



Families in an Age of Austerity:
January 2012

The Impact of Austerity Measures on Households with Children

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Studies

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Foreword from Katherine Rake Chief Executive of FPI

Last year, in January 2011, we raised concerns about the impact which the deficit reduction plan would have on family finances. This year we launch a major programme of research tracking the experiences of 'Families in an Age of Austerity', which will interrogate the impact of cutbacks on local services as well as exploring how fluctuations in household income are affecting family life. A key element of this programme sees us working in partnership with the Institute for Fiscal Studies (IFS) to analyse family income, poverty rates and the impact of tax and benefit changes on work incentives. This paper presents the results of their first detailed analysis across family types and it makes for sobering reading.

Not only do families face a challenging 2012, but looking further ahead we see evidence of more financial strain to come. This research confirms that families with children are shouldering a disproportionate burden, with the IFS finding that the median (middle) income among households with children is set to fall in real terms by 4.2% between 2010–11 and 2015–16: equivalent to an annual reduction in income of £1,250 for a couple with two children. This is significantly higher than the reduction in income among all households of 0.9 per cent (which is equivalent to a fall in income of £215 a year for a couple without children).

This disparity is largely driven by a package of benefit reforms which have affected families with children. As a result of the changes being introduced between January 2011 and April 2014 families are set to lose more than pensioner households and working-age households without children. Looking at the picture before the introduction of Universal Credit we see families with children lose just over 6% of their income, compared to just under 4% for all households and 3% for working age households without children. Pensioners lose less than 2% of their income. It is particularly notable that it is generally those families with the lowest incomes who are losing the most from the reforms. For example, non-working lone parents lose more than 12% of their income on average – equivalent to £2,000 per year. Such a steep drop for lone parents is of very real concern; in order to find work they will have to confront the dual challenges of finding a flexible job in a highly uncertain labour market and meeting the costs of childcare.

This research enables us to go much further than previously possible in pinpointing which groups of families are most affected and how. We see ample evidence that the cuts package will impact most on the least resilient types of family, with the IFS finding that the projected fall in income for families is greatest for those with three or more children, households with young children and those living in private rented accommodation. We are alarmed by the significant financial hit that families with children under 5 will face. Between 2010-11 and 2015-16, 500,000 more children will fall into absolute poverty, and 300,000 of these children will come from households where the youngest child is under five. Median income among this group is projected to fall by 4.9 per cent.

Larger families will also be hit hard, largely driven by the imposition of the cap on the total amount of benefit families can receive, which will be introduced in 2013–14. This has a marked consequence in terms of child poverty rates: 100,000 of the overall increase in absolute child poverty of 500,000 comes from families with four or more children. The IFS find indications of a related rise in poverty rates for Pakistani and Bangladeshi children (who

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tend to live in larger families), highlighting an increase of more than 5 percentage points in both the absolute and relative poverty rate.

We were keen to look beyond parents to include another vulnerable group in our analysis – that of carers. Here, we see another example of households which are often already experiencing financial strain losing more than other groups. The average loss from tax and benefit changes for households claiming carer's allowance is just over 6 per cent, compared to a loss of tax and benefits of around 4 per cent for all households.

We also felt it was important to understand how the introduction of Universal Credit could affect families in the years ahead. Although it is still too early to arrive at a definitive picture, this analysis gives us some important early indications. We are pleased to see that for many low income families, the introduction of Universal Credit will have protective effect on finances. However, as it will only be introduced from October 2013 (for new claimants) and from April 2014 (for existing claimants) we believe the Government should reflect on whether the right financial safeguards are in place to protect those vulnerable groups in the interim. This analysis also highlights some elements of the design of Universal Credit which could create unintended consequences. For example, the biggest winners from its introduction are currently single-earner couples, which means that the incentive for both members of a couple to undertake paid work rather than just one is weakened.

In summary, this research confirms that families are feeling the strain now - with the majority of the fall in income forecast by the IFS to occur during the current financial year of 2011-12. This means that action urgently needs to be taken to protect those at-risk groups identified in this analysis. In particular, those with young children should not be allowed to slide into poverty at such a critical stage of family life or we risk undermining other policies aiming to support families in the foundation years. Furthermore, in light of this new evidence on families with more than three children and those living in the private rental sector, we believe that the Government urgently needs to look again at the damaging impact of cuts to Local Housing Allowance and the Housing Benefit Cap.

Finally, we would like to thank James Browne and the IFS and for carrying out this in-depth analysis, which we hope will generate useful insight for policymakers, campaigners and those working on behalf of families. With our forthcoming programme of research we hope to continue to highlight the challenges facing families during this tough economic period, and to work to minimise the impact of austerity measures on the most vulnerable groups.



Katherine Rake
Chief Executive of the Family and Parenting Institute

Executive summary¹

- This paper examines the prospects for incomes and poverty rates among households with children between 2010 and 2015 and attempts to isolate the impact of tax and benefit changes on household incomes, and on the incentives for parents to do paid work and to increase their earnings slightly.
- We find that the median (middle) income among households with children is set to fall in real terms by 4.2% between 2010–11 and 2015–16. This is greater than the projected fall in overall median income for this period of 0.9%. Median income is projected to fall by more than 4.2% among families with three or more children, households with young children and those living in private rented accommodation, and less than 4.2% among single-child households, those whose youngest child is aged 11 or more and those who own their home outright.
- Relative child poverty is set to increase between 2010–11 and 2015–16 by around 400,000, and absolute child poverty (as defined in the Child Poverty Act (2010)) will increase between 2010–11 and 2015–16 by around 500,000. Again, poverty rates particularly increase among families with three or more children, households with younger children and those living in private rented accommodation, all of which are groups with above average levels of child poverty. As poverty rates particularly increase among large families, both the absolute and relative poverty rate among Pakistani and Bangladeshi children increases by more than 5 percentage points.
- Tax and benefit changes to be introduced during this period are one factor driving these trends. The cap on the total amount of benefit families can receive to be introduced in 2013–14 particularly impacts large families. Reforms such as the abolition of the baby element of the Child Tax Credit and the reduction in the generosity of the childcare component of the Working Tax Credit particularly affect families with younger children, and cuts to Local Housing Allowance only affect those in the private rented sector. Overall, low-income households with children, particularly non-working lone parent households, lose more as a percentage of income on average from tax and benefit changes to be introduced over this period than pensioners, those of working age without children and richer households with children.

¹ This research was authored by James Browne and funded by the Family and Parenting Institute. Co-funding from the ESRC Centre for the Microeconomic Analysis of Public Policy at IFS (RES-544-28-5001) is also gratefully acknowledged. The author would like to thank Carl Emmerson and Paul Johnson for comments on a previous draft.

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- The introduction of Universal Credit partly offsets these trends. The biggest winners from its introduction are single-earner couples. Households with children that are in rented accommodation particularly benefit from its introduction, so much so that once this is in place they will no longer lose more from these reforms, on average, than home owners. Poorer households with children (who also tend to have more children and younger children) also benefit from the additional expenditure. Existing claimants of benefits and tax credits will gradually be transferred to Universal Credit between April 2014 and March 2018.
- Tax and benefit changes introduced in 2011 on average weaken the incentive for those with children to undertake paid work but on average strengthen the incentive for those without children to undertake paid work. Reforms to tax credits increase the amount of benefit received if parents do not work, but reduce the amount of benefit received in work.
- The incentive for those in paid work to increase their earnings is also slightly weakened by these changes, particularly the increases in National Insurance contribution rates and the rate at which tax credits are withdrawn as incomes rise.
- Tax and benefit changes to be introduced in 2012–13 and 2013–14 do not significantly affect financial work incentives, except for those with large families, for whom the introduction of the benefit cap would significantly reduce the amount of benefit they would receive if they left paid work (meaning that the incentive for them to remain in paid work is significantly strengthened).
- The introduction of Universal Credit from October 2013 onwards will significantly strengthen the incentive for lone parents, and those in couples without a partner in paid work, to undertake paid work on average, but tends to weaken the incentive for both members of a couple to undertake paid work rather than just one. It also strengthens the incentive for lone parents, and those with children and a partner not in paid work, to increase their earnings slightly.

1. Introduction

In this paper, we consider the prospects for the living standards of households with children over the period from 2010 to 2015. We then analyse the impact of tax and benefit changes on these households' incomes and on parents' incentives to undertake paid work and to increase their earnings.

2. The prospects for income and poverty rates among families with children from 2011 to 2015

We begin by simulating child income poverty rates and changes in equivalised median (middle) income levels among different types of family from 2010 to 2015. The results in this section are consistent with the presentation on the prospects for living standards given at the IFS post-Autumn Statement conference on 30 November 2011, and the methodology is identical to that used in previous IFS research.² We incorporate the OBR macroeconomic forecasts given in the Economic and Fiscal Outlook published on 29 November 2011 and all tax and benefit policy announcements made in the Chancellor's Autumn Statement on the same day.³ We give results for both the relative and absolute measures of child poverty defined in the Child Poverty Act (2010), for which the government has legally-binding targets to reduce poverty by 2020. The relative child poverty measure gives the proportion of children living in households with less than 60% of the income of the median (middle) household, while the absolute poverty measure gives the number of children living in households with incomes less than a fixed threshold set at the level of the relative poverty line in 2010–11.

Tables 2.1–2.3 give relative and absolute poverty rates and changes in median income for families with children from 2010 to 2015 according to the number of children in the family.

² See R. Joyce (2011), 'What does yesterday's news mean for living standards?', presentation at IFS post-Autumn Statement Briefing, <http://www.ifs.org.uk/publications/5930> and M. Brewer, J. Browne and R. Joyce (2011), 'Child and Working Age Poverty from 2010 to 2020', IFS Commentary 124, <http://www.ifs.org.uk/publications/5711>.

³ See http://cdn.budgetresponsibility.independent.gov.uk/Autumn2011EFO_web_version138469072346.pdf.

Table 2.1: Relative child poverty rate by family size, 2010–2015

Number of children	Relative child poverty rate						Number of children in group, 2010 (millions)
	2010	2011	2012	2013	2014	2015	
1	17.3%	17.3%	17.7%	18.5%	18.9%	19.4%	3.5
2	16.1%	15.9%	16.6%	17.7%	18.2%	18.5%	5.8
3	23.3%	23.0%	24.6%	25.2%	26.1%	26.6%	2.5
4+	33.3%	31.0%	32.4%	37.1%	38.8%	39.5%	1.2
All	19.4%	19.0%	19.9%	21.1%	21.8%	22.3%	13.0
Number (millions)	2.5	2.5	2.6	2.8	2.9	3.0	13.0

Notes: Poverty line is 60% of median income. Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

Table 2.2: Absolute child poverty rate by family size, 2010–2015

Number of children	Absolute child poverty rate						Number of children in group, 2010 (millions)
	2010	2011	2012	2013	2014	2015	
1	17.3%	19.2%	19.4%	20.3%	20.1%	19.8%	3.5
2	16.1%	18.0%	19.2%	19.8%	19.2%	19.3%	5.8
3	23.3%	25.5%	27.2%	27.6%	27.6%	27.6%	2.5
4+	33.3%	34.7%	36.5%	41.1%	40.6%	41.8%	1.2
All	19.4%	21.3%	22.4%	23.4%	23.0%	23.1%	13.0
Number (millions)	2.5	2.8	2.9	3.1	3.0	3.1	13.0

Notes: Poverty line is 60% of median income in 2010–11. Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

Table 2.3: Changes in median income by family size, 2010–2015

Number of children	Change in median income on previous year					
	2011	2012	2013	2014	2015	Total
1	-3.4%	-1.4%	0.0%	1.1%	0.4%	-3.3%
2	-3.6%	-1.2%	-0.5%	1.0%	0.1%	-4.1%
3	-4.7%	-0.7%	-0.9%	0.0%	-0.6%	-6.8%
4+	-1.9%	-0.4%	-2.4%	0.5%	-1.0%	-5.2%
All households with children	-3.3%	-1.4%	-0.6%	1.0%	0.2%	-4.2%
All households	-3.1%	-0.4%	0.2%	1.5%	0.9%	-0.9%

Notes: Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

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We can see from Table 2.3 that equivalised median income among households with children is forecast to fall by 4.2% between 2010–11 and 2015–16. This is equivalent to an annual reduction in income of £1,250 for a couple with two children. This loss is greater than the fall in overall equivalised median income of 0.9%, which is equivalent to a reduction in income of around £215 a year for a couple without children. The majority of the fall in median income among households with children is forecast to have occurred during the current 2011–12 financial year, with incomes then continuing to fall in 2012–13 and 2013–14 before slowly recovering thereafter.

For all family types relative poverty rates fall in 2011–12 before increasing from then on. Poverty rates for larger families change by the largest magnitude over this period, presumably because these families are more highly concentrated around the poverty line, meaning that small changes in their incomes or the poverty line moves larger numbers of them into and out of poverty. Absolute poverty rates increase significantly in 2013–14 before stabilising thereafter. This increase is concentrated among households with four or more children (100,000 of the overall increase in absolute child poverty of 500,000 comes from this group despite less than 10% of children living in households with four or more children): as we can see from Table 2.3, these families see their incomes fall by the most in this year also. This is likely to be driven by the imposition of a cap on the total amount of benefits that can be received at £500 per week: as we shall see in section 3, this particularly affects large families.

Another interesting difference we note from Table 2.3 is that, whereas the incomes of smaller families start growing from 2014–15 onwards, those of larger families continue to stagnate. This is likely to be because of the position of these family types in the income distribution: smaller families are on average richer, and so the median family with one or two children receives a much greater proportion of their income from earnings rather than benefits than the median three- or four- child family. Therefore, when real earnings start to grow from 2014–15, the incomes of the median one- or two-child family grow more quickly than the incomes of the median three- or four-child family.

Tables 2.4–2.6 show the same analysis according to the age of the youngest child in the household.

Table 2.4: Relative child poverty rate by age of youngest child, 2010–2015

<i>Age of youngest child</i>	<i>Relative child poverty rate</i>						<i>Number of children in group, 2010 (millions)</i>
	<i>2010</i>	<i>2011</i>	<i>2012</i>	<i>2013</i>	<i>2014</i>	<i>2015</i>	
Under 5	20.7%	20.6%	22.0%	23.7%	24.3%	24.6%	5.8
5 to 10	18.4%	17.5%	18.0%	19.3%	19.9%	20.6%	4.4
11 to 18	18.2%	18.0%	18.3%	18.5%	19.2%	19.7%	2.9
All	19.4%	19.0%	19.9%	21.1%	21.8%	22.3%	13.0
Number (millions)	2.5	2.5	2.6	2.8	2.9	3.0	13.0

Notes: Poverty line is 60% of median income. Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

Table 2.5: Absolute child poverty rate by age of youngest child, 2010–2015

Age of youngest child	Absolute child poverty rate						Number of children in group, 2010 (millions)
	2010	2011	2012	2013	2014	2015	
Under 5	20.7%	23.3%	24.9%	26.3%	25.7%	25.5%	5.8
5 to 10	18.4%	19.6%	20.6%	21.5%	21.1%	21.6%	4.4
11 to 18	18.2%	19.7%	20.0%	20.2%	20.0%	20.1%	2.9
All	19.4%	21.3%	22.4%	23.4%	23.0%	23.1%	13.0
Number (millions)	2.5	2.8	2.9	3.1	3.0	3.1	13.0

Notes: Poverty line is 60% of median income in 2010–11. Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

Table 2.6: Changes in median income by age of youngest child, 2010–2015

Age of youngest child	Change in median income on previous year					
	2011	2012	2013	2014	2015	Total
Under 5	-3.5%	-1.3%	-0.6%	0.9%	-0.4%	-4.9%
5 to 10	-3.5%	-1.5%	-0.5%	0.8%	0.4%	-4.2%
11 to 18	-2.6%	-1.2%	0.5%	0.9%	0.7%	-1.8%
All households with children	-3.3%	-1.4%	-0.6%	1.0%	0.2%	-4.2%
All households	-3.1%	-0.4%	0.2%	1.5%	0.9%	-0.9%

Notes: Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

We see that households with young children tend to do worse than those where the youngest child is older over this period, both in terms of poverty rates and income. Indeed, of the 400,000 rise in relative child poverty over the period, 200,000 comes from households where the youngest child is under 5, and 300,000 of the 500,000 rise in absolute child poverty. It is likely that some of this is because households with younger children are larger on average, and we saw that larger families see their incomes fall by more than those of smaller families. Again, it is also likely that households without young children receive most of their income from earnings rather than benefits, and so when real earnings start to rise from 2014–15 onwards, the incomes of these households grow more strongly than the incomes of households with younger children who are more reliant on income from benefits.

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Tables 2.7–2.9 perform the same analysis by housing tenure.

Table 2.7: Relative child poverty rate by housing tenure, 2010–2015

Housing tenure	Relative child poverty rate						Number of children in group (millions)
	2010	2011	2012	2013	2014	2015	
Social rented	36.3%	34.0%	33.8%	38.3%	39.1%	40.5%	2.5
Private rented	25.3%	25.5%	30.5%	31.8%	33.4%	32.3%	1.8
Mortgaged	11.2%	11.1%	11.3%	11.6%	12.0%	12.3%	7.3
Own outright	24.2%	22.8%	22.9%	22.2%	22.5%	23.6%	1.4
All	19.4%	19.0%	19.9%	21.1%	21.8%	22.3%	13.0
Number (millions)	2.5	2.5	2.6	2.8	2.9	3.0	13.0

Notes: Poverty line is 60% of median income. Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

Table 2.8: Absolute child poverty rate by housing tenure, 2010–2015

Housing tenure	Absolute child poverty rate						Number of children in group (millions)
	2010	2011	2012	2013	2014	2015	
Social rented	36.3%	39.1%	39.9%	43.1%	41.8%	42.6%	2.5
Private rented	25.3%	29.0%	34.2%	35.3%	34.4%	33.6%	1.8
Mortgaged	11.2%	11.9%	12.4%	12.5%	12.7%	12.6%	7.3
Own outright	24.2%	25.1%	24.6%	24.6%	23.3%	24.2%	1.4
All	19.4%	21.3%	22.4%	23.4%	23.0%	23.1%	13.0
Number (millions)	2.5	2.8	2.9	3.1	3.0	3.1	13.0

Notes: Poverty line is 60% of median income in 2010–11. Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

Table 2.9: Changes in median income by housing tenure, 2010–2015

Housing tenure	Change in median income on previous year					
	2011	2012	2013	2014	2015	Total
Social rented	-2.2%	-0.5%	-1.7%	0.8%	-0.1%	-3.7%
Private rented	-3.8%	-3.2%	-1.0%	0.6%	1.0%	-6.5%
Mortgaged	-3.5%	-1.4%	-0.5%	0.8%	0.8%	-3.7%
Own outright	-2.2%	-0.4%	1.1%	2.4%	0.5%	1.4%
All households with children	-3.3%	-1.4%	-0.6%	1.0%	0.2%	-4.2%
All households	-3.1%	-0.4%	0.2%	1.5%	0.9%	-0.9%

Notes: Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

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The differences by housing tenure are largely driven by reforms to Housing Benefit that are being introduced between 2011 and 2013. Various reforms affecting the private rented sector are being gradually introduced in 2011–12, meaning that the full effect on incomes will not become apparent until 2012–13. Cuts to housing benefit for those deemed to be under-occupying social rented accommodation will be introduced in 2013–14. Therefore it is unsurprising that incomes fall the most and poverty rises the most for those in the private rented sector between 2010–11 and 2012–13, whereas in 2013–14, poverty rates increase and incomes fall for those in the social rented sector.

Those who own their home outright are a relatively small group among those with children, and are more reliant on income from savings than other groups. As interest rates rise from 2013–14 onwards, the income of this group grows particularly strongly, meaning that poverty rates are lower and incomes higher among this group at the end of the period than at the beginning.

Finally, in Tables 2.10–2.12 we perform the same analysis by ethnicity. The sample sizes for ethnic minority groups are not particularly large, so caution should be taken when interpreting these results, but we still find some interesting results. In particular, Pakistani and Bangladeshi families tend to be larger than average, and so it is unsurprising that their poverty rates rise by more than those of other groups in 2012–13 and thereafter. Also, mixed race, Black, Black British and Chinese families are much more likely to be in social rented accommodation, so it is unsurprising that poverty rates among this group increase by much more than among other groups in 2013–14.

Table 2.10: Relative child poverty rate by ethnicity, 2010–2015

<i>Ethnicity</i>	<i>Relative child poverty rate</i>						<i>Number of children in group, 2010 (millions)</i>
	<i>2010</i>	<i>2011</i>	<i>2012</i>	<i>2013</i>	<i>2014</i>	<i>2015</i>	
White	16.4%	16.3%	16.9%	18.1%	18.7%	19.0%	11.2
Mixed	27.8%	31.0%	28.8%	31.6%	33.6%	32.7%	0.2
Indian	22.0%	22.0%	22.5%	22.5%	22.7%	23.1%	0.3
Pakistani/Bangladeshi	49.2%	48.6%	51.6%	52.0%	52.3%	54.6%	0.6
Black or Black British	39.9%	36.3%	37.9%	39.7%	41.7%	43.8%	0.6
Chinese/Other	26.1%	21.9%	22.9%	28.0%	27.0%	26.5%	0.3
All	19.4%	19.0%	19.9%	21.1%	21.8%	22.3%	13.0
Number (millions)	2.5	2.5	2.6	2.8	2.9	3.0	13.0

Notes: Poverty line is 60% of median income. Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

Table 2.11: Absolute child poverty rate by ethnicity, 2010–2015

Ethnicity	Absolute child poverty rate						Number of children in group, 2010 (millions)
	2010	2011	2012	2013	2014	2015	
White	16.4%	18.3%	19.4%	20.2%	19.8%	19.8%	11.2
Mixed	27.8%	31.5%	33.2%	33.5%	33.6%	32.7%	0.2
Indian	22.0%	22.8%	23.2%	23.8%	23.7%	23.5%	0.3
Pakistani/Bangladeshi	49.2%	49.9%	54.4%	54.1%	54.3%	55.8%	0.6
Black or Black British	39.9%	42.1%	42.7%	44.3%	44.6%	45.6%	0.6
Chinese/Other	26.1%	27.2%	27.3%	32.1%	29.2%	28.1%	0.3
All	19.4%	21.3%	22.4%	23.4%	23.0%	23.1%	13.0
Number (millions)	2.5	2.8	2.9	3.1	3.0	3.1	13.0

Notes: Poverty line is 60% of median income in 2010–11. Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

Table 2.12: Changes in median income by ethnicity, 2010–2015

Ethnicity	Change in median income on previous year					
	2011	2012	2013	2014	2015	Total
White	-3.4%	-1.3%	-0.3%	0.9%	0.1%	-4.0%
Mixed	-3.7%	-4.3%	0.1%	0.9%	0.6%	-6.4%
Indian	-1.3%	-0.2%	-3.0%	0.5%	0.9%	-3.1%
Pakistani/Bangladeshi	-0.8%	-5.4%	0.0%	0.9%	0.8%	-4.5%
Black or Black British	-3.7%	-3.9%	-1.6%	3.7%	-1.0%	-6.5%
Chinese/Other	-5.5%	-0.4%	-0.5%	-0.6%	2.0%	-5.0%
All households with children	-3.3%	-1.4%	-0.6%	1.0%	0.2%	-4.2%
All households	-3.1%	-0.4%	0.2%	1.5%	0.9%	-0.9%

Notes: Years refer to financial years.

Source: Author's calculations based on Family Resources Survey 2008–09 using TAXBEN and methodology defined in Brewer, Browne and Joyce (2011).

In the next section we attempt to isolate the impact of tax and benefit reforms on household incomes, excluding other macroeconomic effects that affect household incomes.

3. The impact of tax and benefit reforms on household incomes

Previous IFS analysis of proposed tax and benefit reforms has shown that households with children lose the most on average from tax and benefit changes that are set to be introduced by April 2014 across the income distribution.⁴ This section extends previous analysis in several ways. First, we include measures announced by the Chancellor in his Autumn Statement on 29 November 2011. Second, we include a scenario where Universal Credit is fully in place in our analysis: the government intends to start moving claimants across from the current tax and benefit system to Universal Credit from April 2014, although this process will take four years to complete. Therefore, the true situation in 2014–15 will be somewhere in between the two scenarios we present here with and without Universal Credit (although, on average, somewhat closer to the scenario without Universal Credit in place).⁵ Third, we perform a more detailed analysis of the impacts of the reforms on households with children. We present analyses of the impacts of the reforms according to the number of children in the household and the age of the youngest child, and according to whether anyone in the household is claiming Carer's Allowance. It also examines the impact of tax and benefit changes on the incentives for individuals to do paid work according to whether they are single or in a couple, and if so whether their partner is in paid work and whether they are the higher earner in the couple, and according to the number of dependent children an individual has living with them.

We perform this analysis using the IFS tax and benefit microsimulation model, TAXBEN. Throughout, we do not allow tax and benefit reforms to change either households' behaviour or pre-tax prices in the economy. It is also far from clear that incorporating behavioural responses would make the distributional analysis a better guide to the impact on people's well-being, since (for example) the extra effort of working harder is a cost to the individual as well as bringing the benefit of extra earnings – otherwise they would presumably have chosen to work more even before the reform in question. Our assumption about not allowing pre-tax prices to alter in response to changes in tax and benefit reforms is clearly more plausible in some cases than in others: for example, retailers may not have fully passed on the increase in VAT that took effect in January 2011 and landlords may reduce rents in response to reductions in the generosity of Housing Benefit.

⁴ See, for example, J. Browne 'Personal tax and benefit changes', presentation at IFS post-Budget briefing, <http://www.ifs.org.uk/publications/5524>.

⁵ Note that in section 2 we do model the phase-in of Universal Credit explicitly, meaning that only some families receive Universal Credit in 2014–15 and more in 2015–16 and we also account for transitional protection for those who lose out from the introduction of Universal Credit.

The impact of austerity measures on households with children

The key tax and benefit measures affecting families with children that have already been implemented are as follows:

The income tax personal allowance increased by £1,000 in cash terms for the 2011–12 tax year;

- Increases in all National Insurance rates and increases in the thresholds at which employees' and employers' National Insurance start to be paid;
- An increase in the standard rate of VAT to 20%;
- Cuts to tax credits; in particular a three-year freeze in the basic and 30-hour elements of the Working Tax Credit, an increase in the rate at which tax credits are withdrawn as income rises, the abolition of the baby element of the Child Tax Credit and the withdrawal of the family element of the Child Tax Credit from £40,000 rather than £50,000. These are partly offset by an increase in the child element of the Child Tax Credit;
- Reductions in the maximum amounts of rent that can be claimed in Local Housing Allowance;
- A three-year freeze in Child Benefit rates; and
- The use of the Consumer Prices Index (CPI) to index benefit amounts each year rather than the Retail Price Index (RPI) or Rossi index.

Those to be introduced in 2012–13 include:

- A further increase in the income tax personal allowance above normal indexation;
- Reductions in contracted-out rebates in National Insurance;
- A further lowering of the point at which the family element of the Child Tax Credit starts to be withdrawn (it will be withdrawn as soon as the other elements are exhausted rather than at £40,000 as it is currently);
- An increase in the number of hours couples with children need to work to be eligible for the Working Tax Credit from 16 to 24;
- Changes to the way in which tax credit awards are recalculated when a family's income changes during the year which make the system less generous to such families;
- The withdrawal of child benefit from families containing a higher-rate taxpayer from January 2013; and
- Time-limiting contributory Employment and Support Allowance for those in the Work-Related Activity Group.

Note that freezes in some benefit rates and changes in the indexation method for benefits that started in 2011 will continue in 2012 and in later years and therefore have a larger effect as time goes on.

The tax and benefit changes to be introduced in 2013–14 or 2014–15 that affect families with children include:

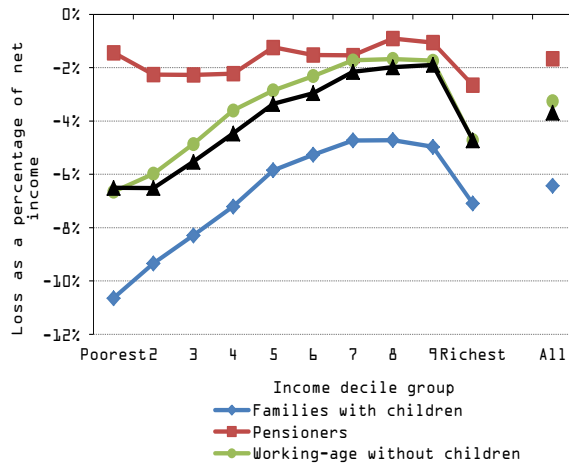
- The localisation of Council Tax Benefit accompanied by a 10% fall in expenditure. We assume that this is implemented by councils means-testing the benefit more aggressively. We do not take into account the Government's recent announcement that pensioners will not lose out from this change; therefore our results show a loss for pensioners that is slightly too large and a loss for those of working age that is slightly too small.
- A medical reassessment of Disability Living Allowance claimants that is forecast to reduce the caseload by 20%.
- As discussed above, existing claimants of benefits and tax credits will start to be transferred to Universal Credit from April 2014. We present two scenarios in our analysis below; one in which Universal Credit is not introduced and a second in which Universal Credit is fully in place.⁶ The variant of Universal Credit we use is that discussed in the Government's White Paper '21st Century Welfare', meaning that we assume Council Tax Benefit is included within Universal Credit whereas in fact it will remain as a separate benefit; this is because it is not clear how the replacement for Council Tax Benefit will operate. We do however incorporate the Government's more recent announcement on how childcare subsidies will be included within Universal Credit. We ignore Free School Meals in our analysis of Universal Credit, effectively assuming that families who receive Free School Meals in the current tax and benefit system continue to do so when Universal Credit is introduced.

Results

Figures 1a and 1b show the average losses from tax and benefit changes to be introduced between 2010 and 2014 for households with children, pensioner households and working aged households without children at different parts of the income distribution, under the scenarios with and without Universal Credit being introduced. The true situation in 2014–15 will be somewhere in between these two scenarios, although as Universal Credit is being phased in over four years from April 2014 for existing claimants of benefits and tax credits it will be, on average, somewhat closer to the scenario without the Universal Credit in place (i.e. Figure 1a).

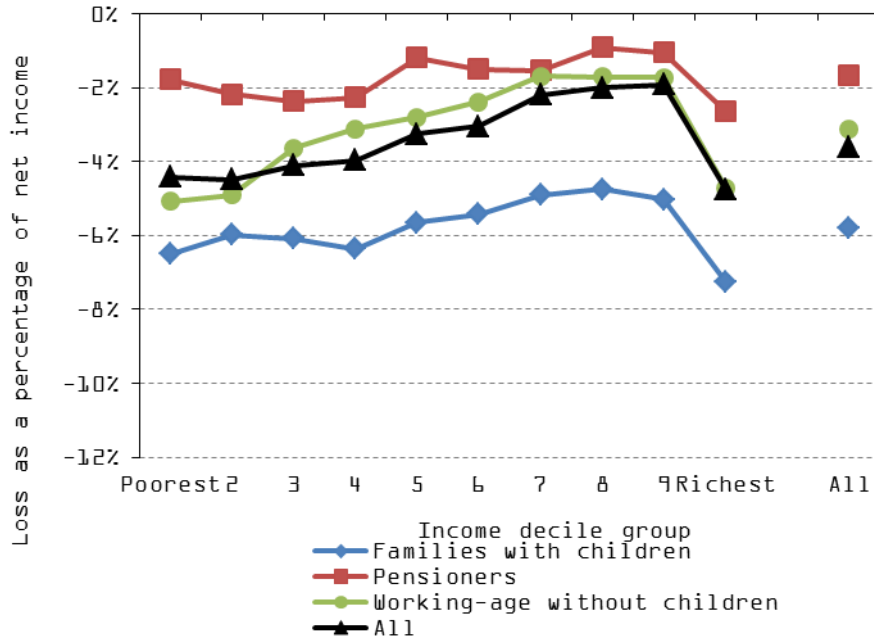
⁶ For more on Universal Credit, see M. Brewer, J. Browne and W. Jin (2011), 'Universal Credit: a preliminary analysis', IFS Briefing Note 116, <http://www.ifs.org.uk/publications/5415>.

Figure 3.1a: Losses from tax and benefit changes to be introduced between January 2011 and April 2014 by income decile group and household type, without Universal Credit



Notes: Income decile groups are derived by dividing all households into ten equal-sized groups according to income adjusted for household size using the McClements equivalence scale. Decile group 1 contains the poorest tenth of the population, decile group 2 the second poorest, and so on up to decile group 10, which contains the richest tenth. Assumes increases in employer NICs are passed on to employees in the form of lower wages. Assumes councils means-test council tax benefit more aggressively when it is localised. Does not include impact of Universal Credit in 2014–15. Source: Author’s calculations using the IFS tax and benefit microsimulation model, TAXBEN run on uprated data from the 2008–09 Family Resources Survey and 2008 Expenditure and Food Survey.

Figure 3.1b: Losses from tax and benefit changes to be introduced between January 2011 and April 2014 by income decile group and household type, with Universal Credit



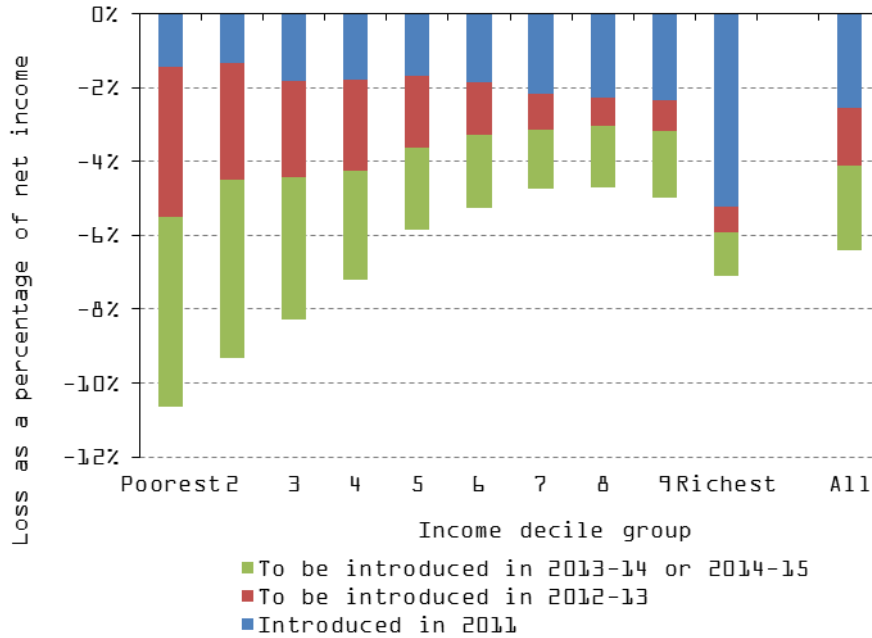
Notes: As Figure 3.1a, but assumes Universal Credit fully in place in 2014–15.

Source: As Figure 3.1a.

We can see that families with children lose more than pensioner households and working-age households without children across the income distribution, irrespective of whether we take Universal Credit into account. Benefits for pensioners have not been significantly affected by the cuts affecting those of working age and pensioners do not pay National Insurance Contributions, meaning that they are the least affected group across the income distribution. As well as pensioners, those without children in the upper-middle of the income distribution lose the least as a percentage of income from these changes. This is because this group is unaffected by welfare cuts and gains the most from policies such as increasing the income tax personal allowance. By comparing the two figures, we can also observe that it is low-income working-age families that gain the most from the introduction of Universal Credit.

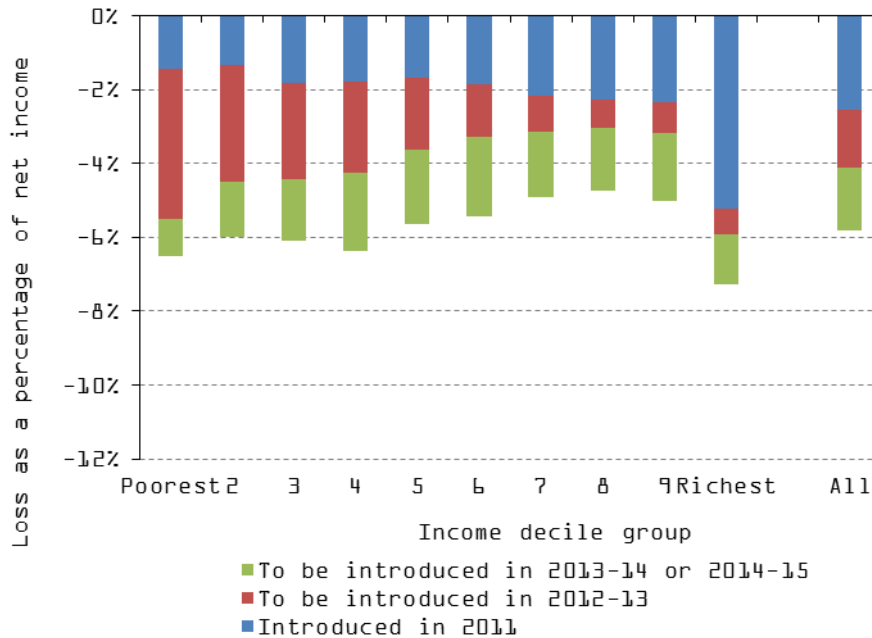
In Figures 3.2a and 3.2b, we break down these losses for families with children in different income deciles into those arising from tax and benefit changes already introduced in 2011, those to be introduced in 2012–13 and those to be introduced by 2014–15.

Figure 3.2a: Losses from tax and benefit changes for households with children across the income distribution arising from tax and benefit changes to be introduced between January 2011 and April 2014, without Universal Credit



Notes and sources: As for Figure 3.1a.

Figure 3.2b: Losses from tax and benefit changes for households with children across the income distribution arising from tax and benefit changes to be introduced between January 2011 and April 2014, with Universal Credit



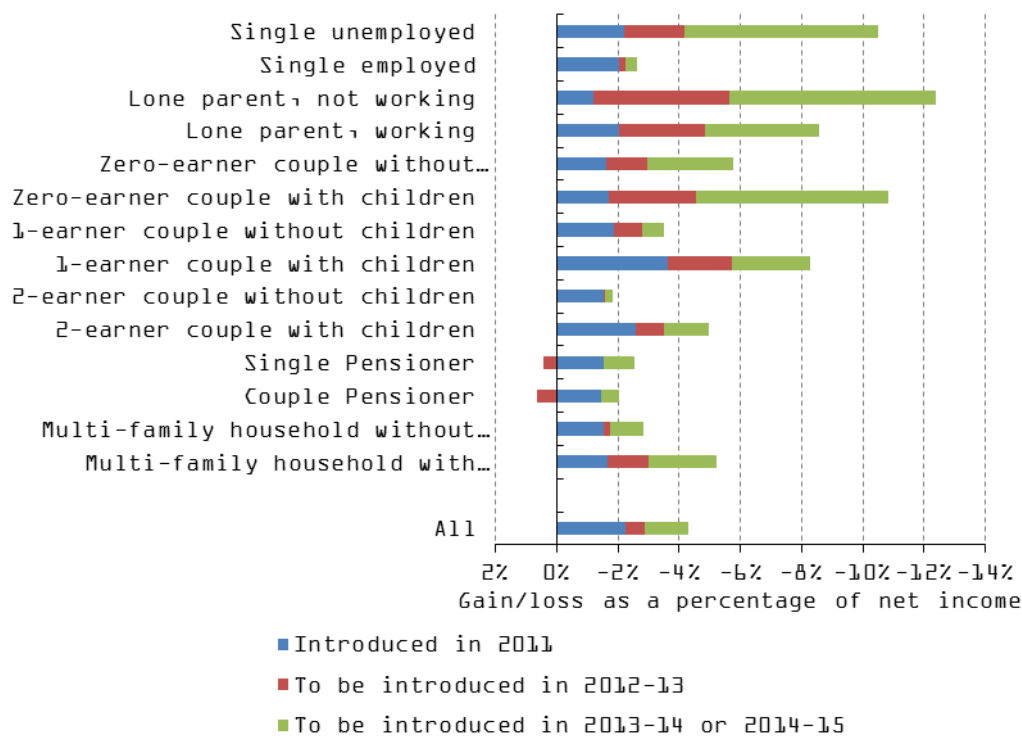
Notes and sources: As for Figure 3.1b.

The impact of austerity measures on households with children

We can see from Figures 3.2a and 3.2b that most of the tax rises that affect higher income households with children have already been introduced in 2011. However, most of the benefit cuts that affect poorer households are yet to be introduced, though at least some of these will be effectively reversed when Universal Credit is introduced. In particular, the shift to CPI-uprating of most benefits has an increasing effect on the incomes of lower-income households as time goes on.

To complement this analysis, we show the impact according to different types of household. We see that those household types with children that tend to have lower incomes (in particular non-working lone parents, who lose more than 12% of their income on average or £2,000 per year, and workless couples with children) lose the most from reforms to be introduced from 2012–13 onward, in line with the results shown in Figures 3.2a and 3.2b above. By comparing Figures 3.3a and 3.3b we can see that it is single-earner couples (both with and without children) who gain the most from the introduction of Universal Credit.

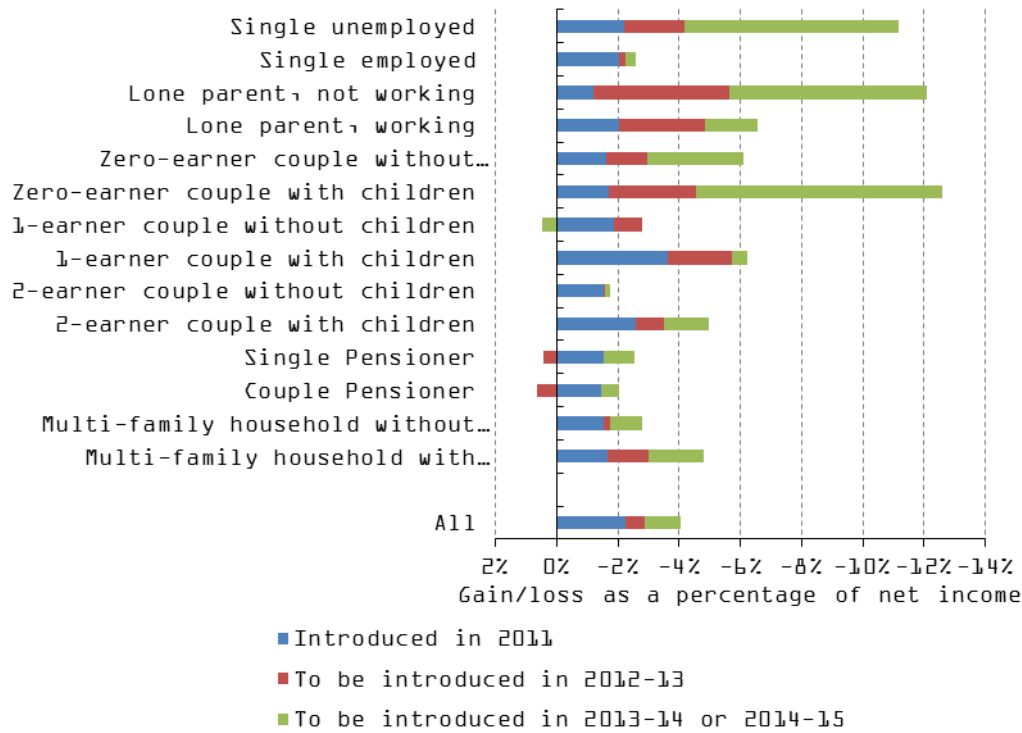
Figure 3.3a: Losses from tax and benefit changes for different household types arising from tax and benefit changes to be introduced between January 2011 and April 2014, without Universal Credit



Notes: Assumes increases in employer NICs are passed on to employees in the form of lower wages. Assumes councils means-test council tax benefit more aggressively when it is localised. Does not include impact of Universal Credit in 2014–15.

Source: Author's calculations using the IFS tax and benefit microsimulation model, TAXBEN run on uprated data from the 2008–09 Family Resources Survey and 2009 Living Costs and Food Survey.

Figure 3.3b: Losses from tax and benefit changes for different household types arising from tax and benefit changes to be introduced between January 2011 and April 2014, with Universal Credit



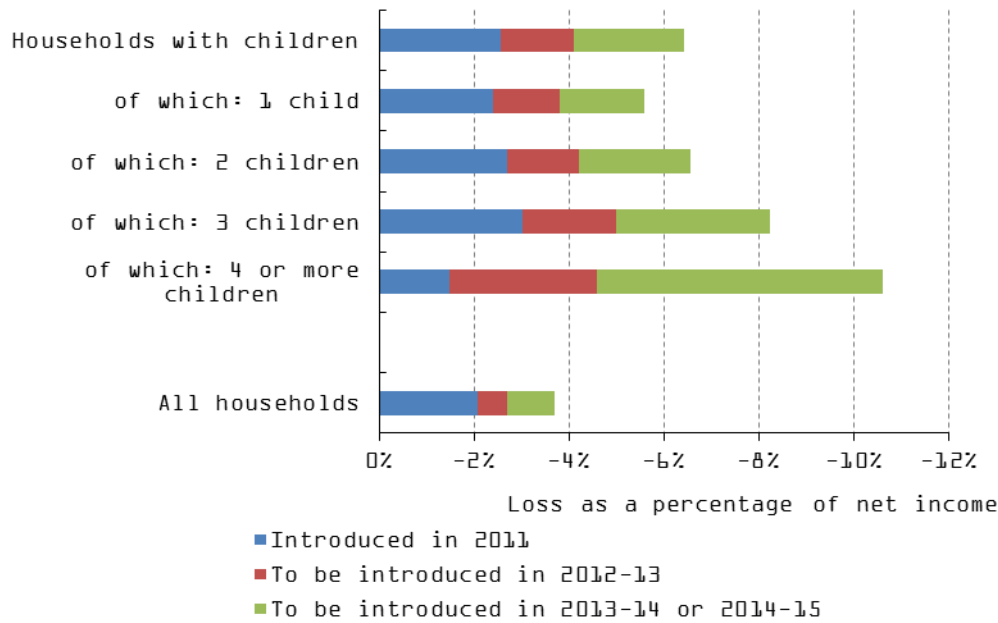
Notes: Assumes increases in employer NICs are passed on to employees in the form of lower wages. Assumes councils means-test council tax benefit more aggressively when it is localised. Assumes Universal Credit fully in place in 2014–15.

Source: Author’s calculations using the IFS tax and benefit microsimulation model, TAXBEN run on uprated data from the 2008–09 Family Resources Survey and 2009 Living Costs and Food Survey.

The impact of austerity measures on households with children

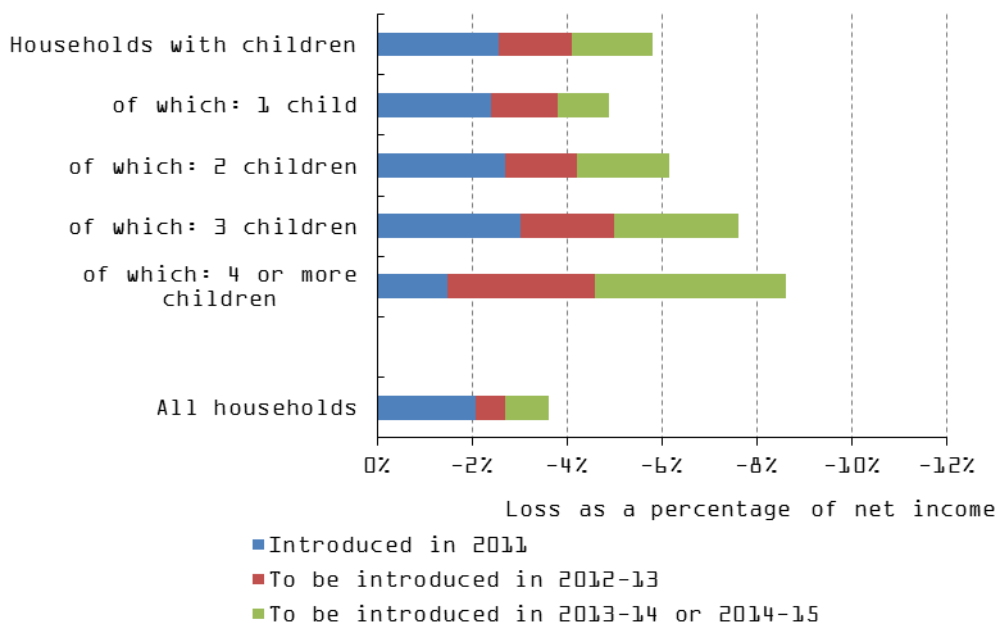
We now go on to investigate how the impact of tax and benefit changes varies according to the number of children in a household, the age of the youngest child, whether the household contains anyone claiming carers allowance and the housing tenure.

Figure 3.4a: Average loss from tax and benefit changes to be introduced between January 2011 and April 2014 for households with children by number of children, without Universal Credit



Notes and sources: As for Figure 3.3a.

Figure 3.4b: Average loss from tax and benefit changes to be introduced between January 2011 and April 2014 for households with children by number of children, with Universal Credit



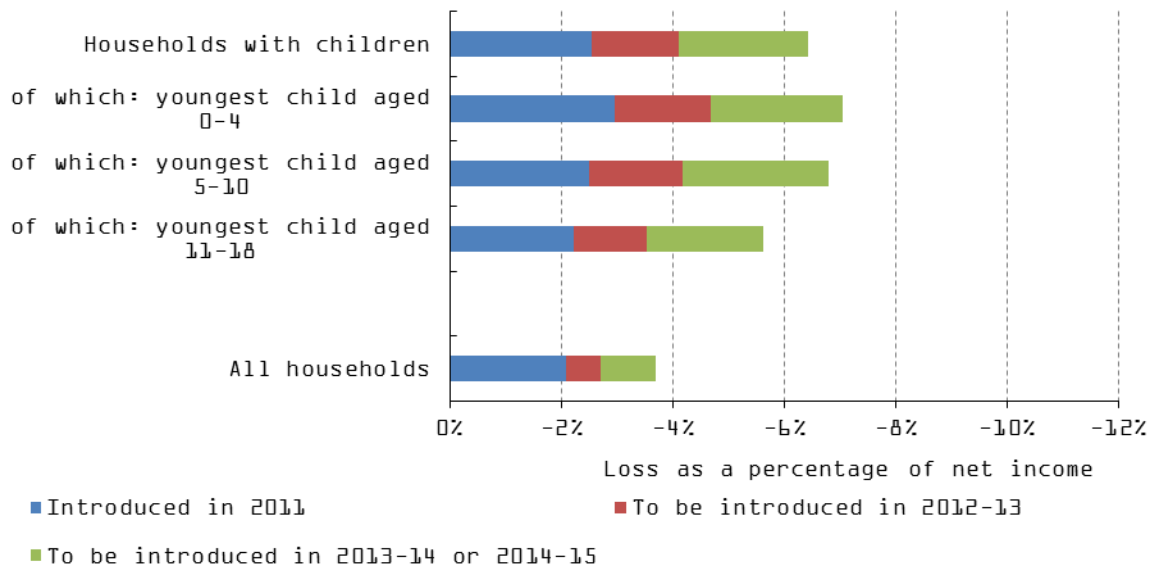
Notes and sources: As for Figure 3.3b.

The impact of austerity measures on households with children

Figures 3.2a and 3.2b showed that the richest households with children have lost most from the tax and benefit changes that have been introduced in 2011. Since (in our data) these households are disproportionately likely to have two or three children, it is households with two or three children that have lost most from these changes. By contrast, households with four or more children have lost the least: this is both because they are the least likely to be among the richest households and because these families gain the most from the increase in the per-child element of the Child Tax Credit. Similarly, as these large families are more likely to be in the lower income groups, they are most reliant on benefits and so lose the most from the welfare cuts that are due to be introduced between 2012–13 and 2014–15, in particular the benefit cap that is set to be introduced in 2013–14. Again, Universal Credit will somewhat lessen the impact in the long run, particularly for larger families who are most likely to be entitled to means-tested benefits and tax credits in the first place, and hence most likely to benefit from the increased generosity of Universal Credit.

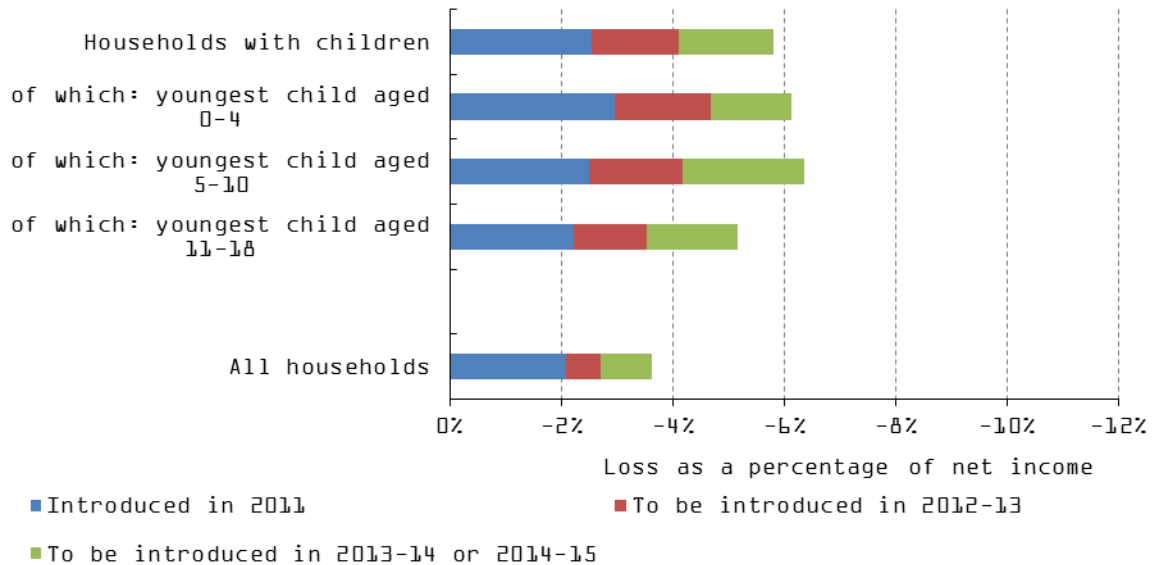
In Figures 3.5a and 3.5b we consider the impact of tax and benefit reforms on households with children according to the age of the youngest child in the household.

Figure 3.5a: Average loss from tax and benefit changes to be introduced between January 2011 and April 2014 for households with children by number of children, without Universal Credit



Notes and sources: As for Figure 3.3a.

Figure 3.5b: Average loss from tax and benefit changes to be introduced between January 2011 and April 2014 for households with children by number of children, with Universal Credit



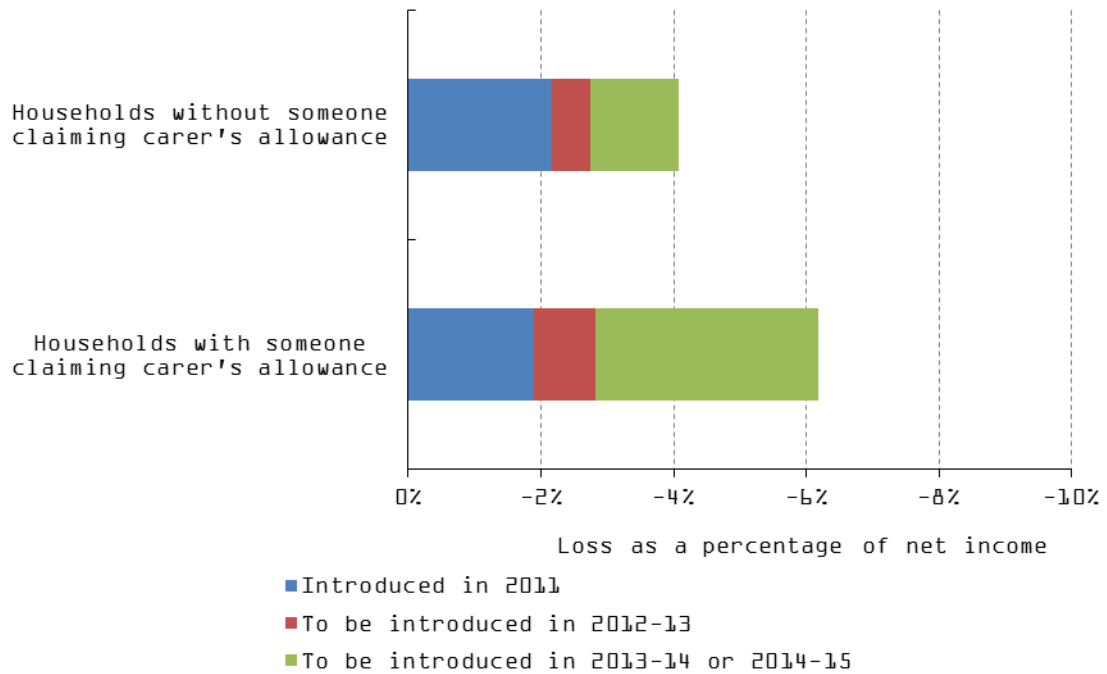
Notes and sources: As for Figure 3.3b.

There is less difference in the impact of the reforms by the age of the youngest child in the household. Two changes were introduced in April 2011 that particularly affected those with new-borns, namely the abolition of the baby element of tax credits and the restriction of the Sure Start Maternity Grant to the first child, so it is unsurprising to see that households with younger children lose more from these changes. Furthermore, households with older children are less likely to use childcare and so lose less on average from the reduction in the generosity of the childcare element of the Working Tax Credit as of April 2011.

More generally, Figures 3.3a and 3.3b showed that two-earner couples with children lose less as a percentage of income than other types of household with children from the welfare cuts being implemented in 2013–14 and 2014–15. As households with older children are more likely to have two earners rather than one, they lose the least from the tax and benefit changes to be introduced in 2013–14 or 2014–15.

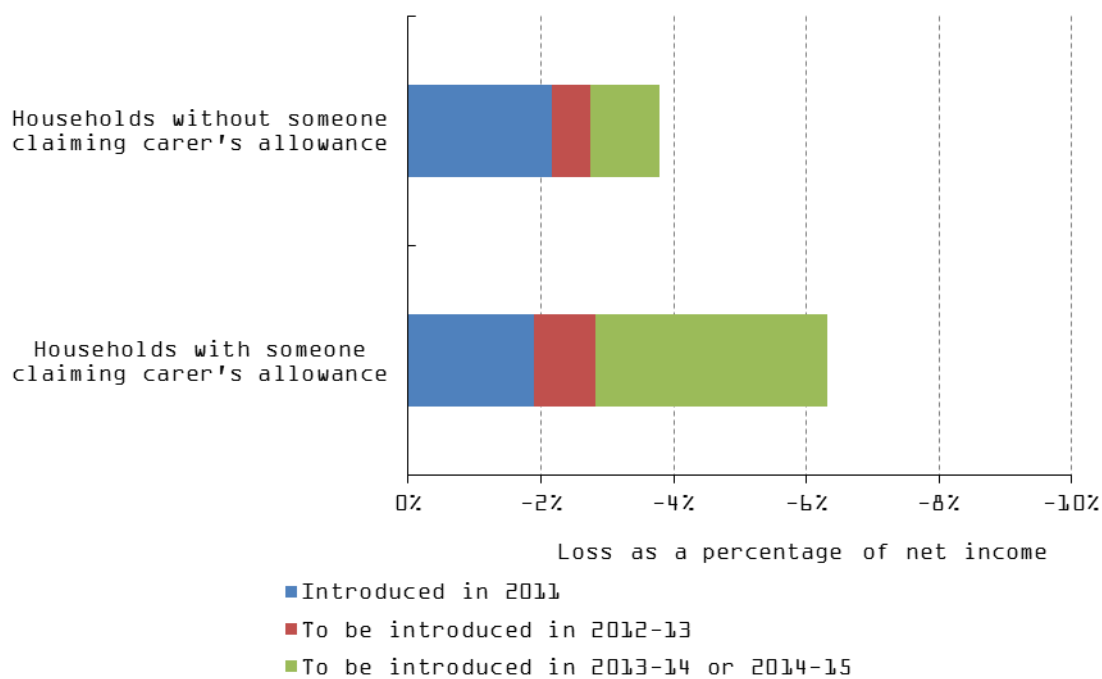
Figures 3.6a and 3.6b we show the impact of the tax and benefit changes on households where someone is claiming carer’s allowance. We see that those households containing a claimant of carer’s allowance lose less, on average, from the tax and benefit changes that have already been introduced in 2011, but lose more from those to be introduced in 2012–13 and thereafter. It is likely that it is the time-limiting of contributory ESA for the Work-Related Activity Group and the new disability test for Disability Living Allowance that is causing this difference: those claiming carer’s allowance often have caring responsibilities for others in their household claiming these benefits. Universal Credit does little to alter this picture.

Figure 3.6a: Average loss from tax and benefit changes to be introduced between January 2011 and April 2014 for households claiming carer's allowance and those not claiming carer's allowance, without Universal Credit



Notes and sources: As for Figure 3.3a.

Figure 3.6b: Average loss from tax and benefit changes to be introduced between January 2011 and April 2014 for households claiming carer's allowance and those not claiming carer's allowance, with Universal Credit

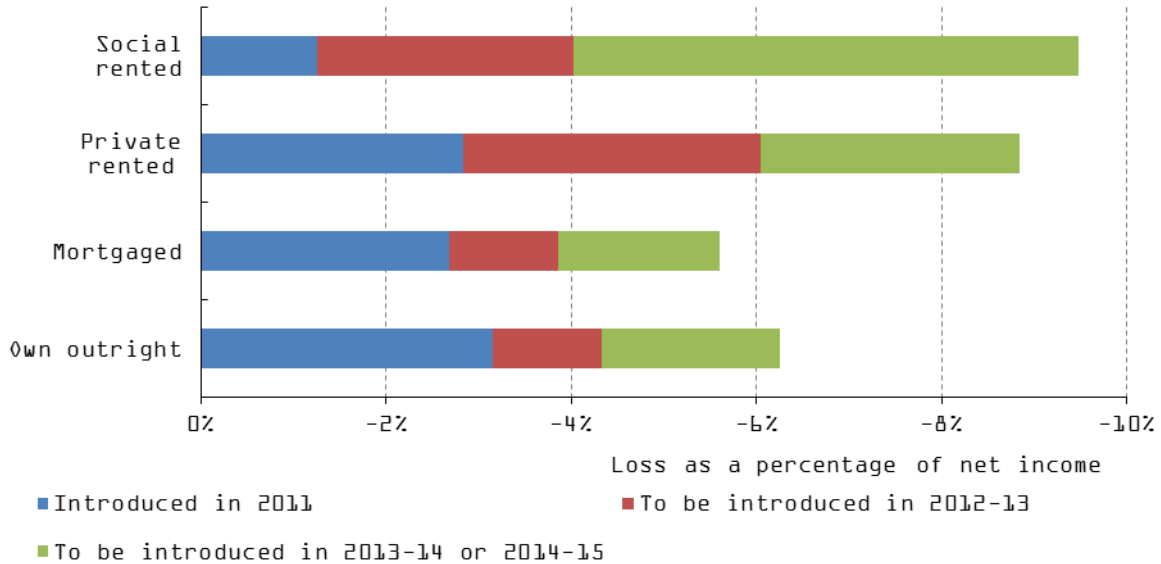


Notes and sources: As for Figure 3.3b.

Finally, we examine the distributional impact among households with children by their housing tenure in Figures 3.7a and 3.7b below. We can see that those in social rented accommodation are the least affected by tax and benefit changes introduced already in 2011. This is because these tend to be the poorest families with children, and as we saw in Figures 3.2a and 3.2b, these families lose the least from these changes. They also are not affected by changes to Local Housing Allowance that only affect the private rented sector (this is why households with children in the private rented sector lose, on average, around the same from these changes in percentage terms as owner-occupiers, despite being poorer on average). Households who rent lose more than owner-occupiers from the changes to be introduced in 2012–13: this is because they are poorer on average, and we saw in Figures 3.2a and 3.2b that poorer families with children lose more on average than richer ones. Tax and benefit reforms to be introduced in later years also affect poorer households with children more than richer ones, meaning that it is unsurprising that households with children who rent lose more as a percentage of their income than owner-occupiers. In particular, those deemed to be under-occupying homes in the social rented sector lose out from the cuts to housing benefit for this group that are to be introduced in 2013–14. However, as we see in Figure 3.7b, Universal Credit significantly reduces the average loss among renters, because it gives more to renters in paid work. One of the key aims of Universal Credit is to strengthen the financial incentive to work for those with the weakest work incentives under the current system, and it achieves this by increasing the amount of benefit these individuals receive if they undertake paid work. As it is renters who have the weakest work incentives under the current system, those who are in rented accommodation and in paid work gain the most from the introduction of Universal Credit. In the next section, we look at the broader impact on work incentives of these reforms.

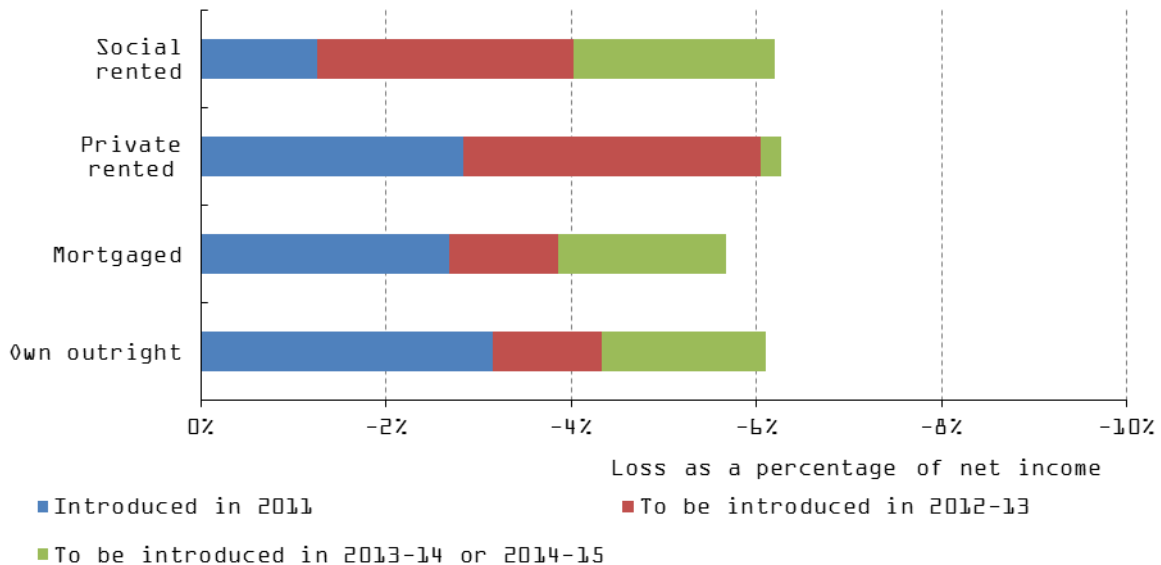
The impact of austerity measures on households with children

Figure 3.7a: Average loss from tax and benefit changes to be introduced between January 2011 and April 2014 for households with children by housing tenure, without Universal Credit



Notes and sources: As for Figure 3.3a.

Figure 3.7b: Average loss from tax and benefit changes to be introduced between January 2011 and April 2014 for households with children by housing tenure, with Universal Credit



Notes and sources: As for Figure 3.3b.

4. The impact of tax and benefit changes on work incentives

This section examines the impact of tax and benefit changes to be introduced between January 2011 and April 2014 on both the incentive to do paid work at all and the incentive for those currently in paid work to increase their earnings. We measure the incentive to do paid work at all by the Participation Tax Rate (PTR): this effectively measures the proportion of earnings that are lost in either higher taxes or lower benefit entitlements when an individual enters work. The incentive for those in paid work to increase their earnings is given by the Marginal Effective Tax Rate (METR): this measures the percentage of a small increase in earnings that is lost in tax or lower benefit entitlement. For more discussion of these measures of work incentives, see Adam and Browne (2010).⁷

Throughout this analysis, we incorporate the effect of employer National Insurance Contributions and indirect taxes in our calculations of PTRs and METRs. This is because employee and employer NICs are effectively, in the long-run, the same tax and so should have the same impact on individual's incentive to do paid work – employers might pay employees more in the absence of employer NI (and similarly employees might work for less in the absence of employee NI). Indirect taxes are as important as direct taxes and benefits, since the attractiveness of undertaking paid work or of earning a little more presumably depends on the quantity of goods and services that one can purchase with the wages earned.⁸

We use a microsimulation model to calculate how much income workers would receive were they not to work and their METR.

For non-workers, an assumption is required about how much they would earn, and how many hours they would work, if they did move into work. Our approach to this is the same as that used in section 2 of Adam and Browne (2010). We use observed characteristics of non-workers (age, sex, years of education, marriage and cohabitation status, number of dependent children, age of youngest child, ethnicity and housing tenure) to predict their earnings conditional on being in each of four different hours bands (1–15, 16–23, 24–29 and 30+) using an ordinary least squares (OLS) regression. We make no adjustment for any selection bias that arises from using the observed earnings of workers to predict the earnings of non-workers. We then use the same characteristics to estimate (using a multinomial logit model) the likelihood of each individual being in each of these hours bands were they to work and we weight the participation tax rate associated with each earnings/hours band combination accordingly.

⁷ Adam, S. and Browne, J. (2010), 'Redistribution, work incentives and thirty years of UK tax and benefit reform', IFS Working Paper W10/24, <http://www.ifs.org.uk/publications/5367>.

⁸ We incorporate indirect taxes by estimating, for each individual the average tax rate paid on their household's spending. This allows for the size of the wedge between income and the value of consumption for that person's household, but this will not quite be an accurate measure of how indirect taxes affect work incentives unless the average tax rate on what additional income is spent on is the same as that on existing purchases.

The impact of austerity measures on households with children

In Table 4.1, we give the average (mean) PTR for all working-age adults and the average METR for those in paid work under the tax and benefit systems in to be in place in 2010, 2011, 2012 and 2014. We again show the results for 2014 with and without Universal Credit in place, thus the impact of Universal Credit can be ascertained by comparing the two figures. We use the tax and benefit system in place in the April of each year; thus our figures for 2010 do not take into account the increases in VAT and fuel duty that took effect in January 2011 and those for 2012 do not take into account the withdrawal of child benefit from higher-rate taxpayers from January 2013.

The impact of austerity measures on households with children

Table 4.1: Participation tax rates for different groups under different years' tax and benefit systems

<i>Person type</i>	<i>Average Participation Tax Rate</i>					<i>Average Marginal Effective Tax Rate</i>				
	<i>2010</i>	<i>2011</i>	<i>2012</i>	<i>2014</i>	<i>2014, with UC</i>	<i>2010</i>	<i>2011</i>	<i>2012</i>	<i>2014</i>	<i>2014, with UC</i>
Single, no children	57.6%	57.1%	56.7%	56.6%	54.3%	50.7%	51.3%	51.3%	51.3%	51.3%
Lone parent	61.8%	62.1%	62.6%	63.8%	54.1%	71.6%	71.5%	70.5%	71.2%	61.8%
All singles	58.4%	58.0%	57.8%	57.8%	54.4%	53.1%	53.7%	53.6%	53.6%	52.8%
Couple without children, partner not in paid work	61.1%	61.5%	61.1%	61.3%	55.3%	55.0%	56.4%	56.9%	57.1%	57.6%
Couple without children, partner in paid work	43.3%	43.2%	42.6%	42.6%	43.8%	48.3%	49.7%	50.0%	50.1%	50.1%
of which: higher earner in couple	47.4%	47.7%	47.3%	47.2%	48.7%	50.5%	52.4%	52.9%	53.0%	53.0%
of which: lower earner in couple	38.7%	38.2%	37.6%	37.6%	38.6%	46.0%	46.7%	46.8%	46.9%	46.9%
All in couples without children	47.9%	47.9%	47.5%	47.5%	46.9%	49.6%	51.0%	51.3%	51.5%	51.6%
Couple with children, partner not in paid work	68.7%	69.4%	70.0%	69.2%	61.6%	68.1%	69.2%	69.2%	69.7%	67.5%
Couple with children, partner in paid work	49.8%	50.1%	49.6%	49.4%	52.6%	51.8%	52.7%	52.4%	52.1%	52.4%
of which: higher earner in couple	58.1%	58.8%	58.7%	58.8%	61.7%	55.3%	57.2%	57.2%	56.9%	56.7%
of which: lower earner in couple	41.8%	41.6%	40.7%	40.3%	43.8%	48.1%	48.0%	47.5%	47.1%	47.9%
All in couples with children	54.3%	54.7%	54.5%	54.2%	54.6%	55.0%	56.0%	55.7%	55.5%	55.3%
All in couples	51.0%	51.2%	50.9%	50.8%	50.6%	52.2%	53.4%	53.5%	53.4%	53.4%
All	53.5%	53.6%	53.3%	53.2%	51.9%	52.5%	53.5%	53.5%	53.5%	53.2%

Notes: Tax and benefit system as applies in April of each year. Assumes that councils means test council tax benefit more aggressively when it is localised and expenditure reduced.

Source: Author's calculations using the 2009 Living Costs and Food Survey.

For those with children, tax and benefit reforms introduced in 2011 weakened the incentive to work at all. This is the result of several factors, some of which also apply to those without children; namely the increase in the VAT rate that took effect in January 2011 and the increase in National Insurance rates that took effect in April 2011, but also changes to tax credits, in particular increasing the per-child element of the Child Tax Credit (meaning that tax credit payments for those not working increased) while increasing the rate at which tax credit payments are withdrawn as income rises and freezing the main and 30-hour elements of the Working Tax Credit (meaning that tax credit payments for those in work were reduced). However, there were other changes introduced in April 2011 that act to strengthen incentives to do paid work, in particular the increases in the income tax personal allowance and the threshold at which National Insurance starts to be paid. These were sufficient to, on average, make the whole package of reforms strengthen the incentive to do paid work at all for single people without children, those in couples without children with a partner in paid work on average and low-earners in couples with children, since increases in income tax and National Insurance thresholds particularly strengthen work incentives for lower earners.

Looking forward to 2012, the further increase in the income tax personal allowance (which increases incomes for those in paid work) and CPI-indexation of out-of-work benefits (which reduces incomes for those not in paid work) will again strengthen the incentive to work overall on average for all groups except lone parents and those in couples with children who do not have a partner in paid work. For these groups, the on-going freeze in Working Tax Credit rates will increase the amount of income they would receive if they did not work but reduce the amount of income they would receive if they worked, weakening their incentives to do so on average. Reforms to be introduced in 2013–14 and 2014–15 do not significantly affect the incentive to work at all, except for lone parents who again see their work incentives weakened by the continued freeze in the Working Tax Credit.

The introduction of Universal Credit significantly strengthens work incentives for lone parents and those with a partner who is not in paid work. However, it slightly weakens the incentive for those with a working partner to undertake paid work. This is because the withdrawal rate for Universal Credit is higher than the withdrawal rate for tax credits.⁹

Turning to the incentives for those currently in paid work to earn more, we can see that reforms that have already been introduced have weakened the incentive to earn more for all groups except lone parents, for whom there is little difference on average. This increase in average METRs is driven by rises in National Insurance Contribution and VAT rates and the rate at which tax credits are withdrawn as incomes rise. However, some low earners see a big fall in their METRs as they are brought out of income tax and National Insurance contributions altogether: a large number of lone parents fall into this group, which is why METRs for lone parents fall very slightly on average in our data.

Reforms to be introduced between 2012–13 and 2014–15 have relatively little impact on METRs. Universal Credit, however, significantly reduces METRs for lone parents and those in couples with children without a partner in paid work. This is because Universal Credit gets rid of the extremely high METRs that can exist for those in this group when they face withdrawal of several means-tested benefits and tax credits simultaneously.

In table 4.2, we show average PTRs and average METRs for those in paid work under the tax and benefit systems in place in 2010, 2011, 2012 and 2014 according to the number of dependent children in the individual's family. We see that those with more children have weaker incentives to do paid work at all, and to increase their earnings. This is because those with more children are entitled to higher levels of means-tested benefits when not working and are more likely to face steep withdrawal of means-tested benefits and tax credits if they increase their earnings. The one striking figure from the table is how much

⁹ For more on the work incentive effects of Universal Credit, see M. Brewer, J. Browne and W. Jin (2011), 'Universal Credit: a preliminary analysis', <http://www.ifs.org.uk/bns/bn116.pdf>.

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average PTRs fall among large families as a result of the tax and benefit changes to be introduced between 2012 and 2014. The key change here is the introduction of the overall benefit cap which only affects large families where no adult is in paid work. Although this change affects relatively few families' incomes as it is introduced, it has an impact on the PTRs of many more who are in paid work since if they were to leave paid work the amount of benefit they would receive would be reduced. It therefore leads to a big strengthening in the incentive for these individuals to remain in paid work.

Table 4.2: Average PTRs and METRs under different years' tax and benefit systems by number of children

Number of children	Average Participation Tax Rate					Average Marginal Effective Tax Rate				
	2010	2011	2012	2014	2014, with UC	2010	2011	2012	2014	2014, with UC
0	52.5%	52.3%	51.9%	51.9%	50.4%	50.1%	51.1%	51.3%	51.4%	51.5%
1	53.6%	53.8%	53.8%	54.0%	53.1%	54.9%	55.6%	55.6%	55.3%	54.5%
2	54.4%	55.0%	54.7%	55.0%	54.3%	56.9%	57.9%	57.4%	57.4%	56.2%
3	60.9%	61.5%	61.5%	61.9%	60.8%	61.7%	62.2%	62.0%	61.7%	61.8%
4+	67.6%	68.3%	68.5%	57.1%	55.2%	65.1%	67.5%	65.8%	66.8%	65.1%
All with children	55.3%	55.7%	55.6%	55.5%	54.5%	56.6%	57.4%	57.1%	57.0%	56.1%

Notes and sources: As for Table 4.1.

There is no such thing as an average family. The Family and Parenting Institute champions families. We are an independent charity working for a family friendly society which recognises the whole family, values families in all their diversity, and promotes conditions which enable families to thrive. We draw on research and evidence to influence policy and offer practical solutions to make society more family friendly.

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