such as two meals a day or heating – these are based on a definition of destitution developed by the Joseph Rowntree Foundation[3]. Worryingly, our survey suggests that half (52%) of clients receiving support through the social security system cannot pay for two or more basic essentials.

These figures reflect the financial vulnerability of those with low incomes affected by problem debt. The majority of clients also have at least one additional vulnerable characteristic, most commonly depression (51%), anxiety (50%), a physical disability or long-term condition (44%), or another mental health condition (12%).

Clients told us that the burden of managing on an inadequate income had often compounded or caused mental health problems.

Unexpected expenses are a particular challenge: 82% of respondents told us that they would not be able to meet an expected expense of £300. The most common strategies to meet an unexpected expense were to ask family and friends for help (26%), sell personal possessions (19%) or cut back on essentials (13%).

Local support had some importance to clients: 39% had used some form of local authority or voluntary support in the last two years, most commonly a food bank (27%) followed by a discretionary housing payment (11%), help from a voluntary organisation or church (7%) and other support from a local authority such as a grant or loan (6%). 2% had received help from a Jobcentre, such as help to attend an interview or pay a childcare deposit.

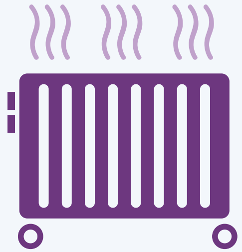
[3] This figure likely reflects in part the composition of survey respondents: approximately 76% of respondents were single adults (with or without children) – the group most at risk of poverty and destitution. In the methodology developed by Fitzpatrick, S. et al (2018), people are destitute if they have lacked two or more of these six essentials over the past month because they cannot afford them or they have an 'extremely low' income (with set thresholds for specific household structures). We are unable to check the proportion of clients who meet the latter thresholds: this means there may be clients who do not meet the 'essentials' criteria but do meet the income criteria. (Fitzpatrick, S. et al (2018) Destitution in the UK 2018. York: Joseph Rowntree Foundation.) [4] StepChange survey of clients

We asked StepChange clients about making ends meet over the past month and we found that...[5]

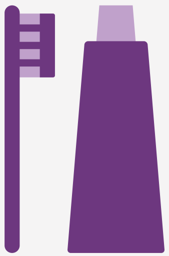
3%
Have had to sleep in temporary accommodation (or without accommodation) for one or more nights

7%
Have been unable to pay for light in their home for five or more days

31%
Have been unable to heat their home for five or more days



46%
Have lacked clothing or footwear appropriate for the weather



36%
Have lacked basic toiletries

53%
Have had fewer than two meals a day for two or more days

31%
None of these

[5] StepChange survey of clients

Inadequate income to meet basic living costs is the primary underlying driver of hardship among clients, but clients also told us that a number of events may drive difficulty.

One of the most common of these was errors and delays: 24% of clients had recently (within the last two years) experienced delays in social security payments, excluding the wait for Universal Credit, and 31% had experienced errors in social security payments – 12% had experienced both.

Almost all (98%) of clients affected said that this led them to cut back on essentials or experience some form of financial difficulty: half of those affected said that they had fallen behind on rent or mortgage payments, 62% said that they had fallen behind on credit repayments, and 71% said that they had needed to ask for financial help from family or friends.

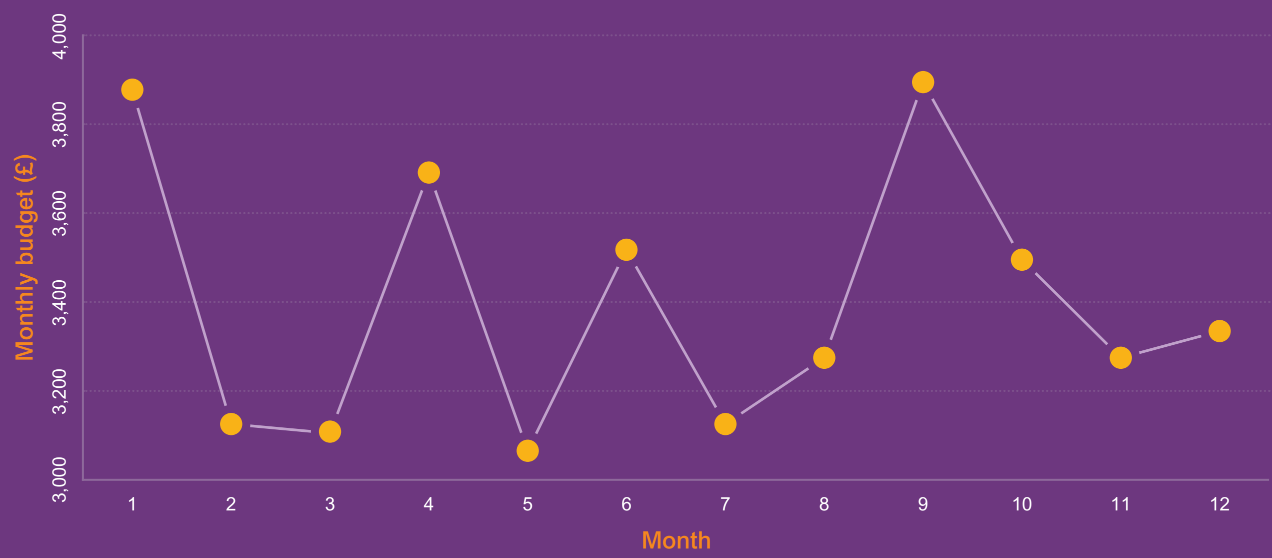
Budgeting for unpredictable expenditure

Unexpected costs are a reality of household budgeting that pose particular challenges for those with low incomes. The detailed budgets developed to calculate the Minimum Income Standard (and in turn the living wage) can be used to estimate typical fluctuations in essential budgeting needs.

The chart below represents a simple model of the minimum budget for a couple with two children (containing 648 items) and indicates how essential expenses can be expected to change from month to month.[6]

The monthly budget ranges from £3,069 to £3,881 – a difference of up to £812 from month to month. These changes are driven by infrequent costs such as replacing appliances and clothes, as well as smaller expenses like haircuts and children's presents.

Those receiving social security support are often constrained in their ability to manage such fluctuating expenses by limited savings and access to affordable mainstream credit; difficulty managing unpredictable costs often results in hardship or harmful high cost credit use that causes or exacerbates financial crisis.



[6] The model reflects an assumption that each expense with a frequency of more than one month but less than one year occurs in a random month of the year (or months for recurring items such as bi-monthly haircuts). All Christmas items were placed in one month and fuel costs, which are given in the MIS budget as an annual expense, were assumed to be met on a monthly basis through a direct debit. Items that occur with a frequency of more than one year were given a probability of occurring based on the item's predicted lifespan (for example, an item with a lifespan of five years were assumed to have a one in five chance of occurring in the budget year and so on). In turn, those items that did occur in the budget year were assigned to a random month. (Budgets estimated using the latest Minimum Income Standard data, www.lboro.ac.uk/research/crsp/mis/results/).

The fall in value of working age social security support

The 'benefits freeze', which comes to an end next year, is the single biggest driver of rising poverty.[7] The freeze, which has been in place since 2016/17 and is scheduled to end in April this year, means simply that most working-age benefits (other than disability benefits) are frozen in cash terms. This affects almost one-third (30 per cent) of UK households.

The freeze comes on top of a long-term erosion of the value of support: the annual increase in the value of working age benefits had been held at 1% for three years from 2012/13 (Child Benefit was frozen for three years from 2011/12 and then increased by 1% in 2014/15). Other elements of support have not been uprated since they were introduced; the family element of tax credits, for example, was never increased from £545 each year after it was introduced in 2003/04.

Housing support has also fallen in real value. Until 2011, the maximum Local Housing Allowance rates (which are used to calculate housing support) were linked to the middle of market rents. From 2011, this was reduced to the bottom third (30th percentile) of rents. The link with rents was then broken: in 2012/13 rates were frozen, uprated in line with CPI for one year and then increased by one per cent for the next two years until the benefits freeze took effect.

The benefits freeze sits alongside cuts in support such as reductions in the Universal Credit work allowances, reduced support for children with disabilities in Universal Credit and changes to tax credits including the abolition of the baby and family elements and the introduction of a two child cap on support.

The table below sets out 'safety net' income as a percentage of the minimum income standard (based on what members of the public think is needed for an acceptable minimum standard of living) between 2009 and 2019, showing a significant decline in the value of working-age support.

Percentage of MIS covered by safety net income[8]

	2009	2019
Single adult	42%	32%
Couple adult	42%	30%
Single with two children	69%	58%
Couple with two children	63%	56%

The real value of out of work support is now lower than it was in the early 1990s, despite a 50 per cent rise in GDP per capita.[9] The long-term erosion of the value of support means that the challenge of re-linking support to living costs is no longer a matter of ending the benefits freeze but a long-term strategic challenge of making up lost ground.

"My arrears keep increasing as a result of errors and gaps in my rent payments despite my rent being paid directly to my landlord."

"Real time information errors between HMRC and UC meant I was paid when I shouldn't have been paid."

"There was overpayment and an immediate stop on payments due to an error their end. This has been incredibly stressful and leaves you feeling uncertain and insecure."

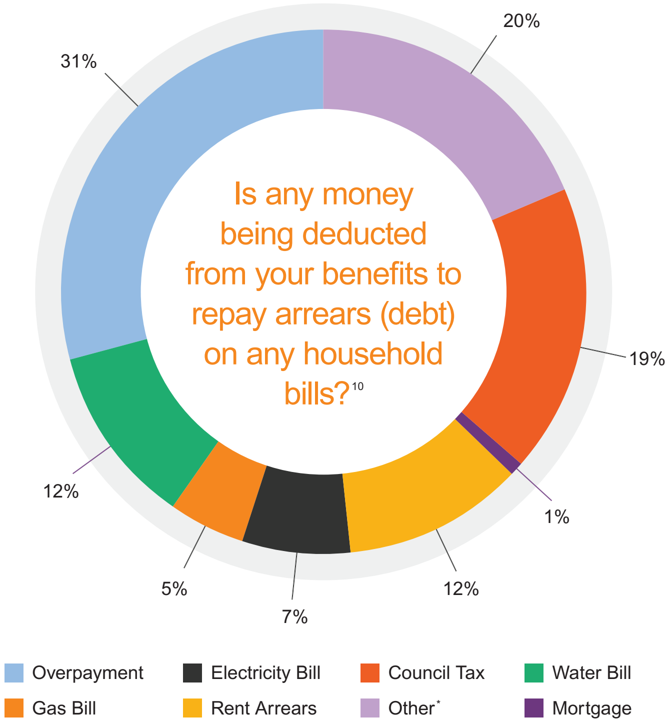
[7] Joseph Rowntree Foundation press release 'End the benefits freeze this year to boost the incomes of working families', 8 March 2019.
[8] Hirsch, D. (2019) A Minimum Income Standard for the United Kingdom in 2019. York: Joseph Rowntree Foundation, p. 26. In this example, children in each household are assumed to be aged 4 and 7.
[9] Corlett, A. (2019) Resolution Foundation Spotlight briefing: 'The benefit freeze has ended, but erosion of the social security safety net continues

02 Unaffordable deductions from Universal Credit

> "I asked them if I could reduce the monthly repayment amount so that I pay it back over a longer period, but they said they were unable to do that."

> "Trying to get a statement or explanation of deductions from the Department for Work and Pensions for 'other' deductions has been impossible."

> "How can you be happy with the repayment amount when you don't have enough to live on through the month?"

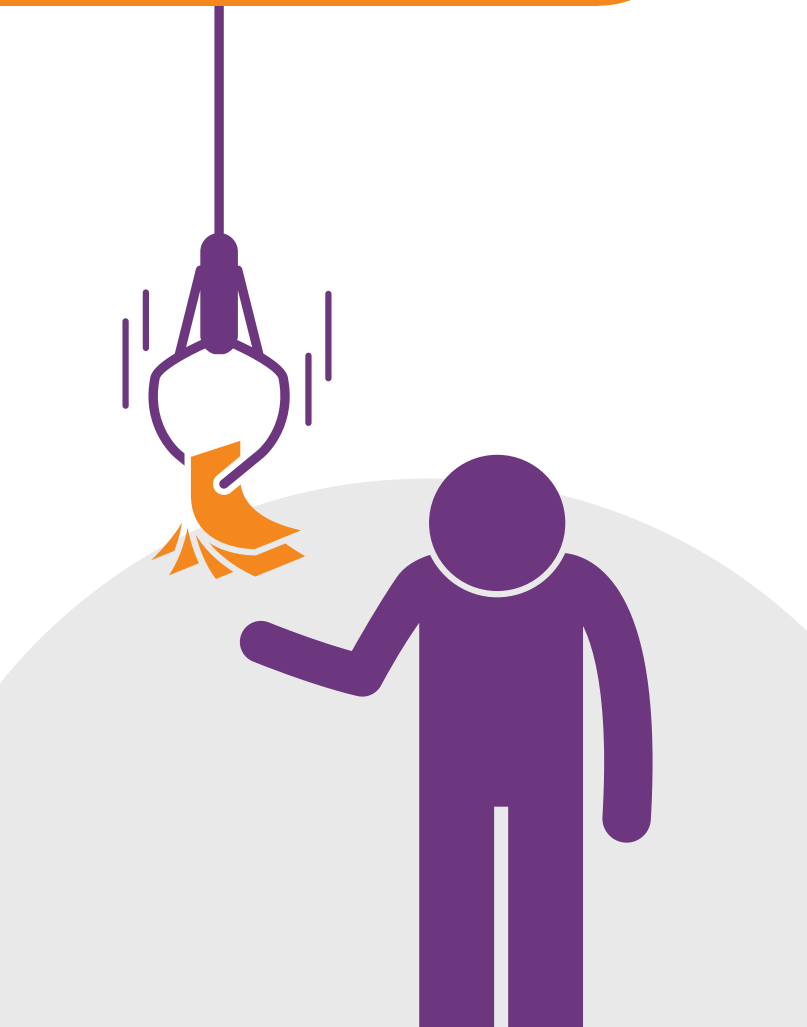


*Including budgeting loans

54% of clients receiving Universal Credit report having at least one deduction in place. This compares to 36% of those receiving legacy payments, reflecting a higher likelihood that those receiving Universal Credit will be repaying an advance payment or a tax credit overpayment. 40% of clients had two or more deductions in place and 15% had three or more.

Deductions are most frequently Universal Credit advances, overpayments and council tax debt, followed by rent and utility arrears. The most common overpaid benefit was child/working tax credit (58%), followed by Housing Benefit (25%), Universal Credit (13%) and Employment and Support Allowance / Incapacity Benefit (12%).

Half (49%) of those who had recently taken out a budgeting loan or advance had experienced repayment difficulty. Among the third who contacted the Department for Work and Pensions to negotiate repayment of a budgeting loan or budgeting advance, over half (55%) did not agree the repayment agreed was affordable; 42% did not know they could discuss repayment with a DWP official.



[10] StepChange survey of clients

Most (93%) of those we surveyed affected by deductions had experienced some financial difficulty or hardship as a result.

These findings reflect a number of problems with the present system of deductions.[11] Deductions are set by default at fixed rates without regard to affordability; moreover, the maximum for individual deductions such as rent and repayment of overpayments is treated as a default amount. Tax credit overpayments are typically automatically attached to Universal Credit.

The inflexibility of the system is compounded by poor communication. This includes insufficient notice, a failure to provide basic information about some deductions, and the absence of a single point of contact for those affected – those seeking to negotiate deductions often have to contact one department to obtain information about the deduction and a second, separate, department to request an affordability assessment.

The result of unaffordable deductions is often counter-productive, causing stress and anxiety, compounding health problems and driving people into unnecessary hardship or to use high cost credit.

Did deductions to repay any arrears on household bills lead to any of the following?[12]

[11] A detailed explanation of the rules governing deductions are set out in the StepChange briefing note (2020) 'Deductions in Universal Credit' available at www.stepchange.org.
[12] StepChange survey of clients

03 Problems with Universal Credit cause hardship

(and undermine the policy goal of supporting people to work)

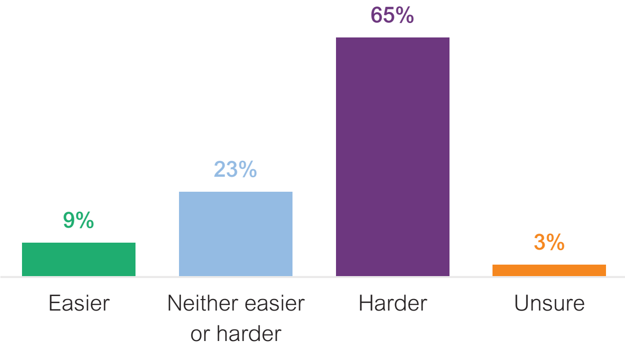
"I am reluctant to get a job now as I know if it doesn't work out that's another six weeks without money."

"I don't earn a constant steady amount of wages so with overpayments… I never know where I am. I was better off mentally and financially when only working 16 hours a week."

"I had an eviction notice because rent wasn't paid on time by Universal Credit."

60% affected by the wait for Universal Credit asked for financial help from family or friends

Has receiving Universal Credit made it easier or harder for you to budget and manage your financial situation?[13]



The roll-out of Universal Credit began in 2013. While 'managed migration' – the transfer of those receiving legacy benefits to the new system – has been paused, 'natural migration' – the transfer to the new system of those who experienced a change of circumstances – means that over two million people are now receiving Universal Credit. This figure is reflected among StepChange clients: among those we surveyed, 44% now receive Universal Credit.

Universal Credit was designed to simplify social security and support people to work. This led to design choices, such as a monthly payment in-arrears structure to 'mirror the world of work', that have proved to be problematic in practice.

The most significant problem linked to Universal Credit is the effect of the waiting period for the first payment and advance loans taken out to help meet expenses. Evidence from our clients reflects the troubling impact of the five week wait: half of clients (47%) had fallen behind on rent as a result of the wait or the subsequent repayment of advances, and more than half (65%) had gone without or cut back on meals and food or relied on family and friends for financial help (60%).

Compared to the shorter payment cycles (typically bi-weekly) of legacy benefits, many people experiencing financial difficulty find the monthly Universal Credit payment challenging. Those struggling with debt face frequent demands for payment from creditors and often find it difficult to protect a sufficient amount of their budget to meet basic expenses for a full month. For many in this group, more frequent payments make it easier to manage expenses in this pressured context and leave less risk of periods when money has run out. When we asked clients how frequently they would like to receive support to budget and manage their finances, two-thirds (66%) said weekly or bi-weekly, with only 17% choosing monthly.

Three quarters of clients receiving Universal Credit who receive support with housing costs receive this support directly (rather than through a payment directly to their landlord). People who have not paid rent in the past continue to be caught out by confusion about this change, and others struggle to preserve sufficient budget through a month to pay their rent. This is both a problem of adequacy and juggling narrow budgeting margins to avoid falling into rent arrears.

[13] StepChange survey of clients

There are 'alternative payment arrangements' (APAs) available to have Universal Credit paid more often than monthly, split between partners or for the housing element to be paid directly to a landlord. (These choices are available, without evidence of need, in Scotland as 'Scottish choices'.)[14] However, applicants must show they are affected by specific vulnerabilities such as 'severe or multiple debt problems', limiting access.

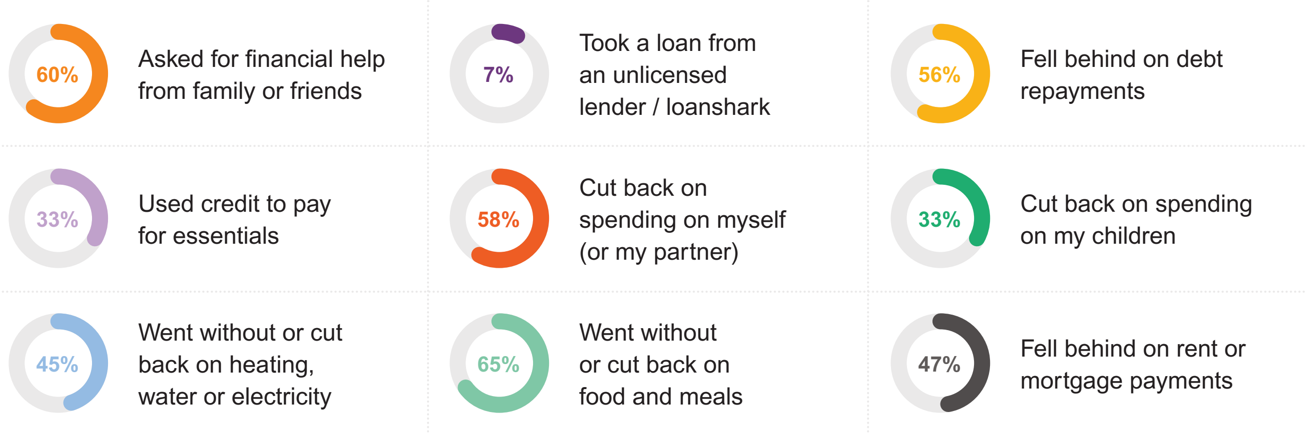
Clients also reported struggling with the instability of Universal Credit payments. Anyone with a fluctuating income is likely to experience fluctuations in their monthly award because Universal Credit does not have a built-in buffer to accommodate changes in income from month-to-month and stabilise payments.

Those with predictable paychecks can also experience a change in support due to the way payroll dates can interact with the fixed dates of a Universal Credit assessment period; for example, where someone is paid early, their income could appear to double in one assessment period. Those who are paid weekly or bi-weekly may also find that their monthly income fluctuates as payment dates shift inside or outside their monthly Universal Credit assessment period dates.

Universal Credit has some similar characteristics to the tax credit system in that a number of changes of circumstances, such as a change in relationship status or the amount of rent paid, must be reported promptly or, if not, may result in an over- or under-payment. Errors remain a common occurrence in Universal Credit, often leading to gaps and delays in payments.

Overall, 65% of clients said that receiving Universal Credit had made it harder for them to budget and manage their financial situation, and 9% easier. These issues cause hardship but can also undermine work incentives: some clients receiving Universal Credit mentioned that they had felt better off when they were not working because their income was more stable, and that they feared moving into temporary work because if their job came to an end it would mean they would again experience the interruption in income caused by the five week wait.

Did the wait for the first Universal Credit payment lead to any of the following?[15]



[14] In Northern Ireland, Universal Credit is paid by default twice monthly and the housing element is also paid by default directly to landlords.
[15] StepChange survey of clients

Social security, loan sharks and informal lending

10% of clients who responded to our survey told us that they had used an unregistered lender as a result of a problem linked to the social security system. We found these experiences involve local loan sharks, online scams (for example, where someone is asked for a deposit to access a loan that is not made) and legal, high cost, short-term credit that people assume to be illegal because the interest charged is so high.

60% of clients also told us that they had needed to ask for help from family and friends as a result of a problem linked to the social security system, reflecting the extent to which those with few other options are forced to turn to informal sources of support.

Recent research commissioned by the Financial Conduct Authority found that illegal lending is most likely to be found in areas of high economic deprivation, particularly within social and rented housing estates (in both urban and rural areas) in 'close knit' communities.[16] However, illegal lending occurs among a variety of social groups and contexts; the common unifying factor among those that use illegal lenders is an income shortfall and an urgent need for money.

The consequences of resorting to a loan shark are often serious, including punitive costs, exploitation or forced work and threats and violence, as well as negative effects on mental and physical health.

"A friend of mine realised that I was struggling and gave me a phone number for a loan shark. I rang him, and after speaking he offered to lend me £500 on the condition that I pay him back £1,200 – I am still paying him back at the moment. I've heard horror stories about the violence others have endured if they haven't paid him back on time."

[16] Financial Conduct Authority (2017) Shining a light on illegal money lending: consumer experiences of unauthorised lending in the UK

Recommendations: 'Debt-proofing' the social security system

StepChange has welcomed the government's focus on financial inclusion, which includes addressing harmful high-cost credit use. However, this report shows that policy decisions within the social security system are undermining financial inclusion policy goals. In fact, as it stands, the social security system would not meet basic regulatory requirements of consumer credit firms to treat customers fairly.

We set out three principles that should shape design decisions to ensure that the social security system does not drive or exacerbate debt problems, alongside specific recommendations for implementation.

1.

Support should be adequate and sufficiently stable to allow people to meet living costs without experiencing financial difficulty and problem debt.

- **As a priority, the government should commit to ensure that social security support meets and keeps pace with the cost of living.** We welcome the end of the 'benefits freeze'; in future, the government should now set out a credible approach to setting and uprating support for working age adults. This should:
  - end the two-child limit;
  - include a sustainable plan to re-link the value of working age support to living costs, prioritising those at risk of hardship;
  - re-establish and maintain the link between housing support and rental prices; and
  - better take account of additional costs (or reduced ability to earn income) associated with children, ill-health or disability and caring responsibilities.
- Minimise fluctuations in Universal Credit payments that don't reflect a meaningful change in underlying circumstances by introducing an annual disregard buffer of at least £2,500 in Universal Credit (to match the disregard provided in the tax credit system) and address infrastructure barriers to ensure the frequency and timing of assessment periods can be aligned with income from work.
- End the five-week wait for Universal Credit by extending the 'run-on' of legacy benefits to tax credits for those receiving legacy benefits and allowing new claimants to backdate applications up to a reasonable period of three months.
- Give people more control over Universal Credit payments by allowing people in England and Wales to choose the frequency of payments and whether housing support is paid directly or to a landlord (defaulting to the landlord if no decision is made).
- As recommended in the recent Bright Blue report 'Helping Hand?' introduce an 'Independent Case Examiner' to determine when compensation is due following detriment caused by administrative errors that are not the fault of the claimant: this would introduce a balance between the responsibilities of the state and the individual, ensure people with low incomes do not lose out financially as a result of seeking support, and help to drive better design and administration[17].

[17] Shorthouse, R. et al (2019) Helping Hand? Improving Universal Credit. London: Bright Blue.

2.

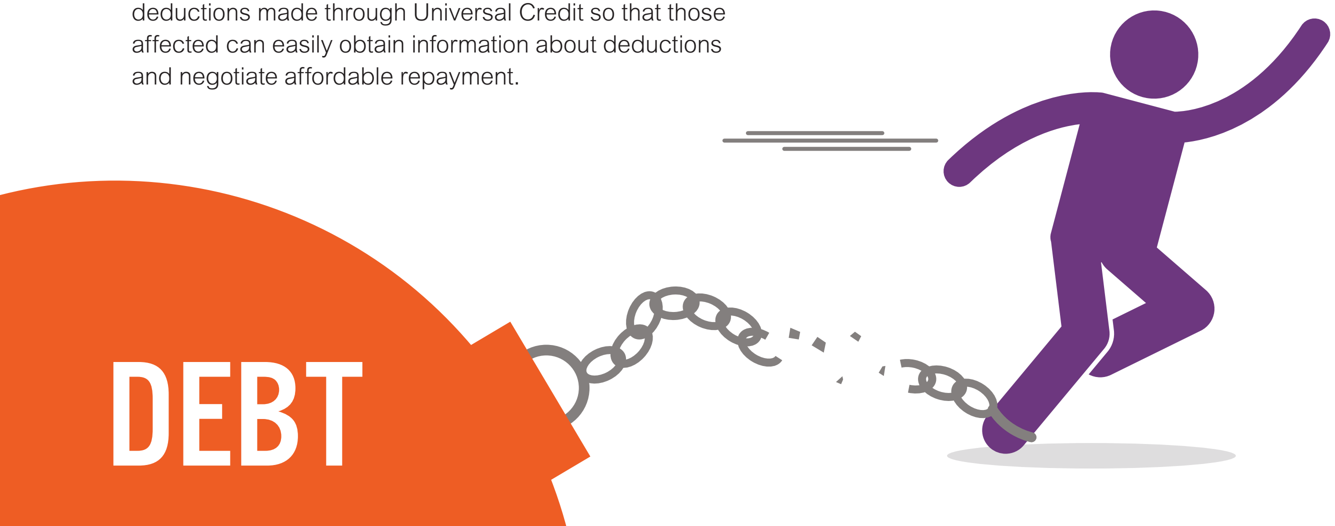
The social security system should support, rather than undermine, sustainable recovery from problem debt.

The government should use the Cross Government Debt Management Strategy, alongside the Breathing Space and statutory debt management plan schemes, to commit to becoming a leader of best practice in debt collection and roll out standards that match or better those of the consumer credit regulatory framework.

To meet this aim, the Department for Work and Pensions should overhaul the system of deductions from Universal Credit, amending legislation and regulations where necessary, to ensure deductions are only made where these are in the interest of the claimant and affordable.

This should include:

- Accepting industry-standard affordability assessments conducted using the single financial statement.
- Introducing a single 'one stop shop' to co-ordinate deductions made through Universal Credit so that those affected can easily obtain information about deductions and negotiate affordable repayment.
- Providing a minimum of 60 days' notice for attachment of non-priority government debt to Universal Credit, signposting to free debt advice and an affordability assessment.
- Requiring third party creditors to give at least 28 days' notice of a priority deduction from Universal Credit, alongside details of free debt advice and who to contact if the proposed deductions are not affordable.
- Automatically disregarding overpayments caused by official error up to a reasonable maximum value and applying an amnesty to historic tax credit debt.



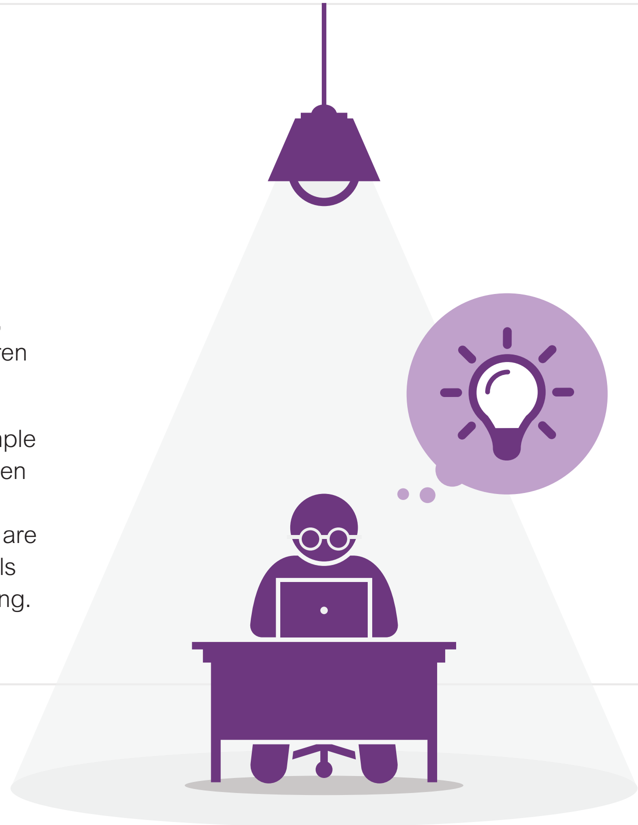
3.

Social security must support people to safely meet peaks in expenditure.

The frequency with which those receiving support are forced to experience hardship or borrow to meet essentials reflects a lack of good alternative options. Alongside ensuring the adequacy of support, the government can help people who receive social security to meet fluctuating and unpredictable essential costs by:

- Changing the way that budgeting advances are provided so that they are better suited to the needs of households with low incomes through more flexible borrowing and repayment terms. This includes removing restrictive eligibility criteria unrelated to affordability, allowing multiple loans (up to the maximum amount) and extending the maximum repayment period to 24 months.
- Introducing 'Discretionary Hardship Payments' for those who cannot afford to repay an advance that functions in a similar way to Discretionary Housing Payments but can be used to meet essential expenses (defined broadly in line with items qualifying for budgeting loans/advances).
- Re-introducing statutory guidance and ring-fenced national funding for local crisis support in England. Local support is too often addressing gaps in the national safety net rather than supporting those affected by crisis. Alongside more national help for those affected by financial difficulty, local crisis support requires statutory guidance to provide a platform for co-ordinated local provision of specialist services, and a sustainable funding settlement.

Methodology



This report is based on research using StepChange debt advice client data, a survey of StepChange clients and national polling.

We analysed data held on clients who completed a telephone or online debt advice session with StepChange in the first six months of 2019 – 190,484 clients.

We conducted a survey of clients between 13 November and 2 December 2019. The survey was sent to a sample of clients who receive at least one form of working age social security support, excluding those who receive only Child Benefit. We received 668 unique responses.

52% of respondents were single adults without children, 27% single parents, 13% couples with dependent children and 7% adult couples.

Large national poll conducted by YouGov Plc. Total sample size was 4,972 adults. Fieldwork was undertaken between 28th November - 2nd December 2019. The survey was carried out online. The figures have been weighted and are representative of all GB adults (aged 18+). Some % totals in this document may not add up to 100% due to rounding.

Support received by survey respondents

% respondents in receipt

- 20% Child tax credit
- 10% Working tax credit
- 8% Child tax credit and working tax credit
- 31% Housing Benefit
- 5% Income Support
- 5% Jobseeker’s Allowance
- 9% Disability Living Allowance
- 23% Personal Independence Payment
- 20% Incapacity Benefit or ESA
- 9% Carer’s Allowance
- 29% Council Tax Reduction
- 44% Universal Credit

**Written by Adam Butler
with polling analysis
by Josie Warner.**

Email: policy@stepchange.org
Web: www.stepchange.org
Twitter: @stepchange

StepChange Debt Charity