

LOW INCOMES TAX REFORM GROUP

COUNCIL TAX BENEFIT: EVIDENCE FROM THE LOW INCOMES TAX REFORM GROUP (LITRG) TO THE COMMUNITIES AND LOCAL GOVERNMENT COMMITTEE – JUNE 2007

Summary

The concern of the Low Incomes Tax Reform Group (LITRG) is that any system of taxation should be transparent, as simple as possible and related to the ability of the individual to pay.

Many people on very low incomes remain liable for some council tax even after they receive CTB. Many more retain a full CT liability because they do not realise that they can apply for CTB. Many suffer the high marginal deduction rates from interactions with other benefits, tax credits, tax and national insurance, and claimants from whom tax credit overpayments are collected directly experience particular disadvantage. The current arrangements for CTB are self-evidently failing because take-up is so low, especially amongst older people.

We suggest the following changes:

- Collection of CT arrears should follow the more measured approach to arrears and overpayments adopted by DWP and HMRC. Local authorities should be instructed to refer council tax arrears to bailiffs only as a last resort, and given power to seek recovery through modest deductions from contributory benefits, as is already the case for means tested benefits.
- CTB should be rebranded as a “rebate”. The change of name should be accompanied by a changed onus upon the local authority, so that it should be responsible for ensuring that people on low incomes only pay CT in the first place at a level appropriate to their financial circumstances.
- HMRC, DWP and DCLG should work together to ensure that opportunities are taken to use the dealings that HMRC, the Pension Service and local authorities have with pensioners, and people approaching state pension age, to reinforce the view that people should only pay what they need to pay based on their financial circumstances.
- It would be desirable to have changes in the liability rules to make the system as simple as possible for the public to understand and for local authorities to operate. We suggest that the government should engage in consultation on how to achieve this.
- The rebate should be backdated for as long as the taxpayer has had the low income which qualifies them for the rebate.

- The saving limit of £16,000 for CTB should be removed both for people of working age and those over state retirement age not in receipt of guarantee pension credit.
- If CT is going to move to a closer alignment with income tax principles and the ability to pay, the notional income rate for savings should be specifically reviewed.
- The scope for aligning systems across local and central government, so that information already held by one part of Government can be used to fix entitlement to a CT rebate, should be examined. Further, the level of CT rebate thresholds should be set with reference to rates and thresholds elsewhere in the tax and benefits systems, not simply in isolation.
- The complex rules about the effect that a non-dependent adult in a household has on CTB should be reviewed.

Introduction

1. The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation to give a voice to the unrepresented in the tax system. As part of that remit we have been involved in the consultations on the future of Council Tax, and made submissions in response to Lyons in April 2005 and March 2006 (available on our website at

http://www.litrq.org.uk/uploadedfiles/document/1_341_lyonsinquirycounciltax110405.pdf
http://www.litrq.org.uk/uploadedfiles/document/1_341_Lyonsinquiry130306.pdf).

2. Our concern is that any system of taxation should be transparent, as simple as possible and related to the ability of the individual to pay. The structure of council tax (CT) as it now exists does not meet these criteria. The report by Michael Orton, for the Joseph Rowntree Foundation, “Struggling to Pay Council Tax” (2006) suggests that more than two million households struggle to pay their council tax each year.

3. The current arrangements for council tax benefit (CTB) are self-evidently failing because take-up is only 62-68% (Lyons, page 250) and is particularly low (53-58%) amongst older owner occupiers.

4. Against this background, we make first some general observations about the structure of CTB, its interactions with other benefits and tax credits, and the way in which CT debt is collected (paras 5 to 9); we then address the specific issues raised by the Committee (para 10 onwards).

General observations.

Structure of council tax benefit

5. People on low incomes, who have a council tax liability, can be assisted with the costs of CT through CTB which is administered by local authorities, alongside housing benefit, according to nationally set rules. Those who receive income-based jobseeker’s allowance, income support or guarantee pension credit are passported to full CTB and generally have their entire CT bill covered, subject to any non-dependent deductions. For people who are not in receipt of those benefits, CTB is calculated by comparing income against an ‘applicable amount’ which is determined by reference to a set level plus the circumstances of the claimant. Those who have income less than or equal to their applicable amount receive full CTB. However,

those whose income is above their applicable amount have CTB reduced by 20p for every £1 of the excess. Possession of capital of more than £16,000 (other than the value of your home) removes eligibility for CTB, except for people over 60 who qualify for the guarantee element of Pension Credit. Any capital above £6,000 has an income imputed to it.

6. These rules mean that many people on very low incomes remain liable for some council tax even after they receive CTB. Many more retain a full CT liability because they do not realise that they can apply for CTB, or find it too humiliating or complex to have to give all the personal financial information to apply. Many people whose sole income is long term incapacity benefit have a residual CT liability because their income is slightly higher than the level of means tested benefits.

Interactions with other benefits and tax credits

7. Those who do not benefit from a passport to full CTB also suffer high marginal deduction rates from the interactions between CTB and other benefits such as housing benefit (HB) and tax credits. Although the withdrawal rate for CTB may only be 20%, it has to be seen alongside the 65% withdrawal rate for HB and 37% withdrawal rate for working tax credit, let alone tax and NIC. We are concerned that this means that people on low incomes can be left little better off as a result of extra income from employment.

8. Those who do not benefit from automatic passport to full CTB are also disadvantaged by the interaction with tax credit overpayments. CTB is calculated using actual tax credits received. If a tax credit claimant is being paid too much in tax credits, CTB will be reduced accordingly. While the overpayment is being recovered from the ongoing award, CTB will increase accordingly. CTB paid therefore balances out in relation to tax credit overpaid or recovered. However, where a tax credit award has finished and the former claimant is having to repay any overpayment on their previous award directly to HMRC, CTB does not take into account any repayments made. While the overpayment is being directly repaid: CTB is no longer increased to compensate. The result, for CTB purposes, is unequal treatment as between those with tax credit overpayments being collected from ongoing awards, and those whose overpayments are being collected from them by direct payment.

Council tax debt

9. People on low incomes who fall behind with their CT are liable to incur additional costs because of the vigorous enforcement of arrears collection that the government requires of local authorities. Court costs and bailiffs' charges can add greatly to the financial burden of CT for low income households as well as causing a great deal of stress. **We consider that collection of CT arrears should follow the more measured approach to arrears and overpayments adopted by DWP and HMRC; that local authorities should be instructed to refer council tax arrears to bailiffs only as a last resort; and that they should be expected and given power to seek recovery through modest deductions from contributory benefits in place of the use of bailiffs, as is already the case for means tested benefits.**

Specific issues raised by the Committee

Rebranding CTB as a 'rebate'

10. The current concept of CTB being a "benefit" for which people must apply in order to reduce the amount of CT they must pay is administratively cumbersome,

ineffective as take-up shows and out of line with Government approaches in other areas, such as income tax or tax credits. No-one suggests that income tax should be based on a flat rate charge and then every citizen should put in a claim for allowances and reliefs in order to receive a rebate. If the principle is that a householder's liability to pay CT should be related to his or her means then the state should only demand the amount that is appropriate to those means. Calling the help available a "rebate" is a step in the right direction but is not enough in itself.

11. The change of name should be accompanied by a changed onus upon the local authority, so that it should be responsible for ensuring that people on low incomes only pay CT in the first place at a level appropriate to their financial circumstances.

The role of the Government in increasing CTB uptake

12. The efforts that the Government has made to increase CTB uptake are welcome. When introducing the new tax credits, the Government wanted to move to a situation where the entitlement was universal based on income levels and the support of children. It wanted to remove the stigma of applying cap in hand for a benefit. This has largely been achieved and take-up rates are high despite some of the administrative failings that have occurred.

13. The claim process for pension credit has long included seeking to record information for a HB and CTB claim, and we are given to understand that by Spring 2008 these processes will become more effective with less responsibility on the claimant to claim CTB. This has now also been introduced into the claim process for working age benefits. These are useful developments, but the low take-up figures suggest that they do not go far enough. In particular more needs to be done to ensure that people on low incomes, who are not in receipt of means-tested benefits, are aware that they may be eligible for help with their CT. This is why it is so important that the concept of a "rebate" of CT should be introduced, and it should be made clear that this rebate is an entitlement for those on low incomes.

14. While we are aware of work already in progress to institute automatic awards of CTB, we suggest that putting the onus on the local authority to check whether an automatic rebate is due might make it clearer to all concerned that this process is all part of the authority arriving at the 'right amount of tax' to be paid.

The Pension Service as a portal for CT rebates, and data sharing

15. The failure of the Pension Service to meet its take-up targets for pension credit (PC) demonstrates how difficult it can be to persuade older people to apply for money to which they are entitled, and also suggests that the PC claimline will not be approached by all the pensioners with a CTB entitlement. Nevertheless, we welcome anything that the PC claimline can do to ensure that low income pensioners receive any CT rebate to which they are entitled, even if they do not qualify for PC. It should be possible for the PC claimline to gather the information for a CTB claim and to pass this on to the local authority for these people, just as they do at present for people awarded PC. **We recommend that the Pension Service should introduce this.**

16. Virtually everyone claims state retirement pension, usually now by telephone. We have not seen the scripts for these calls, but **we suggest that the Pension Service should consider how they could provide the opportunity to try to generate a claim for CTB, as well as for State Retirement Pension and PC.**

Clearly, the caller is more likely to be positive about seeking relief from their CT burden if they are told that this is by means of a 'rebate' and an 'entitlement' rather than a 'benefit'.

17. As the LITRG Report *Older People on Low Incomes – The Case for Tax Reform* (May 2007) points out, large numbers of older people need to have dealings with HMRC over income tax matters. **We see scope for HMRC, DWP and DCLG to work together to ensure that opportunities are taken to use these dealings to reinforce the view that people should only pay what they need to pay based on their financial circumstances, and to ensure that older people receive appropriate help and advice about minimising their CT liabilities.** See also para 25.

Eligibility criteria for CTB, the savings limit, and alignment of CT rebate thresholds with other parts of the tax system.

18. It would be desirable to have changes in the liability rules to make the system as simple as possible for the public to understand and for local authorities to operate. **We suggest that the government should engage in consultation on how to achieve this.** Possible options for debate could be:

- any household which is wholly reliant on benefits for its income to have a nil CT liability (thereby extending nil liability to people dependent on Incapacity Benefit);
- any household with an income of no more than, say, 110% of its applicable amount for means tested benefits to have a nil CT liability.

19. Currently people of working age can only get backdated CTB for up to 52 weeks if they can show they have a good reason for not claiming earlier. People over 60 can generally get 12 months backdating providing they can show that they qualified for the whole period. There is no logic in this age distinction. It means that people on low incomes, including those who have been on means tested benefits, may find themselves being pursued for CT arrears just because they did not apply for CTB as soon as they would have qualified. **We consider that the rebate should be backdated for as long as the taxpayer has had the low income which qualifies them for the rebate.**

20. The supposed justification for the £16,000 saving limit in CTB is that there is a similar limit for income support or income-based jobseekers allowance. This justification becomes anomalous as PC has no such limit. Nor is there a saving limit for CTB for recipients of guarantee pension credit, although, strangely, the limit is retained for those people who receive only savings pension credit. That leads to a cliff-edge situation in which a change of £1 in income or savings can lead somebody going from paying all their rent and CT, to paying none of it – or vice versa. Lyons called for the saving limit for pensioners to be raised to £50,000 immediately and abolished in due course. **We recommend that the saving limit of £16,000 for CTB should be removed both for people of working age and those over state retirement age.**

21. This will not lead to people with free capital escaping CT, since savings will still generate an imputed income. The levels imputed - £2 a week per thousand for over sixties, and £4 a week per thousand for people of working age are much above the interest that they generate. **We believe that if CT is going to move to a closer alignment with income tax principles and the ability to pay, the notional income rate for savings should be specifically reviewed.**

Alignment of rebate thresholds with other parts of the tax system

22. The Committee requests evidence on the case for aligning council tax rebate thresholds with other parts of the tax system. We certainly regard it as undesirable that rates and thresholds in different parts of the tax and benefits systems should be fixed without reference to each other, and some form of alignment is usually preferable where the bases of assessment are the same.

23. On that basis there may be some merit in aligning CT rebate thresholds with income tax allowances so that people with no income tax liability are exempt from CT, and vice versa. But full alignment is impossible while there are different bases of assessment, with income tax being based on individual income and CTB (or its successor) on a couple's joint income. The difficulties of fully aligning tax and tax credits are illustrative of the problem.

24. Moreover, personal allowances within the income tax system give no additional consideration for those with a disability (other than blindness) or dependants, children etc, whereas the current CTB does at least vary the thresholds to take account of such needs or responsibilities.

25. Alignment of rates and thresholds is one thing: more useful from the point of view of people on low incomes is compatibility of systems, so that there can be one contact point with Government to which a citizen can give all the personal information necessary to determine their liability for tax (including CT) together with their eligibility for tax credits, benefits and CT rebates. While such has been an aspiration of Government for some time, practical attainment is still a long way off; but our recommendation in the meantime would be for **Government to consider carefully what scope there may be for aligning systems so that information already available for tax or benefits purposes does not have to be collected yet again from CT rebate claimants.**

26. **We further recommend that whether or not alignment of rates or thresholds of CT rebate with the tax or any part of the benefits system is attainable or desirable, those with policy responsibility for setting such rates or thresholds be encouraged to look across to equivalents elsewhere in the tax, tax credits and benefits systems with a view to achieving a coherent and easily comprehensible rate structure across the board.**

Non-dependent adults

27. There are complex rules about the effect that a non-dependent adult (other than a spouse or civil partner) in a household has on CTB. A particular anomaly is that people who are not working and not getting means tested benefits are expected to contribute £2.30 a week towards CT. **We recommend that these rules should be reviewed.**

Low Incomes Tax Reform Group
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