

**Joint Committee on Human Rights Call for Evidence:
Draft Bereavement Benefits (Remedial) Order 2022
Response from the Low Incomes Tax Reform Group (LITRG)**

1 About Us

1.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to unrepresented taxpayers.¹

2 Introduction

- 2.1 We welcome the opportunity to comment on the Draft Bereavement Benefits (Remedial) Order 2022 ('the remedial order') and accompanying publications².
- 2.2 We submitted briefing papers to both the JCHR and DWP in response to the previous proposed draft in September 2021³. Many of the comments and concerns raised in those briefings remain in point.
- 2.3 Our interest in the remedial order is restricted to the tax and benefits interactions, particularly in respect of retrospective lump sum payments of Widowed Payment Allowance (WPA) and Bereavement Support Payment (BSP) made to the cohabitee partner of deceased individuals.
- 2.4 Whilst many of these issues are not directly addressed by the remedial order itself, or the accompanying explanatory memorandum⁴, the Government has also published a response to representations made on proposals for the draft remedial order ('the Government's response').⁵ The

¹ There is more information about what we do on our website: <https://www.litrg.org.uk/about-us>

² <https://www.gov.uk/government/publications/the-bereavement-benefits-remedial-order-2022-explanatory-memorandum>

³ Both briefing papers can be accessed here: <https://www.litrg.org.uk/tax-guides/bereavement/what-effect-death-state-benefits-and-credits#toc-bereavement-benefits-where-a-partner-has-died-who-was-not-a-spouse-or-civil-partner->

⁴ <https://www.gov.uk/government/publications/the-bereavement-benefits-remedial-order-2022-explanatory-memorandum/explanatory-memorandum-to-the-bereavement-benefits-remedial-order-2022>

⁵ <https://www.gov.uk/government/publications/the-bereavement-benefits-remedial-order-2022-explanatory-memorandum/the-government-response-to-representations-made-on-proposals-for-a-draft-bereavement-benefits-remedial-order-2021-including-the-eighth-report-from>

Government's response sets out current thinking on matters related to associated tax and benefits interactions.

3 Income tax treatment - lump sum payments

3.1 BSP is tax-free, but WPA is taxable¹. As such, the Government response sets out its intention for dealing with the taxation of retrospective lump sums of WPA. The Government response notes that for tax purposes, WPA is treated as income (and is thus taxable) in the year of entitlement rather than in the year of payment. We agree with this and note that this should prevent distorted income tax liabilities that might otherwise occur if the full payments were treated as taxable in the year of receipt.

3.2 In terms of dealing with the collection of tax, the government response states:

*"We will work with HMRC to ensure that the claimants are fully aware of the potential tax impacts, and that a process is in place to allow for the flagging cases for reassessment to HMRC."*²

3.3 We would urge the DWP and HMRC to publish details of this envisaged process as soon as possible to ensure that claimants' tax positions can be correctly calculated and finalised.

3.4 Our view is that this process should ensure that claimants can get closure on their tax position quickly and clearly, and ideally with minimum input being required from the claimants themselves (other than checking and confirming data). It seems probable that many claimants will not have an appointed tax adviser and nor are they likely to be in a position to appoint one. We therefore would like to see DWP sharing the necessary data with HMRC to ensure that the process can be automated, at least to some extent. The use of National Insurance numbers to link up claimant records between the two departments seems an obvious solution.

3.5 It is crucial that claimants are made aware from initial communications (and ideally all subsequent communications on this matter) that WPA payments are taxable. Award notifications should set out the relevant tax years to which payments relate and clearly highlight that tax calculations will need to be made for those earlier years. Further, all communications must set out the process to collect any tax due and clearly state any action required by the claimant.

3.6 There does not appear to be any published intention to withhold tax before payment is made to claimants. However, this may well be a suitable option as part of the overall process and we feel ought to at least be considered. We would be concerned that some claimants may receive their payment and either be worried about the prospect of putting a certain amount aside to settle

¹ As social security income under Sections 577 to 579 ITEPA 2003. It is not subject to national insurance contributions.

² Paragraph 17.6, <https://www.gov.uk/government/publications/the-bereavement-benefits-remedial-order-2022-explanatory-memorandum/the-government-response-to-representations-made-on-proposals-for-a-draft-bereavement-benefits-remedial-order-2021-including-the-eighth-report-from>

potential tax liabilities, or may fail to take notice of communications relating to the taxability of payments.

- 3.7 In an ideal scenario, tax would be withheld from the lump sum based upon an up-front assessment of the likelihood of a tax liability arising. By DWP matching data with HMRC's records, it should be possible to make such an assessment at the time of the claim and withhold an appropriate amount. This would be preferable to withholding a flat percentage to cover any potential tax liabilities, but that might be an option as well, as long as there was an accompanying expedited claims process for refunds of any excess deduction.
- 3.8 Through withholding tax at the time of payment, the claimant might be given the comfort that the cash they receive is 'theirs' and can be spent as needed.

4 Impact of lump sum payments on means-tested benefits

- 4.1 The remedial order provides for retrospective lump sum payments of both WPA and BSP to be treated as capital and disregarded for 12 months for the purposes of calculating certain means-tested benefits, which includes universal credit.¹
- 4.2 However, claimants could receive backdated payments of many thousands of pounds, which raises questions as to how the DWP will apply rules relating to deprivation of capital over that 12 month period. Claimants may wish to use this money in ways that would fall outside of their normal pattern of spending. It would therefore be helpful if DWP could provide some reassurance that they will carefully consider any exceptional payments in the context with which they are being made and look perhaps more sensitively on unusual patterns of spending in the context of deprivation of capital provisions.
- 4.3 The decision to treat the backdated payment as capital (and not income) for universal credit, whilst helpful, is potentially at odds with the tax credit treatment, which could create an unfairness between recipients based on whether they receive universal credit or tax credits.

5 Tax credit treatment of lump sum payments

- 5.1 The Government response provides very little insight as to how tax credit awards will be impacted in the context of retrospective payments of WPA. Paragraph 17.5 of the Government response makes a passing reference that WPA is treated as income for the purposes of working tax credit (this should perhaps read 'tax credits')², but offers no indication as to whether recipients of backdated WPA will have their lump sums treated as capital (and so disregarded as income) for tax credit purposes, in line with the proposed treatment of other means-tested benefits discussed above.

¹ Paragraph 10, and the accompanying Schedule to the remedial order.

² Payments for WPA made under the [Social Security Contributions and Benefits Act 1992](#) are treated as income for tax credits under Regulation 7(1)(a) of [The Tax Credits \(Definition and Calculation of Income\) Regulations 2002](#).

- 5.2 We would urge HMRC to be clear from the outset how tax credit claimants will be treated. We assume the present intention is that backdated WPA will be treated as income in the year in which it accrues, in line with the tax position. However, it is unclear whether this is HMRC's approach as the tax credit legislation refers to the amount of WPA 'payable' as taken into account for tax credit purposes¹.
- 5.3 Either way, it strikes us that there must surely be parity in treatment between individuals who claim (or have previously claimed) universal credit and those who claim (or have previously claimed) tax credits. By bringing retrospective payments into account as income for tax credits, but treating them as capital rather than income for universal credit claimants (with a 12 month capital disregard), an obvious inequality arises between tax credit claimants and universal credit claimants.
- 5.4 In our 2021 briefing paper to the DWP, we set out in some detail our observations and concerns relating to historic tax credits awards in the context of lump sums of WPA². In particular, we noted that once a tax credit decision is made under section 18 Tax Credits Act 2002, the tax credit award becomes 'finalised'.³ Such finalised years can only then be reopened in certain circumstances, such as use of HMRC's discovery powers under s 20 Tax Credits Act 2002.
- 5.5 If HMRC take the view that they will not reopen finalised years, that may go *some way* to resolving the inequality between tax credits claimants and universal credit claimants. However, for those with tax credit years not yet finalised, awards for those open years would be impacted by the attributable proportion of WPA. This would put tax credit claimants at a direct disadvantage to those within the universal credit system, whose awards will not be impacted because the backdated payments are treated as capital rather than income (and disregarded for 12 months as capital).
- 5.6 We would urge HMRC to consider disregarding backdated lump sum payments of WPA under the remedial order for tax credit purposes, perhaps with a specific income disregard.

6 Miscellaneous matters

- 6.1 It is unclear from the remedial order and the accompanying explanatory memorandum whether a claim for retrospective payment will be available where the surviving cohabitee partner has themselves passed away in the intervening period. In such circumstances, will the estate of the second deceased partner be entitled to submit a claim?

¹ If the WPA is taken into account in full in the tax year received for tax credit purposes, this may create unfairness for the recipients compared to if they had received it at the correct time. It may also create knock-on effects if the recipient was to then transition to universal credit as part of the managed migration exercise.

² Paragraphs 4.7.1 – 4.7.6.

³ <https://revenuebenefits.org.uk/tax-credits/guidance/how-do-tax-credits-work/the-yearly-cycle/claims-finishing/>

- 6.2 It is not mentioned whether any interest will be added to retrospective lump sums to compensate for the claimant's intervening loss. If interest is added, this is likely to be taxable under normal principles,¹ so again claimants will need to be made aware of this.

LITRG

11 November 2022

¹ A tax-year-by-tax-year breakdown of any interest would need to be provided to identify any resulting tax liability. It may well be that claimants will have their 'personal savings allowance' available, meaning that no tax is likely to be due on such interest.