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The Prime Minister,  
10 Downing Street,  
London S.W.1.

Dear Prime Minister,

Taxing Unemployment Benefits

At your luncheon party on 23rd November, you asked me if I could think of a way in which Unemployment Benefits might be taxed, and to send you a note on it if I could. I sent a first note on 26th November; and have subsequently been in touch with your Private Secretary. The note I now enclose has been revised following that discussion and others I have had with colleagues here.

Several schemes seemed worth attention. In particular I looked at taxing unemployment and other benefits received during unemployment by:-

- (a) working within the present P.A.Y.E. system;
- (b) additional taxation on return to work;
- (c) a tax adjustment at the end of the tax year; and
- (d) paying benefit net of tax.

Even a cursory examination suggested all had their drawbacks.

On reflection it seemed to me that another approach might be more worth exploring, although I am well aware there may be major disadvantages to it that I have overlooked, especially given the limited time I have had to go into the matter which has had to be snatched from other things.

As with many matters connected with tax, it is far from easy to describe what I have in mind simply, although I believe it to be comparatively straightforward by comparison to some of the alternatives. Its essence is indeed that unemployment and possibly also supplementary benefits, or some part of them, should be regarded as taxable income; and thus should be added to other income when assessing liability for Income Tax. The means suggested for taxing these benefits is through a reduction in the tax rebates currently payable to the unemployed who have been out of work for more than four weeks. The proposal might meet two other of the Government's objectives. It has properties which would act as a disincentive to become unemployed and an incentive to return to work. Also it can bear on strikers as on other unemployed persons.

Although the idea is simple, complications enter because of the need to consider how it can be put into effect: to relate it to other aspects of tax and social security, and to allow for out of the ordinary cases. Therefore I feel myself in a quandary. Practical problems are all important in a case like this; and unless one has an appreciation of them, this proposal will never carry conviction. On the other hand, I am well aware how impossible it is for anyone outside Government to master all the relevant detail and avoid mistakes. I would hope that should you find this note useful and decide to pass it on to those officials concerned, they will show some generosity to an outsider peering into their mysteries and take this for the essay it is meant to be.

The suggestion is my own, but as you might expect we have staff at Coopers & Lybrand with recent experience of working in tax offices. I found it most helpful to draw on this. I have also discussed the issues with one of my senior partners, Mr. Emmitt and our senior tax partner, Mr. Tansley. While they feel able to commend the scheme I am suggesting as not without merit in principle and therefore worthy of attention, you will appreciate that we have not as a firm been able to undertake as thorough a study of the practical problems of its implementation as I feel would be necessary if the proposal were to come to you in the Firm's name. Hence I am putting it forward on a personal basis.

Yours sincerely,



Christopher D. Foster