



HM Revenue and Customs – Technical consultation on draft secondary legislation for the Childcare Payments Bill 2014-15

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 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 comment to the technical consultation on draft secondary legislation for the Childcare Payments Bill (The Bill).

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- 2.2 We submitted a detailed response¹ to the initial 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. We are also due to give evidence to the Public Bill Committee on 14 October in respect of the Bill and have provided written evidence to the Committee ahead of the hearing.
- 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 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. Whilst the scheme itself, viewed as a standalone scheme, is not necessarily complex, its interactions with other schemes (tax credits, universal credit and employer-supported childcare as well as other childcare support schemes) including differences in definitions and rules, create complexity. 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 It is crucial that the Scheme is supported by adequate guidance, materials and support to help parents make the right financial decision but also to understand the differences between the schemes with respect to qualifying rules. This will involve close working between HMRC and other Government departments. Any guidance and materials that are developed will also need to be available to people who are unable to access it online. We cover this point in more detail in our evidence to the Public Bill Committee.
- 2.6 As set out in our response to the initial consultation document and in our evidence to the Public Bill committee, 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;

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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>

- 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 draft secondary legislation.

3 Specific comments on Draft Childcare Payments (Eligibility) Regulations

3.1 Regulation 2 - Interpretation

3.1.1 Under this draft regulation, ‘self-employed’ is defined as ‘engaged in carrying on a trade, profession or vocation on a commercial basis and with a view to profit, either on one’s own account or as a member of a business partnership.’

3.1.2 We think, as far as possible, that definitions should be aligned between TFC and universal credit to make it easier for people to understand and move between the schemes. Regulation 52(a) Universal Credit Regulations 2013 defines earned income as ‘remuneration or profit derived from a trade, profession or vocation’ and ‘paid work’ is defined by Regulation 2 of those same regulations as ‘work done for payment or in expectation of payment...’.

3.1.3 These draft regulations seem to add an additional requirement that the trade, profession or vocation must not only be carried on for payment or in expectation of payment (in order to constitute paid work under draft regulation 9) but it also requires the person to be carrying on self-employment on a ‘commercial basis’. This does not appear in the UC regulations and it seems to us that in order to get childcare support through UC a self-employed person need only be in paid work (meaning the work is done for payment or in expectation of payment).

3.1.4 We suggest that this definition of self-employed be re-written to exclude the words ‘on a commercial basis and with a view to profit’ and replaced with ‘for payment or in expectation of payment’.

3.1.5 If the requirement for it to be carried out on a commercial basis is left in the Regulations then there will need to be detailed guidance about what counts as ‘commercial’ and how this test will be applied.

3.2 Regulation 3 – Eligible persons: partners

3.2.1 Although there is nothing wrong with this draft regulation as a stand-alone clause, we are concerned with the potential confusion with tax credits.

3.2.2 The provision in draft regulation 3(3) states that a person’s partner who is temporarily absent from the person’s household at the date of the declaration is not to be regarded as the person’s partner for the purposes of the Act if the absence exceeds, or is expected to exceed, 6 months.

3.2.3 Under the Tax Credit Act 2002, a married couple are treated as a couple for tax credits even if one is absent from the household for a period of 6 months or more or indeed even if they maintain two separate households¹. This could lead to confusion for people who are considering whether to claim support from tax credits or TFC as their couple status may be determined differently under each scheme.

3.2.4 Whilst we can see that this regulation follows closely the UC definition, the difference with tax credits will need to be communicated to claimants.

3.3 ***Regulation 5: Meaning of a qualifying child***

3.3.1 We offer no comments on the drafting and technical detail of this legislation. However, we would like to highlight that the age limit for children under TFC is very different to the childcare element of tax credits, current employer-supported childcare and universal credit.

3.3.2 This significant difference may be important for parents who have to decide whether to leave employer-supported childcare to claim TFC instead or those who are moving between TFC and UC. Communications and guidance will need to make this very clear.

3.4 ***Regulation 9: The requirement to be in qualifying paid work and Regulation 10: Calculation of expected income***

3.4.1 We outlined concerns about the definition of ‘self-employed’ in 4.1 above. As explained in the consultation notes, Regulation 9 provides that a person must be in paid work to qualify for TFC support and further defines paid work as having a minimum amount of expected income over a specified period (normally 3 months). The minimum amount has been set at around 8 hours at National Minimum Wage.

3.4.2 Regulation 10(1) states that for an employed person, the earnings that must be compared to the threshold is ‘the amount of earnings the person expects to receive’. Earnings are further defined as having the same meaning as Section 62 ITEPA 2003.

3.4.3 For UC purposes, claimants are required to report their ‘net’ income – after the deduction of tax, national insurance and pension contributions. For tax credits, they are required to report their gross income less any pension contributions. However, it seems that Regulation 10(1) will require a different figure again. This will make the creation of better-off calculators and communications for scheme users more complex. Although we appreciate that for TFC you won’t need an actual figure reported instead you will require confirmation

¹ See for example <http://www.hmrc.gov.uk/manuals/ccmmanual/CCM15035.htm>. This is the case as long as the couple are not separated in circumstances in which the separation is likely to be permanent or they are separated under a court order.

they exceed a certain level, however when asking people for income details or asking them if they meet a threshold, you will need to be absolutely clear what income you want to know and where they can find the required information.

- 3.4.4 We do not think that the minimum earnings threshold works for users who are self-employed. Despite one of the benefits of the scheme over its predecessor being that it applies to the self-employed, we are concerned that some self-employed people with fluctuating earnings will not have access to support in some entitlement periods even though over a year they may well exceed the minimum earnings thresholds.
- 3.4.5 For example, consider a farmer who receives the majority of their income in 4 months of the year while the other 8 months of the year they have a 'loss' (when viewed on a month by month basis) as they have expenses but very little income. They will not meet the minimum earnings requirement even though when they declare their income to HMRC for the tax year they would have met the requirement on an annual basis. Similar problems arise for people who have a temporary fall in business, say due to losing a major contract, and need support to continue whilst they try and recover their business.
- 3.4.6 Although we appreciate that Regulation 11 allows a start-up period of 12 months, this does not address the problems identified in 3.4.5.
- 3.4.7 There are a number of potential solutions to this issue. One is to allow the self-employed to meet a minimum hours requirement as an alternative to the minimum income threshold. Another option would be to allow self-employed claimants to confirm that they expect to meet the threshold over a tax year as an alternative to the 3 month entitlement period. The 3 month entitlement period would still need to be maintained to avoid excluding any self-employed people who may qualify in that entitlement period but not over the whole year.
- 3.4.8 Our second concern for the self-employed is the introduction of yet another income measure requiring them to work out and keep records of 'receipts' and 'expenses' and make adjustments for capital expenditure on a basis that is different to both the tax and existing benefit systems (tax credits and UC). There is no guidance in Regulation 10 on what constitutes a 'receipt' or an 'expense'. For example, is an income tax refund a receipt? Is an expense for business entertainment an allowable expense? This will be a further administrative burden on small businesses.
- 3.4.9 If the proposal in 3.4.7, to allow the self-employed to look at their income on an annual basis, is adopted it will be necessary to explain clearly what income the person needs to compare to the threshold when making their declaration of eligibility. Those self-employed who make losses and who may be used to declaring their income for tax credits as 'nil' may immediately think they don't qualify because they do not have earnings above the required threshold, however once capital deductions are added back in they may well qualify.

- 3.4.10 The final point in relation to Regulation 10 is about the use of ‘expected’ income for both the employed and the self-employed. Regulation 10(3) states that the expectation must be ‘reasonable’. Who will deem this to be reasonable and what guidance will parents be given? We can see in the Bill that HMRC will have various penalty powers in relation to inaccurate declarations of eligibility and a specific power to impose a penalty where an inaccuracy is discovered at a later date and a person fails to take reasonable steps to inform HMRC.
- 3.4.11 It is not clear whether these provisions can apply in situations where expected income turns out to be incorrect and further information becomes available to a person further into the entitlement period that could mean their expectation is revised.
- 3.4.12 Users of the scheme will need adequate guidance on how to work out their ‘expected’ income but they will also need certainty that the support they receive based on this expectation is final. We would welcome further conversations with HMRC on this part of the Regulations.
- 3.5 ***Regulation 18: Power to disqualify tax credit and universal credit claimants: changes of circumstances***
- 3.5.1 This regulation sets out a list of changes that will qualify as changes of circumstances for the purposes of Sections 31 and 32 of the Bill. Those sections of the Bill allow HMRC to give a warning notice or disqualify people from TFC where they make a claim for tax credits or UC unless they have a ‘change of circumstances’.
- 3.5.2 Although most major changes of circumstances appear to be covered by the Regulation, and there is a general catch all provision in 18(f), we cannot see that people who find out that they are better-off getting support elsewhere can make a claim without falling foul of Section 31 or 32 provisions because there has been no relevant change of circumstances.
- 3.5.3 We often see people who claim childcare vouchers via employer-supported childcare who would be better off claiming tax credits or vice versa but the guidance and information available to them is not sufficient to enable them to determine this without support. As a result they make the wrong choice as in fact they would benefit more financially in the alternative scheme. Such people should be able to claim tax credits or UC without consequences.

4 Specific comments on Draft Childcare Payments Regulations

4.1 Regulations 6,11 and 20: Declarations of eligibility and opening a childcare account

- 4.1.1 Regulation 6 requires a declaration of eligibility to be made ‘in the form specified by HMRC’. Similarly, Regulation 11 requires that an application to open a childcare account must ‘be in the form specified by HMRC’. Both regulations are subject to Regulation 20 which states that the form must be ‘completed and sent to HMRC by electronic communications’ unless HMRC are satisfied that one of a number of exceptions are satisfied.

- 4.1.2 Whilst we are pleased to see that the regulations attempt to allow exceptions for some people from the digital requirements in other parts of the Bill and regulations, we do have concerns about the wording of regulation 20.
- 4.1.3 On a point of drafting, Regulation 20(2)(c) should have ‘or’ inserted after (i) and (ii) in order to make it clear that age and disability are standalone reasons for not being able to comply with digital requirements and should not be required in addition to (iii).
- 4.1.4 The decision in *LH Bishop Electrical Co Ltd and others v HMRC Commissioners* [2013] UKFTT 522 (TC) (*‘Bishop’*) was that VAT regulations breached the human rights of three of the joint appellants by not providing exemptions from the obligation to file online for those who were prevented from doing so by disability, age or remoteness. In addition to those possible grounds, the Judge also mentioned that the online filing requirement should also take into account any who were prevented from filing online for ‘any other reason’ to reflect the ‘other status’ limb of Art 14 of the European Convention on Human Rights¹ (the human rights anti-discrimination legislation). LITRG supported the joint appellants in *Bishop* and we have been involved in the various VAT consultations that followed the case.
- 4.1.5 We are concerned that Regulation 20(3) is extremely widely drafted and does not provide any certainty about the alternative methods available. It would therefore be open for HMRC to mandate an alternative method that may also not be suitable.
- 4.1.6 We think the best model for this type of exemption is the recently promulgated VAT regulations which provide an exemption from online filing where HMRC are satisfied that ‘it is not reasonably practicable’ for the person to use electronic means. This exemption also echoes the current RTI exemption. The VAT regulations specify that businesses will be permitted to use the telephone where online filing is not ‘reasonably practicable’ and importantly if telephone filing is not ‘reasonably practicable’ either, they will be permitted to file on paper. This should be followed in the TFC regulations otherwise it may well be open to challenge similar to that in *Bishop*.
- 4.1.7 One important feature of the VAT legislation is that taxpayers can appeal against HMRC’s decision to refuse telephone or paper filing. It is important that TFC claimants also have a right of appeal in such a situation.

¹ “The enjoyment of the rights and freedoms set forth in this Convention shall be secured without discrimination on any ground such as sex, race, colour, language, religion, political or other opinion, national or social origin, association with a national minority, property, birth, or **other status**” [emphasis supplied].

LITRG
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