

Low Incomes Tax Reform Group

Evidence to the Work and Pensions Select Committee's inquiry into the future of Jobcentre Plus

1 Executive summary

- 1.1 We welcome the opportunity to respond to this call for evidence. We do so as tax specialists with particular interest and expertise in the tax and related welfare problems of those on low incomes, and we focus on two aspects of the future of Jobcentre Plus: digitalisation, and the self-employed.
- 1.2 Over the years we have campaigned for HM Revenue & Customs (HMRC), in their move to digital by default, to ensure that reasonable and necessary adjustments are in place for those who cannot use computers or access the internet. We assisted three of the lead appellants in a First-tier Tribunal case in which it was decided that to make electronic returns for VAT obligatory without making any adjustment for those who were elderly, or disabled, or lived in remote parts of the country, was contrary to those appellants' human rights. HMRC did not appeal against the decision, but amended the regulations to ensure its systems were compliant with the judgment. We consider what lessons this case might teach the DWP in its ambition to make universal credit digital by default, and we make recommendations (para 4.7, 4.8).
- 1.3 We also look at how the self-employed claimant will be dealt with under universal credit (UC), and whether work coaches in jobcentres will be able to discharge the task assigned to them of deciding whether claimants who come before them are in 'gainful' self-employment, bearing in mind the DWP has no previous experience of paying in-work benefit to the self-employed. Again we make recommendations (see para 5.6, 5.7).

2 Who we are

- 2.1 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.
- 2.1 LITRG works extensively with HMRC 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.
- 2.3 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.

3 Our evidence

- 3.1 LITRG's interest and expertise lies in the field of taxation and associated welfare (eg tax credits, child benefit, national insurance contributions and the benefits to which they give entitlement) rather than in mainstream social security. Nevertheless, we are responding to this call for evidence for two reasons:
1. To share our experience of a system that operates on a digital-by-default basis, and the problems that this can generate for people on low incomes (which is the demographic mainly served by the traditional social security system); and
 2. To express our concerns about the role of work coaches based in jobcentres in relation to self-employed claimants of universal credit, and to what extent they will be equipped to reach decisions on the viability of small businesses and advise claimants accordingly. The CIOT has many members who currently advise small businesses on tax credits alongside their tax affairs, and who view with some concern the prospect of a switch to universal credit and its possible impact on their clients' financial position and long term business prospects.
- 3.2 On both matters we offer recommendations which we believe will mitigate any attendant risks.

4 Digitalisation

- 4.1 UC is to be digital by default, with claimants being required to manage their claims online. The risk in introducing a system that requires claims and ongoing reporting obligations to be

carried out electronically is that significant numbers may be unable to comply through not having the requisite digital access, skills or equipment. Our experience with digitalisation in the tax system has shown that making electronic interaction with HMRC mandatory runs the risk of turning compliant taxpayers into non-compliant ones, because their lack of digital skills or access makes it very difficult or impossible for them to comply – not because they are unwilling to do so.

4.2 The lawfulness of digital mandation (ie making obligatory the use of electronic systems to make reports and claims to a Government department) was explored in the case of *LH Bishop Electrical Co Ltd & Others v HMRC Commissioners* [2013] UKFTT 522 (TC). In that case, the First-tier Tribunal (Tax Chamber) held that regulations which prescribed online filing of VAT returns without regard for the difficulties experienced by three of the appellants were unlawful and a breach of those appellants' human rights. The three appellants between them were either elderly, or had disabilities that made it difficult or painful for them to use computers, or lived in remote parts of the country where there was no or very unreliable broadband connection.

4.3 Although the decision was at the First-tier Tribunal, HMRC did not appeal but issued a consultation as to how the regulations could be amended to make them human rights compliant. The three categories mentioned (disability, age and remoteness of location) featured in the amending regulations which HMRC then enacted (VAT Regulations 1995 (SI 1995/2518) reg 25A(6)(c)):

“A person . . . for whom the Commissioners are satisfied that it is not reasonably practicable to make a return using an electronic return system . . . *for reasons of disability, age, remoteness of location or any other reason* . . . is not required to make [an electronic return]”. (italics supplied)

4.4 In line with the judgment in *Bishop*, the amended regulations added 'or any other reason' to indicate that there could be other grounds on which a person's human rights could be breached by such a requirement – the categories of possible breaches were not closed. The Tribunal did not give any examples, but one example might be poverty, in the sense of inability to afford the requisite hardware or software, or to pay for connection charges, out of their disposable income.

4.5 The 'reasonable practicability' test also appears in the PAYE regulations which require employers to notify HMRC electronically of any payment they make to an employee, on or before making the payment (the 'real time information' or RTI system). The PAYE Regulations (SI 2003/2682 as amended) contain exceptions from electronic reporting for (among others) care and support employers (reg 67D(1)(d)) and those employers to whom a direction has been given under para (11) (reg 67D(1)(e)). A direction may be given under reg 67D(11) where the HMRC Commissioners are satisfied that:

(a) it is not reasonably practicable for an employer to make a return using an approved method of electronic communication; and

(b) it is the employer who delivers the return (and not some other person on the employer's behalf).

- 4.6 The wording of the legislation seems balanced and appropriate and the test of 'reasonable practicability' is, in our view, the right one if properly applied.
- 4.7 How is this to be applied to the world of social security and online claiming? While *Bishop* was a tax case, it laid down certain legal principles which are also applicable in other fields, including social security. Given that the DWP is planning that UC should be digital by default – indeed it already is in some areas – great care should be taken that the poorest individuals and those who are the least skilled in the use of computers and the internet are not excluded from claiming and complying with DWP requirements. We recommend that in order to protect that substantial minority, and to comply with their human rights:
1. DWP should make it possible for those for whom it is not reasonably practicable to make claims or otherwise deal online to use alternative channels, including telephone and paper, and should publish the fact that such channels are available and the criteria they will use for allowing access to them. These criteria should include that the applicants exhibit the same characteristics as the appellants in *Bishop* (disability, age, remoteness) but also, we would submit, that they are unable to afford the requisite equipment, software and subscriptions;
 2. Where claimants wish to transact online but are unable to do so using their own resources, either they should be able to visit a jobcentre or other (eg, voluntary sector) office where they can be given free online access within no more than two bus rides from their home, or (if they are unable to leave home through disability or childcare commitments) jobcentre officials should be available to visit them in order to assist them make a claim or report online;
 3. The second recommendation above would probably best be implemented by the DWP setting up a service similar to HMRC's Needs Enhanced Support (NES) service for its more vulnerable customers, whereby face-to-face support can be offered at a convenient location for the customer, or in the customer's own home;
 4. Local Authorities, who have been tasked with helping people online with UC claims under the Universal Support model, should be adequately funded, have best practice and guidance shared with them, and be given enough notice of the roll-out of UC in their areas.
- 4.8 For those who do interact with DWP digitally, there is the question of how evidence is collated and retained of claimants' documents submitted online or by smartphone, and how the claimant can gain access to such records if they should need to. On this matter we recommend:
5. Evidence should be retained both of online claims and reports to the DWP by UC claimants, and of telephone calls (in the form of easily accessible tape recordings) to enable facts to be determined in the event of a future dispute. Claimants should be

provided with print-outs of their claims and reports and copy recordings of their telephone calls on request.

5 The role of work coaches

- 5.1 Under UC, DWP jobcentres will for the first time be required to handle claims to working age welfare by self-employed individuals. Hitherto, under working tax credit (WTC) and working families' tax credit before it, self-employed claimants have dealt with HMRC, a department with considerable experience of self-employment through its administration of the tax system. Working tax credit is to a great extent aligned with income tax self-assessment – both systems are based on the tax year, 6 April to 5 April; and to declare their self-employed income for the purposes of claiming or renewing a claim, all the WTC claimant has to do is to transcribe the profit figure for self-assessment to the appropriate tax credit claim or renewal form. Even trading losses are computed in the same way as for tax, although the way in which loss relief is given for tax credits differs from the method used for self-assessment. The result is a minimal administrative burden for the self-employed trader – once the figures are worked out for self-assessment, they can be re-used for WTC with little or no adjustment.
- 5.2 The environment under UC will differ in two important ways. First, red tape will increase greatly. Instead of one set of figures and one assessment period for both tax and benefit, UC will require claimants to report results monthly, not annually. Secondly, having calculated their profits in one way for tax purposes, UC claimants will have to prepare a completely different calculation to ascertain their results for benefit purposes. Those results will be calculated month by month on a fairly crude cash basis rather than the generally accepted accounting basis normally used for tax,¹ taking account of the minimum income floor once the start-up period has expired.² Those rules will apply to claimants judged to be 'gainfully' self-employed – in other words, where their business activity is their main employment, the earnings from it are self-employed earnings, and it is organised, developed, regular and carried on in expectation of profit³.

¹ Since 2013 it has been possible to account for tax purposes on a cash basis similar to that used for universal credit, but the difference in assessment period (yearly for tax, monthly for UC) and in loss relief computation, along with the minimum income floor in UC, will mean that the claimant must still work out one set of figures for tax and a different set of figures for universal credit, and for UC purposes repeat the exercise every month.

² The minimum income floor limits a self-employed UC claimant's monthly award to the equivalent amount that would be paid to them if they had worked for the national living wage for (usually) 35 hours a week throughout the month, in any case where the claimant's actual monthly 'profit', calculated on a cash-in cash-out basis, falls below that amount.

³ Universal Credit Regulations 2013, SI 2013/376, reg 64.

- 5.3 This gives the work coaches in jobcentres two very difficult tasks to perform when they conduct ‘gateway’ interviews with self-employed claimants: first, to check the accuracy and validity of their reported monthly ‘profit’ and other earnings, and whether the expenses they have claimed are allowable; and secondly, to assess from that, and from their equivalent earnings in other periods, whether they are ‘gainfully’ self-employed. Both will involve an exercise of judgment on the part of the work coaches, particularly when deciding whether claimants are gainfully self-employed. Factors to be taken into account in making that decision will include hours spent on the activity, earnings derived from it and the claimant’s intentions and goal, whether the activity is undertaken for financial gain, any business plan or steps taken to increase it, HMRC’s view of it, how much work is in the pipeline, what the claimant is doing to advertise or market the business, and other things besides.
- 5.4 While the question whether a claimant is gainfully self-employed may be straightforward in many cases, it will not always be, particularly where the business is seasonal (eg farming or agricultural, bed-and-breakfast or tourism), or where earnings typically fluctuate (eg entertainment, construction), or where a business is taking longer than the one-year start-up period⁴ to start earning a profit (eg authors, artists, a business that requires a higher than average initial investment in capital equipment or stock, or any situation in which a person is taking time to try out business ideas). Besides, there are times when remuneration from the business is not just in strict cash terms – for example, a tenant farmer where the value of the farmhouse in the farm tenancy should by any reckoning be taken into account in determining whether the farm is providing gainful self-employment.
- 5.5 There is a risk that work coaches may be conditioned by the philosophy underpinning UC that for a business to be viable a self-employed claimant should be earning at least as much, month by month, as their employed counterpart. The fact that this is a fallacy should be evident to anyone familiar with – to take just one example – farming, a business in which losses are routinely incurred for several months of the year when no produce is sold, during which the self-employed farmer must still pay his employed labourers the national living wage. But it may not be evident to a work coach based in a jobcentre who has little or no experience of running a business, or observing how different kinds of businesses operate.
- 5.6 We therefore recommend:
1. Work coaches should receive training and where possible actual experience (perhaps by way of secondment) in the small business world, particularly of atypical businesses, so that they are better equipped to judge the viability of business activities;

⁴ The first twelve months of a new business activity during which the minimum income floor (see footnote 2) is not applied.

2. Guidance provided for work coaches on these matters should be robust, with input from external specialist organisations, and specialist teams should be developed and available to provide more support;
3. The DWP should align its understanding and definition of self-employment with that of HMRC, in view of the latter's long experience of the business world from the tax perspective;
4. Where an individual has an HMRC-issued unique tax reference (UTR) for self-assessment purposes they should automatically be regarded as gainfully self-employed by the DWP work coach unless they opt for conditionality instead of being subject to the minimum income floor;
5. Where a self-employed earnings figure submitted for UC purposes is the same as, or is verifiable by reference to, the equivalent profit figure accepted by HMRC, the DWP should accept it without further enquiry unless there is a particular reason not to;
6. Where HMRC has accepted a particular item of expenditure as allowable for tax purposes, the DWP should also allow it as a deductible expense for UC purposes;

5.7 Finally, it is worth noting that HMRC are moving towards mandatory digital record-keeping and quarterly reporting for small businesses. There will be very considerable disadvantages for businesses if the two systems are not aligned, particularly in terms of additional unproductive administration; but until we know in rather more detail exactly what is proposed we cannot make a firm recommendation.

LITRG

9 June 2016