CITY INTELLIGENCE

A cumulative impact assessment of tax and welfare reform in London

July 2019

Summary

Since 2010 there has been significant change in the tax and benefits system in England and Wales.

The period covered by this analysis has been one of significant fiscal retrenchment with a range of cost-saving measures introduced alongside tax cuts and measures to boost incomes.

The analysis in this report seeks to demonstrate the extent to which specific groups of Londoners have been affected by the cumulative impact of these changes over the period between 2010 and 2021-22 – the year by which the changes are anticipated to have fully taken effect.

Headline findings

As a result of the modelled changes:

Poorer Londoners will see their incomes reduce the most. Overall, the programme of changes is regressive – that is, poorer Londoners will experience a reduction in household income while richer Londoners will experience an increase. The hardest hit group are those Londoners in the second poorest 10% of households, who, by 2021-22, will be receiving £610 a year less than they otherwise would have been as a result of benefit changes – a 2.7% loss – mainly the four-year freeze to working-age benefits.

Households with children will lose the most of all household types – particularly those households headed by lone parents. This is a result of real-terms cuts to benefits received by parents such as child tax credits and child benefit. On average, lone parent households will receive £2,400 a year less by 2021-22 – an 8% loss – a result of the combination of the benefit cuts and the limited ability of lone parents to benefit from tax cuts due to their position on the income distribution.

Disabled households will lose out substantially. Households where someone is disabled will receive £1,910 a year less on average. Again, this is due to a combination of cuts to benefits that are directly targeted at disabled households, cuts to non-disability benefits, and the fact that disabled households are more likely to be lower on the income distribution.

MAYOR OF LONDON

Households with both children and a disabled person will be particularly affected due to a combination of the effects described above**.** Households in this group will receive £3,760 a year less on average by 2021-22 – a 9.8% loss.

People from London's black ethnic groups lose more than Asian or white groups. The poorest black Londoners will receive an average of £870 a year less by 2021-22 – a 5.3% loss – largely as a result of their position on the income distribution.

Women lose more than men. Depending on the approach used to model the impact of changes on families, women stand to lose up to an average of £600 a year, while men could gain as much as £470 a year.

London's renters will lose more than homeowners, with those renting in social housing losing the most (an average of £1,200 each year – a 4.4% loss).

Child poverty will be significantly higher in London. Some 100,000 more Londoners, 75,000 of whom will be children, will be in relative poverty after housing costs have been accounted for in 2021-22 compared to a scenario where the changes had not been made.

Conclusions

These findings highlight the importance of understanding the *cumulative* impact of policy and fiscal changes on the incomes of different household types and groups sharing protected characteristics[1].

In London – as with the rest of the country – the combined impact of the cost-saving and income-boosting measures has been for Londoners in the bottom half of the income distribution to experience a significant reduction in household incomes and those in the top half to experience an increase. Within this, there are specific groups – households with children, households with a disabled person, black households – that experience particularly significant losses.

Transparent analysis of the cumulative impact of future Budget and spending review decisions will enable a more informed and constructive debate on the impact of tax and benefit changes on people with protected characteristics.

[1] The following characteristics are defined in the Equality Act 2010: race, sex, disability, sexual orientation, gender reassignment, age, marriage or civil partnership, pregnancy and maternity, and religion or belief.

1 Introduction

Policy context

The analysis in this report examines the effect of welfare changes and government spending decisions including the Welfare Reform Act 2012, the Welfare Reform and Work Act 2016 and changes to the taxation system brought about by a number of finance bills, including changes made at the last two Autumn Budgets.

The **Welfare Reform Act 2012** introduced a number of measures, including:

- the introduction of Universal Credit to replace six legacy benefits: Income-based Jobseekers Allowance, Income-based Employment and Support Allowance, Housing Benefit, Child Tax Credit, Working Tax Credit and Income Support.
- capping the total amount of benefit that some households can claim ('the benefit cap').
- replacing Disability Living Allowance with the Personal Independence Payment.
- restrictions to Housing Benefit for social housing tenants ('the bedroom tax').
- increasing Local Housing Allowance rates by the Consumer Price Index, rather than being based on rent increases.
- replacing Council Tax Benefit with Local Authority designed Council Tax Reduction schemes.

The **Welfare Reform and Work Act 2016** enacted measures announced in the 2015 Budget to make a further £12 billion in welfare savings by 2019-20.

Measures introduced included:

- reducing the benefit cap from the equivalent of £26,000 a year to £20,000, or £23,000 in Greater London.
- a four-year freeze in certain social security benefits and tax credits for working-age people.
- limiting the amount of support provided by Child Tax Credit for families, and the child element of Universal Credit to a maximum of two children ('the two-child limit').
- cuts to disability benefits, including removing the work-related activity component in Employment and Support Allowance and the limited capability for work element in Universal Credit.
- reductions in social housing rents of 1% a year for four years.

In addition, a number of changes to Universal Credit that reduced its generosity were announced in 2016. These included lowering 'work allowances' (how much a person can earn before their benefits are reduced) and increasing the 'taper rate' (the rate at which benefits are reduced above the work allowance threshold). These changes were partially reversed in the October 2018 budget through increased work allowances and reduced taper rates, restoring some of the lost generosity from the earlier changes.

The tax system was also changed to reduce the amount of tax that people pay on their income by raising the **personal tax allowance** - the amount a person can earn before paying income tax. The coalition government's original target of increasing the personal tax allowance to £10,000 by 2015 was achieved in 2014. Since then, the personal tax allowance has steadily increased so that it now stands at £12,500.

People earning below this threshold do not pay income tax. **The higher rate threshold** of income tax – above which a person pays an income tax rate of 40% - was increased to £50,000 in 2019/20, a year ahead of the government's original commitment. Those earning more than £100,000 move into the next income tax bracket and lose the personal allowance at a rate of £1 for every £2 earned above £100,000. The effect of these tax changes is to reduce the amount of tax that people pay on their income, without changing the underlying rates of tax.

There have also been changes to the government's policy on incomes. The **National Living Wage** is an obligatory minimum wage payable to workers in the United Kingdom aged 25 or over. Coming into effect on 1 April 2016, the rate of the National Living Wage was set at a significantly higher level than the preceding National Minimum Wage. The aim of the policy is for the wage to reach 60% of median UK earnings by 2020 – estimated to be at least £9 an hour.[2]

Previous analysis and stakeholder responses

The changes detailed above represented a significant programme of change to the UK's tax and benefit systems. Some of the changes have the effect of reducing household incomes, others of increasing household incomes.

While budget announcements such as the changes referred to above are accompanied by Tax Information and Impact Notes (TIINs) which contain some equality impact assessment, these tend to be limited. A major limitation of many of these assessments is their failure to consider cumulative impacts across the range of changes. Numerous individual assessments have been published – with 70 impact assessments published as part of the two main welfare reform acts.

Several pieces of analysis have gone further in attempting to quantify the regional or local impact of different welfare changes. These tend to focus on the number of people affected, or the total loss of benefit income in different parts of the country as a result of individual policy changes[3].

Despite calls from organisations such as the **Women's Budget Group (WBG)** for more meaningful government equality impact assessments of *all* spending and taxation decisions, there has until recently been little analysis of the cumulative impact of changes to taxes and benefits. WBG and **Runnymede Trust's** 2016 analysis[4] highlighted how low-income black and Asian women had lost the most from tax and benefit changes since 2010.

More recently, the **Equality and Human Rights Commission (EHRC)** published a cumulative impact analysis of tax and benefit changes[5] in the context of the Public Sector Equality Duty, with a view to influencing the government's approach to future Spending Reviews and tax and spending decisions A key recommendation of that report was for the Treasury to extend its analysis of the combined impacts of tax and spending decisions across people sharing different protected characteristics.

Looking at the cumulative impact of benefit and tax changes is essential to understanding how different groups are affected by a programme of reforms, as well as how poverty rates may rise or fall. The

[2] The National Living Wage should not be confused with the Living Wage Foundation's official Living Wage, or the London Living Wage. The latter is a wage based on the cost of living and voluntarily paid by over 5,000 employers. It currently stands at £9 an hour, and £10.55 in London.
[3] Beatty and Fothergill (2016) The uneven impact of welfare reform
[4] WBG (2016) New research shows poverty, ethnicity & gender magnify the impact of austerity
[5] Reed and Portes (2018) The cumulative impact of tax and welfare reforms

analysis in this report applies the approach taken in the two reports listed above to London's population.

A note on methodology

To describe the way that tax and benefit changes have had different effects on richer and poorer Londoners, this report refers to 'income deciles' or 'quintiles' to describe households' position on an income distribution.

Each income decile represents 10% of the population arranged in order of increasing income. So those in the first, or bottom, income decile are those in the poorest 10%, whilst those in the 10th, or top, decile are those in the richest 10%. Similarly each income quintile represents 20% of the population arranged in order of increasing income.

To ensure the analysis in this document relates Londoners' situations to the wider society in which they live, it presents results according to London households' position in the national income distribution, rather than just the London income distribution[6].

Figure 1 below shows how the distribution of London households by income broadly mirrors the national distribution, other than at the very top.

Figure 1: Median annual net income by national income decile

National income decile	Median annual net income, before housing costs (UK)	Proportion of London households in this decile
1 (poorest)	£9,776	11%
2	£14,976	9%
3	£17,888	9%
4	£20,748	8%
5	£23,920	8%
6	£27,456	8%
7	£31,460	8%
8	£36,140	10%
9	£43,680	11%
10 (richest)	£62,608	18%

Source: Department for Work and Pensions (2019) Family Resources Survey: Financial Year 2016/17 and Landman Economics tax-transfer model using FRS pooled dataset 2013–14 to 2016–17

The charts in this report demonstrate the impact of tax, benefit and income changes by different combinations of household type, characteristic and position on the national income distribution. In all cases we present these against a hypothetical 2021-22 scenario in which none of the modelled changes took place.

The calculations in this report are based on the tax-transfer microsimulation model developed by Landman Economics in conjunction with the Institute for Public Policy Research.

There is a full methodology note in Appendix 1.

[6] This is in keeping with how analysis such as that based on the Indices of Multiple Deprivation is presented.

2 The distributional effect of tax and benefit changes on Londoners

Summary

This section examines how the changes to tax and benefits policy has affected poorer and richer households. The main findings are:

- overall the programme of tax, benefits and income policy changes implemented since 2010 has been regressive, with the impact of benefit changes on those with the lowest incomes far outweighing any boost to incomes provided by the increased personal allowance and the introduction of the National Living Wage.
- households in the second income decile (the second poorest 10%) are set to lose the most - an average of £610 a year by 2021-22.
- the four-year freeze to working-age benefits is the single measure that has had the biggest effect to reduce household incomes – amounting to an average loss of £380 a year for households in the second income decile.

The uneven impact of tax and benefit changes

The total anticipated savings resulting from the welfare benefit changes implemented since 2010 has been estimated at £27bn[7].

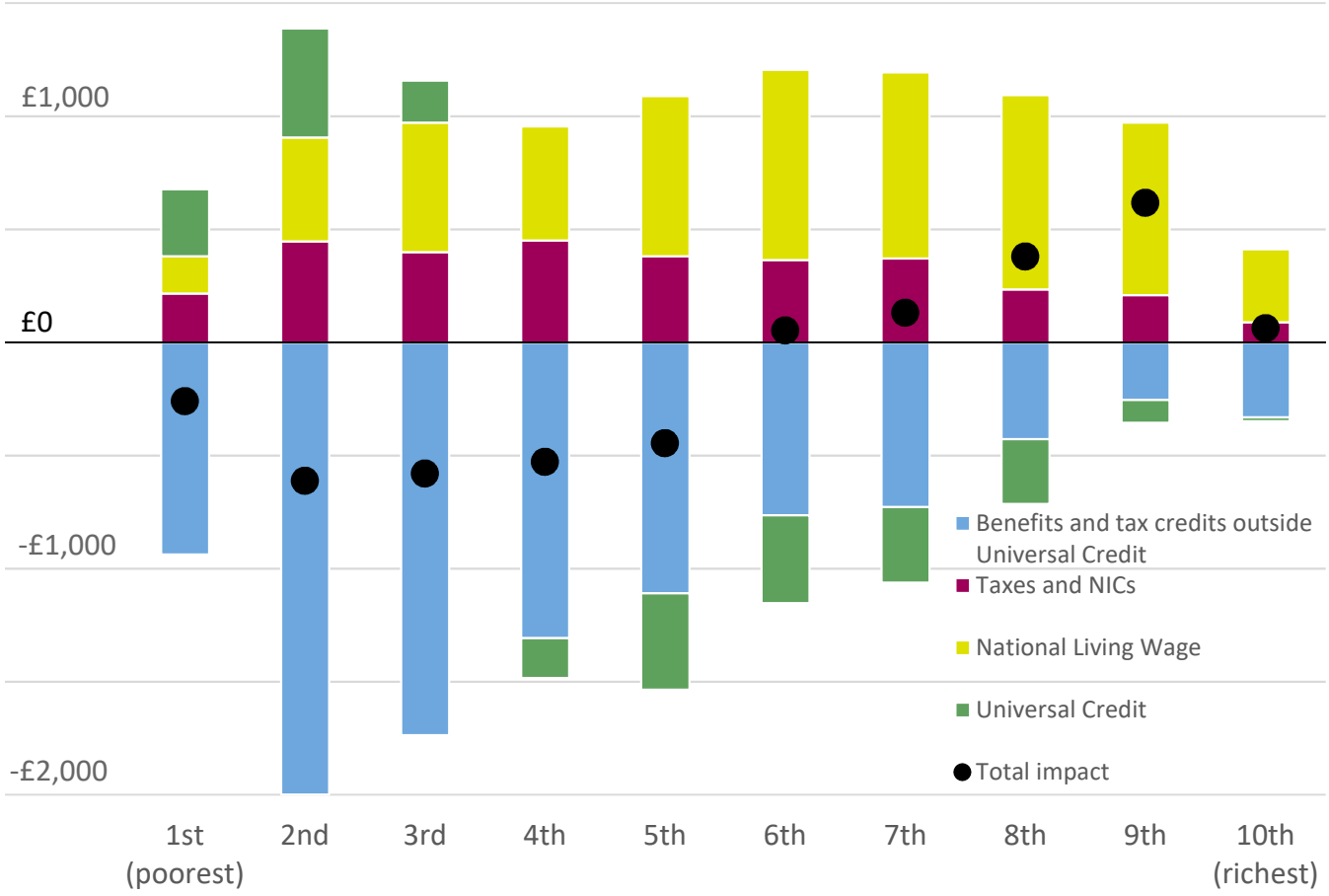
The results of this cumulative impact analysis show that the effects of this reduction in spending will not fall evenly across the population.

Figure 2 below shows the average annual cash impact of a number of individual changes[8] on households in London depending on their positions within the UK income distribution. The black line shows the cumulative impact, taking all changes together.

[7] Beatty and Fothergill (2016) The uneven impact of welfare reform

[8] The changes include those to welfare benefits and tax credit; to gross incomes through the minimum and National Living Wage); income taxes and National Insurance Contributions; and the additional impact of the introduction of Universal Credit.

Figure 2: Cash impact of tax and welfare changes and the introduction of the National Living Wage by household net income decile and type of reform, 2021-22 compared to a baseline 2021-22 scenario in which none of the modelled changes took place: London households



Note: Figures show average annual change in household net income (before housing costs) in 2018/19 prices
Source: Landman Economics tax-transfer model using FRS pooled dataset 2013–14 to 2016–17

The chart shows that Londoners in the bottom half of the income distribution will lose out overall, while those in the top half will gain.

The hardest hit will be those in the second-poorest group, losing an average of £610 a year – a 2.7% loss. As we go up the income distribution the losses get smaller, with those households in the richest 50% nationally expected to gain £210 a year on average as a result of the changes.

For households in the bottom three deciles – the poorest 30% – the loss of income expected through changes to benefits and tax credits (such as the benefit freeze) is greater than any boost to income they are expected to experience from changes to income tax and the introductions of Universal Credit and the National Living Wage.

Those households in the 4th income decile and upwards are expected to experience losses from the introduction of Universal Credit, as well as from changes to legacy benefits and tax credits. For those in

the 4th and 5th deciles these combined losses outweigh the gains expected from income tax changes, and from changes affecting gross incomes such as the introduction of the National Living Wage.

While tax changes, such as above-inflation increases in the tax-free personal allowance, were ostensibly made with a view to helping low to middle-income households by 'taking them out of tax', this positive impact is in fact smallest for households in the bottom decile, the poorest 10%. These people have, on average, lower taxable incomes and so are expected to gain less from reductions in tax rates or increases in tax bands.

The positive effect of the change increases as one moves up the income distribution until the highest income deciles, where the positive effect of the change begins to be lost as personal allowance is progressively withdrawn for earnings above £100,000 until it is removed altogether for those earning above £125,000.

Similarly, the impact of positive changes affecting gross incomes, such as the introduction of the National Living Wage, is felt across the income distribution (albeit to a lesser extent by those in the very lowest and highest income deciles), limiting its effectiveness as a measure targeted at those on the lowest incomes.

The impact of specific changes

Figure 3 below presents a summary of an analysis of individual reforms on London households.

Together, these changes account for around a third of the total modelled changes to welfare, in terms of financial impact. They are assessed across London households by their position in the UK income distribution.

Figure 3: Cash impact of selected welfare reforms by household net income decile, pre and post-Universal Credit implementation, 2021-22, compared to a baseline 2021-22 scenario in which none of the modelled changes took place: London households

	Poorest				Household income decile					Richest
	1	2	3	4	5	6	7	8	9	10
Benefit freeze	-£180	-£380	-£300	-£190	-£120	-£90	-£50	-£20	-£10	£0
Two-child limit	-£40	-£160	-£110	-£60	-£30	£0	-£10	£0	£0	£0
Work allowance changes	-£10	-£20	-£10	-£20	-£20	£0	£0	£0	£0	£0
Introduction of Personal Independence Payment	-£30	-£40	-£120	-£120	-£190	-£170	-£210	-£90	-£10	-£20
Bedroom tax	-£20	-£20	-£10	-£20	-£10	-£10	-£10	£0	£0	£0
Local Housing Allowance changes	-£20	-£80	-£60	-£50	-£40	-£20	-£10	-£10	£0	£0

Source: Landman Economics tax-transfer model using FRS pooled dataset 2013–14 to 2016–17

Figure 3 shows that, for households in the poorest 50% (deciles 1-5), the individual change that has the biggest impact on their incomes is the freeze to most working-age benefits. This change alone is

expected to reduce net incomes in the 2nd decile by an average of £380 a year. For households in the 3rd decile, it reduces incomes by an average of around £300.

Other changes with a significant effect include the two-child limit. Although this reform has a smaller average impact than the benefit freeze, it affects a smaller number of households to a much greater extent[9]. Not shown in figure 3 is the impact on households with three or more children (totalling around 150,000 households in London); irrespective of their position in the income distribution, the two-child limit is expected to reduce incomes within this group by over £840 a year on average.

There are similar, albeit smaller, effects arising from changes to disability benefits[10], the bedroom tax among social housing tenants, and the Local Housing Allowance changes among private renting households. While the impact of these changes across all households (as shown in figure 3) is relatively small, for those that are directly affected by them the losses are much more significant.

For example, while the annual cash impact of the bedroom tax on all London households in the bottom income decile is just £20, for London households in the social rented sector it is £39. For those that are actually affected by the bedroom tax it will be higher still – we know that London tenants affected by the bedroom tax have lost an average of £22 a week[11].

Following the decision to partially reverse cuts to the work allowances in Universal Credit at the October 2018 budget, the changes to allowances are expected to be small, reaching a maximum of £20 a year for households in the 2nd, 4th and 5th income deciles[12].

Commentary

Clearly, measures that reduce the real-terms value of welfare benefits will inevitably have the biggest effect on the incomes of those who are most reliant on welfare benefit payments. The analysis presented in this section demonstrates the scale of this effect, and the particular policies making the biggest contribution towards it.

Equally, the analysis confirms[13] that tax cuts are a poorly targeted measure for supporting low to middle-income households in London, with increases in the personal tax allowance disproportionately benefitting those at the top of the income distribution.

Following the decision to partially reverse the cuts to work allowances, the introduction of Universal Credit is now expected to have a positive impact on the incomes of Londoners in the poorest 20% of households, and to a lesser extent those in the next poorest 10% too.

[9] London is significantly affected by this policy. Recently published research shows London accounts for 16 of the top 100 most-affected Parliamentary constituencies. It also indicates that orthodox Jewish and Muslim households are disproportionately affected by the policy "due to strong cultural norms and deeply held religious beliefs that favour large families". London has large populations of both. See Sefton et al. (2019) All Kids Count: the impact of the two-child limit after two years

[10] This relates to the transfer of recipients of Disability Living Allowance onto its replacement benefit, Personal Independence Payment

[11] London Councils (accessed 2019) The Bedroom Tax

[12] Equivalent analysis conducted at the national level before the partial reversal of the cuts to work allowances showed that this change had the largest negative effects for households in the 2nd and 3rd income deciles. See Reed and Portes (2018) The cumulative impact of tax and welfare reforms

[13] Corlett, Whittaker and Kelly (2014) Missing the target: tax cuts and low to middle income Britain

The overall positive effect on incomes arising from the introduction of Universal Credit is partly as a result of take-up – by bringing together six benefits into one, more Londoners are expected to claim the benefits they are entitled to than is the case under the legacy benefit system. (Note – this analysis was unable to include a consideration of the impact of the technical issues and implementation errors that have characterised the roll out of Universal Credit and which have had particularly pronounced effects on low-income Londoners.[14])

However, the programme of welfare benefit changes implemented since 2010 negate the impact of this potentially positive outcome. People in London's poorest households will experience the biggest reductions in their incomes as a result of these changes. The income lost through benefit cuts easily outweighs any income gained from the government's tax changes, or changes to the National Living Wage.

[14] Work and Pensions Select Committee (2019) Universal Credit: tests for managed migration

3 The effect of tax and benefit changes on different demographic groups

Summary

The tax and benefit changes modelled in this analysis can have both direct and indirect effects, such as:

- direct effects occur when cuts are made to benefits that are specifically targeted at a certain group of household type – for example, disability benefits or child benefits.
- Indirect effects occur when certain groups or household types are more likely to be lower or higher on the income distribution and are therefore more or less exposed to cuts to public transfer payments and more or less able to benefit from tax cuts.

Where a household experiences both direct and indirect effects from the benefit changes, the scale of the cumulative impact is magnified. This accounts for the extremely high losses experienced by households with children where at least one member has a disability[15] (an average loss of £3,760 a year in 2021-22 compared to 2010) and lone parents (£2,410 a year on average).

The impact of tax and benefit changes on different groups of Londoners

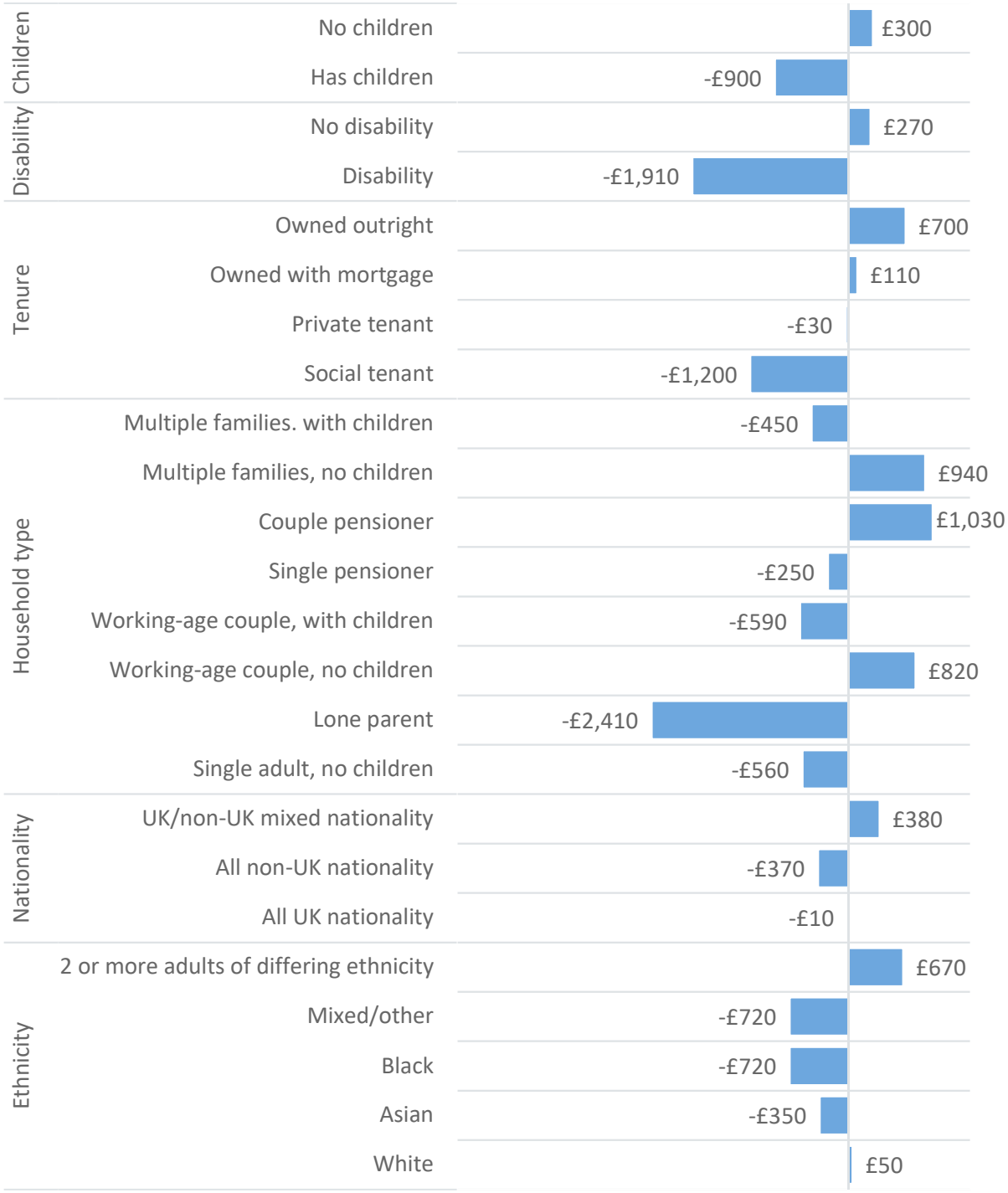
The previous section described how the programmes of tax and benefit changes was lowering the incomes of poorer London households whilst increasing those of richer households, and the contributions that specific policy changes will make towards that overall effect.

Within that overall picture, a number of specific demographic groups are set to experience particularly large reductions in their household income.

Figure 4 below shows how the overall cash impact of tax and welfare changes varies by household characteristics.

[15] This analysis defines disability as “a physical or mental impairment with a substantial and long-term adverse effect on a person's ability to carry out normal day-to-day activities”.

Figure 4: Cash impact of tax and welfare changes by household demographics, 2021-22, compared to a baseline 2021-22 scenario in which none of the modelled changes took place: London households



Source: Landman Economics tax-transfer model using FRS pooled dataset 2013–14 to 2016–17

Key results from this analysis include:

- **Disability -** households with one disabled person or more are expected to lose substantial amounts (on average £1,910 a year). Households with no disabled adults are expected to gain an average of £300.
- **Household composition -** lone parent households are expected to lose £2,410 a year on average, considerably more than other household types. For example, couple households with children are expected to lose, on average, almost £590.

Households with specific combinations of these two characteristics face particularly significant losses. For example, households with children and a disabled person are expected to lose £3,760 a year on average.

Further results include:

- **Tenure -** social housing tenants are expected to lose the most, on average £1,200 a year. Those who own a home outright or with a mortgage are expected to gain on average. Around half of social tenant households in London has a person with a disability, against one in five private tenants and a third of owner-occupiers.
- **Nationality -** households where all members are of non-UK nationality are expected to lose an average of £370 a year. This compares to an average loss of £10 among households where all members are UK nationals.
- **Ethnicity[16] -** those in the black or mixed/other ethnicity categories are expected to lose the most on average (£720 a year in both cases). Households where all adult members are of a white ethnic background are expected to gain £50 on average, and those with a mix of ethnic backgrounds among adult household members are expected to gain £670 on average.
- **Gender -** under virtually all scenarios, women lose more income from the changes compared with men – by as much as £600 a year in one scenario.

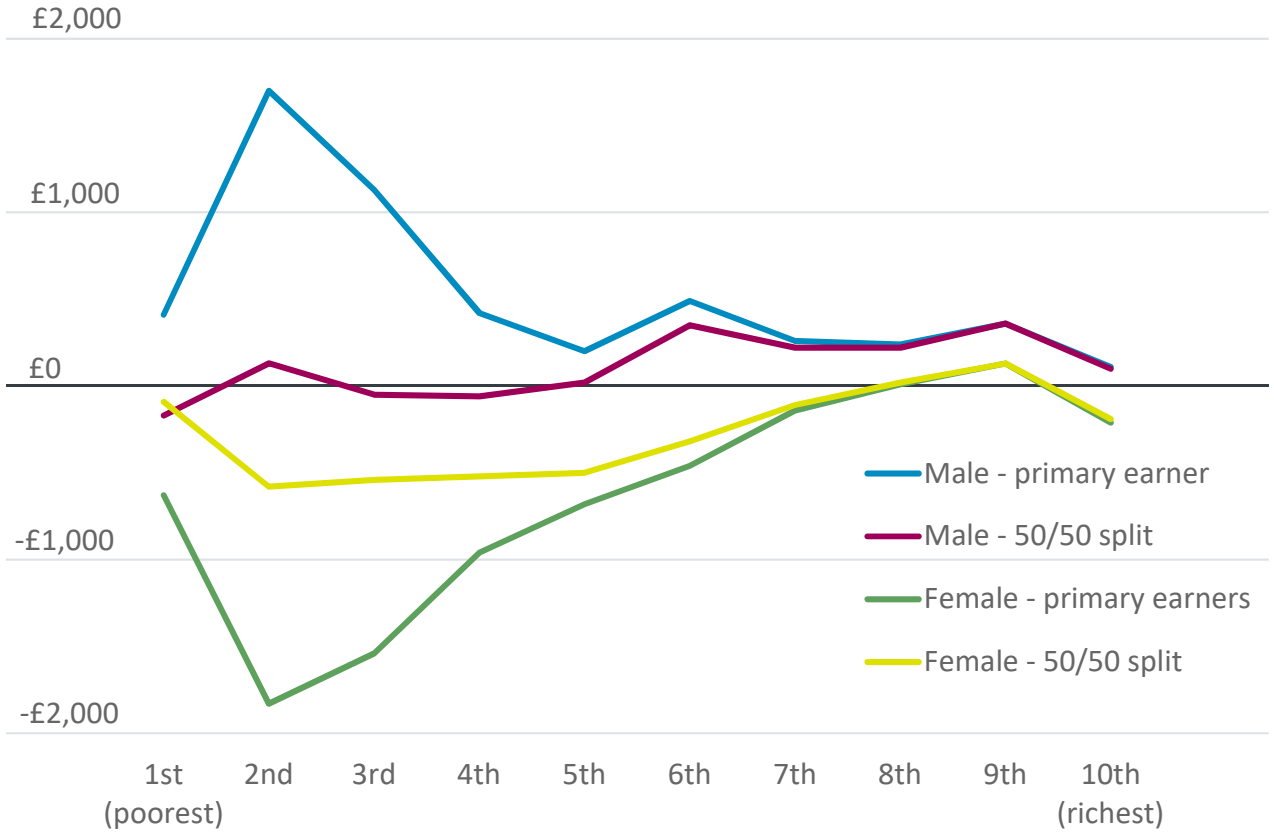
By modelling impacts at both an individual and household level, this analysis allows for an assessment of the impact of tax and welfare change by gender. Doing so demonstrates the way benefits are paid to households under Universal Credit can have a pronounced impact on women.

Under the current rules, couples must nominate a single bank account to receive payments. In most cases this forces them to choose which partner receives the payments.[17] The analysis models two scenarios for allocating Universal Credit - the first assumes the payment goes to the primary earner, the second assumes a 50/50 split (see figure 5 below).

[16] The modelling groups households into five ethnicity categories, including four categories where all adult household members are of either a white, Asian, black or mixed/other ethnic background. In addition, it models households with two or more adult members of differing ethnicities.

[17] Although couples are allowed to nominate a joint account.

Figure 5: Cash impact of tax and welfare changes by gender and household net income decile, 2021-22, compared to a baseline 2021-22 scenario in which none of the modelled changes took place and benefit income is split on a 50:50 basis: London households



Source: Landman Economics tax-transfer model using FRS pooled dataset 2013–14 to 2016–17

Overall, both scenarios lead to women losing out – an average loss of £600 a year in the primary earner scenario, and £250 a year in the 50/50 split scenario. Men gain an increase in income of £470 and £110 a year respectively.

This result holds across the income distribution: on average, men stand to gain more, or lose less than women, regardless of their income level.

The one exception is for individuals in the poorest 10% of households, in the hypothetical scenario under which benefit income is split on a 50:50 basis. This probably reflects a limitation in the hypothetical scenario being modelled – two-adult households in the bottom income decile are more likely to be single-earner households, and the single-earner is generally a man. Therefore an assumption that in these households benefit income is split on a 50:50 basis, would represent a hypothetical transfer of resources within the household that, when combined with the overall low-level of earning, leaves the woman in a comparatively better position.

Intersectional impact

In some cases, it is possible to assess the impact of tax and welfare changes on households by a combination of characteristics, for example, low-income households where members are of a particular ethnic background.

Figure 6: Cash impact of tax and welfare reforms by household characteristics and household net income quintile, 2021-22 tax year: London

		Household income quintile		
		1 (poorest)	2	3-5 (richest)
Ethnicity	White	-£260	-£580	£250
	Black	-£870	-£840	-£550
	Asian	-£530	-£390	-£220
Nationality	All UK nationality	-£160	-£830	£210
	All non-UK nationality	-£740	-£390	-£180
Age	18 to 34	-£150	-£90	£680
	35 to 44	-£680	-£850	-£450
	45 to 64	-£630	-£1,190	£140
	65+	-£190	-£160	£280
Tenure	Social tenant	-£1,100	-£1,430	-£1,120
	Private tenant	-£80	-£110	£10
	Owned with mortgage/outright	£10	£0	£510
Disability	No disability	-£300	£35	£500
	Disability	-£1,050	-£2,350	-£1,980
Children	No children	-£120	-£160	£520
	Children	-£970	-£1,080	-£790

Source: Landman Economics tax-transfer model using FRS pooled dataset 2013–14 to 2016–17

This analysis shows us that black London households stand to lose the most of any ethnic group from the changes, across the income distribution.

Looking at the results for households of different nationalities, we find that across household income quintiles average losses are greater for non-UK households than UK households, except in the second quintile where they are larger for UK households.

Two groups that lose out from changes regardless of their position on the income distribution are disabled households, those in social housing and, to a lesser extent, black and Asian households.

Households with a disabled person lose more throughout the income distribution than households with no disabled person.

Generally, social and private tenants are expected to lose out, whereas those households who own their home either outright or with a mortgage are expected to gain. Private tenants in the richest 40% of households are expected to gain, versus average losses among social tenants. (It should be noted there are relatively few social tenants in London in the richest 40% of households).

Commentary

Many of the cash losses being experienced by different groups will reflect the fact that those groups are more likely to be characterised by having lower household incomes and so more negatively affected as a result of deriving a greater proportion of their income from benefits and tax credits.

They will also, by definition, have lower taxable incomes and be less well placed to benefit from the increases in personal tax thresholds seen since 2010. In other words, the programme of tax and benefit changes has an indirect impact on the specific group in question.

Elsewhere, there will be groups experiencing losses as a direct result of the design or intention of a policy change – for example, the losses experienced by social housing tenants are a direct effect of the changes aimed at reducing expenditure on housing benefit. While it is not possible to disaggregate the cumulative impact of the tax and benefit changes on specific groups into direct and indirect components, we can begin to understand why some groups are affected more than others.

Figure 4 shows that **households with children** are more likely to be negatively affected by tax and benefit changes, and to a greater extent. Households with children have, on average, higher incomes than those with no children, as a range of benefits reflect the additional cost of children in eligibility calculations. Many of the changes that have been implemented to welfare since 2010 have directly affected the amount that can be claimed for children.

For example, child benefit has been limited to below-inflation increases for several years. Other changes such as the two-child limit and the benefit cap have an impact on larger families, who are more likely to be in receipt of a higher level of benefits and so more likely to be affected by the cap[18]. Among lone parent households the effects are compounded: as lone parents have lower incomes than couple families, rely more on benefits as a source of income, and are less likely to benefit from a more generous tax system.

Households with a disabled member are also more likely to be negatively affected by welfare changes. In particular, this negative impact observed across the income distribution highlights how these households – like lone parent households – are affected by tax and benefit changes both directly and

[18] The two-child limit will apply to any Universal Credit claim where a third or subsequent child is born after 6 April 2017.

indirectly. Disabled households derive a greater proportion of their income from benefits while also having lower taxable incomes. This leaves them more vulnerable to cuts in benefit income and less well placed to benefit from tax cuts. But a number of the major changes to welfare since 2010 have directly affected disability benefits, including the transfer from Disability Living Allowance to Personal Independence Payment.

Where a household contains both children and a disabled person, we observe an even greater effect.

For BAME groups and non-UK nationals, the cash impacts highlighted by this analysis are more likely to be indirect – relating to their positions on the income distribution and household structures. Around 30% of London's black, Asian and mixed/other households are located in the poorest 20% of households nationally, versus 16% of London's white households. In addition, 45% of London's black, Asian and mixed/other households have children, versus 26% of London's white households. Meanwhile, non-UK national households have lower average incomes and are slightly more likely to have children than UK national households.

The small sample sizes make it harder to draw meaningful conclusions about the cumulative effect of tax and benefit changes on specific ethnic groups. However, there do appear to be some meaningful trends. The larger losses that black London households experience beyond the bottom of the income distribution are likely to reflect different household characteristics.

For example, black households are generally younger than other ethnic groups[19]. This means they are likely to have lower earnings, are more likely to have children (and so have lost out from cuts to child benefits), and are less likely to contain pensioners (who have benefited from the triple lock on the state pension and protection of other pensioner benefits).

The disproportionate impact on **women** is likely due to several factors: more than 90% of lone parents in London are women[20]. Women's incomes are more than 25% lower on average than men. In addition, women are much more reliant on income from benefits and tax credits, equivalent to 24% of their net income on average, compared with 10% among men.

With couples required to nominate which bank account Universal Credit is paid to, in comparison to legacy benefits which were paid by default to the primary child carer (typically the woman), the two scenarios presented in this analysis demonstrate the significant potential for this reform to enable domestic financial abuse.

There is clear value in knowing what the cumulative impact of the government's tax and benefit changes is for different groups. As well as ensuring that policy makers are taking decisions fully appraised of the likely impact of those decisions, it helps to identify those groups that may need transitional protection or mitigating action.

[19] For example, 30% of black African Londoners – the most populous black group – are aged 15 or younger, and just 5% aged over 65. By comparison, 16% of white British Londoners are aged 15 or younger and 18% aged over 65; and for Indian Londoners – the most populous Asian group – 17% are younger than 15, and 12% older than 65. Source: GLA (2017) GLA Population and Household Projections.
[20] Source: GLA (2019) Equality, Diversity and Inclusion evidence base for London.

4 The effect of tax and benefit changes on poverty rates in London

Summary

This chapter examines the impact of tax and benefit changes on poverty rates. By 2022:

- The total number of Londoners in poverty in 2021-22 will be 100,000 higher than the projected level of 2.2 million without these changes.
- 75,000 of these will be children – increasing the child poverty rate in London by four percentage points to 42% from the projected baseline level of 39%.

Impact on child and adult poverty

Figure 7 below shows the projected effect of the changes by some of the different commonly used measures – a relative poverty measure based on a threshold of 60% of modelled median income in 2021-22, and an absolute poverty measure defined as 60% of the 2010/11 median income, increased in line with inflation. Both are presented on a before housing costs (BHC) and after housing costs (AHC) basis.

Figure 7: impact of tax and welfare changes on the number and rate of children in poverty, Before Housing Costs (BHC) and After Housing Costs (AHC)/relative and absolute measures, 2021-22 tax year: London

	BHC, relative poverty measure	BHC, absolute poverty measure	AHC, relative poverty measure	AHC, absolute poverty measure
Change in the number of adults in poverty	-25,000	25,000	25,000	25,000
Impact on adult poverty rate	**0%**	**0%**	**0%**	**0%**
Change in the number of children in poverty	50,000	75,000	75,000	75,000
Impact on the child poverty rate	**3%**	**4%**	**4%**	**4%**

Source: Landman Economics tax-transfer model using FRS pooled dataset 2013–14 to 2016–17

The most commonly used poverty measure is the AHC relative poverty measure[21], which calculates the proportion of people in poverty against a threshold defined by median UK household income levels once housing costs have been taken into account.

In the absence of the tax and benefit changes modelled in this analysis, the child poverty rate by this measure was projected to have reached 39% by 2021-22. The effect of the tax and benefit changes

[21] The relative poverty rate is based on the number of households with income equivalent to below 60% of the national median (midpoint), after housing costs have been taken into account. For example, for a couple with no children, the poverty level for 2017-18 equates to around £262 a week, counting all income and deducting taxes and basic housing costs.

modelled is to increase this rate to 42%. This equates to an increase in the total number of children living in poverty from 725,000 to 800,000.

We expect adult poverty to be relatively unchanged by the modelled changes, expecting it to either fall or rise by around 25,000 depending on the measure used. This will have a negligible impact on the adult poverty rate.

Commentary

Child poverty rates in London are already significantly higher than in the rest of the country once housing costs are taken into account – 700,000, or 37% of London's children currently live in poverty.

In the scenario whereby none of the government's tax and benefit changes had been implemented, those figures would still be expected to be higher – 725,000 children, or a 39% rate. The effect of the government's changes is to push these figures higher still, to 800,000 or 42%.

This impact is in addition to other drivers of poverty, including London's high housing costs, low pay and underemployment.

5 Conclusion

Under the Public Sector Equality Duty, all public bodies are obliged to have 'due regard' to the impact of their policies on groups that share a protected characteristic.

Assessing the impact of a whole fiscal event such as a Budget, or a set of related tax and benefit policies, is undoubtedly a complex task but as this analysis demonstrates, it can be done. As the Treasury Committee[22] and the Runnymede Trust and the Women's Budget Group[23] have previously noted, a deficiency of data in respect of some groups or protected characteristics is not a reason for failing to produce an analysis in respect of others for whom data is available.

Regular publication of equality impact assessments would also help prompt further consideration of where changes have direct and indirect impacts on specific groups – both are important.

The analysis in this report confirms that poorer Londoners are experiencing the largest reductions in their household incomes as a result of benefit changes, and which have not been sufficiently offset or mitigated by tax cuts or higher earnings.

In addition to revealing the scale of these losses of income – an average of £610 a year for the hardest hit group (those in the second poorest 10%) - it also demonstrates how the effect of the changes has also been felt particularly sharply by specific demographic groups, including those with protected characteristics under equalities legislation. These include:

- disabled households
- lone parent families
- certain BAME groups
- women
- social housing tenants

There is also a projected striking increase in child poverty rates in London - with an extra 100,000 Londoners in poverty by 2021-22, 75,000 of whom will be children.

A number of specific changes have contributed to these outcomes, through a range of direct and indirect effects, and with the four-year freeze to working-age benefits having the biggest impact. The findings here endorse the recommendations of the EHRC's 2018 report[24] that the level of welfare benefits should be reviewed to provide an adequate standard of living for the poorest households. Elements of the benefit system which should be included in any such review include the:

- working-age benefit freeze
- two-child limit
- reduced work allowances in UC
- social sector size criteria (the 'bedroom tax')
- reassessment of DLA claimants for PIP

[22] Treasury Committee (2019) Budget 2018
[23] WBR (2017) Intersecting Inequalities: The impact of austerity on Black and Minority Ethnic women in the UK
[24] Reed and Portes (2018) The cumulative impact of tax and welfare reforms

- the household benefit cap

This analysis highlights the value to policymakers of analysing the cumulative impact of a programme of policies or fiscal changes, and the impact of individual changes. The government should make more use of this approach at major fiscal events such as the Budget and the forthcoming spending review.

In addition, as a matter of good practice, impact assessments – both at the policy and programme level – should explore the impact of changes on those on low incomes who may not share a protected characteristic covered by legislation.

6 Methodology

The cumulative impact assessment in this report uses the tax-transfer model (TTM), a microsimulation model developed by the Institute for Public Policy Research, Landman Economics and the Resolution Foundation. The TTM uses data from the Family Resources Survey (FRS), a national survey of family and household incomes.

TTM projects the impact of policy changes in future years by estimating financial values observed in the FRS using existing projections of economic factors such as earnings, rents and inflation. It then applies the rules of the social security, income tax and national insurance system to calculate net incomes for every adult, family and household in the FRS.

By comparing household incomes under different scenarios for these rules, TTM helps us to understand the level of household incomes under different policy regimes. The baseline used throughout this analysis is the system pre-May 2010, with the level of means-tested benefits projected in line with inflation (using the Rossi index until May 2015, followed by CPI thereafter). A variety of policy scenarios, representing policy changes since May 2010, have been assessed against this baseline.

The sample size of London in any given year of the Family Resources Survey is small. Using single years does not therefore allow for detailed analysis of the impact of policy changes on sub-groups in London's population. To improve sample sizes, four years of the FRS have been combined in this analysis (2013/14 through to 2016/17), giving an overall sample size of 6,551 London households.

Changes that have been included in the modelling include changes to:

- income tax and National Insurance Contributions (NICs)
- means-tested and non-means-tested social security benefits
- tax credits
- the introduction of Universal Credit (UC)
- National Living Wage (NLW)

The impacts of these changes are assessed at the household and individual level, and across a range of characteristics, including:

- position within the UK household income distribution
- gender
- ethnicity
- nationality
- household composition
- housing tenure
- disability

Impacts assessed include changes in net income (both in cash terms and as a percentage of net income) and relative poverty. It is important to note that the modelling is static, taking no account of possible behavioural responses to changes to the tax and welfare system.

Detailed results are available in the accompanying data tables, including average age of household, number of children, disability scores, material deprivation among children and work status[25].

Measuring household income: deciles and quintiles

To assess how the impact of tax and welfare changes varies between poorer and richer households, this analysis ranks all households in the UK by their 'equivalised' net income. Equivalisation adjusts income to take account of household size and composition. This is important because larger households require more resources to achieve a similar standard of living, and adults tend to have higher living costs than children. Once income has been adjusted in this way, households with the same equivalised income can be regarded as having a similar standard of living.

All households are then divided into ten groups, or 'deciles', each containing the same number of households and with progressively higher equivalised net income. Households are similarly divided into five groups, or 'quintiles', again with equivalised net income rising from the 1st to the 5th quintiles.

Policies included in the analysis

The modelling of policies presented in this report builds on work by Landman economics for the Equality and Human Rights Commission, including the policies and assumptions detailed in their 2014 and 2018 UK-wide reports.[26]

This analysis adds modelling of several policy changes announced since the publication of the 2018 Equality and Human Rights Commission Report. These are:

Autumn budget 2017

- **council tax -** increasing the maximum empty homes premium to 100%
- **National Insurance Contributions -** maintaining Class 4 NICs at 9% and delaying the abolition of Class 2 NICs for one year (subsequently cancelled).
- **social rented sector -** cancelling the planned cap on local housing allowance in the social rented sector.

Autumn budget 2018

- **Universal Credit -** partially restoring the value of work allowances by £1,000 a year from April 2019.
- **Universal Credit -** extending the 12-month exemption from the minimum income floor from July 2019.

Other welfare changes

- **Personal Independent Payment -** reinstatement of the mobility component of PIP for some claimants.
- **Universal Credit -** reinstatement of the housing costs element for 18 to 21year-olds.

[25] Accompanying data tables are Available on the London Datastore

[26] See Reed and Portes (2014) Cumulative Impact Assessment: A Research Report by Landman Economics and the National Institute of Economic and Social Research (NIESR) for the Equality and Human Rights Commission and Reed and Portes (2018) The cumulative impact of tax and welfare reforms for a full description of the methodology and policies modelled in this report.

- **Universal Credit -** those with assets over £16,000 are ineligible, but those who are claiming tax credits will now have capital over £16,000 disregarded for 12 months after they move to Universal Credit.

In addition, Landman Economics have refined their modelling of changes to Local Housing Allowance (LHA) rates. The new method uses detailed information on how LHA rates vary between different areas of London to match respondents rent levels in the Family Resources Survey (FRS) to groups of broad rental market areas. This allows for the modelling to reflect how LHA rates have changed in more geographic detail than the method used previously.

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