

House of Commons Public Bill Committee – Childcare Payments Bill 2014-15

Written evidence 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 the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.
- 1.2 LITRG works extensively with HM Revenue & Customs and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.
- 1.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

2 General comments

- 2.1 We welcome the opportunity to provide evidence to the House of Commons Public Bill Committee on the Childcare Payments Bill 2014-15 ('The Bill').

- 2.2 We submitted a detailed response¹ to the initial HM Treasury and HMRC consultation on the design of the Tax-Free Childcare (TFC) scheme in October 2013. We also submitted a short response² to the consultation on account providers in June 2014. At the same time as this request for evidence to the Committee, HMRC has also published³ a technical consultation on draft secondary legislation relating to the Bill. We refer to that consultation and the draft regulations in this response.
- 2.3 As noted in both the original consultation document and the Impact Assessment for the Bill, finding reliable, high quality, affordable childcare is a major concern for working families. The high costs and availability of childcare are two of the biggest challenges that parents face. The costs of childcare can be prohibitive to parents looking to enter the workplace or increase their hours. It is clear that this needs to be addressed in order to improve work incentives for parents and we welcome the Government's commitment to tackling this issue.
- 2.4 However, we are concerned that the proposed TFC scheme set out in the Bill and the draft secondary legislation will lead to complexity and confusion for many parents and advising them will be a difficult and expensive task. This is particularly a concern for those who may have to make decisions about whether to be in the TFC scheme or to receive support through universal credit (UC), tax credits or employer-supported childcare (ESC).
- 2.5 We noted in our response to the initial consultation document on the scheme design that to be successful, both administratively and from a work incentive perspective, any new scheme needs to:
- Operate seamlessly with universal credit so that people can easily move from one to another;
 - Allow people to choose whichever scheme is best for them in financial terms;
 - Be simple and straightforward for parents to operate;
 - Ensure that it provides support at the critical times when costs are at their highest (e.g. during school holidays);
 - Strike the right balance between responsiveness and simplicity; and
 - Be easily explained to parents, advisers and relevant organisations.

It is against this criteria that we offer comments on the Bill. The following section sets out some more detailed comments about the Bill clauses and the overall TFC scheme.

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http://www.litrg.org.uk/submissions/2013/131015_LITRG_taxfree_childcare.htm?WBCMODE=PresentationPublished%2cPresentationPublished%2cPresentationPublished

² <http://www.litrg.org.uk/submissions/2014/tax-free-childcare-account-provision>

³ <https://www.gov.uk/government/publications/draft-legislation-tax-free-childcare-childcare-payments-eligibility-regulations-and-draft-childcare-payments-regulations-2015>

3 Specific comments on Childcare Payments Bill 2014-2015

3.1 *Interaction with other childcare support*

- 3.1.1 Perhaps one of the most important parts of the TFC scheme is how it interacts with other systems that offer childcare support.

Employer-supported childcare (ESC)

- 3.1.2 In the Government's response to the consultation on design and operation, they noted that TFC would be a significant step forward compared to ESC as it will be open to a much wider range of working families and will not be dependent on employers offering the scheme. It will also mean those who are self-employed and those who earn national minimum wage will be able to benefit from the scheme.
- 3.1.3 The intention, as confirmed by Clause 12 and paragraph 8 of the explanatory notes to the Bill, is that people currently in an ESC scheme can either remain in that scheme (providing their employer continues to operate it) or they can choose to receive support through the TFC scheme instead.
- 3.1.4 Whilst this seems straightforward in theory, claimants will need to fully understand not only the financial support available under each scheme in order to decide which is better for them in financial terms, but also the qualifying criteria. For example, the ESC scheme offers support for children up until 1 September following their 15th birthday (1 September following their 16 birthday if the child is disabled) whereas the TFC scheme will only cover children up to the last day of the week in which the 1 September following their 11th birthday falls (1 September following their 16th birthday if they are disabled).

Tax Credits and Universal Credit

- 3.1.5 Clause 29 automatically terminates a person's tax credit award, or a tax credit award made to their partner, in its entirety, when they make a valid declaration of eligibility under the scheme. According to the explanatory notes, this prevents anyone from receiving support with their childcare costs under both tax credits and the new scheme. Clause 30 provides for a similar provision in relation to universal credit.
- 3.1.6 Although the explanatory notes (paragraph 136) specifically refer to Clause 29 preventing people receiving 'support with their childcare costs' under both tax credits and TFC, the wording used means people who are not eligible for childcare support in the tax credits system are also caught by the provision and we believe it is wider than is necessary.
- 3.1.7 For example, a couple who are both working part time (16 hours and 14 hours) will qualify for working tax credit and child tax credit. They will not qualify for any childcare support

through the childcare element of working tax credit because to claim that element both¹ must be working at least 16 hours. Although they will meet the minimum income threshold required to claim TFC, if they make a claim for TFC they will lose their tax credits award. Therefore when such a family are considering whether to remain in tax credits or claim TFC, they will need to understand that the comparison is between their whole tax credits award and the amount they could get under TFC. We expect that many claimants will find this confusing.

- 3.1.8 There are a number of ways to address this, some more complex than others. One option would be to allow people to claim TFC in addition to support through tax credits. This would mean overpayments would not occur and it would make explaining people's options easier. Another option would be to draft Clause 29 to terminate a tax credit award only where the childcare element of working tax credit was included in an award of tax credits.
- 3.1.9 We are also concerned about the automatic nature of Clause 29. According to the explanatory notes (paragraph 136) the provision means that 'a person on tax credits who decides to move to the new scheme does not need to do anything in relation to their tax credit award: the award will simply terminate when they move across'. A similar provision exists in relation to universal credit claims.
- 3.1.10 Whilst automatic termination has benefits because it means that claimants do not have a separate obligation to notify Tax Credit Office if they start claiming TFC and thereby it reduces overpayments, it is possible that the automatic system will fail meaning that in a small number of cases the tax credits award may continue. In such a situation, we would like assurance from HMRC that any resulting overpayment will be written off.
- 3.1.11 Clause 31 (and Clause 32 in relation to UC) seems to introduce an anti-abuse provision that stops tax credit claimants from getting a top-up payment from TFC (or gives them a warning notice) if they make a claim for tax credits while they are receiving support under the TFC scheme. Although it does not apply where the circumstances of the person or the person's partner have changed after the beginning of the TFC entitlement period, we are concerned about how this will work in practice. This provision could make people hesitant about moving between the schemes readily.
- 3.1.12 In their consultation response, the Government state that most people in receipt of tax credits or UC will get a higher level of support in those systems than can be gained from TFC. However, for those with higher household incomes, it is recognised that some people might be better off leaving the UC (or tax credit) system and claiming TFC instead. The Government estimate that this may involve some 50,000 families. It is also clear that the Government's intention is to allow these families to move back to UC/tax credits if their circumstances

¹ There are exceptions to the requirement for both people in a couple to work 16 hours where one person is working at least 16 hours and their partner is incapacitated, in prison, in hospital or entitled to carer's allowance.

change again meaning they will receive more support than in TFC. There appears to be no limit on the amount of times a person can move between the schemes.

- 3.1.13 Whilst any better off calculation between the schemes is complex enough, it is not clear whether the Government have considered things which may cause even more complexity. One example of this is passported benefits. For example, if someone is passported to free school meals because they are in receipt of UC, when determining whether they should move to TFC the value of the passported benefit (in this case free school meals) will also need to be taken into account. This makes decision making extremely difficult, if not impossible, for the majority of families. Other complexities such as childcare support through housing benefit, conditionality in universal credit and transitional protection upon migration from tax credits to universal credit could all play a part in whether someone is better off in one system or another.
- 3.1.14 Although the ability to opt-out of UC and tax credits, if to a family's advantage, is desirable we are concerned that in practice making such a choice, especially each time circumstances change, will prove impossible for families given the complexity of the scheme rules (both TFC and UC/tax credits).
- 3.1.15 Further work should be carried out to fully understand all of the interactions between the systems and the factors that claimants will need to take into account in making a decision and whether this is possible given the complexity. It may be that alternatives need to be considered, which although requiring additional cost may be somewhat paid for by reducing the need for complex better-off calculators and guidance.

3.2 ***Guidance and communications***

- 3.2.1 There is going to be a wide spectrum of TFC claimants in terms of communication needs. Some people will be outside of all of the existing childcare support schemes and will therefore benefit fully by claiming TFC with no choices to be made. At the other end of the scale will be the people mentioned in Section 3.1 of this evidence who are currently claiming tax credits or UC and will need to decide whether to leave those schemes and move to TFC and possibly decide again at a later date whether to move to UC or tax credits if their circumstances change. Those with the greatest information and support needs are likely to be those on the lowest incomes and include some of the most vulnerable claimants.
- 3.2.2 The success of the scheme will depend entirely upon how well the provisions are explained to parents; yet the complexity of the proposals as they stand will make this challenge extremely difficult to meet.
- 3.2.3 Any 'better-off' calculator will need to be able to calculate tax credits and UC awards in their entirety, be capable of considering other factors such as passported benefits, housing benefit and conditionality as well as being able to give parents projections if their circumstances change. However, given our experiences of the HMRC childcare indicator (which compares ESC childcare vouchers to tax credits) we are doubtful whether this could be achieved to allow accurate results in anything but the most basic situation.

- 3.2.4 In addition to understanding the financial implications, claimants will also need to understand the intricacies of the rules and the subtle differences that may mean they qualify under one scheme but not another. Information will need to be clear and accurate. We are already concerned about the inaccurate information on GOV.UK about the scheme.

3.3 ***Definitions and clarity***

- 3.3.1 In our response to the initial consultation document on the design of the scheme, we said that the opportunity should be taken to ensure that key definitions between TFC and UC should be consistent where possible to bring certainty and reduce administration.

- 3.3.2 It appears from both the Bill and the draft regulations that there are some differences in definitions which is unfortunate and will add to the complexity that families face when deciding between the various schemes. For example, in Clause 2 for childcare to be qualifying ‘the main reason, or one of the main reasons’ for incurring the costs of the childcare must be to enable the person to work. This is slightly different wording from the UC test. In some respects, the TFC scheme is more generous than UC, and whilst this is welcome for the majority of scheme users we urge HMRC to consider aligning definitions where possible.

- 3.3.3 The other area of concern for us is that some definitions around work are linked to ‘expected’ earnings. For example, Clause 10 states that a person meets the condition of eligibility in that section if ‘the person’s expected income for the relevant tax year is not greater than an amount specified’. We are concerned about what HMRC will do if these expectations turn out to be wrong and how well claimants will be supported in establishing accurate expectations at the time they are required to make their declarations. We would not expect any consequences to follow if claimants make reasonable estimates using the information available to them at the time and we would expect HMRC to take a reasonable approach to compliance.

3.4 ***Self-employed***

- 3.4.1 Clause 9 requires that a person and his or her partner must be in qualifying paid work in order to meet the eligibility criteria. The draft regulations go on to define qualifying paid work. As well as being in work, the person’s expected income from that work in the 3 month entitlement period, must be greater than or equal to the ‘relevant threshold’. The Government’s response suggests that the relevant threshold will be around £50 a week (£605 per entitlement period).
- 3.4.2 We are disappointed that such a threshold was introduced and our initial response to the consultation on the design of the scheme proposed that no threshold exist. This would make administration easier but also align the position with UC where people are eligible to receive support with childcare no matter how many hours they work.
- 3.4.3 One of the positives attributed to TFC compared to the current ESC scheme is that it is open to the self-employed. We welcome this extension of support for self-employed workers.

However, we are extremely concerned that the qualifying criteria are linked to a set earnings level each week as in many cases this is not compatible with the income patterns of many self-employed claimants who often do not have consistent income. It may therefore be that in an entitlement period they could be working full time but due to say a large tax bill and a large insurance premium pay out that they make a 'loss' in that period and therefore will not qualify for any support. We have similar concerns for those in seasonal trades or trades dependent on weather (such as farming) where income may be subject to great fluctuations across the year.

3.4.4 As noted above, we would advocate the removal of the relevant earnings threshold, however if a threshold is needed we think number of hours would be more appropriate for the self-employed.

3.4.5 We are also concerned with the HMRC proposals in their consultation response to check the figures provided by the self-employed in some sort of annual check with the figures declared via self-assessment for the tax system as the legislation seems only to ask for 'expected income' for a period with no provisions for reconciliation. This is an area that needs work to ensure that the self-employed are not treated differently to their employed counterparts.

3.5 ***Penalties and compliance***

3.5.1 We noted in paragraph 3.3.3 above some concerns about use of the term 'expected' in relation to earnings without any clarification as to what action may follow if the expectation turns out to be wrong.

3.5.2 Clause 41 gives HMRC power to issue a penalty for a careless or deliberate inaccuracy in relation to a declaration of eligibility (which includes expected earnings). Clause 41 states that an inaccuracy is careless if it is due to a failure by the person to take reasonable care. It is important that HMRC use these powers reasonably and take into account the information available to the person at the time they made the estimate, including that which HMRC provide to people in working out their expected income, otherwise we cannot see that they will be justified in invoking these penalty powers.

3.5.3 Clause 41(3) also allows a penalty to be charged where a declaration contains an inaccuracy, which is discovered by the person after the declaration is made and the person 'fails to take reasonable steps to inform HMRC'. We seek assurance from HMRC that this Clause will not be used in situations where a person makes a reasonable estimate of their expected income, which in the event turns out to be inaccurate. A penalty should not be levied for honest error, only where the estimate itself was carelessly made given the circumstances at the time.

3.6 ***Payments from a childcare account***

3.6.1 We welcome the fixed three month entitlement periods which will ensure that users of the scheme have certainty for those three months even if their circumstances change. However we are concerned that the way the Bill has been drafted means that if circumstances change

so that the person is no longer in work a month into the period, they will not be able to spend any top-ups that they have been awarded even though they can continue to accrue them (by paying in during the remaining part of the period).

- 3.6.2 This is because Clause 20 states that payments can only be made out of the account in respect of 'qualifying childcare'. Clause 2 defines qualifying childcare as being for the purposes of registered or approved childcare and also where the main reason (or one of the main reasons) for incurring the costs is to enable the person to work. If the person has lost their job mid-way through the entitlement period it would appear that on a strict interpretation, they cannot then spend the top-up payments they have accumulated in that entitlement period.
- 3.6.3 We think that this will be incredibly difficult for HMRC to police. In any case, it is unlikely that many people will seek to manipulate the system within an entitlement period. We also think that this rule adds complexity for parents. We propose that Clause 20 should be amended so that the only requirement for payments to be made is that it is for registered or approved childcare.
- 3.6.4 Instead, as part of the declaration of eligibility, parents should be asked whether they expect the 'main reason' for their use of the payments to be to enable them to work over the entitlement period. That will still allow HMRC to check cases where they think someone may be abusing the system but will not penalise other parents who find themselves in difficult situations and need the childcare support in order to help them while they look for work, or remain on an agency's books ready to take an assignment at short notice, before the next entitlement period begins.

LITRG

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