

TAXREP 15/03

EMPLOYER-SUPPORTED CHILDCARE

Memorandum submitted in May 2003 by the Tax Faculty of the Institute of Chartered Accountants in England and Wales to the Inland Revenue

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EMPLOYER-SUPPORTED CHILDCARE

WHO WE ARE

1. The Tax Faculty is the focus within the Institute of Chartered Accountants in England and Wales for those Chartered Accountants working in the area of tax. It is a centre of excellence and the authoritative voice for the 123,000 members of the Institute on taxation matters. The Tax Faculty makes representations to Government and other authorities, and public pronouncements on major tax issues. Chartered Accountants are advisers to all of the top 100 FTSE companies and our members include those in tax practices and in businesses ranging from the largest to the smallest concerns.

GENERAL COMMENTS

2. The Tax Faculty has formulated ten principles that we believe should underpin all tax legislation, which are attached as an Appendix. We are pleased that the proposals for employer-supported childcare are broadly in line with these tenets, although we remain concerned in relation to:

Tenet three - Simple: the tax rules should aim to be simple, understandable and clear in their objectives.

Tenet four – Tax should be easy to collect and to calculate.

As we outline in more detail in our specific comments below, we believe that in order to encourage the take-up of these proposals it is vital that any changes are flexible, practical and not unduly burdensome. We also note that these proposed changes come on top of an already complex set of rules for employment income and are not readily reconcilable with the new system of Tax Credits.

3. In general we welcome aspects of the proposals and in particular agree that there is no reason why the employer should itself bear the responsibility for the provision of childcare. However, we believe that the changes suggested in the consultation paper favour employees at the expense of the self-employed. Tax relief should similarly be available for self-employed women or men who also need their children looked after so that they can work to support their families.
4. We believe that this particular consultation document is looking in isolation at one aspect of a much larger issue. The Government wishes to encourage people to return to work and to provide assistance with childcare to enable that to happen. This is a principle which underpins, for example, the Tax Credit regime. However, in order to achieve such an aim, what is required is a broad and practical vision of how this can be achieved. Just as the implementation of the introduction of Tax Credits has not adequately dealt with the practicalities of childcare and childcare provision, so this consultation appears to have overlooked certain key aspects which are outlined below. We would suggest that there is a need to take a step back and look at the overall aims and strategy behind Government assistance in relation to childcare to ensure that all aspects of the system operate from the same starting point and that no one group of individuals are disadvantaged. One important aspect of this is the use of tax reliefs and exemptions and what part they can play in this

area. We would be happy to participate in any such discussions.

The self employed

5. We are particularly concerned that these proposals have not been broadened to consider the issue of the self employed. We can see no logic as to why some form of tax advantaged childcare assistance should not be equally available to an employee as to a self employed individual. This may be an area the Revenue is intending to look at separately but we believe this is a good opportunity to consider tax reliefs for the employed and self employed in tandem.
6. There has been a great drive by the Government towards encouraging incorporation (e.g. a nil rate of corporation tax on the first £10,000 of profit) and potentially these proposals are a further force driving the self-employed to form themselves into limited companies in order to obtain the benefit of this proposed relief. Considering the situation of the self employed as part of a broader consultation would send a positive message that incorporation should only be for sound commercial business reasons rather than for tax advantages.

School fees

7. Child care provision is a long-term issue for all parents. We would welcome consideration of the many varieties of childcare required e.g after-school, term time, holidays etc in any proposals. There are also situations where the availability of types of childcare can be problematic. For example, in the Consultation Document we have some difficulties with the distinction between school fees and childcare for pre-school children. Whilst the suggested exemption is not intended to cover private education, it might be that pre-school fees would still apply in areas where Early Years funding is not available. A clear definition of school fees would help.

Quality of childcare

8. One of the stated policy objectives of these proposals is to increase the availability of good quality childcare places. Whilst these proposals may increase the amount of childcare which is needed, this will not be a guarantee of improved quality. Furthermore, we are concerned that imposing bureaucracy will also not necessarily improve the quality of childcare. Targeting the exemptions on registered and approved childcare will bring with it associated paperwork for a sector of the economy which is traditionally less able to cope with it. A considerable amount of support will be needed. For example, what of a new child minder who has recently registered but who has yet to receive their documentation? The weekly childcare costs would need to be paid, but the employer could not operate the PAYE exemption.

SPECIFIC COMMENTS

9. Tax Faculty responses to the questions (reproduced in italic) set out on page 15 of the consultation document now follow.
10. *(a) Do you consider that extending the current workplace nurseries tax exemption to all forms of registered and approved childcare will encourage greater support of childcare by employers?*

11. We agree that this extension is likely to encourage greater support of childcare by employers.
12. The current tax exemption applies to forms of childcare which are used by the minority of working parents. In the IFS report '*Mothers' employment and childcare use in the UK*' formal childcare was shown to be used by only 27% of working mothers with pre-school children and by 10% of mothers with school age children. Widening the scope will increase the number of working mothers who could benefit and so is likely to increase employer participation.
13. *(b) Do you agree that the tax and NIC treatment of employer-supported childcare should be consistent?*
14. We agree that consistency in the tax and NIC treatment of employer-supported childcare should be consistent. It is unhelpful both to employers and to employees to have to comply with two sets of rules. Furthermore, it is important that consistency should be extended to PAYE rules as well as income tax, in relation to any element of benefit left within the charge to tax.
15. *(c) Do you agree that employers should not be required to be involved in the management of the childcare in order to qualify for this exemption?*
16. We agree that employers should not be required to be involved in the provision nor the management of the childcare in order to qualify for this exemption.
17. The majority of employers have few employees at any one time that have the same childcare need in the same place. It is not practical for an employer to have to be involved in the provision of care at every location for babies, toddlers, primary school and secondary school children. It is also impractical and uneconomical for very small employers to have this degree of involvement.
18. *(d) Should the criteria specify the level of funding for which the employer should be responsible? We would like your views on how the requirement for employer funding can be made clearer.*
19. We do not think that it is reasonable for the criteria to specify any particular level of funding for which the employer should be responsible. A cap is reasonable but employers should be encouraged to offer whatever support they can, remembering that many people are employed by small firms and businesses.
20. *(e) Do you agree with the requirement for employers to make childcare support generally accessible to all employees where a childcare support scheme is operated? If not why not?*
21. We do not agree that this should be a requirement. For example, in businesses with high staff turnover, it would be entirely reasonable to defer eligibility until employees have been there for an agreed period. Having to offer the same benefits, on the same terms, to new starters might well be a disincentive to operating a scheme at all. This would also be impracticable in those smaller businesses which do not have clearly defined HR policies.

22. It is also not in the best interests of a child to have their care arrangements linked to the parent's employment. The more flexible the new arrangements are, the more stability will be achieved for the children.
23. The Revenue's concern is presumably that management could exploit the tax break. We believe that the very restrictive financial limit makes this extremely unlikely. A tax-free benefit of £50 per week towards the cost of childcare is unlikely to be of paramount importance to higher-earning employees. In any case, a well targeted anti-avoidance rule to prevent abuse, such as that the average cost to the employer must not significantly or materially exceed the financial limit, should be sufficient.
24. *(f) The option proposes a £50 per week financial limit for the tax and NICs exemption. Is this the right amount? If not, why not, and what amount would be more appropriate?*
25. We doubt that the suggested amount of £50 per week will persuade many more employers to adopt this scheme, nor encourage more additional mothers to return to work. An employee purchasing full-time childcare, for even one child, will pay much more than this. The new Tax Credit rules recognise a weekly credit of up to £200 per week.
26. We presume that this limit is intended to apply per employee, rather than per child, so that the number of children is irrelevant. Would this mean that each spouse, if both were employees, could claim vouchers giving a tax-free amount of £100 per week?
27. The consultation document also does not mention part-time employees or those with irregular working patterns. There are many employees who only work during school term time. Many parents will work different hours during the school holidays. These same parents will also incur different childcare costs during school holidays. Those with school age children may only incur costs during the holidays. The new arrangements need to be flexible to deal with such requirements. We have recently identified significant problems with the new system of Tax Credits, which initially failed to take account of such changing circumstances.
28. Any financial limit should be kept under careful and regular review. For example, there should be an annual increase in line with the annual increase in earnings (not the retail price index).
29. We are not convinced that providing an exemption from income tax and NIC exemption for child care costs will be sufficient encouragement to employers to increase their arrangements for child care and child care support. If the Government wishes to encourage employer provision of childcare, then it may need to provide further incentives. Ultimately, this is a policy question for Government, but if it was considered appropriate the enhanced incentives for research and development and vaccines research might be suitable models.

30. *(g) We would like your views on the extent to which take up of childcare vouchers would grow under the proposals?*
31. We think that the take up of childcare vouchers would be likely to grow under these proposals. However, the rules must be simple and consistent with existing legislation. They must tie in with Tax Credits rules and other Government benefit or regulatory requirements.
32. We should also like to emphasise our belief that the most commonly used form of childcare is informal, whether this is paid or unpaid care. In fact for older children this type of care may well be the only option. If the voucher scheme were available to these families then the take up would grow very rapidly.
33. In addition to the rules being simple, it is important that the accompanying administrative system is also easy and inexpensive to operate. For example, the process to achieve approval as a home childcarer must not be unduly burdensome.
34. *(h) Do you agree that childcare vouchers should receive equal treatment for tax and NICs as other employer-supported formal childcare provision?*
35. Yes. Employer-supported childcare covers a small proportion of families. Informal childcare provided by other family members is not demonstrably less beneficial either to the child or to the wider family and should be encouraged. Extending the vouchers in this way would support families and communities rather than profit making businesses.
36. *(i) Please comment on whether £50 per week per employee is an appropriate limit for the exemption on childcare vouchers.*
37. Our answer to this repeats the comments in (f) above. However, it is important that the limit is the same for both.
38. *(j) Do you think that better guidance along the lines above would help to encourage employers to increase support for childcare provision?*
39. We believe that employers will support childcare provision when it is in their interests to do so. It is also, however, important that the rules should be clear and unambiguous. We are concerned that the fact that the impact of employer support for formal childcare provision, on a person's entitlement to the childcare element of the Working Tax Credit, will not easily be understood. In our opinion it does not make much sense to allow a tax-free benefit (a positive impact on family income) on the one hand, whilst reducing a tax credit (a negative impact on family income) on the other. The practical interaction of these needs careful thought, particularly where penalties for failing to report a change in childcare costs are in point.
40. It will be important to allow time for these incentives to bed down before any changes are considered.
41. *(k) Do you have any other ideas about what the guidance should contain?*

42. It would be helpful if any accompanying documentation provided evidence that an employer will benefit from providing help with childcare. The rules (and any accompanying guidance) must be simple to understand and attractive so that outsourcing is a possibility for smaller businesses through arrangements with approved providers.

Conclusion

43. We are happy to discuss any of the issues raised in this response with you in more detail if that would be of assistance.

AM

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