TAXREP 27/01

NEW TAX CREDITS

Memorandum submitted in October 2001 to the Revenue by the Tax Faculty of the Institute of Chartered Accountants in England and Wales in response to a consultative document issued in July 2001

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NEW TAX CREDITS

INTRODUCTION

1. We welcome the opportunity to comment on the consultative document issued in July… .

2. We do not propose to make detailed comments but recommend that further consideration be given to certain issues which we detail below.

CLAIM YEAR

3. It is proposed that information supplied to the Revenue for tax purposes will be used as the basis for ascertaining the income on which a claim for a year will be assessed. A year's taxable income would apply to fix tax credits for a year, subject to the ability to reassess if circumstances warrant.

4. Using a year's income to set tax credits for a future year will mean that the information is out of date. For example, the income of a self-employed person with a 30 April year end would affect tax credits for a period at least 25 months in the future, which is inconsistent with matching social security benefits to current needs.

5. Following the above approach, it appears to us that this arrangement will mean that the earliest practical start date for a claim year might have to be in July. This would enable information from forms P14 to be captured and processed, but would not provide sufficient time to take into account benefits-in-kind and other income. If benefits and other income are to be taken into account, then the claim period may well need to commence later.

INCOME TO TAKE INTO ACCOUNT

6. Notwithstanding the processing problems, we consider that given that the new tax credits will extend to those with above average earnings, benefits-in-kind should be included on the grounds of equity. To not do this would beg questions like why two people working for the same firm, doing the same job for the same overall pay package and with the same family circumstances should be entitled to different tax credits when one person has a company car and the other has opted for cash in lieu of a car.

CAPITAL LIMITS

7. We note that consideration is being given to not having an upper capital limit. If the upper capital limit is abolished, it would be unfair not to take into account investment income in some way as different people with the same capital will invest in different assets producing different income returns. There is however an alternative argument that the differences are made up for through potential gains, which would also not be measured as income for tax credits.

8. The present tariff principle for dealing with investment income has much to commend it. It treats all alike, regardless of the potential for capital gain in an asset and is simple to assess. The difficulty with the present tariff is not its existence per se but the rate, as it assumes a well over 20% per annum rate of return. This has its origins in a time when the capital limit was much lower and the high rate was partly designed to catch up on the uncounted income

on the first £3,000 of capital. But although the capital limits have increased considerably over the last 5-10 years, the tariff rate has remained unaltered and therefore has become even more punitive. We consider that where capital exceeds a certain figure of capital, a more realistic tariff would be 5%.

PAYMENT

9. We welcome the fact that child tax credits will not be paid through the payroll but find it regrettable that the present burden on employers will not be eased but merely replaced with the employment tax credit.

14-122-18
PCB/
18.10.01