The Universal Credit (Surpluses and Self-employed Losses) (Digital Service) Amendment Regulations 2015 (S.I. 2015 No.345)

Report by the Social Security Advisory Committee under Section 174(1) of the Social Security Administration Act 1992 and statement by the Secretary of State for Work and Pensions in accordance with Section 174 (2) of the Social Security Administration Act 1992.

Presented to Parliament pursuant to Section 174(2) of the Social Security Administration Act 1992.

This publication is available at www.gov.uk/government/publications

Any enquiries regarding this publication should be sent to us at WORKINGAGE.BENEFITSSTRATEGY@DWP.GSI.GOV.UK

Print ISBN 9781474115438
Web ISBN 9781474115445

ID 13021522 02/15

Printed on paper containing 75% recycled fibre content minimum

Printed in the UK by the Williams Lea Group on behalf of the Controller of Her Majesty's Stationery Office

Statement by the Secretary of State for Work and Pensions in accordance with Section 174 (2) of the Social Security Administration Act 1992

The Universal Credit (Surpluses and Self-employed Losses) (Digital Service) Amendment Regulations 2015

INTRODUCTION

1. Universal Credit is a new benefit being introduced in the UK for those on a low income or out of work, replacing certain other benefits. As Universal Credit is both an in and out of work benefit, claimants' levels of earnings are taken into account on a monthly basis when the level of Universal Credit award they are entitled to is being calculated.

2. The purpose of the Universal Credit (Surpluses and Self-employed Losses) (Digital Service) Amendment Regulations 2015 is to mitigate against unintended consequences where claimants may have genuinely irregular earnings, as well as to remove perverse incentives for employers and employees to manipulate earnings payment patterns to maximise Universal Credit awards. Under these regulations, when a claimant returns to Universal Credit within six months of a previous award ending, the Department for Work and Pensions ("the Department") may take into account earnings during the intervening period.

3. Additionally, in December 2012 the Government responded to the Social Security Advisory Committee ("the Committee") report on the draft Universal Credit Regulations 2013 and agreed with the Committee's recommendation to revisit the issue of carry forward of losses for self-employed claimants. The Government has reviewed this issue and agreed that under these regulations, self-employed claimants will be able to carry forward a loss from one month into the next monthly assessment period, for up to eleven assessment periods.

4. These regulations will only apply to the Universal Credit 'Digital Service' and are scheduled to come into force from April 2016.

5. These Regulations relate to the introduction of "surplus earnings" and "self-employed losses" in Universal Credit. Proposals for regulations were presented to the Committee at its meeting on 1 October 2014. The Committee decided to take the proposals on formal reference and received these on 10 October 2014.

6. The Committee held a public consultation on the draft regulations, open to organisations and individuals, between 17 October and 7 November 2014. As part of this consultation the Committee held a workshop on 6 November with representatives of small business, the self-employed and other specialists to discuss the potential impact of the proposals on the self-employed. This was attended by 13 representatives of relevant organisations. In addition, the Committee received 28 written responses to their consultation: 24 from representatives of organisations, local authorities or groups, and four from individuals contributing in a personal capacity. The Committee subsequently delivered its report to the Department on 15 December 2014.

7. In line with the recent changes to guidelines on policy making, the Department has applied ‘The Family Test’ to these regulations and reflected on this analysis alongside reading the Committee’s consultation report. The outcome of this test will be published alongside the regulations.

The Committee’s Report and the Government Response

8. The Department welcomes the Committee’s report on the draft regulations and is grateful to the organisations who responded to the Committee’s consultation for their considered and insightful contributions.

9. The Committee’s report includes five key recommendations, covering the level of the de minimis, preventing abuse, carry forward of self-employed losses, averaging self-employed earnings, and exemptions from the surplus earnings regulations for victims of domestic violence. These recommendations and the Department’s responses are set out below.

THE COMMITTEE’S RECOMMENDATIONS AND THE DEPARTMENT’S RESPONSE

The report of the committee makes the following recommendations: -

Level of the De Minimis

The Committee recommends that the de minimis figure be set at a higher figure in order not to penalise those who ought to be the principal beneficiaries under Universal Credit – those who take additional work or additional hours in order to move off benefit and be self-sufficient.

Response -

10. Ministers have carefully considered the Committee’s recommendation and the thoughtful contributions from those responding to its consultation. The surplus earnings regulations are primarily designed to address the unintended consequence of someone receiving significantly more or less Universal Credit than another claimant with the same circumstances based simply on their payment pattern. The regulations were not designed to be a punitive measure for those experiencing small fluctuations in earnings, for instance as a result of a bonus.

11. The draft regulations included a de minimis of £100, so that only fluctuations in earnings that were more than £100 above the nil Universal Credit threshold would be taken into account. In reviewing whether the policy will deliver this principle, the Government has reconsidered the level at which the de minimis should be set. The Government accepts the Committee’s observation that a number of relatively low-paid workers, whose employment may be of a temporary or insecure nature, could be within the scope of the regulations as originally drafted. As it is not the Government’s intention to target the policy at those with only small fluctuations in earnings, Ministers have taken the decision

to accept the Committee's recommendation, and to increase the de minimis from £100 to £300.

12. Under our most recent analysis, we expect that increasing the de minimis to £300 will significantly reduce the number of households impacted by surplus earnings to 0.1-0.2million per month, compared to 0.3-0.4million under the previous de minimis level of £100. With the de minimis set at £300, the vast majority of Universal Credit claimants (80-85%) are expected to receive some, or all, of their usual Universal Credit award in the assessment period in which they reclaim Universal Credit, and the impact of the policy will therefore be targeted only on those with higher levels of earnings.

13. As the policy is focused at only those with higher earnings, we believe it is reasonable to expect these individuals to have managed their earnings so that they are not at risk of hardship when these regulations are applied.

14. The Department has made a firm commitment to providing claimants with clear advice and guidance so that they understand this policy and how it may affect them. This will enable claimants to manage their spending decisions in the periods after their Universal Credit award ceases on the basis that any surplus earnings may be taken into account should they return to Universal Credit within six months.

15. The Department rejects any assertion that the application of surplus earnings serves as a disincentive to claimants taking on work, even where that work may be part time or temporary. It is important to note that the generous work allowances and single taper rate of 65% mean that Universal Credit claimants will still be better off in work as they will be able to keep a considerable amount of their earnings before their Universal Credit award begins to reduce. Some examples to illustrate how claimants are better off in work can be found at Annex A.

Preventing Abuse

Rather than having to consider introducing further layers of complexity to counter such arrangements in future, the Committee wonders whether it might be more appropriate to adopt a more strategic approach where all such countering measures are addressed in a general anti-abuse provision.

Response –

16. The surplus earnings policy is primarily designed to prevent Universal Credit claimants from being unfairly advantaged or disadvantaged simply based on the structure and frequency of their income. The Government does not expect that this would necessarily be the result of malicious manipulation. Rather, we expect this would result from perfectly legitimate payment models.

17. Therefore, a general anti-abuse measure would not meet the intention of this policy as it would only be effective in circumstances where a claimant or

employer manipulate payment patterns in order to gain or increase their entitlement to Universal Credit.

18. We do share the Committee's concern to prevent abuse and collusion and Universal Credit has protections against such behaviour under regulation 60[1] of the Universal Credit Regulations 2013.

Carry Forward of Self-Employed Losses

On self-employed losses we recommend that the Government should re-visit the policy and come up with a solution which achieves greater parity of treatment between the employed and the self-employed. The difficulties caused by the operation of the MIF stands out as needing to be addressed.

Response –

19. The Committee raised several queries and concerns in relation to the self-employed. The response to this recommendation has been set out under the subheadings below, to address each point individually.

20. Within these regulations, the Government has recognised the unique challenges of self-employment and introduced the principle of 'carry forward of losses' to acknowledge that self-employed claimants may be more susceptible to irregular earnings. This provision will allow self-employed claimants to set-off a deficit in one assessment period against profits in succeeding assessment periods, up to a maximum of eleven assessment periods . The introduction of this provision will provide additional support to self-employed claimants when they have to make key business decisions, for instance a financial outlay to invest in new equipment to support the growth of their business.

Stakeholder Advisory Group

21. The Government regards the input of stakeholders as key to the successful implementation of these regulations and the wider support package for self-employed Universal Credit claimants. In response to the Committee's recommendation in their September 2014 report '*Social Security and the Self-Employed*' the Government established a 'Universal Credit Self-Employment Stakeholder Advisory Group' to advise the Department on the effective delivery of the Universal Credit policy and legislation in relation to self-employed claimants.

22. We plan to continue to draw on the expertise of the Self-Employment Stakeholder Advisory Group as Universal Credit continues to roll out.

[1] http://www.legislation.gov.uk/uksi/2013/376/regulation/60

The Minimum Income Floor

23. The Minimum Income Floor (MIF) in Universal Credit is a separate policy and is not altered by these regulations. To apply the MIF for the period in which surplus earnings are being taken into account is consistent with the policy approach for self-employed claimants where there has not been a break in award.

24. The MIF is designed to ensure that self-employment is gainful and to support self-employed claimants to grow a profitable business. The Government believes that it is right to continue to apply the MIF within the period of surplus earnings being taken into account, and believes that to introduce an exemption in such circumstances would undermine the wider purpose of the MIF policy.

Length of Time over which to Carry Forward Losses

25. The Committee has questioned whether eleven assessment periods is a sufficient period in which to expect deficits to be absorbed. The Government's position remains that eleven assessment periods is an appropriate point at which to cap the carry forward of losses to ensure that claimants have a significant amount of time to offset losses on a rolling basis. This is more generous than the six month period which is used when considering any surplus. The Government believes that an extension beyond eleven assessment periods would be disproportionate in addressing this issue and feels this length of time is a reasonable period in which to expect losses to be balanced against profits.

Pensions Contributions

26. The Committee raised a concern in relation to the pension contributions of self-employed claimants. The Committee's report suggested that there was a 'disparity' between the employed and the self-employed in this respect. In fact, the current policy regarding pension contributions is consistent for both the employed and the self-employed. Pension contributions are fully offset against any income in the assessment period in which they are made, so that claimants will be able to make pensions contributions to the level they wish, up to the point that this reduces their award to zero. This will allow claimants to invest in a pension without being penalised through a reduction in their Universal Credit award.

27. However, the Government is keen to ensure the Universal Credit system is designed to support and encourage investment in pensions, and will therefore keep the impact of this policy on self-employed pension contributions under review. The Department plans to use the Universal Credit Self-Employed Stakeholder Advisory Group to assist in monitoring this policy in future.

Cross-subsidy – Employed and Partner's Earnings

28. The Committee queried whether an individual would be able to use their employed earnings to 'cross-subsidise' their self-employed business or, in the

case of a joint claim, if one member of a household may be able to 'cross-subsidise' the business, trade or vocation of another.

29. Currently, the Universal Credit 2013 Regulations require the self-employed earnings for each assessment period to be calculated by taking the 'profits' of each trade profession or vocation carried on by the claimant (that is the actual receipts less permitted expenditure in the assessment period) and then making deductions for tax, national insurance and pension contributions. If a person is carrying on two businesses, the expenditure from one cannot be offset against the other.

30. These regulations simplify this to allow for an element of 'cross-subsidy'. The profit or loss of each separate trade, profession or vocation (or, if it is a partnership, the claimant's share) is calculated for the assessment period by deducting actual expenses from actual receipts. These are combined to give an overall profit or loss from which any tax or national insurance payments in the same period are deducted.

31. Universal Credit supports people to be self-employed where self-employment is the best route for them to become more financially independent. It is not the intention that losses from self-employment have the effect of reducing an individual's employed earnings in order to increase their Universal Credit award.

32. In the case of a joint claim, the Committee are correct that one member of a household cannot use their self-employed earnings to subsidise the self-employed business of another member of that household (although if they are jointly carrying on a single business they will, for the purposes of Universal Credit, share the profits and losses of that business in the same way as any other partnership). This is an important distinction to retain in order to ensure transparency for tax reporting. Although the individuals may share one household award for Universal Credit, they will still have individual personal tax allowances and submit their tax returns to HMRC separately. Allowing one individual to subsidise the self-employed venture of another does not align well with the amount of tax an individual owes to HMRC.

33. The Department therefore does not consider it appropriate to allow cross-subsidy for either employed or partner's earnings.

Interface with Tax Credits

34. The Committee raised a question about how losses incurred whilst on Tax Credits would be treated when those claimants made the transition to Universal Credit.

35. Although the regulations for transition from Tax Credits to Universal Credit have not yet been drafted, the Department recognises the importance of getting transitional arrangements right to ensure that those making the transition to Universal Credit are treated fairly. As such, the Department has noted the Committee's remarks within their report and will ensure these are taken into account at the point when those regulations are drafted.

Treatment of Losses Before or After Trading

36. The Committee's report raised the question of how 'losses' would be treated that are incurred prior to the commencement or after the cessation of trading. Whether losses incurred prior to the beginning of trading are considered or not will depend on whether or not the claimant had been classed as 'self-employed' within Universal Credit at this point. Claimants who have established themselves as being 'self-employed' in Universal Credit and then go on to accrue a loss will be allowed to carry this forward, regardless of whether their business has commenced trading yet or not.

37. After a business ceases trading, claimants would only be able to carry forward losses to off-set against future self-employed earnings. For example, if they went on to form a new business within eleven assessment periods of the previous one ceasing trading, thereby becoming self-employed again.

Interaction with the Tax System

38. The Committee raised a query as to how self-employed claimants would identify income tax paid on self-employed income when the tax system does not separate this out for claimants with multiple sources of income within a tax year. The Department agrees that this is an important question. We are committed to simplifying, as far as possible, the interactions between the tax and benefit system. The Department intends to discuss this issue at the Self- Employed Stakeholder Advisory Group, and will continue to work with HMRC to agree a clear approach to helping self-employed claimants identify tax paid in relation to their self-employed earnings in practice.

39. It is worth noting that, for Universal Credit purposes, the Department is not concerned with an individual's tax liability but rather the tax they have actually paid. This amount will form part of their award calculation and therefore determine what amount of Universal Credit the claimant is awarded.

Averaging of Self-Employed Earnings

Although the Department appears disinclined to introduce any averaging of earnings in Universal Credit, we believe it bears consideration for some self-employed people whose monthly profit and loss accounts can be volatile.

Response –

40. Universal Credit is a monthly benefit and earnings are taken into account on a monthly basis to ensure that the amount claimants receive through Universal Credit accurately reflects a claimant's financial circumstances. To introduce averaging of earnings would undermine this fundamental principle of Universal Credit and therefore the Government does not accept this recommendation.

41. Furthermore, the Department does not feel that introducing averaging of earnings for this period is advisable in practical terms. The Committee has

already raised concerns about adding complexity to the Universal Credit system and the Department is clear that Universal Credit should be as simple and easy to administer as far as possible. Introducing a policy of averaging earnings would add further complexity to the system and is not an approach the Department believes is necessary or proportionate.

Other Points Raised in the Committee's Report

Relationship with Waiting Days Rule

42. The Committee's report makes reference to the relationship with the proposal to introduce "Waiting Days" within Universal Credit which the Committee has also consulted on. The Minister for Welfare Reform has written to the Committee to confirm that he is fully considering their comments and will write again in due course.

Domestic Violence

43. In addition to their key recommendations, the Committee suggested an exemption from the surplus earnings policy for victims of domestic abuse, citing concerns that such individuals may not have ready access to earnings which have been accrued during the period between Universal Credit awards.

44. The Government has considered this issue in light of the Committee's report and agrees that an exemption for victims of domestic violence is appropriate in this instance. The Department agrees that there is a risk that a claimant may not have access to the surplus earnings if they have been subject to recent domestic abuse. In addition, the Department agrees that there must be no potential financial disincentive to an individual leaving an abusive relationship. Therefore the Department **will not** apply the surplus earnings policy to victims of domestic abuse.

45. The criteria for establishing who qualifies for a domestic violence exemption will be consistent with the conditions set out in the Universal Credit Regulations 2013 under Regulation 98.

CONCLUSION

46. The Department is grateful for the Committee's constructive report and its recognition of the policy intent behind the proposed regulations.

47. In response to the recommendations made by the Committee, the Secretary of State is pleased to confirm that the Department will:
    a. increase the level of the de minimis from £100 to £300;

b. continue to run the Self-Employed Stakeholder Advisory Group, which was set up following the recommendation made by the Committee in its September 2014 report '*Social Security and the Self-Employed*';

c. introduce an exemption from the surplus earnings policy for victims of domestic abuse.

48. **These changes retain fairness between those who have the same annual salary but are paid in different ways, as well as allowing for investment in claimants' businesses.**

49. The Department will now proceed with amending and laying the regulations to come into effect within Universal Credit Digital Service from 2016.

ANNEX A

Surplus earnings and work incentives

These examples show the impact of surplus earnings on work incentives.

A household is better off increasing their earnings even where the surplus earnings regulations apply. This is because of the single taper which means that every £1 of surplus earnings[2] accounted for in the Universal Credit ("UC") calculation only reduces a household's UC award by 65p.

The exact amount a household is better off depends upon their circumstances and pattern of earnings as illustrated in the examples below.

Please note: numbers may not sum due to rounding and are based on 2014/15 rates.

Example One

George is single and currently unemployed. He rents a room in a house share for £282 per month. He is currently claiming UC and is looking for work.

His circumstances entitle him to a maximum UC award of £597 per month. He receives this amount in Assessment Period (AP) 1.

In AP 2 he starts a job on a temporary four month contract. This will pay £1,700 in net earnings per month. These earnings are high enough to take him off UC and to start accumulating surplus earnings. At the end of AP 2 he accumulates £370 of surplus earnings.

In AP 5 he receives his final pay and his temporary contract ends. Over the four months he has been in work he has accumulated £1,481 of surplus earnings.

In AP 6 George is unemployed and has £1,481 of surplus earnings. At the end of AP 6 his surplus earnings are added into the UC calculation. As the amount of surplus earnings exceeds his 'no UC threshold' of £1,030 he receives no UC in this assessment period.

In AP 7 George continues to be unemployed and has £152 of surplus earnings remaining. These are added into the UC calculation resulting in a UC award of £571.

From AP 8 he has no surplus earnings left and continues to be unemployed. He now receives his maximum UC entitlement of £597. This continues to AP 12.

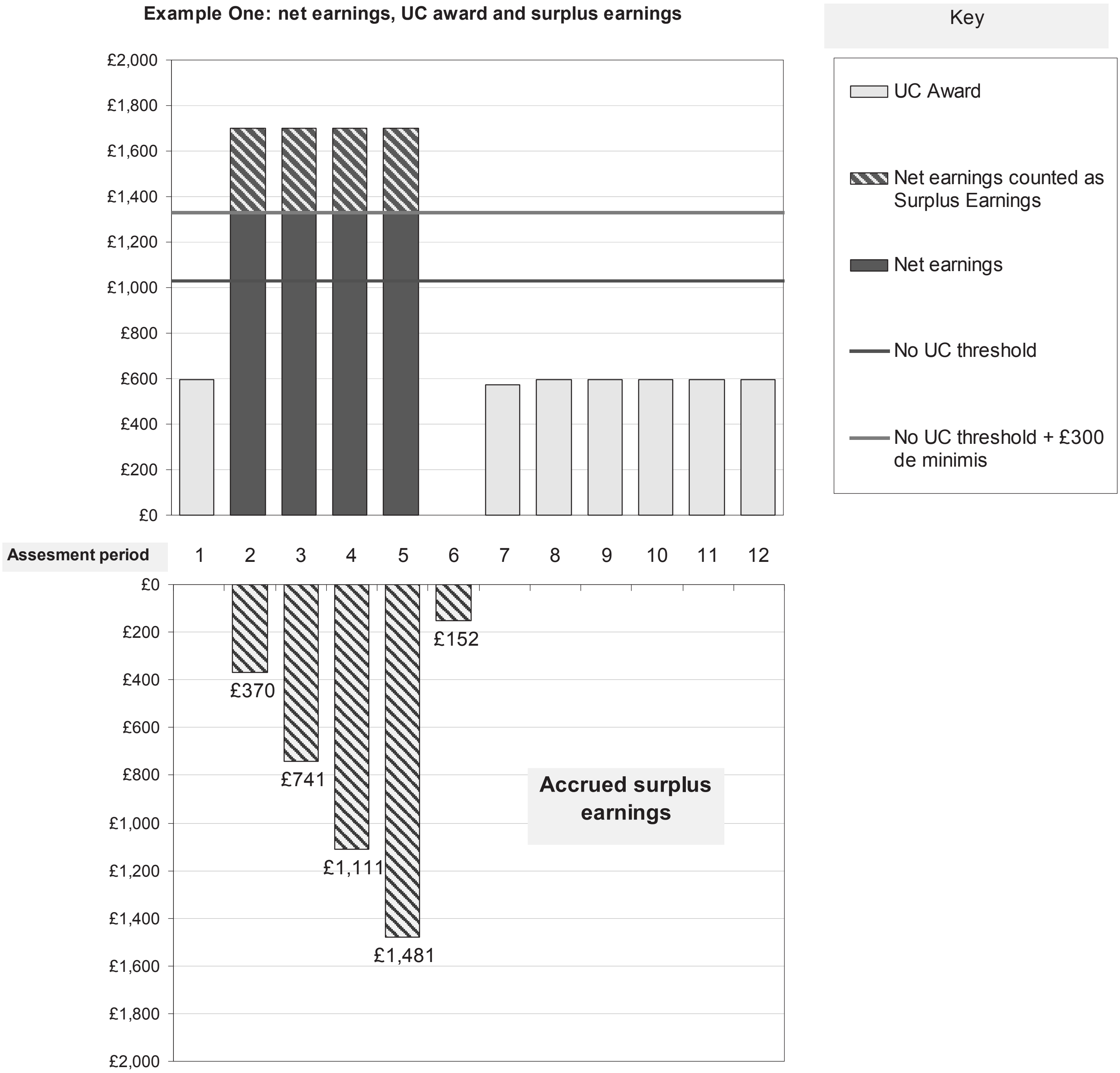
[2] i.e. every £1 above the nil UC threshold plus the £300 de minimis

Comparison of total income

Over the period George earns £6,800 from employment and receives £4,153 in UC; a total income of £10,953.

If he had not taken the temporary job then his total income from UC would have been £7,165.

By taking the temporary work George is £3,788 better off.



Example Two

Lloyd and Joan Fenwick live together in a three bedroom house with their two school aged children. They pay £521 per month in rent and both are in work.

Their circumstances entitle them to a maximum UC award of £1,519 per month.

Normally, Lloyd works 40 hours per week earning £15 per hour and Joan works 10 hours per week earning £7.50 per hour. This gives them net earnings of £2,345 per month.

From AP 1 to AP 4, the household net earnings are £2,345 per AP and they receive £139 in UC in each AP.

For AP 6 Joan is able to increase her hours to 35 per week for one month to cover a colleague's holiday. This increases the household's net earnings to £3,041 and sets their UC to zero. As their household net earnings exceed their 'no UC threshold + a £300 de minimis' of £2,859 they accumulate surplus earnings of £182.

In AP 7 Joan's hours return to 10 hours per week bringing their total household net earnings back to £2,345. The £182 of surplus earnings from the previous AP is added into the UC calculation. The total amount of earnings used in the UC calculation is £2,527 and results in the household receiving £21 of UC.

By AP 8 they have exhausted their surplus earnings and with household net earnings of £2,345 their UC award returns to £139. In AP 8 their household net earnings remain at £2,345 and they receive £139 of UC.

In AP 9, Joan is able to increase her hours to 35 hours per week. Again, they move off UC and accumulate £182 of surplus earnings.

In AP 10, their household net earnings fall to £2,345 and their surplus earnings of £182 are added into the UC calculation. They receive £21 of UC.

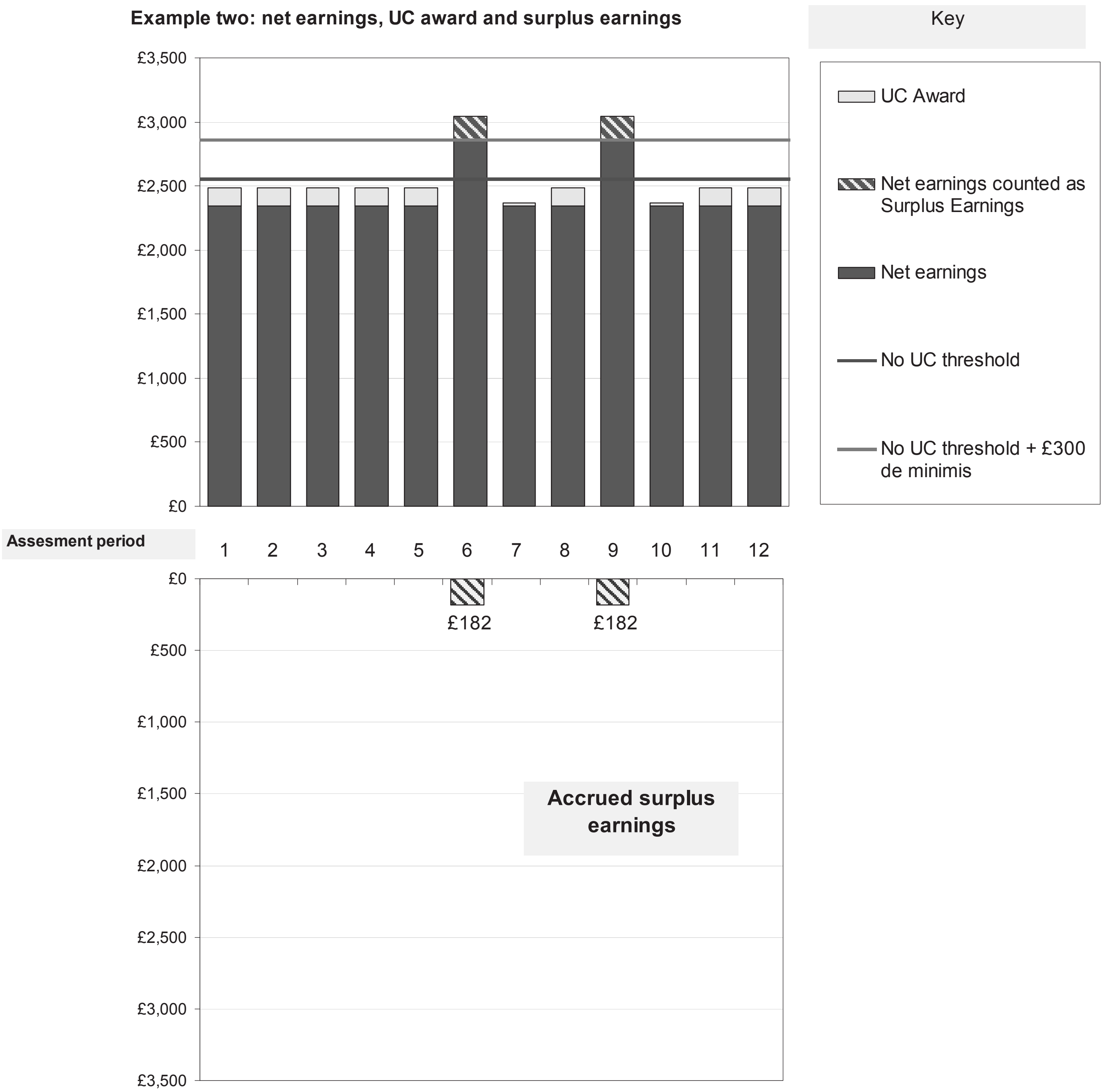
In AP 11 and AP 12 their household net earnings remain at £2,345 and they receive £139 of UC in each AP.

Comparison of total income

Over the period the Fenwick family have total earnings from employment of £29,535 and receive £1,154 in UC; a total income of £30,688.

If Joan decided not to take the extra hours their total income would have been £29,811.

By taking the extra hours the Fenwick family are £877 better off.


Example two: net earnings, UC award and surplus earnings
Key
UC Award
Net earnings counted as Surplus Earnings
Net earnings
No UC threshold
No UC threshold + £300 de minimis
£3,500
£3,000
£2,500
£2,000
£1,500
£1,000
£500
£0
Assesment period
1
2
3
4
5
6
7
8
9
10
11
12
£182
£182
Accrued surplus earnings

Example Three

Neelam is single and rents a room in a three bed house share for £369 per month. She works as a self employed electrician and is subject to the MIF.

Her MIF is set at 35 hours x National Minimum Wage (£6.50) per week. This equates to a monthly gross MIF of £989.

She has a steady flow of work throughout the year and experiences seasonal increase income during the uptick in house sales.

From AP 1 to AP 4, her income varies from month to month but she remains in receipt of UC.

In AP 5, AP 6, AP 7 and AP 8 she is able to secure new business that increases her income by £600 in each AP and this increase takes her off UC.

In these assessment periods, her income exceeds her 'no UC threshold + £300 de minimis' and she accumulates a total of £547 of surplus earnings in this period.

In AP 9 Neelam's work slows and her income falls to £500. Her accumulated surplus earnings are added to her income. This gives a total of £1,047 to be used in the UC calculation. This results in a UC award of £76.

From AP 10 to AP 12 her income increases and varies from month to month but she remains on UC.

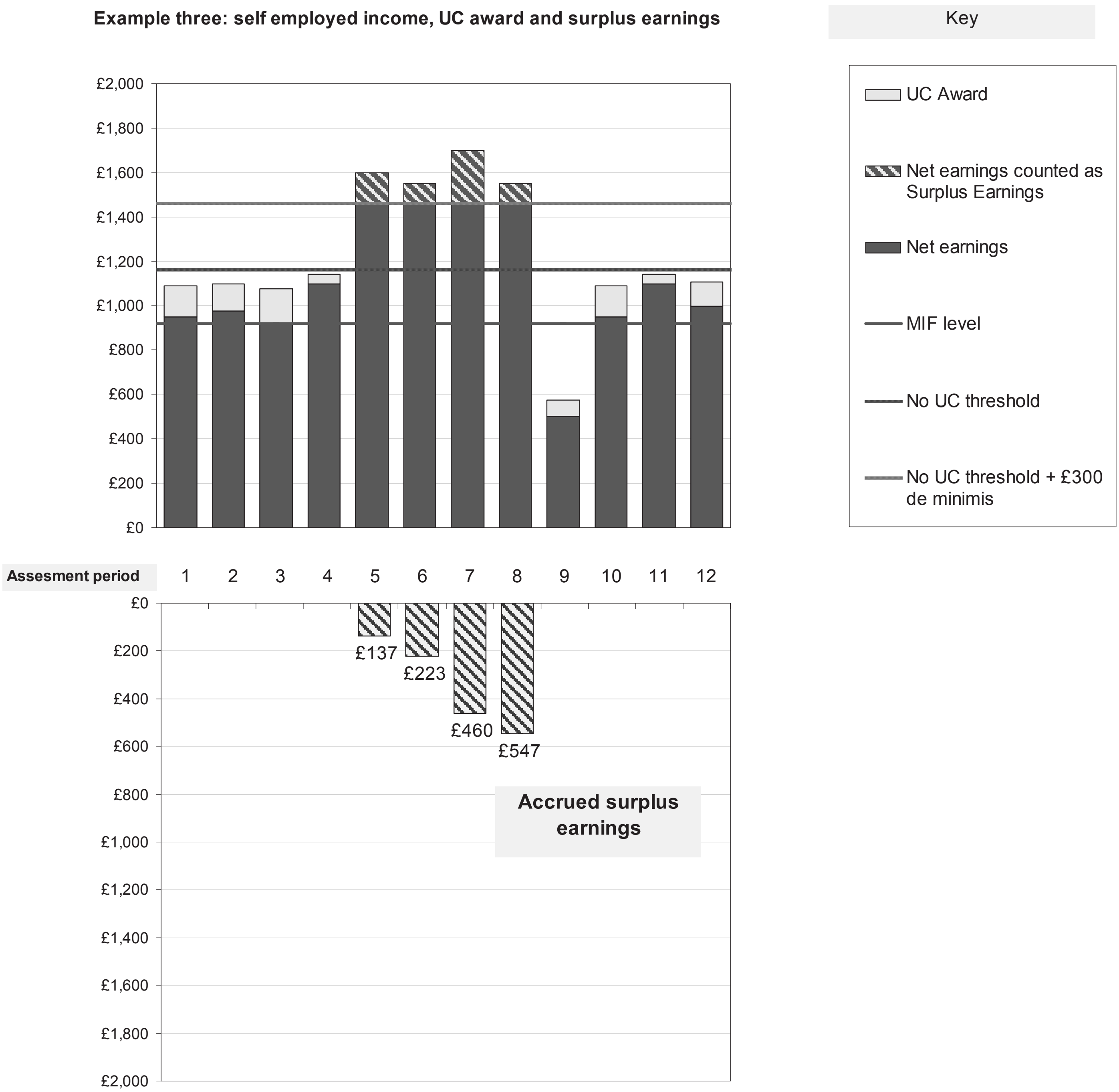
Comparison of total income

Over the period Neelam has total self employed net income of £13,895 and receives £822 in UC; a total income of £14,717.

If Neelam decided not take the extra business in AP 5 to AP 8 her total income would have been £12,825.

By taking the extra business Neelam is £1,892 better off.

Example three: self employed income, UC award and surplus earnings



Family Test – The Universal Credit (Surpluses and Self-employed Losses) (Digital Service) Amendment Regulations 2015

1. **What kind of impact might the policy have on family formation?**

   The Government does not believe that the proposed regulations will have an impact on family formation. The Department's most recent analysis shows that 80-85% of Universal Credit claimants will receive a Universal Credit award within their first assessment period back. This demonstrates that many claimants will not be impacted by the policy and that where a claimant is affected the impact on the claimant is likely to be for a brief period only. The Government therefore believes it is highly unlikely that family formation would be adversely affected by these proposals.

   In addition, several measures have been put in place to protect claimants who may have had slight variations in their levels of earnings during the period of surplus earnings, including a generous de minimis amount of £300 and for self-employed claimants, the ability to carry forward losses for up to eleven assessment periods after the loss incurred.

2. **What kind of impact will the policy have on families going through key transitions such as becoming parents, getting married, fostering or adopting, bereavement, redundancy, new caring responsibilities or the onset of a long term health condition?**

   The Government does not believe that these proposals will impact a claimant's decision making with regard to the key transitions listed. For families taking on new responsibilities, such as becoming parents, getting married, fostering or adopting or becoming a carer, there is significant support built into Universal Credit to ensure families are supported through these transitions. For example, a couple becoming parents would then be entitled to the Child Element which would increase their monthly Universal Credit award by up to £274.58 a month.

   The Limited Capability for Work element will be paid to those who have been diagnosed with a long term health condition which has been assessed by the Work Capability Assessment and found to restrict the individual's ability to work. For Carers, the Carer Element of up to £148.61per month will provide support to account for this transition.

   In some circumstances, a claimant's change of circumstances may see them impacted by these proposals when they would not have been affected had their circumstances stayed the same. For example, where a couple separate or bereavement takes place that has an impact on an individual's Universal

Credit award (such as the death of a partner in a joint claim). In these circumstances, a claimant's Universal Credit threshold may reduce to a level that would bring them into the scope of the surplus earnings policy. This is consistent with how a claimant's earnings threshold would be handled had they not experienced a break in award. The Government therefore does not consider these proposals to introduce any adverse impacts on families going through these transitions.

3. **What impacts will the policy have on all family members' ability to play a full role in family life, including with respect to parenting and other caring responsibilities?**

The Government does not expect these proposals to have any adverse impact on family members' ability to play a full role in family life. There is significant support built into Universal Credit for parents and carers and these elements are not impacted by the introduction of the proposed regulations.

4. **How does the policy impact on families before, during and after couple separation?**

Where a claim is made for Universal Credit by a new couple (that is a couple who have not previously had a joint Universal Credit award) the Department will consider whether either partner has a surplus that needs to be taken into account. If either of them had an award that ended within the past six assessment periods with a surplus, the Department will look back to the previous award and calculate the individual's surplus taking account of that person's individual earnings in the period off Universal Credit.

Where a single person claims Universal Credit and they previously had a joint award that ended in the last six assessment periods with a surplus, that surplus will be apportioned so that it reflects the claimant's own earnings in the assessment period in which the previous Universal Credit award terminated.

Where a surplus is being calculated in relation to a claimant who was previously part of a joint award and has since separated or a claimant who was previously single and has since formed a couple, the relevant threshold for use between the old and new awards may be based on the previous or the current circumstances, whichever is most favourable.

Claimants and their families will therefore not be adversely impacted by the introduction of these proposals should they separate or form a couple within the period in question.

5. **How does the policy impact those families most at risk of deterioration of relationship quality and breakdown?**

   The Government does not believe that this policy will impact families at risk of deterioration of relationship quality and breakdown. However, the Government does recognise the unique challenges faced where domestic abuse has taken place within a relationship. In relation to these particular proposals, the Government is conscious that where a claimant has been a victim of domestic abuse within a joint claim, they may not have access to surplus earnings accrued within the period in question. To mitigate this risk, the Government has introduced an exemption from the policy for victims of domestic abuse.

SOCIAL SECURITY
ADVISORY COMMITTEE

The Right Honourable Iain Duncan Smith MP
Secretary of State for Work and Pensions
Caxton House
London
SW1H 9NA

12 December 2014

Dear Secretary of State,

The Universal Credit (Surpluses and Self-Employed Losses) Regulations 2014

1. Introduction

1.1 The draft Universal Credit (Surpluses and Self-Employed Losses) Regulations 2014 were presented to the Committee at its meeting on 1 October. We decided to take the proposals on formal reference in accordance with the statutory legislation.[3] Having heard from Departmental officials about how the legislation was intended to operate, we wanted to know from the perspective of those likely to be affected by the proposals whether they felt the regulations would operate in a fair and reasonable way. We also wanted to explore whether the balance between simplicity and equity was a reasonable one. Accordingly, the Committee held a public consultation between 17 October and 7 November 2014.

1.2 Universal Credit is based on a number of key principles, one of which is monthly assessment periods. Each monthly period is assessed independently so that, to put it at its simplest, household income for the month is set against household needs for the month.[4] The net sum gives the monthly Universal Credit entitlement. However it is widely recognised – both within and outside of the Department – that such an approach can produce arbitrary and unfair results if income levels are not stable. For the majority of people in regular low-paid employment, Universal Credit works as intended. But for those whose outgoings and needs cannot be properly contained within compartmentalised monthly blocks, the current approach for Universal Credit is limited. For that reason the Department highlighted, at an early stage of policy development, the need to identify an alternative approach. *The*

---

[3] **Sections 172(1) and 174(1) of the Social Security Administration Act 1992.**
[4] **Household needs are determined by adding together the allowable components under Universal Credit: the standard allowance for the claimant and any partner, amounts in respect of responsibility for children and young persons, housing costs and any amount for other particular needs such as disability.**

Universal Credit (Surpluses and Self-Employed Losses) Regulations reflect the Government's conclusions on what that alternative approach should be.

1.3 The proposals are designed to allow for a degree of carry-over from one monthly assessment period to the next. In the event of a claimant making a further claim within six months of a previous award ending, the Department may take into account amounts earned during the intervening period. In the case of self-employed claimants, it enables a deficit in one month to be carried forward into the next monthly assessment period.

1.4 In signalling its intention to make monthly assessment periods a foundation stone of Universal Credit, the Department effectively rejected other options:[5]

- averaging of earnings over a recognisable cycle as traditionally used in most income-related DWP benefits before UC; and

- annual reconciliations, as favoured by HMRC in assessing claims for tax credits.

1.5 Although some of the respondents to our consultation recommend a return to one or other of those two approaches, we believe it is unrealistic to expect the Department to reverse its entire policy at this stage of the roll-out of Universal Credit. We deal later with whether there may be some scope for the averaging of earnings in the case of the self-employed. As it is, the option being put forward by the Government retains the principle of a monthly assessment period for all, but modifies it so that each period is not quite the closed entity it is under the existing legislation.

1.6 The Department recognises that these draft regulations complicate the present system. The Committee agrees – they are complex and many will find them difficult to understand (including staff within the Department). The Government itself acknowledges that, in this instance, simplicity is being sacrificed for equity.

1.7 During the scrutiny of these draft regulations, the Committee was of the view that the aspect of the proposals which related to the deficits of the self-employed being carried forward were sufficiently technical that a workshop involving representatives of small businesses, the self-employed and other specialists would be beneficial. We therefore convened a workshop on 6 November to discuss the likely impact of these proposals upon the self-employed. This was attended by 13 representatives of relevant organisations.[6]

---

[5] **See paragraph 1.5 of the Explanatory Memorandum https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/364573/uc-earnings-Explanatory_Memorandum.pdf**

[6] **A list of the organisations that participated in the workshop is at appendix 3.**

1.8 In addition, the Committee received 28 written responses: 24 from representatives of organisations, local authorities or groups, and four from individuals contributing in a personal capacity.[7]

1.9 The Committee is grateful to the organisations and individuals who attended the workshop and/or contributed to the consultation exercise. The contributions we received were important in clarifying our understanding about the likely effect of the proposals on those Universal Credit claimants who are either self-employed or whose earnings take them in and out of benefit. The Committee's consultations are always important in ensuring that we have the best possible insight to the potential impacts and unintended consequences that might arise from a particular set of draft proposals. The insight provided by our stakeholders was especially welcome on this occasion given the very technical and complex nature of some aspects of the draft regulations relating to the self-employed. In the Committee's report '*Social Security Provision and the Self-Employed*' (published in September 2014) we recommended that the Government should establish a working group specifically to address concerns about the policy and roll-out of Universal Credit for the self-employed.[8] Our experience of scrutinising these regulations, and the value we derived from the input of stakeholders with significant expertise in this area, has strengthened our opinion of the value of this approach.

1.10 Finally, the Committee acknowledges the very helpful and constructive support of DWP officials throughout this process. They have been refreshingly open about some of the challenges that they are grappling with, and the Committee hopes that its intervention has been helpful to them.

2. Self-Employed Losses

2.1 From the point at which the Universal Credit Regulations 2013 were passed into law, the Government has accepted that, without amendment, there was potential for the self-employed to fare less favourably when compared to someone in employment. The fact that it has taken some considerable time for alternative proposals to emerge, with some existing Universal Credit recipients already turning to self-employment and being subject to the current rules, underlines the scale of the challenge in finding a workable alternative.

2.2 For the self-employed who have erratic patterns of income and expenditure, the term "loss" is misplaced. Referring to "losses" conjures up the idea of a failing business, when in fact monthly deficits in some businesses are not only commonplace, but essential. Without them the business would not grow, for example investment in new equipment.

2.3 What that means in the context of these proposals, however, is that in such cases there will need to be adjusting calculations month after month. This will bring both legs of these proposals into play (i.e. surplus earnings rules as well

[7] **A list of the organisations and individuals who responded to the consultation exercise is at appendix 1.**
[8] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/358334/Social_security_provision_and_the_self-employed__FINAL_24_SEPT__.pdf

as self-employed losses rules). That would, almost inevitably, create additional burdens for many.

2.4 The proposals are not intended to come into force until April 2016 at the earliest. At that stage, or relatively soon afterwards, the Department intends to start the process of gradually transferring existing self-employed people in receipt of tax credits to Universal Credit. Anyone already on Universal Credit who enters self-employment will continue to be treated in accordance with the current legislation. That means that they may benefit from not having surplus earnings rules, but may be disadvantaged through having deficits in some months which cannot be carried forward. Having people in identical circumstances treated differently within Universal Credit is becoming more commonplace. For example, the administration of a benefit and the amount payable can vary depending on whether an individual enters Universal Credit under the Department's 'live' service or the 'digital' service. This marks a significant change from the way UK benefits have been administered in the past. While we recognise the advantages of a roll-out timetable which allows for a 'test and learn' approach, having such a variation exist for people in similar circumstances is undesirable.

2.5 The precise number of self-employed people that will be in receipt of Universal Credit under existing rules at the time the amendments come into force is unclear. Neither is it clear what impact the amended rules will have on the self-employed as much depends on the monthly balance sheet of each business. Nonetheless there is potential for the considerable divergence of treatment. Whether this raises a legal question will be for the courts to resolve, but it certainly raises an ethical question as to whether the Department should take reasonable steps to identify those who would lose out and compensate them in some way, perhaps through extra-statutory payments or an element of discretion, as a temporary measure until the amendments take effect.

2.6 The Committee addresses the issue of communication later in the report, but observes at this point that any difficulties faced by the Department in communicating these changes will be multiplied if two different systems are running in parallel.

2.7 These proposals therefore represent the Government's intention to secure a greater equity between the way the earnings of both the self-employed and those in employed earner's employment ("the employed") are treated in Universal Credit. Compartmentalised monthly assessment periods have the clear potential to disadvantage seriously any self-employed person who has a significant financial commitment in any month. For accounting purposes, the effect of that outlay is factored in over the course of the financial year (or years), but for current Universal Credit purposes its effect is confined to the single month in which the outlay occurs. Even a self-employed occupation that might be expected to produce fairly consistent monthly accounts throughout the year, for example a driving instructor, will experience the occasional month where outgoings are abnormally high. An obvious example would be a month in which a business vehicle is repaired or serviced in order to pass its MOT. From a business perspective, the driving instructor might need several months to recover financially. The Universal Credit provisions as they currently stand do not acknowledge that.

2.8 The proposed solution is to spread one monthly deficit over succeeding months, up to a maximum of eleven assessment periods. In principle this appears sensible, but a number of drawbacks have been identified by our respondents.

The adequacy of eleven assessment periods

2.9 The first issue is whether eleven assessment periods is sufficient to absorb deficits that may have been incurred. There are many businesses where it would be, but there are others, particularly where the business is heavily reliant upon capital investment, where losses may need to be spread over a longer period. For example, farmers face a number of external factors that are beyond their control: the vagaries of the weather, reliance upon crop yields, the devastation caused by infectious diseases and the need for occasional investment in expensive farm machinery. All of this means that monthly income and monthly expenditure can be erratic and, for some, limiting the carrying forward of deficits to eleven assessment periods is insufficient and does not address the reality of the business.

> *"… it is entirely feasible for a thriving viable established farm business to make losses as a result of uncontrollable external factors, something which many farmers who have suffered two years of losses as a result of severe flooding in the Somerset Levels can attest to."*
>
> **National Farmers' Union**

Complexity

2.10 Few who responded to our consultation on this aspect of the regulations failed to mention this. The proposed rules seem to be predicated on an assumption that the month in which a deficit occurs will be an isolated irregularity and that adjustment in the succeeding months will bring the accounts back on to an even keel. Whilst that may be true with some businesses, the very nature of the self-employment in other cases means that there is nothing predictable about the pattern of income or expenditure apart from excessive variability month on month.

> *Our initial concern is that the regulations, as currently drafted, are going to add layers of complexity to this benefit, which has already been criticised publicly for being over complicated. UC, when introduced, was promoted as making the benefits system easier to understand. These regulations represent a definite backwards step in achieving that aim.*

Association of Taxation Technicians

The Effect of the Minimum Income Floor

2.11 The third and most significant drawback to these proposals is the effect of the Minimum Income Floor (MIF). The MIF only applies to the self-employed who are held by the Secretary of State to be in gainful self-employment.[9] A person who wishes to set themselves up in business is granted an initial exemption period of twelve months.[10] The intention is that they are given one year in which to make it a viable enterprise. Once that period has elapsed, the MIF operates so that, if the claimant's earned income in an assessment period is less than the MIF, the claimant is treated as having earned income equal to it.[11]

2.12 The MIF itself is determined on the basis of the number of hours a person who is subject to all work-related requirements is expected to work, multiplied by the National Minimum Wage set for a person of the claimant's age and converted into a monthly figure.[12]

2.13 How the MIF operates in the context of self-employed losses is that, if there is a deficit in a monthly assessment period, the deficit will be carried over into the following month. If that is a month in which income exceeds expenditure but, for the sake of illustration, not by much, entitlement for that month will be determined by reference to the MIF. The end result is that the self-employed person can lose out significantly when compared to someone in employed earner's employment.

…the proposed solution is very unfair to those low income self-employed people whose income comes in large lump sums once or twice a year with no income in between. Such people are already likely to be disadvantaged under current regulations. Under the proposed new regulations they will be disadvantaged still further because of the way the minimum income floor interacts with this policy.

Citizens Advice

2.14 We are grateful to Citizens Advice who have provided the following charts which illustrate how the proposals, rather than ensuring a greater degree of

---

[9] **Whether a person is in 'gainful self-employment' is for the Secretary of State to determine in accordance with regulation 64 of the Universal Credit Regulations 2013. The trade, profession or vocation in question must be the claimant's main employment. The earnings derived from it must be self-employed earnings, and it must be organised, developed, regular and carried on in expectation of profit.**

[10] **A further 'start-up' period is allowed after five years have elapsed since the initial period and provided the claimant is undertaking a different trade, profession or vacation (regulation 63 of the Universal Credit Regulations 2013).**

[11] **Regulation 62 of the Universal Credit Regulations 2013.**

[12] **Regulation 90 of the Universal Credit Regulations 2013.**

parity with employed people, actually leave some self-employed people worse off than they are already. The charts show annual Universal Credit income for a self-employed claimant in gainful employment all year who meets the MIF when calculated on an annual basis. In each case the claimant's circumstances are identical except for the way in which they are paid.

2.15 Chart 1 shows Universal Credit income for a self-employed person with a regular monthly income throughout the year (for example this might be typical of a handyman or window cleaner). Their entitlement will not change with the proposals and will be consistent with an employed person on the same income. Assuming a monthly Universal Credit entitlement of £200, the total UC received in a full year for this claimant will be £2,400.

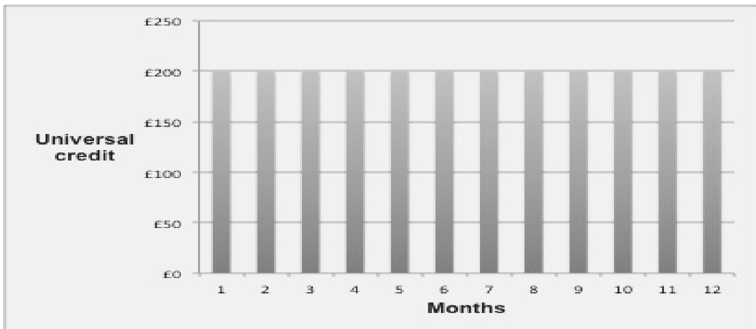


Chart 1: Annual net self-employed earnings of £12,000 a year paid in regular monthly amounts

2.16 Chart 2 shows how the current regulations would apply when a self-employed person receives the same annual income but in two lump sums. The claimant would receive no UC in the two months in which the lump sum payments were received, but would receive £200 UC for each of the remaining ten months (£200 UC is paid because the claimant is treated as receiving earnings of £908 – the MIF). Over the course of the year they will receive £2,000 in all.

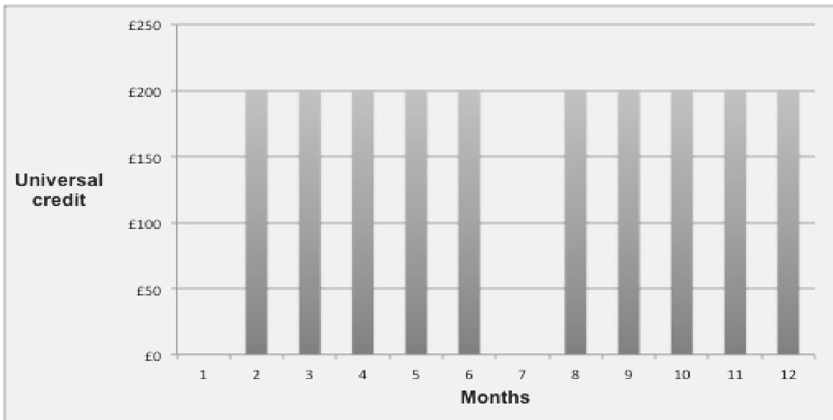


Chart 2: Current regulations: annual net self-employed earnings of £12,000 a year paid in two lump sums

2.17 Chart 3 takes the same scenario as in chart 2 but applies the proposed new rules. Here the surplus amount of earnings paid in the month of non-entitlement is carried forward into the following month, less £100. In the example the result is that the self-employed person is ruled out of UC for six months in the year. But in the remaining six months, the MIF will assume earnings of £908 so that the monthly UC payment will still be £200. Annual UC entitlement will therefore be £1,200 – exactly one half of what a claimant with the same income but spread evenly over the course of the year, would receive.

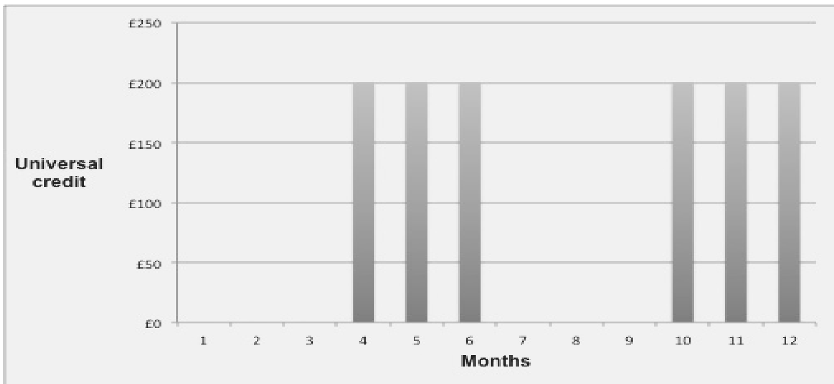


Chart 3: Proposed regulations: annual net self-employed earnings of £12,000 a year paid in two lump sums

2.18 The Committee is concerned that there is such a wide disparity of treatment between the employed and the self-employed, and we do not believe that this could have been the Department's intention. It is, therefore, possible that the sheer complexity of the rules has meant the effect of the MIF on calculations involving self-employed losses has been overlooked and led to this unintended consequence. Previous commitments made by Ministers strengthen our view that there may have been an oversight in modelling the effect of the policy. For example, the Low Incomes Tax Reform Group has drawn our attention to an exchange on 17 September 2012 when the House of Commons' Select Committee on Work and Pensions took oral evidence from the Secretary of State and the Minister for Welfare Reform.

> *"We are going to make sure that there is parity between self-employed and employed…To the extent that there is not, we will sort that out. That is a technical issue that we will sort."*[13]
>
> **Minister for Welfare Reform**

Pension Contributions

2.19 There is a further disparity between the way in which the employed and the self-employed will be treated under the proposals – and that is over pension contributions. In determining whether an assessment period shows a deficit, the self-employed cannot include pension contributions. The Department advises that it wishes to avoid people maximising their benefit and effectively getting the taxpayer to subsidise their pensions by making additional pension contributions in months that show a deficit. The difficulty with this is that it

[13] **Q.288 – http://www.publications.parliament.uk/pa/cm201213/cmselect/cmworpen/576/120917.htm**

penalises the regular pension contributor who pays the same amount each month. We understand that those self-employed earners who have precarious cash flow positions are likely to wait until the accounting year has ended before deciding whether or not to invest in a pension. This group would be penalised for being prudent. The respondents to this consultation have noted that the policy has been driven primarily by the aim of preventing abuse. Whilst it is a legitimate aim of Government policy to shut down areas where individuals are tempted to arrange their circumstances artificially to maximise benefit entitlement, finding a fair and equitable way to deal with fluctuating earnings and deficits in Universal Credit should be the starting point.

It seems that this policy will penalise a large number of well-intentioned people in order to punish a small minority.

Manchester City Council

It ought to be obvious where manipulation has taken place and it should be up to DWP to identify these cases, if they arise, and deal with them appropriately rather than establish a policy that effectively excludes relief on pension contributions for all self-employed claimants with losses.

Association of Taxation Technicians

Cross-subsidy

2.20 The regulations allow for what is called 'cross-subsidy'. This applies when the self-employed person has more than one trade, business or vocation. In calculating the monthly accounts for Universal Credit purposes, profits or losses are determined for each trade etc by setting actual expenses against actual receipts. Those separate figures are then computed together to give an overall profit or loss figure from which tax liabilities and national insurance contributions are deducted. If the resultant figure is negative, the individual has nil self-employed earnings for that monthly assessment period and the deficit is carried forward into the next period. If positive, pension contributions and previous unused losses are deducted. If the overall result is positive that amount constitutes the earnings from self-employment for that period. If negative, the deficit is again carried forward.

2.21 The principle of cross-subsidy under the proposals is, however, limited to trades, businesses and vocations of the individual self-employed person. It stops short of allowing cross-subsidy between earnings and self-employed earnings. Neither do the regulations allow for the cross-subsidy of the separate self-employed earnings between members of a joint claim for Universal Credit. Those who contributed to our consultation were positive on the decision to allow cross-subsidy, but queried whether it is necessary to limit it in the way proposed. If, for example, a member of a couple is determined as being in gainful self-employment, why should cross-subsidy not be allowed with the earnings of the other member, especially as Universal Credit is based upon assessing them jointly in a particular assessment period?

Interface with tax credits

2.22 It is important that the “loss” provisions under Universal Credit are considered in relation to the transition from tax credits if fairness is to be achieved. It is unclear to the Committee whether losses already established under tax credits will be forfeited, or whether there will be double counting of income.

Unresolved issues

2.23 This consultation has also highlighted that there are a number of issues regarding the self-employed and their incomes which require clarification, for example:

- How “losses” that are incurred prior to the commencement or after the cessation of trading should be treated (tax law has specific provisions to ensure equity).
- How tax paid on self-employed income (which can create a “loss”) is to be identified when the tax system does not separate it out for claimants with multiple sources of income within a tax year.

This list is not intended to be exhaustive, but gives a flavour of the issues that require further clarification.

Self-employed losses: conclusion

> *It is crucial that DWP do some further analysis and modelling to look at how surplus earnings and loss relief work together in a variety of situations to ensure there are no adverse consequences and no disparity is created between the employed and self-employed.*
>
> **Low Incomes Tax Reform Group**

2.24 When considering regulations such as these, the Committee endeavours to evaluate the impact upon claimants, not just from the narrow perspective of a particular DWP provision, but from the claimant perspective as to how any new requirement sits alongside additional demands placed upon the claimant by other government departments. For the self-employed, even the straightforward question of "what is your income" is increasingly becoming a challenge. They need to have due regard to who is asking the question. If it is HMRC’s income tax team, the answer will be one figure; if it is HMRC’s tax credits section it may be another figure; if it is the Housing Benefit team with a local authority it can be another; and the Council Tax support section of a local authority may ask for yet another. This can be compounded by different requirements of the Department of Health under the NHS Low Income

Scheme, or by the Department of Education for acquiring a grant to study.

2.25 Therefore, while the Committee supports the Government's intention to limit the extent to which the self-employed are treated differently from the employed, we are of the strong view that these proposals should not go forward without significant adjustments being made. In short we do not believe the draft legislation attains the aims the Department has set itself in finding a fair and equitable method of treating those with fluctuating earnings. This view is shared with a strong degree of unanimity amongst the specialists and professionals we consulted. Clearly more work needs to be done in order to find a solution that results in an equity of treatment, or even a greater parity of treatment. There are cross-Government initiatives to encourage and support people in setting up their business which will provide a viable livelihood for them. In our view, these proposals would seriously undermine Government policy with regard to self-employment and provide a very strong incentive for people to limit themselves to employment.

3. Surplus Earnings

3.1 Regulation 3 of the draft regulations presented to the Committee contains proposals which relate to the other side of the equation –income. Unlike the proposals on self-employed losses, the rules on surplus earnings relate to both self-employed and employed earnings. They therefore stand to affect a wider range of claimants.

Surplus earnings rule - purpose

3.2 The purpose of the surplus earnings rule is twofold. On the one hand it prevents employers from using the current design of Universal Credit to maximise support for their staff by arranging that their wages be paid at far longer intervals – for example bi-annually or quarterly. In that way they could possibly claim Universal Credit for the months in which no wages were received. To that extent it is not designed to catch the low-paid but the relatively well-off worker who can afford to budget over a much longer time span. The other purpose is to ensure that fluctuating earnings are neither unduly penalised nor unfairly rewarded.[14]

3.3 On the basis of the evidence available, a number of respondents have questioned the need for an anti-abuse measure. It should be recognised, however, that the Department is seeking to anticipate potential opportunities for manipulating the system to access or maximise payments of Universal Credit, therefore hard evidence showing the degree to which people will manipulate their earnings to take advantage of the system may not yet exist to the degree that stakeholders would want to see. The Committee supports the Government's intention in seeking to protect taxpayers' money and ensuring that benefits go to those who need them and, therefore, we accept the Government's purpose behind this measure.

---

[14] **Explanatory memorandum paragraph 1.2**
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/364573/uc-earnings-Explanatory_Memorandum.pdf

3.4 Nonetheless we do think there is merit in reflecting further on whether the proposed solution is the best or simplest option available. For example, the Low Incomes Tax Reform Group (LITRG) has recommended that the Secretary of State should be given discretion to average the earnings of an individual over a recognisable cycle in cases where it reflected the reality of the working pattern. Apart from anything else, even if the proposals came into force as they currently stand, it would still be possible for someone to manipulate their earnings for the most determined individuals who were sufficiently comfortable financially to be able to arrange the payment of their income at intervals of just over six-months.

3.5 Despite the Department's best efforts to prevent individuals maximising their Universal Credit entitlement through re-arranging the dates on which earnings are received, the new rules themselves are not devoid of anomalies. If, for example, someone leaves a highly paid job having been in receipt of Universal Credit five months earlier, an immediate claim for Universal Credit might result in a period of disallowance for several months. On the other hand, should they delay making a claim for one month (ie until the six months period dating from the end of the previous award has elapsed and RTI details are no longer available), entitlement could commence far sooner.

Relationship with waiting day rule

3.6 The Committee has recently reported to the Secretary of State for Work and Pensions on the Department's proposals to introduce seven waiting days – a period of non-entitlement – before an award of Universal Credit can begin.

3.7 The surplus earnings rules and the proposed rule on waiting days are mutually exclusive. The proposed waiting days do not have to be served if two awards link because the gap between them is less than six months; conversely, the surplus earning rules do not apply if the gap since the previous award is equal to, or exceeds, six months. This means that an individual cannot be subject to both rules operating in conjunction at the same time. In both cases, however, inroads are liable to be made into what would otherwise be the start of an individual's entitlement. In the case of new claims, waiting days may need to be served. In the case of repeat claims within six months, the surplus earnings rule may apply.

3.8 We are concerned by this prospect. Many of our respondents have drawn attention to the financial hardship and uncertainty which will be faced by a fair proportion of those affected by the surplus earnings rule. The same considerations apply here too. The only difference between the two sets of rules would appear to be over certainty. A new claimant for Universal Credit can be assured that they will need to serve seven waiting days. A repeat Universal Credit claimant may or may not be affected by the surplus earnings rule; and, if affected, will be disallowed benefit for a shorter or longer period, depending upon individual circumstances.

The de-minimis rule

3.9 In its emphasis upon preventing abuse the Department is clearly focusing upon what might colloquially be called "a few big fish". However, in incorporating a de minimis rule of £100 a month, the Department is effectively trawling with small mesh nets. Whilst it will catch most of the big fish as intended, it will inevitably sweep up a lot of small fry as well.

3.10 The Department states in paragraph 3.13 of the Explanatory Memorandum that it feels that the design of the de minimis rule is "*generous and fair*." We disagree. As the TUC has noted, £100 a month equates to around £23 a week. It is worth pausing to reflect on what that might mean in practical terms for someone taking up work. A claimant may need to buy clothes for work, have additional travel and childcare costs, and lose access to passported benefits such as free prescriptions (£8.05 for a single prescription) or free school meals. If an individual has two school age children whose daily school meals cost £2.50 each, the de minimis amount has been exceeded through that one additional expense alone.

> *A basic travel pass in Warrington (Day Rover) is £5.50 per day, (5 days over 4 weeks is £110.00) this will not even cover travel costs.*
>
> **Golden Gates Housing Trust**

> *…a parent may be offered a short term contract which means they have higher costs in childcare during their employment; or someone may have high travel to work costs if they are prepared to travel for 90 minutes as is outlined in the Claimant Commitment. The contract may be of huge benefit to their future employment prospects, but they are unlikely to be able to save their surplus earnings.*
>
> **Manchester City Council**

3.11 The Committee believes that there are likely to be a significant number of relatively low-paid workers, whose employment is of a temporary or insecure nature, who will be caught by this rule. Whilst we accept that their period of disentitlement to Universal Credit is unlikely to be extensive, we are concerned that the start date of their entitlement will be pushed back by this measure. We recognise the need to consider the interests of taxpayers, but do not believe that this is an appropriate area for cutting costs. In the Committee's recent report regarding waiting days in Universal Credit, we recommend that the Government should consider whether or not there are other aspects within the range of the Department's Annually Managed Expenditure which could yield similar or greater savings and with a less significant impact. We re-emphasise that recommendation here.

3.12 The analysis the Committee received from DWP indicates that the amount of earnings a claimant would need to have in order to delay entitlement for the full 6 months is considerable. For example, a family with two children and housing costs of £500 per month would need to have built up surplus earnings of around £15,000 (over and above their nil threshold plus de-minimis of around £1,600 per month). DWP modelling suggests that no-one will fall into this category. Nonetheless the figures show that just over half of those affected will be ruled out of UC for the first month following their repeat claim.

Month	Proportion of the 100,000 to 200,000 claimants estimated to be affected by the surplus earnings rule	
	Receive no UC	Receive some UC (in full or in part)
Month 1	55%	45%
Month 2	25%	75%
Month 3	15%	85%
Month 4	10%	90%
Month 5	0%	100%

3.13 A number of people moving off Universal Credit to take up work will take the opportunity to use some of their income to pay off debts – some of which may have accrued as a result of the waiting day rule.

Good advice from any financial adviser or debt counsellor to someone in his position would be to pay down debts (which carry high rates of interest) with any surplus income, not to save it.

Professor Elaine Kempson

3.14 In such cases the effect of the surplus earnings rule could be to return them back into indebtedness once again. It would be demoralising for someone in this position to be told that they were obliged to fund the period before entitlement could begin from their own resources.

…claimants will have been on Universal Credit prior to having taken up employment, during which time they may have very likely accrued debts including rent arrears – especially given the proposal of a seven day wait before being able to claim benefit… It will be all the harder for them therefore to break a cycle of indebtedness.

Scottish Federation of Housing Associations

3.15 Some of the criticisms of the surplus earnings rule would dissipate entirely if the Department increased the de-minimis limit. Returning to the illustration, the mesh size needs to be a lot larger. That would still catch the big fish whilst allowing the little ones to swim through. There is, of course, a judgment to be made about whether the increased complexity renders the overall policy worthwhile.

A substantially higher disregard – say £500 a month – would still not be over-generous. Beneficiaries would still be very low-paid. But it would mean that people who had taken the risk of an apparently insecure job would be less likely to be penalised for precisely the behaviour we want to encourage.

TUC

Coming off Universal Credit – the first six months

3.16 The surplus earnings rules effectively mean that individuals coming off Universal Credit to take up employment or better paid employment will, for the first six months, be expected to continue to live their lives as if they were in receipt of the same income as provided previously through Universal Credit. We agree that it is sensible and prudent to prepare for a rainy day, but very few of us in that situation would be able to resist using the opportunity of having work – or better paid work – to improve the living conditions of our family. Unless people can see some tangible benefits from their employment they are liable to be demotivated into thinking that the effort was not worthwhile. This would be counter-productive to the aims of Universal Credit and the claimant behaviours that we would want to encourage.

The expectation for claimants on a low income to be able to manage their financial affairs to project future possible reductions in income is not realistic.

Tameside MBC

Uncertainty – a malign influence?

3.17 Universal Credit was designed to be both simple and transparent. The complexity of these proposals is a recurring theme throughout this report, but they are also likely to engender a great deal of uncertainty. Nobody knows how the next six months of their lives may unfold. Many take out insurance policies to cover the major contingencies of life, and then live their lives without having to worry unduly about what the future may hold. This policy denies that comfort to people coming off Universal Credit.

"…the regulation will require people to actively monitor their earnings against their entitlement, and manage their finances so that they are in a position to support themselves in the event that they become unemployed following a period where their earnings outstrip their allowances. This is a potentially complex task for people, who are already faced with the challenges or adjusting to a new job following a period of unemployment."

London Borough of Camden

3.18 Not only is it building in uncertainty during the first six months, but there is further uncertainty over how long any individual would be required to live without Universal Credit if they made a repeat claim within six months. It is hard to imagine circumstances in which an individual would be able to predict with any certainty the precise period of disallowance created by their surplus earnings. This would be especially true of working couples or those with multiple employments. What does a work coach or benefit adviser tell someone coming off Universal Credit to take up employment who asks how long they would need to wait if the job ended within six months? Or, if they were taking up a temporary job and asked about re-claiming Universal Credit when it ended? Nothing specific can be said with confidence and certainly no period of disallowance could be predicted. The claimant would simply need to be told that the surplus earnings rule could well apply and that they ought to prepare for that eventuality, but that is all. Of course few of us can plan for the future with complete certainty, but the Committee is of the view that claimants need to have a clearer understanding of the position when they are being encouraged to take up work and move off benefit.

> *As a household's income increases it gives an opportunity to replace such items that may be broken, worn out or outgrown. This policy removes that opportunity as families will be anxious about what will happen if their income then decreases again.*
>
> **NAWRA**

Work Disincentive

3.19 It follows from this that there will be some people who will find the uncertainty surrounding having to re-claim Universal Credit enough to put them off taking up employment, particularly if it is insecure or temporary. Others will reason that if their surplus earnings are going to be taken into account in the event of a re-claim, what is the point of having them?

> *People will not feel that their contribution is valued – it could involve dangerous or difficult work – if it is immediately eroded by the impact of this proposed regulation.*
>
> **Wheatley Group**

3.20 This is particularly the case for seasonal workers. As such it could impact those areas of the country that are heavily reliant upon the summer tourist trade or rural areas where agricultural work is seasonal. Some claimants may consider that the Department will put them in the invidious position of being threatened with a sanction if they refuse to take a seasonal job on offer, but believing that taking the job will not allow them to do anything other than live as though they were still on benefit. It will, for some, bring into question whether work always pays under Universal Credit.

…the surplus earnings rule might make [seasonal] work unviable as what they might earn, for example, by working in a hotel for 2 weeks over Christmas and the New Year would not increase their overall family income. It would therefore not incentivise them to work. This could potentially increase the reasons to avoid registering economic activity and drive more activities into the informal economy.

Community Housing Cymru Group

This is a significant disincentive to work in areas of rural poverty where summer holiday jobs are the only employment opportunities for many people in places such as Cornwall or Pembrokeshire.

Mid-Wales Housing Association

Complexity

3.21 The rules on surplus earnings are complicated. Even the experts we consulted admitted that they struggled to grasp the intricacies of the rules. The starting point is what is called the ‘nil Universal Credit threshold’. This is monetary figure which, if exceeded, means that benefit entitlement for the claimant in question is lost. The nil threshold will vary from individual to individual and is based upon their circumstances at any given point in time. It follows therefore that a person could have a different nil threshold point at different times. The £100 de minimis amount is added to that amount and the result is termed the ‘relevant threshold’. This is applied to a monthly assessment period, or what would be a monthly assessment period if Universal Credit entitlement had continued.

3.22 When a person makes a repeat claim for UC within six months of their previous award ending, their earnings in each monthly assessment period is set against the relevant threshold which applied when their previous award ended. The surplus in each month is added together to produce an overall figure which is then set against the amount of UC to which they would be entitled under the new claim, were it not for the surplus earnings rule. If surplus earnings are substantial, it may take several months before they are completely eroded and entitlement can be established.

3.23 Any complexity is further compounded in relation to couples splitting and forming. In any new Universal Credit claim from a couple the question of whether either partner has had a previous award of Universal Credit and whether there are any surplus earnings to be taken into account will be raised. If so, the earnings need to be apportioned. In the same way, if a Universal Credit claim is made by a single claimant who was once a member of a joint household, the issue of surplus earnings again needs to be considered. The rules provide that the relevant threshold of the claimant when a joint claimant will be compared with the relevant threshold of the claimant as an individual, and the threshold most favourable to them will be adopted by the Department. Suffice to say, the rules are highly convoluted and it is likely to be difficult for couples splitting or forming to work out precisely what will happen.

3.24 The draft legislation assumes that earnings will be apportioned evenly. No allowance is made, for example, in the case of someone who suffers domestic abuse and has to leave. As the rules stand the surplus earnings rule would apply, regardless of whether or not they were in actual possession of any of those earnings.

> *With regards to couples dissolving, the proposed apportioning of surplus earnings from a previous joint award is based on problematic assumptions and has the potential to unduly penalise individuals for financial decisions that they did not freely and actively consent to. At the very minimum, we would like to see an exemption for recent victims of domestic violence, where the violent partner was the joint claimant on the award that generated surplus earnings.*
>
> **The Salvation Army**

3.25 The legislation covers the situation where a couple splits or forms. Two simple scenarios are therefore presented. In practice however situations can be far more fluid and unstable. A couple can form and then split again shortly afterwards. An individual can have one partner and, after a brief spell of living alone, have a further partner. How the surplus earnings rule would work in these kinds of situations is almost impossible to ascertain. Although we accept that simplicity cannot always be achieved within the benefits system, it is our view that these rules go too far in the other direction.

> *In the history of income-related benefits, there has always been a trade-off between fairness and complexity. Fairness is about catering for as many individual circumstances as possible through introducing more and more rules. Simplicity implies fewer rules and allowing some apparent unfairness to exist in the interest of a system which is easier to administer and less prone to error. This proposed rule abandons simplicity in pursuit of a perceived fairness of treatment, without properly acknowledging the trade-offs...*
>
> *One of the aims of Universal Credit is to make work pay and support progression in work. It may be counterproductive to penalise people for earning above the 'relevant threshold'...*
>
> *Simplicity comes at a cost. Introducing regulations that allow the DWP to take past earnings into account would deliver savings to the DWP, but so would many other measures that compromise the principle of a benefit system that is both simple to understand and*

administer.

Policy in Practice and Welfare Reform Club

3.26 We can also see further complications arising in connection with claimants who are disentitled to benefit on the grounds of the surplus earnings rule. That in itself is likely to generate mandatory reconsiderations and appeals. Will claimants in this situation be told to go away and make a repeat claim at the point at which surplus earnings will have expired? If so there will be more administrative costs. It is possible that the Secretary of State will treat the claim as made from an advance date and award Universal credit prospectively, but there could be changes of circumstances which would lead the Secretary of State to revise his decision as to when the surplus earnings were exhausted. The question as to the readiness of the Secretary of State to backdate a claim made when a claimant had miscalculated the date on which surplus earnings expired also needs answering. In all these are unresolved issues which will only complicate the processing of administering claims where these rules apply.

3.27 When considering complexity, it is important to take into account how this set of regulations sits with those that have been introduced in recent months and others that may be in the pipeline. It is not possible to assess absolute complexity of these provisions without taking all interactions into account. For example, childcare cost spreading rules were introduced through the Early Childhood Care and Education Scheme in September 2012 which requires a claimant to understand and assess how they interact with surplus earnings. Similarly the Department has very recently introduced provisions which will treat certain tax refunds as employed earnings for Universal Credit purposes and take into account certain asset "sales" as income. All of these provisions require a deep understanding of the rules and require extensive records to be kept; they all may interact with the surplus earnings or the self-employed loss rules.

3.28 The way that passported benefits interact with either of these proposed provisions is unclear.

The Family Test

3.29 We note that the Prime Minister has recently initiated a 'Family Test' which should be applied during the formation of all new Government policies with effect from the end of October 2014. There are two issues within these proposals which stand out as possibly vulnerable to a rigorous application of the Family Test. The first is the general matter of denying benefit at the start of an award and the impact that that may have upon the families and children of those affected. The other is the more specialised issue of couples who split or form and who may find that the dynamics of the household finances do not match the assumptions underpinning the legislation. In both cases the rules are difficult and generate uncertainty.

3.30 As the Family Test has only been introduced very recently, the Committee has not specifically scrutinised the regulations from this perspective but, as the lead Department responsible for the Family Test, we would encourage DWP to do so.

Changes of circumstance

3.31 One of the difficulties with the relevant threshold is, as previously stated, that it is only applicable for one particular monthly assessment period. A person in receipt of Universal Credit for six months has the potential for having up to six different nil thresholds. It follows that a person coming off Universal Credit could have different relevant thresholds in successive months. And yet the starting point for the policy on surplus earnings is that it is the relevant threshold which applied when the award ended which matters. This could be to the claimant's advantage or disadvantage, depending upon whether any relevant changes occurred in their circumstances and what they were.

3.32 The reason for taking the relevant threshold at a point in time and assuming that it continues unchanged is for administrative ease. For understandable reasons the Department wants to avoid the complicated task of assessing what Universal Credit amount would have been applicable in each case had the claimant remained in receipt of it. This however has a potential for claimants to lose out if circumstances change during the course of the intervening period. Many of our respondents have noted this point.

> *We would be particularly concerned where peoples' circumstances changed as a result of bereavement or change to caring responsibilities (a child or elderly relative falls ill and needs care), and they were left with no money. We think that should be addressed as part of decision makers' discretion, taking into account any mitigating factors in the claimant's situation and recognising any particular challenges they face at that time.*
>
> **London Borough of Camden**

Secretary of State's discretion

3.33 On the point about having regard to changes of circumstances in the period between the end of an award of Universal Credit and the start of another, and for the purposes of determining surplus earnings, the draft legislation effectively leaves the door ajar. Although the Secretary of State begins with the relevant threshold as it stands when the previous awards ends, the legislation gives him the discretion to take into account changes of circumstances. The precise wording of the provision is –

> *"…and, in determining those amounts in relation to the period between the termination of the old award and the commencement of the new award, the Secretary of State may make such assumptions as to the claimants circumstances as the Secretary of State considers appropriate;"*

3.34 Whilst there have always been areas where scope has been given to the Secretary of State to exercise discretion (for example, determining good cause for failing to make a claim within the prescribed time or, in deciding whether or not a claimant is in hardship), in our experience the approach proposed is unprecedented in social security legislation.

3.35 The approach raises a number of questions. Clearly the onus is being placed upon the claimant to raise a query if it is felt that the Secretary of State's assumptions about circumstances being unchanged throughout the intervening period is misplaced. Will claimants be asked as to whether their circumstances have remained constant, or will it be left to them to speak up if they are unhappy? Also, what will count as "circumstances" in this situation? A self-employed man in a traffic accident who may only be insured "third party" may be obliged to purchase a replacement vehicle. This is a significant expense for him, but it would not be seen as a "change of circumstances" in the traditional sense that that concept is used in DWP legislation. Will the Secretary of State be able to have regard to it? Similarly can the Secretary of State have regard to money which was used to clear outstanding debts?

This seems entirely one-sided to us. It is DWP that are introducing regulations to look at claimants' circumstances and income whilst they are outside of UC because they believe it is necessary to counter potential abuse. If they wish to introduce such a policy then they should be prepared to use their own resources to get this right rather than opt out of the parts that will be difficult for them.

Association of Taxation Technicians

3.36 The Committee understands the Department's reluctance to undertake a detailed trawl through past circumstances every time an erstwhile claimant seeks to return to Universal Credit. Nonetheless it is difficult to see how the approach set out in the legislation will avoid it. The Secretary of State is under a legal obligation to act reasonably in accordance with the general principles of public law. Any claimant whose circumstances had changed in a way that the claimant considered would reduce or extinguish the surplus earnings figure decided by the Secretary of State may well be advised to challenge the decision.

3.37 If we are right in our assessment on this point then the Department may be shouldered with a far greater degree of burdensome evidence- gathering than it may have allowed for in establishing the DEL costs for these proposals. From the point of view of the claimant, the spectre of a long wait for the surplus earnings period to elapse might be overtaken by an even longer wait as the process of determining a claim on bits of accumulated evidence from the intervening period is stretched out by inherent difficulties.

If DWP have made a decision to introduce a complex policy to take *into account surplus earnings, they should not be able to choose only to take into account factors that are easy for them to determine when this may be to the detriment of the claimant…*

The regulations themselves seem to be worded in such a way as not to specify what circumstances should be used when calculating the nil UC threshold in the intervening months. The only fair way to do this is to ensure the regulations are clear that both income and circumstances in the intervening period will be taken into account. Whilst this may be an administrative burden for DWP, it is inequitable for one to be considered but not the other.

Low Incomes Tax Reform Group

3.38 Additionally it puts an onus upon claimants to do their own record-keeping in the intervening period. Self-employed people who may appreciate being freed from some of the time-consuming chores required in monthly assessments, may then face the unwelcome news that they will need to carry on maintaining such records. For their own good they may well be advised to go further and keep records of other changes in their circumstances by way of evidence, should it be needed.

[In the context of keeping records by the self-employed after coming off UC] – "Such entrepreneurs are notoriously optimistic and would not anticipate their results sliding back again within the next few months. If they did, they would understandably contemplate just giving up. Insisting on them keeping records after their claim has stopped, sends a very negative message."

Institute of Chartered Accountants in England and Wales

Communications

3.39 If these proposals proceed, the Department has the unenviable task of communicating these new rules to the target audience - which will include work coaches and other DWP staff - in a way that is simple to understand. The message about surplus earnings needs to be conveyed to every claimant who, for whatever reason, leaves Universal Credit. That task will be made all the more difficult by the fact that people coming off benefit will largely assume that any communications from the Department cease to have any relevance to them.

There is a need for clear communication from the DWP to claimants and potential claimants. Clear guidance needs to be produced so both claimants and advisers know what exactly constitutes surplus earnings and what information/evidence would be needed to make and then challenge a decision.

3.40 Employers too will need to understand how these rules work. Universal Credit is intended to make it easier for employers to find people to work to the patterns that suit their business. To be effective, employers need to appreciate how their own employment and recruitment practises can affect or be affected by Universal Credit. A communications strategy should include careful consideration of messages for employers.

4. Recommendations

4.1 The purpose of this report is not to question the Government's intentions in introducing these measures; we acknowledge and welcome the attempt to address what has emerged as a major problem, particularly for the self-employed. Neither do we under-estimate the difficulties in introducing an equitable and workable solution for those with widely fluctuating earnings in the context of Universal Credit's monthly assessment periods. We have therefore restricted our report to whether the proposals meet the goals the Department has set for itself. The Committee's conclusion is that they do not and we have highlighted some issues on which the Department may want to reflect further.

Surplus earnings

4.2 Having considered the proposals relating to surplus earnings, the Committee **recommends that the de minimis figure be set at a higher figure in order not to penalise those who ought to be the principal beneficiaries under Universal Credit – those who take additional work or additional hours in order to move off benefit and be self-sufficient**. For them we agree with the Secretary of State that work should always pay.

4.3 A major motivation for the introduction of the surplus earnings rules is to prevent exploitation that might arise through collusion between an employer and an employee. These rules only address one aspect of the potential for such collusion and, as the regulations come under closer scrutiny, other opportunities to manipulate incomes will become evident. **Rather than having to consider introducing further layers of complexity to counter such arrangements in future, the Committee wonders whether it might be more appropriate to adopt a more strategic approach where all such countering measures are addressed in a general anti-abuse provision.**

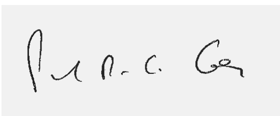
Self-employed losses

4.4 **On self-employed losses we recommend that the Government should re-visit the policy and come up with a solution which achieves greater parity of treatment between the employed and the self-employed. The difficulties caused by the operation of the MIF stands out as needing to be addressed.**

4.5 **Although the Department appears disinclined to introduce any averaging of earnings in Universal Credit, we believe it bears consideration for some self-employed people whose monthly profit and loss accounts can be volatile.** As was pointed out by LITRG, there is already a precedent for the averaging of earnings in Universal Credit for the purposes of determining conditionality. Providing for averaging for a discrete group of claimants would not be without some other difficulties, particularly for those with both employed and self-employed earnings, but we do not see those as insurmountable obstacles. Importantly though, it would not be breaking new ground entirely.

4.6 In closing, we should emphasise that the proposals are very complex and **there can be no question that there will be additional potential unintended consequences or other challenges introduced by these proposals that we have not identified. With that in mind, we strongly recommend that the Government accepts an earlier recommendation made by the Committee in its report *Social Security and the Self-Employed* that '*DWP establish a working group to address a number of concerns on the policy and application of Universal Credit for the self employed*'.**

4.7 These proposals are scheduled for introduction in 2016, the Government therefore has some limited opportunity to look again at this issue. As we have highlighted before, we believe there would be considerable merit in seeking input from technical experts from outside of the Department. Such input would be invaluable in considering the inconsistencies and complexities our scrutiny has highlighted – and to identify others. They may also be able to help devise a workable and pragmatic solution which achieves the right balance between complexity and fairness – for the claimant, for the Department's staff and for the taxpayer.



Paul Gray
Chair

APPENDIX 1

List of organisations and individuals who responded to the consultation exercise

Association of Taxation Technicians
Camden, London Borough of
Citizens Advice
Colchester Borough Council
Community Housing Cymru Group
Derby City Council
Enable Scotland
Golden Gates Housing Trust
Henderson, Keith
Kempson, Professor Elaine
Institute of Chartered Accountants in England and Wales
Low Incomes Tax Reform Group
Manchester City Council
Milton Keynes Council
National Housing Federation
NAWRA
National Farmers' Union
Papworth Trust
Peabody
Policy in Practice and Welfare Reform Club
Salvation Army
Scottish Federation of Housing Associations
Tameside MBC
TUC
Walker, Professor Janet
Wheatley Group
Wigan and Leigh Homes

APPENDIX 2

Members of the Social Security Advisory Committee

Paul Gray (Chair)
John Andrews
Adele Baumgardt
John Ditch
Keith Faulkner
Colin Godbold
Chris Goulden
Jim McCormick
Gráinne McKeever
Matthew Oakley
Seyi Obakin
Judith Paterson
Nicola Smith
Diana Whitworth

APPENDIX 3

Participants in the workshop on The Universal Credit (Surpluses and Self-employed Losses) Regulations 2014

6 November 2014

Phil Agulnik	Entitledto
Frances Corrie	TaxAid
David Finch	Resolution Foundation
Anita Monteith	ICAEW
Jane Moore	Institute of Chartered Accountants in England and Wales
Gareth Morgan	Ferret
David Nash	Federation of Small Businesses
Michael Parker	National Farmers' Union
Sue Royston	Citizens Advice
David Samson	Turn2us
Alison Ward	Association of Tax Technicians
Robin Williamson	Low Incomes Tax Reform Group
Derek Fisher	Prince's Trust
James Wolfe	DWP
Michelle Odgers	DWP
Colin Godbold	SSAC member
Adele Baumgardt	SSAC member
John Andrews	SSAC member
Paul Mackrell	SSAC Secretariat

APPENDIX 4

Department for Work & Pensions

Universal Credit
Policy Division
3rd Floor
Caxton House
6-12 Tothill Street
London. SW1H
9NA.

Phone: 020 7449 5267
Michelle Odgers

Denise Whitehead
Secretary, Social Security Advisory Committee
Caxton House
Tothill Street
London
SW1H 9NA

10th October 2014

Dear Denise

THE UNIVERSAL CREDIT (SURPLUSES AND SELF-EMPLOYED LOSSES) REGULATIONS 2014

The Department for Work and Pensions ("the Department") proposes to make amendments to the Universal Credit Regulations 2013[15] ('the 2013 Regulations') via The Universal Credit (Surpluses and Self-employed Losses) Regulations 2014 ('the 2014 Regulations') to support the continuing implementation of Universal Credit (UC).

The proposed 2014 Regulations affect UC claimants who have had an award of UC that ends and who then re-claim UC within six assessment periods of their previous UC award ceasing. If a person reclaims more than 6 assessment periods after the last day of their previous UC award terminating, surpluses are ignored.

The effects of the regulations are summarised as follows:

- **Regulation 2** inserts regulation 57A into the 2013 Regulations to allow previous losses from self-employment to be considered when assessing self-employed earnings in future assessment periods. In order to support this we will also allow self-employed workers to off-set losses between multiple self-employed

[15] http://www.legislation.gov.uk/uksi/2013/376/contents/made

businesses (although claimants will still need to report on a business by business basis). Any losses will only be available to be used once and will be considered for a maximum of 11 assessment periods following the one in which the loss arose.

- **Regulation 3** inserts regulation 64A into the 2013 Regulation so that surplus earnings can be calculated and applied to UC awards for a maximum of six assessment periods where:

  - paid workers (employed and self-employed) have lost entitlement to UC for up to six assessment periods; and
  - they have subsequently regained entitlement to UC within six assessment periods of the last day of their previous entitlement (either as an individual or as part of a joint claim).

Regulation 64A also deals with the calculation of surplus earnings where paid workers regain entitlement to UC but:

- have formed a couple; or
- have separated from their partner.

Along with the draft Regulations, I enclose an Explanatory Memorandum which gives more detail of the proposed amendments and provides background to the regulations. I have also enclosed a Keeling version showing the proposed amendments in place.

Officials attended the Committee's 1st October meeting and following this discussion we understand it would be helpful to clarify the following points.

(1) Where a claimant continues to receive the same amount of earnings but their circumstances change and their UC award decreases, then the level of earnings that reduce their award to nil will also change at the same time. A simple example would be a couple where one person works. If the couple separate and the working person claims UC their new award will be at a single person rate and their earnings will reduce that award.

If their earnings are such that as a single person they are not entitled to UC, then a surplus might be considered but only if they return to UC within six assessment periods of their award becoming nil. This might be because their earnings have reduced or their circumstances have undergone further change.

(2) The Committee also expressed an interest in the interaction between surplus earnings policy and redundancy payments. If a claimant loses their job but has not had an award of UC within the previous six assessment periods (either as a single person or a member of a couple) then no surplus will apply to them. Statutory redundancy payments are treated as capital rather than earnings for UC purposes and the UC capital rules will apply. Other final earnings payments such as pay in lieu of notice and accrued holiday pay are taken into account as earnings for UC purposes.

I hope this letter and enclosures will be helpful to the Committee. I would be happy to provide any further information the Committee may require.

Yours sincerely

By email

Michelle Odgers

Universal Credit Division **Strategy Policy and Analysis Group**	**EXPLANATORY MEMORANDUM FOR THE SOCIAL SECURITY ADVISORY COMMITTEE**
	THE UNIVERSAL CREDIT (SURPLUSES AND SELF-EMPLOYED LOSSES) REGULATIONS 2014
For the meeting of the Social Security Advisory Committee on 1st October 2014	DWP Department for Work and Pensions

Contents

1. Introduction

1.1 The Department for Work and Pensions ("the Department") proposes to make amendments to the Universal Credit Regulations 2013[16] ('the 2013 Regulations') via The Universal Credit (Surpluses and Self-employed Losses) Regulations 2014 ('the 2014 Regulations') to support the continuing implementation of Universal Credit (UC).

1.2 Currently, where earnings are received by a UC claimant that reduce their UC award to nil in an assessment period, these earnings are applied only to the UC award within that assessment period. This means entitlement to UC will cease for that one assessment period. Continuing to apply this 'one assessment period approach' results in the following risks:

- employers and paid workers will realise that certain payment patterns maximise UC entitlement and there is potential for manipulation to take advantage of this; and
- paid workers with fluctuating earnings patterns are either unduly penalised or unfairly rewarded by receiving less/ more UC than they would if they earned the same amount but were paid monthly.

1.3 See **annex 1** for an example which illustrates the current treatment of earnings.

1.4 The Department therefore wishes to change the current approach so that large payments of earnings can be taken into account for more than one assessment period. This will apply where a claimant receives a payment of earnings that is sufficient to nil their UC entitlement but then regains entitlement to UC within six assessment periods of the last day of their previous entitlement.

1.5 The proposed surplus earnings policy seeks to address both the issues outlined above in a way that supports the use of Real Time Information (RTI) and avoids the case by case insight required by the current benefit system to average and attribute earnings. It also seeks to avoid the process of annual reconciliation, which potentially results in overpayments or future awards not reflecting a claimant's needs.

1.6 This proposed surplus earnings policy applies both to employed and self-employed earnings. However, in the case of a self-employed claimant it would be unfair to carry forward a large amount received in one assessment period without also recognising the expenditure that the claimant has had to incur in previous assessment periods in order to earn that amount. Accordingly the proposed Regulations also make changes to the way that self-employed earnings are assessed so that previous losses can be taken into account (up to a maximum of 11 assessment periods following the assessment period in which the loss occurred) as part of that calculation..

[16] http://www.legislation.gov.uk/uksi/2013/376/contents/made

1.7 This policy will be introduced from 2016 when Universal Credit commences transition from legacy benefit systems to the enhanced Universal Credit service[17] for more complex claimant types across the country. This will ensure time for households to prepare and adjust; and enable the Department to test the right processes and communications to guide households, and employers, through this change.

2. Commencement and application of the proposed changes

2.1 The overall effect of these amendments is outlined below. The 2014 Regulations are subject to the negative resolution procedure and are planned to come into force in April 2016. This date is provisional and therefore subject to change.

3. Explanation, purpose and effect of the proposed changes

Universal Credit – self-employed losses

3.1 **Regulation 2** deals with the changes needed to the calculation of self-employed earnings to give effect to the surplus earnings and self-employed losses policy. Currently, regulation 57 of the 2013 Regulations requires the earnings for each assessment period to be calculated by taking the 'profits' of each trade profession or vocation carried on by the claimant (that is the actual receipts less permitted expenditure in the assessment period) and then making deductions for tax, national insurance and pension contributions. If a person is carrying on two businesses, the expenditure from one cannot be offset against the other.

3.2 In order to simplify this and allow for previous losses to be taken into account the proposed Regulations will allow for an element of 'cross- subsidy'. The profit or loss of each separate trade profession or vocation (or, if it is a partnership, the claimant's share) is calculated for the assessment period by deducting actual expenses from actual receipts. These are combined to give an overall profit or loss from which any tax or national insurance payments in the same period are deducted:

- If this produces a negative amount then the self-employed earnings are nil and there is a loss that can be carried forward and set off against future receipts.
- If this produces a positive amount then any pension contribution paid in the assessment period and previous unused losses (within the previous 11 assessment periods) are also deducted. If this produces a positive amount then that will be the self-employed earnings for the assessment period.

3.3 Although this represents a change to current policy, we believe that making limited provision for 'cross-subsidy' or sideways loss relief would provide support that better reflects the UC claimant's current circumstances

[17] Also known as the 'Digital Service'.

whilst limiting long term support for unviable businesses. It is not the intention to allow cross-subsidy between self-employed and employed earnings or between the earnings of joint claimants as Universal Credit also considers the conditionality for claimants on an individual basis and supports them to increase their earnings wherever possible.

3.4 The previous losses that can be taken into account are dealt with in the new **regulation 57A.** Where the claimant's receipts from any business carried on in the assessment period are more than the expenditure, a loss from one of the previous 11 assessment periods can be offset against those receipts. A loss can only be offset once. If the claimant loses entitlement to UC due to an increase in earnings and regains it within six months then the losses from those periods are also taken into account when considering whether surplus earnings should be applied to their UC award.

3.5 The way these losses are applied to the UC award to enable surplus earnings to be calculated is explained in more detail in example 2 in **annex 1**.

Universal Credit – surplus earnings

3.6 **Regulation 3** provides for surplus earnings. Regulation 3(2) deals with the interaction of surpluses with the Minimum Income Floor (MIF) and regulation 3(3) inserts a new regulation 64A into the 2013 Regulations that sets out how the surplus is calculated.

Calculating surplus earnings

3.7 Where a UC claimant has an award that ends because their earnings are higher than the relevant threshold (that is the 'nil UC threshold' plus a £100 'de minimis') and then re-claims UC within six assessment periods of their previous UC award ceasing, the Department will look at earnings information obtained via RTI. If they were self-employed or they had opted not to have RTI information collected they will be asked to provide information on the earnings that they have received over that period.

3.8 This earnings information will then be used to calculate whether any surplus earnings should be applied to the claimant's new UC award. To work this out we will add the original surplus from the assessment period in which the previous award ceased to the earnings in the next assessment period (or to be more precise, the month that would have been an assessment period if they had stayed on UC). If that exceeds the relevant threshold, any excess will be carried forward and treated as earnings in the next assessment period.

3.9 If the person claims UC in an assessment period where their earnings plus any surplus are greater than the relevant threshold they will not be entitled to UC. If their earnings plus any surplus do not exceed the threshold they may be entitled to a reduced amount of UC. If a person reclaims more than six assessment periods after the last day of their previous UC award terminating, surpluses are ignored.

3.10 The ‘nil UC threshold’ is the amount that a person can earn without losing entitlement to UC, which will vary according to individual circumstances. The starting point for calculating a surplus is the ‘nil UC threshold’ that applied in the assessment period in which earnings reduced entitlement to nil. In order to determine the appropriate level of the ‘nil UC threshold’ in any intervening period from that point to the new claim to UC, the Department may make assumptions about the claimant’s circumstances over the period while they were not receiving UC.

3.11 In most cases the threshold will continue to be based on the circumstances when the previous award ended (but see below regarding couples that split or form). This is to avoid complexity and the need to gather large amounts of evidence in relation to the period when UC was not being awarded.

3.12 The Department has introduced the ‘de-minimis’ into the surplus earnings calculation so that small fluctuations in earnings, for example, due to small bonus payments or slight increases in earnings that are above the ‘nil UC threshold’, can be ignored.

3.13 The Department feels that this design gives a generous and fair way to ensure that claimants can benefit from slight increases in earnings while balancing the need to address potential manipulation of the current UC system.

3.14 The Department’s view is that if someone’s UC award has been nilled for six months then they are highly unlikely to be seeking to manipulate the system, and it is reasonable to disapply the surplus earnings policy for people who return to UC after that point. This supports our aim of promoting sustainable employment and also helps to keep the administration and data collection requirements of the policy proportionate to its aim.

3.15 For an illustration of how surplus earnings are calculated please see example 3 in **annex 1**.

Treatment of surpluses where couples split and form

3.16 Where a claim is made for UC by a new couple (that is a couple who have not previously had a joint UC award) the Department will consider whether either partner has a surplus that needs to be taken into account. If either of them had an award that ended within the past six assessment periods with a surplus, the Department will look back to the previous award and calculate the individual’s surplus taking account of that person’s individual earnings in the period off UC.

3.17 Where a single person claims UC and they previously had a joint award that ended in the last six assessment periods with a surplus, that surplus will be apportioned so that it reflects the claimant’s own earnings in the assessment period in which the previous UC award terminated.

3.18 Where a surplus is being calculated in relation to a claimant who was previously part of a joint award and has since separated or a claimant who was previously single and has since formed a couple, the relevant threshold for use between the old and new awards may be based on the previous or the current circumstances, whichever is most favourable.

Interaction with the Minimum Income Floor (MIF)

3.19 The surplus earnings policy is concerned with the way earnings are calculated before the MIF is applied. Accordingly, earnings that a person is treated as having by virtue of the MIF are not counted in the calculation of surplus earnings. When a single self-employed person reclaims UC and has a surplus this will simply be regarded as part of their actual earnings when the MIF is applied.

3.20 However, if a self-employed person is part of a couple, it may make a difference as to which member of the couple the surplus earnings are attributed to. The Department considers that the fairest way to calculate any existing surplus earnings will be to attribute the surplus in the way that is most advantageous to the claimants.

3.21 For an illustration of how this would work please see example 4 in **annex 1**.

Interaction with capital limits

3.22 The surplus earnings policy does not affect the way capital limits or tariff income rules apply. Where a person has a large amount of surplus earnings so that they build up a substantial amount of capital that is still available to them when they make a new claim for UC, this will be taken into account in the usual way i.e. in line with Part 6 of the 2013 Regulations.

Reduction of surplus earnings

3.23 Where a paid worker has returned to UC within six assessment periods of a previous award because their earnings have reduced, they have ceased employment or their circumstances change, any surplus earnings to be taken into consideration will be reduced in line with their relevant threshold i.e. their nil UC point plus the ‘de minimis’ until either the surplus has been reduced to zero or a total of six assessment periods have passed since their last UC award terminated.

4. Financial Implications

4.1 The surplus earnings policy as proposed here is expected to generate overall savings and analysis suggests that the potential AME savings could be between £200 million and £300 million per annum in steady state.

5. Impacts of the proposed changes

Volumes affected

5.1 Our analysis suggests that 100,000 - 200,000 households are estimated to have a fluctuation in earnings that gives them surplus earnings in a given assessment period[18].

5.2 This represents a very small proportion of UC claimants – in any given assessment period around only 2% of the total UC caseload (around 5% of the UC caseload in work) will see an increase in earnings that would trigger this policy. This estimate is based on the total number of UC claimants who are expected to have a fluctuation in earnings that takes them above their nil UC threshold (including the £100 de minimis). We do not currently have an estimate of the proportion of this group that would be expected to return to UC within the following five assessment periods. These figures do not include any claimants who may be affected by this policy if their earnings remain the same but their UC claim ends due to an unrelated change of circumstances that results in a lower nil UC threshold (for which we currently have no estimate).

5.4 Analysis suggests that the majority of those affected have a relatively small amount of surplus earnings to take into account, and are affected in the first assessment period only.

5.5 The median amount of surplus earnings is around £200, meaning that half of all households with surplus earnings would have total surplus earnings of £200 or less. This would equate to the UC award being reduced by a maximum of £130 or less for half of all households affected (and this is ignoring work allowances).

5.6 The majority (65%) of households affected would only see their UC award reduced for one assessment period (with 75% receiving partial or full UC award from the second assessment period).

Impact on equality

5.7 In terms of the equality analysis, higher earners are more likely to experience fluctuations that give them surplus earnings. Households containing males, and containing individuals aged between 30 and 50 are each more likely to be earning within the higher earnings bands and so are more likely to be affected by this policy.

5.8 For those UC claimants that fall into other protected groups the introduction of surplus earnings policy is not expected to result in any particular advantage or disadvantage (see **annex 2** for full Equality Analysis).

---

[18] The analysis has been done on the basis of fluctuations in earnings (i.e. a claimant will get surplus earnings if their earnings fluctuate above the 'nil UC threshold' plus £100). It does not include cases where earnings are stable but the claimant's circumstances change so that their 'nil UC threshold' moves down.

Impact on complexity and operations

5.9 Although the introduction of the proposed treatment of surplus earnings does add an element of complexity to the current design of UC, the Department feels this added complexity is warranted as a result of the need to address the potential risks outlined in paragraph 1.2.

5.10 However, to limit administrative complexity the proposed new surplus earnings policy would only be introduced from 2016 when Universal Credit commences transition from legacy benefit systems to the enhanced Universal Credit service.

5.11 Operational guidance, current processes and learning and development would be developed to cover any changes by the Department.

6. Consultation on the proposed changes

6.1 We have not undertaken an external consultation on this issue, although a number of stakeholders (including SSAC) have suggested to us that some form of consideration for surplus earnings or losses may be appropriate.

6.2 The proposal does not impact on legislation in respect of Housing Benefit so no consultation with the Local Authority Associations was required.

7. Information and communications strategy for the proposed changes

7.1 The proposed changes would be communicated to operational staff through implementation updates and updates to operational guidance at the appropriate time.

7.2 The Department will also communicate any changes to external stakeholders.

8. Monitoring and evaluation of the proposed changes

8.1 The Universal Credit Evaluation Framework, published in December 2012, sets out the Department's broad intentions for evaluation, including impact measurement.[19] This provides an overview of plans for evaluating the introduction, implementation, delivery and impact of UC. Changes to UC policy and/ or regulations will be reviewed in line with the framework as we continue with national rollout of UC.

[19] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/180879/universal-credit-evaluation-framework.pdf

ANNEX 1

Example 1 –Comparison of current treatment of paid earnings

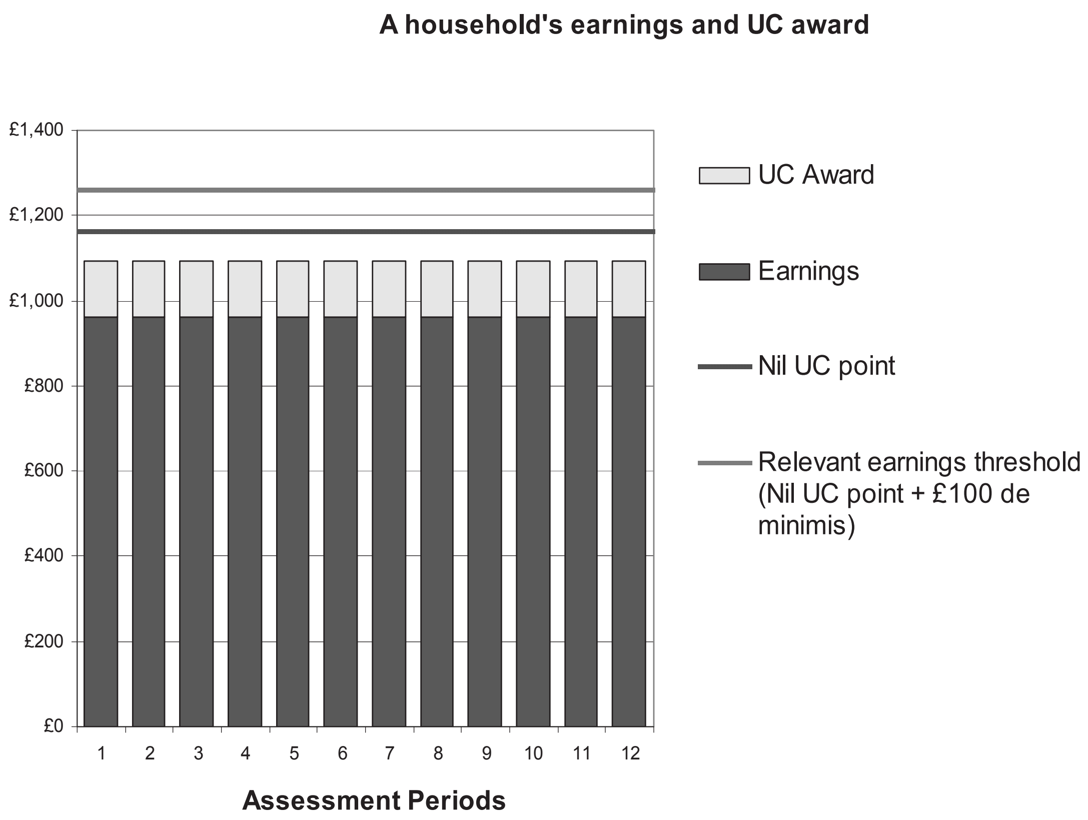
Summary

Barry and Paul have the same nil point under UC and earn the same amount over a year, but one with regular and one with irregular earnings. Under these examples, without the proposed changes to treatment of surplus earnings, Barry gets £1,580 from UC awards throughout the year, whilst Paul gets £6,839. With the proposed treatment of surplus earnings applied Barry would get £1,580 from UC awards and Paul would get £1,956[20].

Fixed income

Barry is paid £961 in net earnings each month. He is entitled to UC and his earnings result in a UC payment of £132. Barry has a total income of £1,093 in each assessment period. Over the year he earns £11,528 and is paid £1,580 in UC (see **Graph 1**).

Graph 1

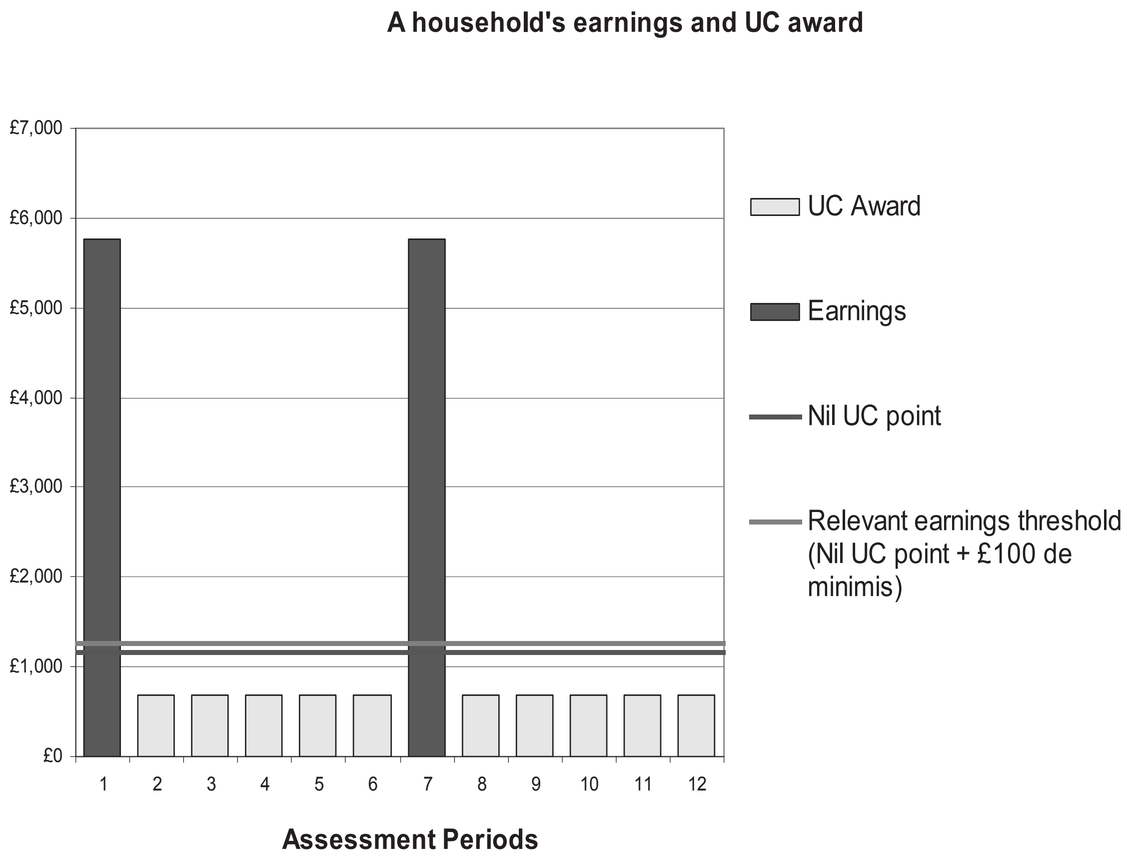


[20] Rounding has been applied to these calculations.

Fluctuating income

Paul is paid twice a year. He receives two payments of £5,764, net of tax, making his total net earnings over the year the same as Barry's. Under the current system, where surplus earnings are not taken into acount, in the assessment period where he is paid he receives £0 in UC, but in the other assessment periods as his earnings are zero he receives his maximum award of £684. Over the year Paul earns £11,528 and receives £6,839 in UC (see **Graph 2**).

Graph 2



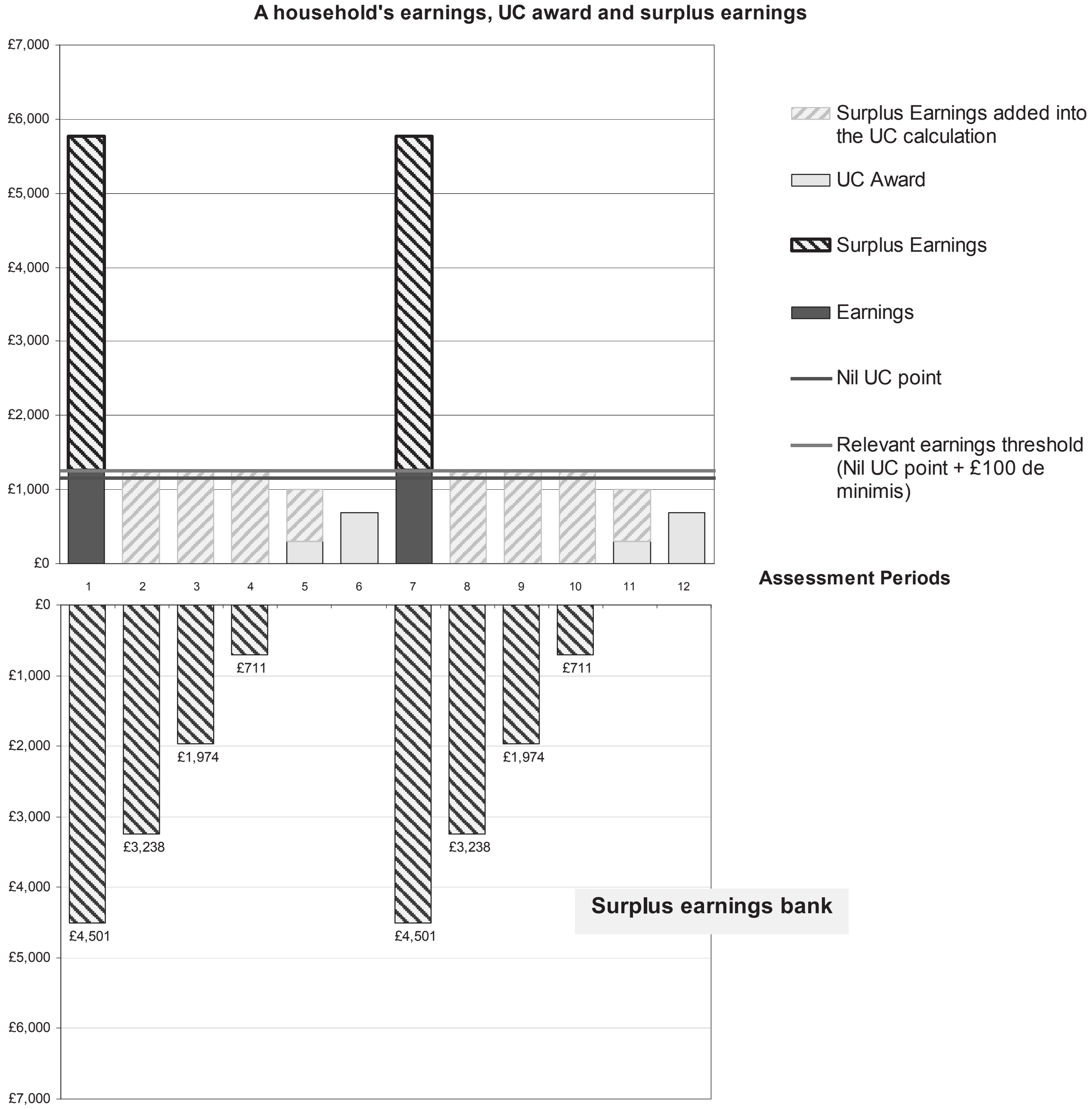
Comparison between fixed and fluctuating earnings payment

Therefore, even though Barry and Paul's total earnings over the year are the same, Paul gets an extra £5,259 in UC. This demonstrates the potential unfairness and possible incentive for households to manipulate their patterns of pay to increase their UC entitlement.

Earnings with surplus earnings policy applied

Paul is paid twice a year and for the intervening time he receives a full UC award of £684. During the year he receives two payments of £5,764, net of tax. When these earnings are received he is assessed to see whether any surplus earnings need to be applied to his UC award (see **Graph 3**).

Graph 3



In assessment period one he earns £5,764. His ‘nil UC point’ plus a £100 ‘de minimis’ (the relevant threshold) is £1,263. This results in £4,501 being placed in his ‘surplus earnings bank’. As a result Paul’s UC award is £0 for that assessment period.

The £4,501 in his surplus earnings bank (£5,764 - £1,263) is then applied to his UC entitlement (plus the £100 ‘de minimis’) for the subsequent assessment period. In each assessment period the amount in his surplus earnings bank is added onto actual earnings until either the ‘relevant threshold’ (including £100 ‘de minimis’) is reached, or they run out.

This process continues until the surplus earnings run out or six months has passed. This means that:

- In the first assessment period the £4,501 surplus earnings from his bank will be applied reducing his UC amount to £0, so there is no entitlement.
- In the second assessment period he has £3,238 of surplus earnings still to be applied in his UC award in his surplus earnings bank i.e. £4,501 - £1,263. This means his UC award is reduced to £0.
- This continues until his surplus earnings bank reduces to zero.
- Over the year, Paul again earns £11,528 but receives a lower total UC award of £1,956. This is due to the surplus earnings policy increasing the amount of Paul’s earnings used in the UC calculation.
- The surplus earnings policy is not intended to provide an exact average of a claimant’s earnings, and the calculation of surplus earnings (including the £100 ‘de minimis’) explains the difference in the amount of UC received by Barry and Paul over the year.

Example 2 – Allowing 'cross subsidy' within the Universal Credit self-employed policy

A loss made in one business currently is not allowed to offset profits from another. The rationale behind this was to not allow a claimant to 'prop up' a failing business with one which is succeeding.

In order to allow for a single figure to be recorded and taken forward under the proposed treatment of surplus earnings and losses we have allowed for a certain degree of cross subsidy although claimants will be required to report certain business expenses separately for monitoring purposes. In working out the amount of their earnings from self-employment in each assessment period, the loss calculated from one business may be offset against a profit from another in the same assessment period. For example (see **table 1**); in the current system a claimant could report:

Table 1

Self-employed earnings report: example assessment period.	**Business 1**	**Business 2**
Receipts	£1,000	£1,000
Expenses paid	-£2,000	-£500
Total per business for UC purposes	£0	£500
Self-employed earnings total for UC	£500 (£0 + £500)	

In the current system the negative figure would be treated as a zero and the claimant's total self-employed earnings would be £500 (they may though be subject to a MIF). Under the new system (see **table 2**) the figures would be reported separately but added together forming a more accurate picture of a claimant's circumstance but allowing for profits from one company to be offset against another.

Table 2

Self-employed earnings report: example assessment period.	**Business 1**	**Business 2**
Receipts	£1,000	£1,000
Expenses paid	-£2,000	-£500
Total per business for UC purposes	-£1,000	£500
Self-employed earnings total for UC	£0 (earnings to be taken into account cannot be less than nil)	
Loss carried forward	-£500	

In this circumstance in order to allow for the treatment of surplus earnings a figure of -£500 would be taken into account as a loss for up to eleven future assessment periods. The claimant's UC award would still be based on earnings of £0 (or a minimum income floor if applicable).

We wish to allow for national insurance and income tax payments to be taken into account as losses. However, we do not intend to allow claimants to carry forward contributions to a pension as an ongoing loss as this is within the claimant's control and would provide a route to artificially maximise their UC entitlement and manipulate their surplus earning figure or loss carried forward.

Essentially this means sideways loss relief, which is currently allowed in accruals accounting but not HMRC's version of the cash basis. It is important to note that, when calculating a person's tax liabilities, profits and losses are combined together by HMRC (using the cash basis system) to issue a single bill.

Example 3 – Surplus earnings calculation

Bob is a 27 year old who is employed as a car salesman relying mainly on commission. He has recently moved in with his parents and has no housing costs, has no children and has no other income.

Bob claims UC and is awarded £314.67 a month. His assessment periods begin on the 1st of each month. For a few months his earnings are well below his relevant threshold level (which includes the 'de minimis') which, based on his circumstances is £695.11[21].

However, Bob's sales begin to pick up and in May he receives £1,500, which means that this UC award terminates and he has surplus earnings of £804.89. The Department continues to receive RTI information about Bob's earnings (he could have opted out if he wished, but would have to provide the information if he reclaimed UC within six months of his old award ending).

In June Bob also earns £1,500 which is added to his original surplus of £804.89, making a total surplus of £1,609.78 once the relevant threshold (including £100 de minimis) has been taken into account. In July and August he continues to earn £1,500 which raises his surplus earnings to £3,219.56 and this is carried forward to September (see **table 1**). Unfortunately, in September Bob's employment ends and he reclaims UC. As a result £3,219.56 surplus earnings are carried forward and applied to his UC award.

Table 1

Assessment periods	Assessment period in which the award ends (May)	One (June)	Two (July)	Three (August)
Actual earnings	£1,500	£1,500	£1,500	£1,500
Relevant threshold	£695.11	£695.11	£695.11	£695.11
Surplus earnings in each assessment period	£804.89 (£1,500 - £695.11)	£804.89 (£1,500 - £695.11)	£804.89 (£1,500 - £695.11)	£804.89 (£1,500 - £695.11)
Total accrued surplus earnings	£804.89	£1,609.78 (£804.89+ £804.89	£2,414.67 (£1,609.78 + £804.89)	£3,219.56 (£2,414.67 + £804.89)

[21] Relevant threshold = Nil UC threshold (maximum award of UC (£314.67 single UC award) – (unearned income (£0) x 100/65 (UC taper)) + a Work Allowance of (£111) = £595.11) + the 'de minimis' (£100) = £695.11.

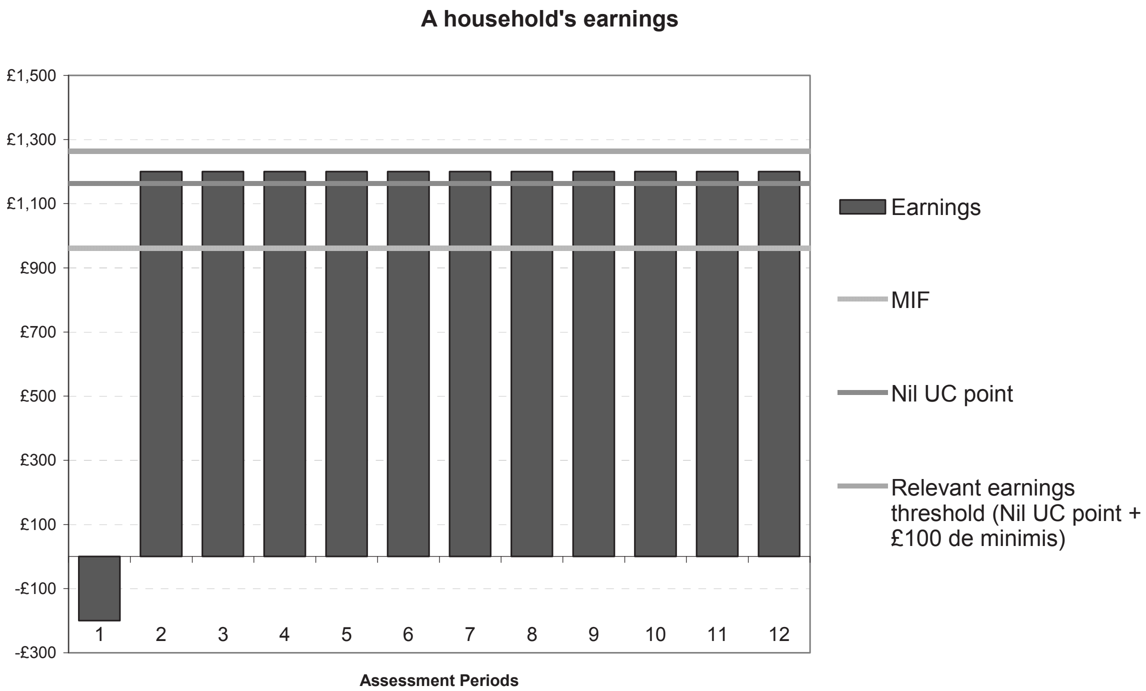
Example 4 – Self-employed earnings with surplus earnings policy applied

This example shows the impact of applying the proposed surplus earnings policy where a self-employed person has had a 'loss' in one assessment period, and the interaction with the Minimum Income Floor (MIF). There are two steps.

Step One – losses and earnings

Colin is self employed. In assessment period one he reports a loss of £200 as he buys materials for the coming months. In each of the following 11 assessment periods he earns £1,200 net of any tax and national insurance liability. In each assessment period except the first his earnings are above the MIF and above his Nil UC point. He does not gain any surplus earnings as his earnings are below the relevant threshold. **Graph 1** shows his earnings over the year.

Graph 1



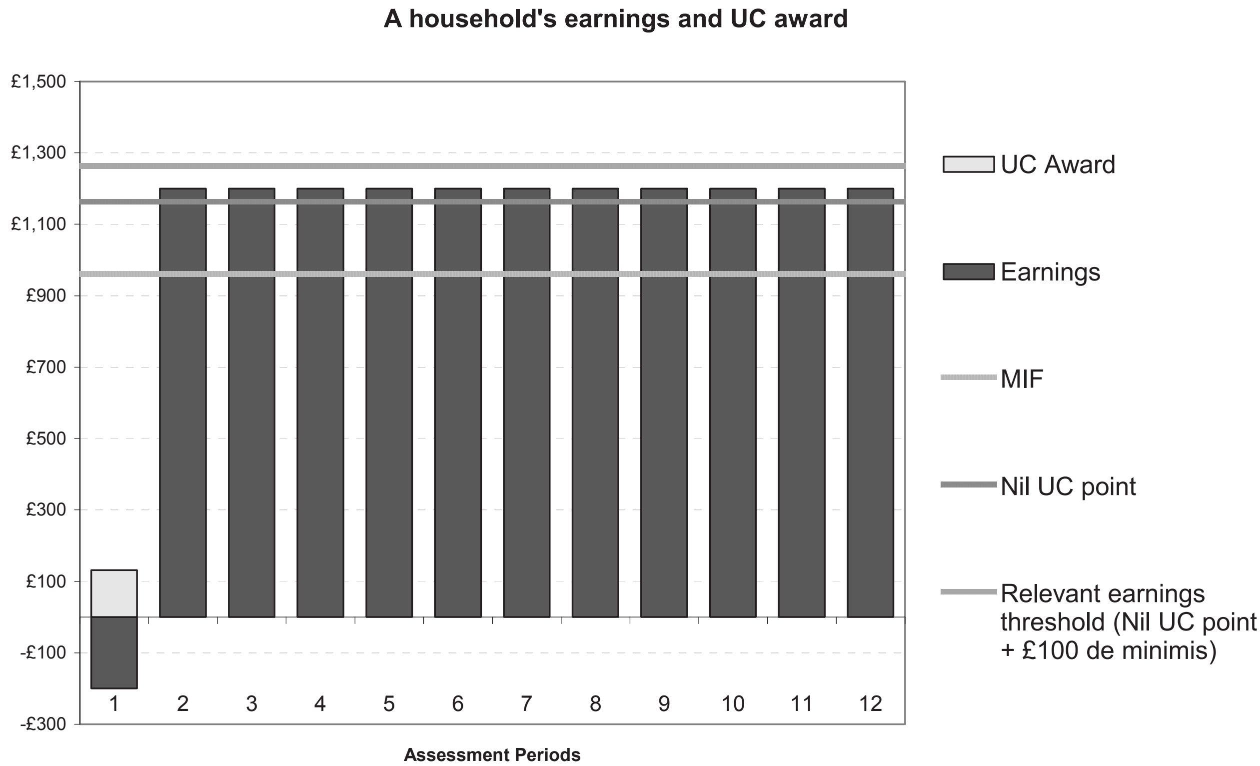
Step Two

Without the offsetting of losses:

If Colin's losses are not carried forward in future months then in the first assessment period the MIF applies and he receives £132 of UC. In assessment periods 2 to 11 as his earnings are above his Nil UC point he does not receive any UC. This is shown in **Graph 2**.

Over the year Colin has net earnings of £13,000 and receives £132 in Universal Credit.

Graph 2



With the offsetting of losses

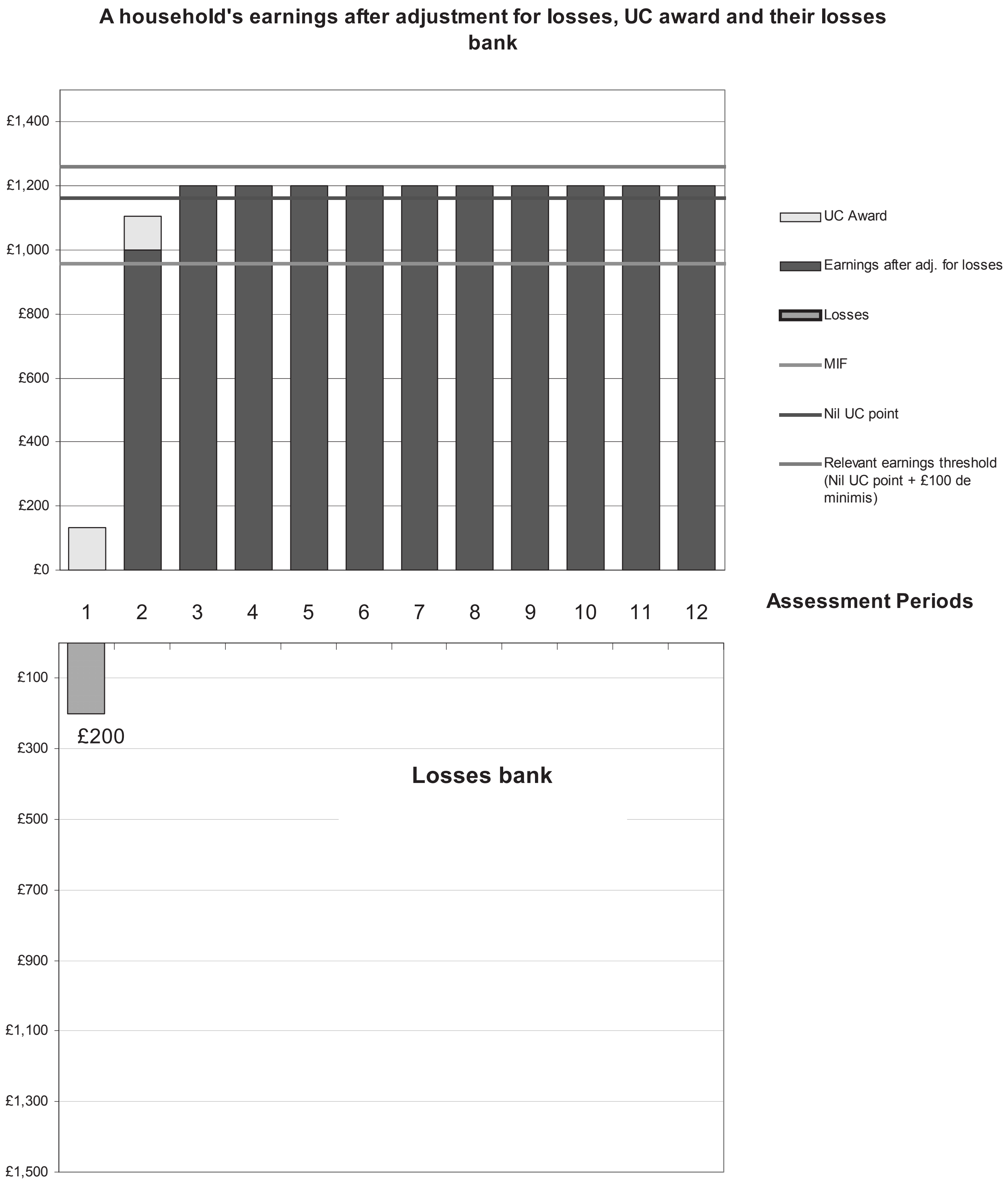
Under the proposed changes, Colin's loss of £200 in the first assessment period is taken into account to offset earnings in the subsequent month. **Graph 3** shows how the £200 will reduce earnings over the next assessment period.

In assessment period two, his earnings are reduced from £1,200 to £1,000. Since his earnings are still above the MIF after the loss is taken into account, this increases his UC award to £106 in assessment period two. In the event that a loss reduced earnings below the MIF then the MIF would still apply.

From assessment period three onwards Colin's UC award returns to £0 as he has no more losses to offset earnings.

Over the year Colin has net earnings of £13,000 and receives £238 in Universal Credit.

Graph 3



Example 5 – Separation and surplus earnings policy

Bob and Mary are both 28, have one child and currently live with Bob's parents. They have no income for UC purposes other than what they get from paid work. In May their joint UC award ends when their combined earnings exceed their relevant earnings threshold of £1,818.35[22] and they continue to have combined earnings above the threshold of £1,818.35 which prevents them from being entitled to a new award of UC for the next three assessment periods (see **table 1**).

Table 1

Assessment periods	Assessment period in which the award ends (May)	Month 1	Month 2	Month 3
Bob's earnings	£1,500	£500	£1,000	£900
Mary's earnings	£500	£2,000	£1,900	£1,850
Bob's and Mary's total earnings	£2,000	£2,500	£2,900	£2,750
Relevant earnings threshold	£1,818.35	£1,818.35	£1,818.35	£1,818.35
Bob's and Mary's surplus earnings	£181.65 (£2,000 - £1,818.35)	£681.65 (£2,500 - £1,818.35)	£1081.65 (£2,900 - £1,818.35)	£931.65 (£2,750 - £1,818.35)
Bob's and Mary's total accrued surplus earnings	£181.65	£863.30 (£181.65 + £681.65)	£1,944.95 (£1081.65 + £863.30)	£2,876.60 (£931.65 + £1,944.95)

Mary and Bob separate and Mary claims Universal Credit

Bob and Mary separate in month 4 and Mary makes a claim for UC as a single person; their child stays with Bob and she moves in with her parents. As a result the following calculation is performed to work out what, if any, surplus earnings are attributed to Mary. This involves apportioning the surplus from the assessment period in which the surplus arose (the previous joint award) and then treating Mary as a single person for the intervening periods up to her new claim.

[22] Relevant earnings threshold = (Nil UC threshold of (maximum award of UC (£493.95 joint UC award + 274.58 (Child element) – unearned income (£0) x 100/65 (UC taper) + a Work Allowance of (£536) = £1,718.35) + the 'de minimis' (£100) = £1,818.35).

- The earnings Mary received in the assessment period that the previous award terminated in (£500) is worked out as a percentage of the total earnings for the couple (£2,000) in that assessment period. This means that 25% of the surplus in that month (£181.65) is attributed to Mary in assessment period one;
- Mary's total surplus earnings are then worked out over the intervening assessment periods. The threshold that applies for those periods can be either the one relevant to her old or new award – whichever is most advantageous to her. In Mary's case this is the previous relevant earnings threshold of £1,818.35 of the joint UC award. Her individual earnings are considered against that threshold in the intervening assessment periods to determine if a surplus continues to apply (see **table 2**).
- This means when Mary returns to UC she has total accrued earnings of £340.36 to be applied to her UC award. Her UC nil point and relevant earnings threshold will be calculated from this point on based on her new circumstances[23].

Table 2

Assessment periods	**Assessment period in which the award ends (May)**	**Month 1**	**Month 2**	**Month 3**
Mary's earnings	£500 (+£1,500 as assessed as couple)	£2,000	£1,900	£1,850
Relevant earnings threshold (from old award)	£1,818.35	£1,818.35	£1,818.35	£1,818.35
Mary's surplus earnings	£45.41 (25% of couple surplus of £181.65)	£181.65 (£2,000 – £1,818.35)	£81.65 (£1,900 - £1,818.35)	£31.65 (£1,850 - £1,818.35)
Total accrued surplus earnings	£45.41	£227.06 (£45.41+ £181.65)	£308.71 (£81.65 + £227.06)	£340.36 (£31.65 + £308.71)

[23] Relevant earnings threshold = (Nil UC threshold of (maximum award of UC (£314.67 single UC award) – unearned income (£0) x 100/65 (UC taper) + a Work Allowance of (£111) = £595.11 + the 'de minimis' (£100) = £695.11).

Example 6 – Couple formation

Armand is a 27 year old who is employed as florist. Any information relating to Pay as You Earn earnings are received through Real Time Information (RTI) on the 28th of each month. He has recently moved in with his parents and has no housing costs and has no children.

Armand claims UC. His assessment periods begin on the 15th of each month. In each of Armand's assessment periods from April 15th – May 14th to June 15th – July 14th his earnings increase to £1,500. As a result Armand's UC award terminates in his April 15th – May 14th assessment period. When his relevant earnings threshold level (which based on his circumstances) of £695.11[24] is taken into account he has surplus earnings of £804.89 in each of his assessment periods (see **table 1**)

Table 1

Assessment periods	**(April 15th – May 14th)**	**(May 15th – June 14th)**	**(June 15th - July 14th)**
Actual earnings	£1,500	£1,500	£1,500
Relevant earnings threshold	£695.11	£695.11	£695.11
Surplus earnings	£804.89 (£1,500 - £695.11)	£804.89 (£1,500 - £695.11)	£804.89 (£1,500 - £695.11)
Total accrued surplus earnings	£804.89	£1,609.78 (£804.89 + £804.89)	£2,414.67 (£1,609.78 + £804.89)

Armand forms a couple with Elise on 20th June who also has no children and lives with her parents. Elise's assessment period runs from the 5th to the 4th of the month. Elise has not been in paid work whilst receiving UC.

Armand and Elise are treated as making a joint claim for UC, using the assessment period from Elise's award (5th June to 4th July) and they move in with Armand's parents. When Armand and Elise are treated as making a joint claim his relevant earnings threshold changes as he is now part of a couple rather than a single person with no housing costs. His new relevant earnings threshold is £970.92[25].

As Armand has surplus earnings present in his old award, these are attributed to Armand and Elise's new joint award. When these are attributed the surplus earnings from his April 15th – May 14th assessment period are used and applied to his and Elise's new joint assessment period of June 5th – July 4th. This is because the April 15th – May 14th assessment period is the last full assessment period of Armand's old award before the first assessment period of the new joint award.

[24] Relevant earnings threshold = (Nil UC threshold of (maximum award of UC (£314.67 single UC award) – unearned income (£0) x 100/65 (UC taper) + a Work Allowance of (£111) = £595.11 + the 'd -minimis' (£100) = £695.11).

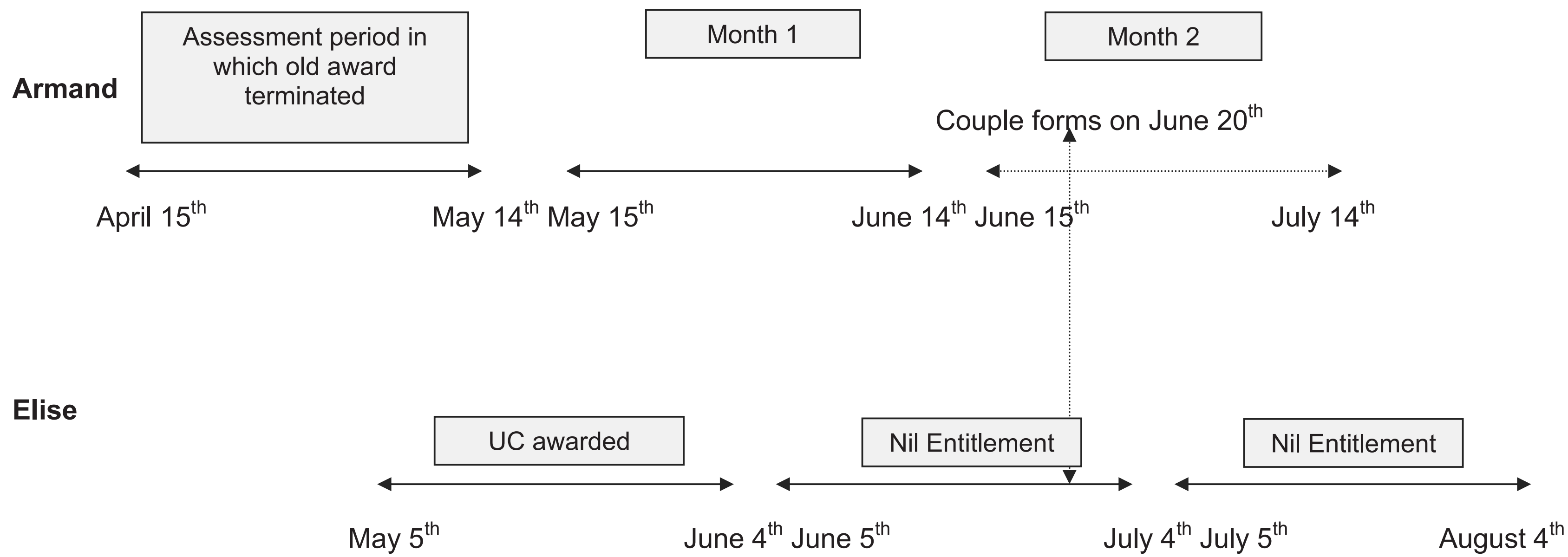
[25] Relevant earnings threshold = (Nil UC threshold of (maximum award of UC (£493.95 joint UC award) – unearned income (£0) x 100/65 (UC taper) + a Work Allowance of (£111) = £870.92) + the 'de minimis' (£100) = £970.92).

The result is that because of Armand's surplus from his "old" award and his earnings in their first assessment period as a couple, Elise and Armand do not become entitled to UC and will have £1333.97 surplus earnings applied to their UC award (see **table 2 and diagram 1**).

Table 2

Assessment periods	**(June 5th – July 4th)**	**(July 5th – 4th August)**	**(5th September – 4th October)**
Armand's earnings	£1,500	£0	£0
Elise's earnings	£0	£0	£0
Armand 's and Elise's total earnings	£1,500	£0	£0
Relevant earnings threshold	£970.92	£970.92	£970.92
Earnings used to calculate UC award in this Assessment Period	£970.92	£970.92	£363.05
Armand's and Elise's surplus earnings this assessment period	£529.08	£0	£0
Armand's and Elise's total accrued surplus earnings	£1333.97 (£804.89 from old award + £529.08	£363.05 (£1333.97 accrued surplus – £970.92 relevant earnings threshold)	£0.00 (£363.05 accrued surplus is less than £970.92 relevant earnings threshold)

Diagram 1 – Armand and Elise's assessment periods



Example 7 – Reduction of surplus earnings upon returning to Universal Credit

Davina is a 27 year old, who lives with her parents and has no children. Davina claims UC and is awarded £314.67 a month. Her assessment periods begin on the 1st of each month. For a few months her earnings are below her relevant earnings threshold (which includes the de minimis) which, based on her circumstances is £695.11[26].

However, in May her earnings increase to £1,500 and she is no longer entitled to UC. The Department continues to receive RTI information about Davina's earnings (she could have opted out if she wished, but would have to provide the information if she reclaimed UC within six assessment periods of her old award ending).

In June Davina also earns £1,500 which is added to her original surplus of £804.89, making a total surplus of £1,609.78. In July and August she continues to earn £1,500 which raises her surplus earnings to £3,219.56 and this is carried forward to September (see **table 1**).

Table 1

Assessment periods	**Assessment period in which the award ends (May)**	**Month 1 (June)**	**Month 2 (July)**	**Month 3 (August)**
Actual earnings	£1,500	£1,500	£1,500	£1,500
Relevant earnings threshold	£695.11	£695.11	£695.11	£695.11
Surplus earnings	£804.89 (£1,500 - £695.11)	£804.89 (£1,500 - £695.11)	£804.89 (£1,500 - £695.11)	£804.89 (£1,500 - £695.11)
Total accrued surplus earnings	£804.89	£1,609.78 (£804.89+ £804.89	£2,414.67 (£1,609.78 + £804.89)	£3,219.56 (£2,414.67 + £804.89)

Unfortunately, in September Davina's employment ends and she reclaims UC. As she had an award of UC which ended less than six assessment periods before her new claim, the £3,219.56 surplus earnings are carried forward and applied to her UC award.

From September Davina has no earnings so the surplus earnings she has accrued in the past four assessment periods are reduced in line with her relevant earnings threshold of £695.11 (see **table 2**).

Although there is still a surplus outstanding at the end of the October assessment period this does not get taken forward into the next assessment period. This is because it is six

[26] Relevant earnings threshold = (Nil UC threshold of (maximum award of UC (£314.67 single UC award) – unearned income (£0) x 100/65 (UC taper) + a Work Allowance of (£111) = £595.11 + the 'de minimis' (£100) = £695.11.

assessment periods since Davina was last entitled to UC (30th April). Once a claimant has ceased to be entitled to UC for six assessment periods any remaining surplus is reset to zero.

Table 2

Assessment periods	**Month 4 surplus (September)**	**Month 5 surplus (October)**	**Month 1 New entitlement (November)**
Total surplus earnings £3,219.56	£2,524.45 (£3,219.56 - £695.11)	£1,829.34 (£2,524.45 - £695.11)	Nil Claimant has been "off" UC for six assessment periods; surplus reset to zero.
Relevant earnings threshold	£695.11	£695.11	£695.11
UC award	£0	£0	Entitled (zero surplus & zero earnings)

Example 8 – Employment ceases but Universal Credit not re-claimed straight away.

Victoria is a 27 year, who lives with her parents, has no children. Victoria claims UC and is awarded £314.67 a month. Her assessment periods begin on the 1st of each month. For a few months her earnings are below her relevant earnings threshold (which includes the 'de minimis') which, based on her circumstances is £695.11[27].

However, in May her earnings increase to £1,500 and she is no longer entitled to UC. The Department continues to receive RTI information about Victoria's earnings (she could have opted out if she wished, but would have to provide the information if she reclaimed UC within six assessment periods of her old award ending).

In June Victoria also earns £1,500 which is added to her original surplus of £804.89, making a total surplus of £1,609.78. In July and August she continues to earn £1,500 which raises her surplus earnings to £3,219.60 and this is carried forward to September (see **table 1**).

Table 1

Assessment periods	**Assessment period in which the award ends (May)**	**Month 1 (June)**	**Month 2 (July)**	**Month 3 (August)**
Actual earnings	£1,500	£1,500	£1,500	£1,500
Relevant earnings threshold	£695.11	£695.11	£695.11	£695.11
Surplus earnings	£804.89 (£1,500 - £695.11)	£804.89 (£1,500 - £695.11)	£804.89 (£1,500 - £695.11)	£804.89 (£1,500 - £695.11)
Total accrued surplus earnings	£804.89	£1,609.78 (£804.89+ £804.89	£2,414.67 (£1,609.78 + £804.89)	£3,219.56 (£2,414.67 + £804.89)

Unfortunately, in September (after four assessment periods) Victoria's employment ends but she does not re-claim UC straight away as she decides to live off her savings for one assessment period.

If she had re-claimed UC straight away she would have had £3,219.56 surplus earnings applied to her UC award, but because she lived off her savings for one assessment period, when she returns to UC in October, her surplus has reduced by her relevant earnings threshold (£695.11) to £2,524.45. This means in October £1,829.34 surplus earnings are applied to her UC award i.e. £2,524.45 minus the relevant threshold level of £695.11 and she receives £0 UC. However, because the following assessment period is the sixth

[27] Relevant earnings threshold = (Nil UC threshold of (maximum award of UC (£314.67 single UC award) – unearned income (£0) x 100/65 (UC taper) + a Work Allowance of (£111) = £595.11 + the 'de minimis' (£100) = £695.11).

assessment period since her previous UC claim ceased no surplus earnings are applied to her UC award from that point and because her circumstances have not changed since her previous claim, she receives £314.67 UC (see **table 2**).

Table 2

Assessment periods	**Month 4 surplus (September)**	**Month 5 surplus (October)**	**Month 1 New award (November)**
Total surplus earnings £3,219.56	Victoria lives off her savings.	£1,829.34 (£2,524.45 - £695.11)	Nil Claimant has been 'off' UC for six assessment periods; surplus reset to zero.
Relevant earnings threshold	Surplus is reduced to £2,524.45 by deducting the relevant earnings threshold of £695.11 even though no new UC claim is made i.e. £3,219.56 - £695.11.	£695.11	£695.11
UC award	N/A	£0	£314.67

ANNEX 2

Equality Analysis for the introduction of the treatment of surplus earnings in Universal Credit

1. Introduction

1.1 This document records the analysis undertaken by the Department for Work and Pensions (“the Department”) to enable Ministers to fulfil the requirements placed on them by the Public Sector Equality Duty (PSED) as set out in section 149 of the Equality Act 2010. The PSED requires the Minister to pay due regard to the need to:

- eliminate unlawful discrimination, harassment and victimisation and other conduct prohibited by the Act;
- advance equality of opportunity between people who share a protected characteristic and those who do not; and
- foster good relations between people who share a protected characteristic and those who do not.

1.2 In undertaking the analysis that underpins this document, where applicable, the Department has also taken into account the United Nations Convention on the Rights of Persons with Disabilities, and in particular the three parts of Article 19 which recognise the equal right of all disabled people to live in the community, with choices equal to others, and that the Department should take effective and appropriate measures to facilitate full enjoyment by disabled people of this right and their full inclusion and participation in the community.

2. Brief outline of policy or service

Current treatment

2. 1 Currently, where earnings are received by a Universal Credit (UC) claimant that reduce a UC award to nil, in an assessment period, these earnings are applied to the UC award within that assessment period. This means entitlement to UC will cease for that one assessment period. The Department now proposes to refine this approach in order to:

- ensure employers and paid workers cannot manipulate their payment patterns to maximise Universal Credit entitlement
- ensure paid workers with fluctuating earnings patterns are neither penalised nor unfairly rewarded by receiving less/ more UC than they would if they earned the same amount but were paid monthly.

2.2 The Department therefore wishes to change the current approach so that large payments of earnings can be taken into account for more than one assessment period. This will apply where a claimant regains entitlement to UC within six assessment periods of the last day of their previous entitlement.

2.3 The surplus earnings policy seeks to address both the issues outlined above in a way that supports the use of Real Time Information (RTI) and avoids the case by case insight required by the current benefit system to average and attribute earnings. It also seeks to avoid the process of annual reconciliation, which potentially results in overpayments or future awards not reflecting a claimant's needs.

Future treatment

Introduction

2.4 The following Equality Analysis covers the impact of the policy once fully rolled out nationally. This policy will be introduced from 2016 when Universal Credit commences transition from legacy benefit systems to the enhanced Universal Credit service[28] for more complex claimant types across the country. This will ensure there is time for households to prepare and adjust; and enable the Department to test the right processes and communications to guide households, and employers, through this change.

Surplus earnings

Calculating surplus earnings

2.6 Where a UC claimant has an award that ends and then re-claims UC within six assessment periods of their previous UC award ceasing, the Department will look at earnings information obtained via Real Time Information (RTI). If they were self-employed or they had opted not to have RTI collected they will be asked to provide information on the earnings that they have received over that period.

2.7 This earnings information will then be used to calculate whether any surplus earnings should be applied to the claimant's new UC award. To work this out we will add the original surplus from the assessment period in which the previous award ceased to the earnings in the next assessment period (or to be more precise, the month that would have been an assessment period if they had stayed on UC). If that exceeds the relevant earnings threshold, any excess will be carried forward and treated as earnings in the next assessment period.

2.8 If the person claims UC in an assessment period where their earnings plus any surplus are greater than the relevant earnings threshold they will not be entitled to UC. If their earnings plus any surplus do not exceed the 'nil UC threshold' they may be entitled to a reduced amount of UC. If a person reclaims more than six assessment periods after the last day of their previous entitlement to UC, surpluses are ignored. The 'nil UC threshold' is the amount that a person can earn without losing entitlement to UC and this will vary according to an individual's circumstances.

2.9 The Department has introduced the 'de-minimis' into the surplus earnings calculation so that small fluctuations in earnings, for example, due to small bonus payments or slight increases in earnings that are above the 'nil UC threshold', can be ignored.

2.10 The Department feels that this design gives a generous and fair way to ensure that claimants can benefit from slight increases in earnings while balancing the need to address potential manipulation of the current UC system.

[28] Also known as the 'Digital Service'.

2.11 The Department's view is that if someone's UC award has been nilled for six months then they are highly unlikely to be seeking to manipulate the system, and it is reasonable to disapply the surplus earnings policy for people who return to UC after that point. This supports our aim of promoting sustainable employment and also helps to keep the administration and data collection requirements of the policy proportionate to its aim.

Self-employed losses

2.12 Currently, the earnings for each assessment period are calculated by taking the 'profits' of each trade, profession or vocation carried on by the claimant (that is the actual receipts less permitted expenditure in the assessment period) and then making deductions for tax, national insurance and pension contributions. If a person is carrying on two businesses, the expenditure from one cannot be offset against the other.

2.13 However, with the introduction of the surplus earnings policy the Department believes that in the case of a self-employed claimant it would be unfair to carry forward a large amount received in one assessment period without also recognising the expenditure that the claimant has had to incur in previous assessment periods. There for the Department will allow losses from previous assessment periods to be taken into account.

2.14 In order to allow for previous losses to be taken into account, some changes are need to the way self-employed earnings are calculated from each assessment period. First, the profit or loss of each separate trade profession or vocation (or, if it is a partnership, the claimant's share) is calculated for the assessment period by deducting actual expenses from actual receipts. These are then combined to give an overall profit or loss from which any tax or national insurance payments in the same period are deducted:

- If this produces a negative amount then the self-employed earnings are nil and there is a loss that can be carried forward and set off against future receipts.
- If this produces a positive amount then any pension contribution paid in the assessment period and previous unused losses (within the previous 11 assessment periods) are also deducted. If this produces a positive amount then that will be the self-employed earnings for the assessment period.

It is not the intention to allow losses to reduce employed earnings or the earnings of a joint claimant.

3. Evidence and Analysis

3.1 Our analysis suggests that, once UC is fully rolled out, between 100,000 and 200,000 households in a given assessment period are estimated to have a fluctuation in earnings that gives them surplus earnings. This is approximately 5% of the UC working caseload.

3.2 We have produced estimates of the characteristics of these households in order to consider the potential equality impacts of the surplus earnings policy. We did this by looking at the likelihood of households in different earnings bands receiving fluctuations that give them surplus earnings (earnings above their 'nil UC threshold' plus £100). We then combined this with the likelihood of households containing people in the protected groups receiving net earnings within those earnings bands.

3.3 This therefore assumes that all households within each earnings band are equally likely to receive a fluctuation of the same size, regardless of any other characteristic. As such the estimates should be treated as an indication of the potential equality impacts of this policy.

3.4 For the analysis below, the term ‘households with surplus earnings’ is used to mean households who receive a fluctuation in earnings in a given month that gives them surplus earnings. Proportions have been rounded to the nearest five percentage points.

- **Age**

3.5 The analysis in **table 1** suggests that around 35% of households with surplus earnings contain an individual under age 30, which is the same proportion as in all working households receiving UC.

3.6 Around 70% of households with surplus earnings are estimated to contain an individual between age 30 and age 50, compared to 60% of all working UC households. This is because our analysis shows that households containing individuals aged 30 to 50 are more likely to be earning within the higher earnings bands and that “higher earners” are more likely to experience fluctuations in earnings that give them surplus earnings.

3.7 Around 10% of households with surplus earnings are estimated to contain an individual over age 50, compared to 10% of all working UC households.
Table 1:

	Working households receiving UC	**Households with surplus earnings**
Contains an individual under age 30	35%	35%
Contains an individual between age 30 and age 50	60%	70%
Contains an individual over age 50	10%	10%

Note: Figures do not sum to 100% because a household can contain an individual in more than one of the age groups.

- **Disability**

3.8 We estimate that around 30% of households with surplus earnings will contain an individual who has a Disability Discrimination Act (DDA) defined disability. This is compared to around 30% of working households receiving UC. Therefore people with a DDA defined disability are not expected to be over- or under-represented in those affected by this policy.

- **Gender reassignment**

3.9 We have no reason to believe that this policy would result in particular disadvantage to claimants on grounds of gender reassignment.

- **Marriage and civil partnership**

3.10 The information held by the Department on its administrative systems does not distinguish between different types of partnership. However, UC provisions do not treat those who are married differently from those in civil partnerships so we have no reason to believe that this policy would result in particular advantage or disadvantage to claimants in different types of partnership.

- **Pregnancy and maternity**

3.11 We have no reason to believe the policy will result in a particular advantage or disadvantage to claimants on grounds of pregnancy or maternity.

- **Race**

3.12 We estimate that around 20% of households with surplus earnings will contain an individual from an ethnic minority group. This is compared to around 20% of working households receiving UC. Therefore people from ethnic minority groups are not expected to be over- or under-represented in those affected by this policy.

- **Religion or belief**

3.13 We have no reason to believe the policy will result in a particular advantage or disadvantage to claimants on grounds of religion or belief.

- **Sex**

3.14 **Table 2** suggests that around 70% of households with surplus earnings contain a male, compared to around 60% of working households receiving UC. This is because our analysis shows that households containing males are more likely to be earning within the higher earnings bands, and that higher earners are more likely to experience fluctuations in earnings that give them surplus earnings.

Table 2:

	Working households receiving UC	**Households with surplus earnings**
Contains a male	60%	70%
Contains a female	90%	90%

3.15 Our analysis also suggests that around 90% of households with surplus earnings contain a female,[29] compared to the same proportion in working households receiving UC.

[29] A higher proportion of working UC households contains a female than a male because working UC households mainly comprise couples and lone parents, and lone parents tend to be female.

- **Sexual Orientation**

3.16 The Department does not hold information on its administrative systems on the sexual orientation of claimants. However, as UC rules treat claimants the same regardless of sexual orientation we have no reason to believe the policy will cause particular advantage or disadvantage to claimants on grounds of sexual orientation.

4. Conclusion on the introduction of surplus earnings

4.1 The analysis suggests that higher earners are more likely to experience fluctuations that give them surplus earnings. We found that households containing males, and households containing an individual aged between 30 and 50, are each more likely to be earning within the higher earnings bands and so are more likely to be affected by the surplus earnings policy.

4.2 Although this is the case, the Department feels that this design still gives a generous and fair way to ensure that all claimants can benefit from slight increases in earnings while balancing the need to address potential manipulation of the current UC system.

4.3 For those UC claimants that fall into other protected groups i.e. those UC claimants who:

- are aged below 30 or above 50;
- have a DDA defined disability;
- have undergone gender reassignment;
- are married or are in a civil partnership;
- are pregnant or are on maternity;
- have a particular race, religion, belief or sexual orientation;
- are female.

the Department feels that the introduction of the surplus earnings policy would not result in any particular advantage or disadvantage for these claimant groups.

Impact of a ‘dual running approach’

4.4 When considering the introduction of surplus earnings and the associated changes to how self-employed losses are treated the Department has taken into account the impact on DWP operations and claimants. On this basis, the Department has decided the policy should only be implemented from 2016 when Universal Credit commences transition from legacy benefit systems to the enhanced Universal Credit service for more complex claimant types across the country.

4.5 As a result, claimants who receive UC prior to 2016 will continue to be dealt with under the existing provisions. Claimants with higher incomes and the self-employed, who are most likely to be affected by this policy, will not have made the transition from legacy benefit systems to the enhanced Universal Credit service and therefore the Department believes that any adverse impacts that might temporarily be experienced will be a proportionate means of meeting this legitimate aim.

5. Monitoring and evaluation

5.1 The UC Evaluation Framework, published in December 2012, sets out the Department's broad intentions for evaluation, including impact measurement[30]. This provides an overview of plans for evaluating the introduction, implementation, delivery and impact of UC. Changes to UC policy and or regulations will be reviewed in line with the framework as we continue to roll UC out nationally.

6. When will the potential impacts be reviewed?

6.1 The UC "Test and Learn" framework is a key element of the broader Departmental approach to evaluating UC policy. The impacts of changes of policy will be reviewed on an on-going basis as part of this process.

Sign off

7.1 Lord Freud 26th September 2014.

[30] https://www.gov.uk/government/publications/universal-credit-impact-assessment

STATUTORY INSTRUMENTS

2014 No.

SOCIAL SECURITY

The Universal Credit (Surpluses and Self-employed Losses) Regulations 2014

Made - - - -	***
Laid before Parliament	***
Coming into force - -	***

The Secretary of State for Work and Pensions, in exercise of the powers conferred by paragraph 4(1), (3)(a) and (4) of Schedule 1 to, the Welfare Reform Act 2012(**a**), makes the following Regulations:

[In accordance with section 172(1) of the Social Security Administration Act 1992, the Secretary of State has referred the proposals for these Regulations to the Social Security Advisory Committee.]

Citation and commencement

1.—(1) These Regulations may be cited as the Universal Credit (Surpluses and Self-employed Losses) Amendment Regulations 2014 and come into force on [.. ..] 2016.

Self employed earnings – treatment of losses

2.—(1) The Universal Credit Regulations 2013 are amended as follows.

(2) In regulation 57 (self-employed earnings) for paragraphs (2) and (3) substitute—

"(2) A person's self-employed earnings in respect of an assessment period are to be calculated as follows.

Step 1

Calculate the amount of the person's profit or loss in respect of each trade, profession or vocation carried on by the person by—

(a) taking the actual receipts in that assessment period; and

(b) deducting any amounts allowed as expenses under regulation 58 or 59.

Where a trade, profession or vocation is carried on in a partnership, take the amount of the profit or loss attributable to the person's share in the partnership.

(a) 2012 c.5.

Step 2

If the person has carried on more than one trade, profession or vocation in the assessment period, add together the amounts resulting from step 1 in respect of each trade, profession or vocation.

Step 3

Deduct from the amount resulting from step 1 or (if applicable) step 2 any payment made by the person to HMRC in the assessment period in respect of—

(a) Class 2 contributions under section 11(1) or (3) of the Contributions and Benefits Act or Class 4 contributions under section 15 of that Act, and

(b) income tax incurred by virtue of carrying on a trade, profession or vocation.

If the amount resulting from steps 1 to 3 is nil or a negative amount, the amount of the person's self-employed earnings in respect of the assessment period is nil (and ignore the following steps).

If the amount resulting from steps 1 to 3 is a negative amount, the person has a loss of that amount for the assessment period (and see regulation 57A as to the use of that loss in a subsequent assessment period).

Step 4

If the amount resulting from step 3 is greater than nil, deduct from that amount any relievable pension contributions made by the person in the assessment period (unless a deduction has been made in respect of those contributions in calculating the person's employed earnings).

If the amount resulting from this step is nil or a negative amount, the person's self-employed earnings in respect of the assessment period are nil (and ignore the following step).

Step 5

If the amount resulting from step 4 is greater than nil, deduct from that amount any unused losses (see regulation 57A), taking the oldest first.

If the amount resulting from this step is greater than nil, that is the amount of the person's self-employed earnings for the assessment period.

If the amount resulting from this step is nil or a negative amount, the amount of the person's self-employed earnings in respect of the assessment period is nil."

(3) In regulation 57(4) for "paragraph (3)" substitute "paragraph (2)".

(4) After regulation 57 insert—

"Unused losses

57A.—(1) For the purposes of step 5 in regulation 57(2), a person has an unused loss if—

(a) the person has a loss for any of the previous 11 assessment periods (see step 3 in regulation 57(2)), and

(b) the amount of the loss has not been extinguished in a subsequent assessment period.

(2) For the purposes of paragraph (1)(b) a loss is extinguished if no amount of the loss remains after it has been deducted at step 5 in regulation 57(2).

(3) Where a person was entitled to a previous award of universal credit and the last day of entitlement in respect of that award fell within the 6 months preceding the first day of entitlement in respect of the new award, for the purposes of this regulation the Secretary of State may, if the person provides such information as the Secretary of State requires, treat

the assessment periods under the previous award and any months between that award and the current award as assessment periods under the current award."

(5) In regulation 58 (permitted expenses) in paragraph (3) omit sub-paragraph (b).

Carry forward of surplus earnings

3.—(1) The Universal Credit Regulations 2013 are amended as follows.

(2) In regulation 62 (minimum income floor) after paragraph (4) insert—

(4A) Where this regulation applies in respect of an assessment period in which surplus earnings are treated as an amount of earned income under regulation 64A (surplus earnings), that amount is to be added to the claimant's earned income before this regulation is applied and, in the case of joint claimants, it is to be added to the earned income of either member of the couple so as to produce the lowest possible amount of combined earned income after this regulation is applied.

(3) After regulation 64 insert—

"Surplus earnings

64A.—(1) This regulation applies in relation to a claim for universal credit where—

(a) the claimant (or either of joint claimants) was entitled to an award of universal credit that terminated within the 6 months ending on the first day in respect of which the claim is made ("the old award"); and

(b) there were surplus earnings in the assessment period in which the old award terminated.

(2) Where this regulation applies, and there are also surplus earnings in the month that would have been an assessment period for the old award (had it continued) which immediately precedes the first assessment period for the new award, the amount of those surplus earnings is to be treated as earned income for the purposes of—

(a) determining whether there is entitlement to a new award; or

(b) if there is entitlement to a new award, calculating the amount of the award in the first assessment period.

(3) Whether there were surplus earnings in the assessment period in which the old award terminated, or whether there are surplus earnings in any of the subsequent 5 months that would have been assessment periods for the old award (had it continued), is to be determined as follows.

Assessment period in which the old award terminated

There are surplus earnings in the assessment period in which the old award terminated if the total earned income for that assessment period exceeds the relevant threshold. ("the original surplus")

Month 1

There are surplus earnings in the first month after the assessment period in which the old award terminated if the original surplus, combined with the total earned income for that month exceeds the relevant threshold.

Month 2

There are surplus earnings in the second month after the assessment period in which the old award ended if the earned income for that month, including any surplus earnings from the previous month, exceeds the relevant threshold.

Months 3, 4 and 5

Surplus earnings for the third, fourth and fifth month are to be calculated in the same way as for the second month.

(4) For the purposes of paragraph (3)—

(a) where, in the case of a joint claim, there is an old award for each claimant (because each of the claimants was previously entitled to universal credit as a single person or as a member of a different couple) the surplus earnings are to be calculated separately in accordance with paragraph (3) as if the claimant were a single person and if there is an amount of surplus earnings in relation to both old awards, both amounts are to be treated as earned income for the purposes of the new award; and

(b) if—

(i) a single claimant in relation to the new award was entitled to an old award as a joint claimant, or

(ii) if either of the joint claimants in relation to the new award was entitled to an old award as a member of a different couple,

the original surplus is to be apportioned in the first month so that the amount to be attributed to the claimant bears the same proportion to the whole of the original surplus as the claimant's earned income in the final assessment period of the old award bears to the total earned income in that assessment period;

(6) In this regulation—

"total earned income" is the earned income of the claimant or, if the claimant is a member of a couple, the couple's combined earned income, but does not include any amount a claimant would be treated as having by virtue of regulation 62 (the minimum income floor);

"the nil UC threshold" is the amount of total earned income at which there would be no entitlement to universal credit, expressed by the following formula—

$$(M - U) \times 100/65 + WA$$

Where—

M is the maximum amount of an award of universal credit;

U is unearned income;

WA is the work allowance (see regulation 22),

and, in determining those amounts in relation to the period between the termination of the old award and the commencement of the new award, the Secretary of State may make such assumptions as to the claimants circumstances as the Secretary of State considers appropriate;

"the relevant threshold" is the nil UC threshold plus £100.

Saving

4.—(1) These Regulations do not apply to an award of universal credit that has been made by virtue of any of the following orders—

(a) the Welfare Reform Act 2012 (Commencement No. 9 and Transitional and Transitory Provisions and Commencement No. 8 and Savings and Transitional Provisions (Amendment)) Order 2013(**a**);

(b) the Welfare Reform Act 2012 (Commencement No. 11 and Transitional and Transitory Provisions and Commencement No. 9 and Transitional and Transitory Provisions (Amendment)) Order 2013(**b**);

(c) the Welfare Reform Act 2012 (Commencement No. 13 and Transitional and Transitory Provisions) Order 2013(**c**);

(a) S.I. 2013/983 (C. 41).
(b) S.I. 2013/1511 (C. 60).
(c) S.I. 2013/2657 (C. 107).

(d) the Welfare Reform Act 2012 (Commencement No. 14 and Transitional and Transitory Provisions) Order 2013(**a**);

(e) the Welfare Reform Act 2012 (Commencement No. 16 and Transitional and Transitory Provisions) Order 2014(**b**);

(f) the Welfare Reform Act 2012 (Commencement No. 17 and Transitional and Transitory Provisions) Order 2014(**c**),

unless it is an award to which paragraph (2) applies.

(2) This paragraph applies to—

(a) an award made to members of a couple jointly as a consequence of a previous award having ended when the couple formed; or

(b) an award made to a single claimant as a consequence of a previous award having ended when the claimant ceased to be a member of a couple,

where either member of the couple in question was entitled to an award of universal credit that was made by virtue of *[commencement order for the digital service area]*.

Name
Address Parliamentary Under Secretary of State
Date Department

EXPLANATORY NOTE

(This note is not part of the Regulations)

(**a**) S.I. 2013/2846 (C. 114).
(**b**) S.I. 2014/209 (C. 7).
(**c**) S.I. 2014/1583 (C.61).

ISBN 978-1-4741-1543-8

9 781474 115438