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CABINET

GREEN PAPER ON PERSONAL TAXATION

Memorandum by the Chancellor of the Exchequer

In my Budget speech last year I promised to publish a Green Paper on the reform of personal taxation, and outlined the ground it would cover and the general approach it would take (see Annex).

2. I now attach a draft Green Paper which has been agreed by an ad hoc group under the chairmanship of the Prime Minister. Subject to colleagues' approval, I propose to publish it on Budget Day this year.

THE CASE FOR REFORM

3. Since 1979, we have made a great deal of progress in reforming many aspects of the tax system, with the aim of creating a simpler and fairer tax structure and one that is more favourable to enterprise, growth and employment. In particular, I introduced a fundamental reform of the corporate tax system in my 1984 Budget. But we have not yet tackled the personal income tax system, which remains essentially as it emerged after the war, forty years ago. And this is despite the fact that there is growing dissatisfaction with the present system, as was very clearly brought out in the responses to the then Chancellor of the Exchequer's Green Paper, "The Taxation of Husband and Wife". (Cmnd 8093), published in 1980.

4. Although there is no clear agreement on what should replace it, the present system is almost universally seen as unfair and indefensible. In particular, the fact that a wife's income is deemed to be that of her husband is widely resented by married women.

THE GREEN PAPER

5. Part I of the Green Paper describes, without commitment, a system of allowances under which everyone would have a tax allowance in their own right; and where one partner in a marriage could transfer the balance of that allowance to their spouse, if they had insufficient income of their own to use it up. Such a system would be better attuned to the life cycle of families. Most married women nowadays take paid work for a good part of their working lives. But the present tax system is hardest on married couples at just that time when they have the responsibility of a young family and the wife is least able to take paid work. As paragraph 3.23 of the Green Paper illustrates, the proportion of a couple's income taken in

tax typically increases when a wife gives up work to have a child, and falls again when she resumes paid work. Under transferable allowances, a couple's tax allowances would not depend on whether a wife was working, so the proportion of a couple's income taken in tax would not increase when the wife was unable to take paid work.

6. Though this is not, of course, its principal rationale, a move to transferable allowances can be presented as a coherent package with the proposals in the Secretary of State for Social Services' Social Security Bill, by providing a structure in which any subsequent increase in allowances would take more people out of the poverty and unemployment traps than is possible under the present system for the same cost.

7. Part II of the Green Paper describes other changes designed to ensure privacy and independence for married women in tax matters and end all the existing tax penalties on marriage. These include the independent taxation of investment as well as earned income.

8. Part III of the Green Paper discusses, again without commitment, a number of other possible long term changes to the tax system. It considers in particular the relationship between tax and social security, a subject in which there is considerable Parliamentary interest. Complete integration is shown to be impractical - but also undesirable because it would blur the distinction between earnings and benefits. But there is scope for rationalisation. The Secretary of State for Social Services' proposed changes already go some of the way, and we should ensure that opportunities for closer alignment of the two systems are taken whenever it is sensible to do so.

9. Other possibilities discussed are the scope for integrating income tax and employees' National Insurance contributions (a change which would gravely weaken the contributory principle); and moves to self assessment and a non-cumulative system of Pay As You Earn (PAYE).

PRACTICAL IMPLICATIONS

10. None of the ideas in this Green Paper are for this Parliament. A move to transferable allowances is dependent on computerisation at the Inland Revenue, and, should we wish to go ahead, the change could not begin before 1990 at the earliest. But the computerisation of PAYE is now well under way, and if we wish to take the opportunity to reform the structure of personal tax we need to plan for it in advance; hence the need for a Green Paper now.

11. Any tax reform necessarily involves gainers and losers, at least in relative terms, and a move to transferable allowances is no exception (although of course the same couple might well be gainers at one period in their lives and losers at another). This means that, in practice, it is most unlikely that we will want to implement the reform except in such a way that no couple would suffer a reduction in cash terms in their total allowances during the period of the change. This would involve staging the introduction of the new system over a number of years, to spread its cost. The Green Paper explains how this would be done.

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12. It also means that the reform can be introduced only as and when resources permit, given competing claims on resources which will need to be assessed at the time.

CONCLUSIONS

13. I believe that the reform of personal income tax described in this Green Paper would be attractive to a wide range of political opinion, both within and outside the party - and especially to women voters. The response to the then Chancellor of the Exchequer's Green Paper showed that there is a substantial body of opinion in favour of radical reform of the personal tax system. Informed opinion is aware of the opportunities created by the computerisation of PAYE. Since my Budget speech there has been sustained and generally favourable interest both in the press and the party in anticipation of the Green Paper.

14. Subject to detailed drafting amendments, I seek colleagues' agreement to publication of the Green Paper on Budget Day.

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Treasury Chambers

21 February 1986

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EXTRACT FROM HANSARD, TUESDAY 19 MARCH, Vol 75,

Col 794 - 795

TAX REFORM

Mr. Lawson: I now turn to taxation.

This Budget carries forward the theme of tax reform I set out last year. Reform designed to make life a little simpler for the taxpayer. And above all reform designed to improve our economic performance over the longer term, on which the jobs of the future will depend.

In my Budget last year I announced a radical reform of the corporation tax system. This had been preceded by the Green Paper on corporation tax issued by my predecessor in 1982.

I am satisfied that the right way to proceed with major tax reform is to issue a Green Paper first, as a basis for full and informed discussion, followed by legislation when the results of that discussion have been fully digested.

I therefore propose to issue a Green Paper later this year on the reform of personal income tax.

The computerisation of PAYE makes this the right time to review the system of personal taxation. Most of the work will be complete by the end of 1987 and the full range of facilities will be available by 1989. The Green Paper will therefore discuss a range of options opened up by computerisation, from non-cumulation to closer integration between the tax and benefit systems, and including in particular a reform of the present system of personal allowances.

It is the Government's firm policy to reduce the burden of income tax, but we need to make sure that the reliefs we can afford are concentrated where they will do most good.

The present structure of personal income tax is far from satisfactory. Too many young people start paying tax at too low a level, and too many families find themselves in the poverty and unemployment traps. The system discriminates against the family in which the wife stays at home to look after the children. It denies to the partners in a marriage the independence and privacy in their tax affairs which they have a right to expect.

There is therefore a strong case for changing to a new system of personal allowances more suited to today's economic and social needs. Under this, everyone, man or woman, married or single, would have the same standard allowance; but if either a wife or a husband were unable to make full use of their allowance, the unused portion could be transferred, if they so wished, to their partner.

This reform would produce a more logical and straightforward system. Far more people could be taken out of the poverty and unemployment traps, and indeed taken out of tax altogether, for a given sum of overall tax relief than is possible under the present system. It would end the present discrimination against the family where the wife feels it right to stay at home, which increasingly nowadays means discrimination against the family with young children.

Husbands and wives would each be taxed separately on their own income irrespective of the income of the other. The aggregation for tax purposes of a wife's earned income and investment income with her husband's would end, thus removing what has become an increasing source of resentment among women.

The Green Paper will set out full details of the proposals I have just outlined, as a basis for public discussion. After an appropriate period for consultation, it would be possible to legislate in 1987 and have a system on these lines in place by the end of the decade.

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1. INTRODUCTION

1.1 The Government regard it as of major importance to reduce the burden of income tax. Obviously, there are certain services that the State has to provide for the community as a whole - for example defence, policing, justice - and, as a matter of policy, governments provide other services, such as education and health care and support for the elderly and others in need. These have to be paid for, wholly or mainly, by general taxation. Beyond that provision the Government believes that people should be left to spend their own money as they wish. This maximises their freedom of choice. It gives incentives to effort and enterprise. And it produces an economy that is responsive to changing tastes and circumstances. For all these reasons taxes must be kept as low as possible, and their incidence made as fair and efficient as it can be.

1.2 The Government have already done much to ease the burden of income tax. The basic threshold at which income becomes liable to tax has been raised by 20 per cent in real terms since 1979, taking 1¼ million people out of tax altogether. The basic rate of tax has been reduced from 33 to 30 per cent; and the top rate from 98 to 60 per cent.

1.3 But further progress is needed. Tax thresholds are still too low in relation to earnings. Before the last war a married man on average earnings paid no income tax. In 1950 the tax threshold for a married man was 60 per cent on average earnings; now it is 39 per cent. The married man on average earnings now pays nearly a quarter of his income in tax.

1.4 If the tax burden is to be further reduced the first need is to contain public expenditure. Over the 20 years from 1964 to 1984 public expenditure rose from about 35 per cent of gross domestic product (GDP) to about 45 per cent. The upward trend

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has now been reversed. The second need is to ensure that tax reductions are concentrated where they can do most good. This raises questions about the structure of our personal tax system.

1.5 Any major structural reform of income tax is bound to shift the relative burden of tax between individuals. But if that is considered unacceptable, then no tax reform would ever be possible. Indeed, it is one reason why so little reform of income tax has been undertaken. But there has also been another reason. The pay-as-you-earn (PAYE) system, which is such an efficient and simple method of collecting tax, could not, while operated manually, cope with radical changes. The computerisation of PAYE now under way, and due to be complete by the end of 1987, offers an opportunity to change the structure of the tax system in radical and imaginative ways that were not possible before. As the Chancellor said in his Budget speech, when announcing this Green Paper, "The computerisation of PAYE makes this the right time to review the system of personal taxation".¹

1.6 The first part of this Green Paper deals with the reform of personal allowances and the tax treatment of husband and wife. Chapter 2 describes the present system and sets out the arguments for change. It explains how the present system makes it expensive to give tax reductions where they are most needed, denies married women the opportunity for independence and privacy in their tax affairs and has the effect of imposing penalties on marriage. Chapter 3 considers closely a new system of transferable personal allowances which could meet these shortcomings.

1.7 The second part of the paper, Chapters 4 and 5 considers the implications of a system of transferable allowances for particular groups such as the elderly and single parents; as well as the implications for other areas of the tax system.

1.8 The third part of the paper, Chapters 6-8, considers how the tax system might develop in the longer term, and in particular

¹ Official report 19 March 1985 col 794.

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the relationship between the tax and social security systems. It also examines possible developments in the way the tax system is administered, and in particular considers the arguments that have been advanced for moving to a different system.

1.9 Computerisation gives us the opportunity to change the structure of personal taxation. To be able to take maximum advantage of it, we need to examine the present system, and how it could best be reformed. This is the purpose of this Green Paper.

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PART I - PERSONAL ALLOWANCES

2. ARGUMENTS FOR REFORM

The present system

2.1 The amount of income tax people have to pay depends on the rate of tax and on the personal allowances to which they are entitled. The personal allowance is essentially a slice of tax-free income.

2.2 The structure of the basic personal allowances has remained virtually unchanged since 1942.

- Single people have an allowance, currently £2,205.
- Married men have approximately $1\frac{1}{2}$ times the single person's allowance, currently £3,455.
- The wife's earned income allowance is equal to the single person's allowance but, as its name implies, can only be set against the wife's own earned income.

2.3 The income of a married couple is added together ("aggregated") for tax purposes and treated as if all the income belonged to the husband. All personal allowances (including, in law, the wife's earned income allowance), are given against the husband's income (which is taken to include his wife's income).

This means that:

- A married couple where both are in paid work (a "two-earner couple") have approximately $2\frac{1}{2}$ times the single allowance, (married man's allowance of $1\frac{1}{2}$, plus wife's earned income allowance of 1).
- A married couple where only the husband is in paid work (most "one-earner" couples) have approximately $1\frac{1}{2}$ times the single allowance, through the married man's allowance.

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- But, where only the wife is in paid work the couple have approximately 2½ times the single allowance. This is because all the income is treated as the husband's for tax purposes, so he can set against it both his married man's allowance and the wife's earned income allowance.

Annex 1 gives further details of the present system.

2.4 The Government have looked at the case for reforming the structure of personal allowances, with three main objectives in mind:

- To give married women the same opportunity for privacy and independence in tax matters as their husbands.

- To remove discrimination against marriage and the family.

- To be able to raise tax thresholds cost effectively in terms of reducing the tax burden on families with low incomes. The present low tax thresholds for many such families contribute in no small measure to the poverty and unemployment traps.

TREATING HUSBAND AND WIFE EQUALLY

2.5 The present system rests ultimately on tax law dating back to the start of the last century, which treats a married woman's income as her husband's for tax purposes. In the words of the legislation:

"A woman's income chargeable to income tax shall ...(for any year) during which she is a married woman living with her husband be deemed for income tax purposes

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to be his income and not to be her income.⁽¹⁾

A number of features of the system flow from this, and have attracted widespread criticism.

2.6 A married woman does not have an allowance of her own to set against income other than earnings. Partly because of this, and partly because a wife's investment income is added to her husband's for tax purposes, some 350,000 married couples pay more tax than two single people with the same incomes.

2.7 The husband is legally responsible for a couple's tax affairs. This means that the husband has to include his wife's income on any tax return he gets, and hence that a married woman cannot have privacy in her financial affairs. A system of transferable allowances would reflect the Government's belief that a married woman should have the same right to deal with her own affairs as any other taxpayer.

2.8 These matters were considered in the earlier Green Paper "The Taxation of Husband and Wife"⁽²⁾. The discussion of transferable allowances in Chapter 3 below takes account of the responses to that Green Paper and of the public debate about these issues since, including the report from a House of Lords Select Committee: "Income Taxation and Equal Treatment for Men and Women".

A BETTER DEAL FOR THE FAMILY

2.9 Although, in a number of ways, the tax system takes account of the shared responsibilities of married people, in other ways it bears more harshly on married than on unmarried couples. This applies to the taxation of investment income and capital gains, to the additional personal allowances for single parents and to the relief allowed on mortgage interest. For all these the

⁽¹⁾ Section 37 Income and Corporation Taxes Act 1970, though the wording has been in substance the same since 1806.

⁽²⁾ Cmnd.8093

present system operates in a way that can mean that a couple would pay less tax if they were unmarried. Many of these effects stem from the basic rule that for tax purposes a married woman's income is treated as her husband's. All this is seen as a tax penalty on marriage.

2.10 The present tax system also bears hardest on many married couples at times when they have the responsibilities of a young family. Under the present system, if a one-earner married couple and a two-earner couple have the same income, the two-earner couple will pay substantially less tax (see Chart 2.1). In most other countries, as can be seen from Annex 7, there is no such discrimination between one-earner and two-earner couples.

2.11 Most couples nowadays find that at times both partners are earning and at other times only one is earning, depending on where they are in their life cycle. The vast majority of married men below retirement age are in the job market, as are over 60 per cent of married women of working age. Almost all women will be in paid work at some point during their married lives. Chart 2.2 shows how the proportion of married women going out to work has increased since the 1930s. Most women who do not have a paid job have specific reasons for not going out to work: many are looking after children or other relatives; others suffer from ill-health, or find it difficult to enter the labour market after an absence caused by domestic responsibilities. Chart 2.3 illustrates this, drawing on the results of a survey (taken in 1980) of the reasons given by married women for not being in paid employment. Annex 5 gives more details of married women's employment patterns.

2.12 Thus in many marriages both partners will typically have paid jobs until the wife leaves work to have children. She may then go out to work again as the children grow older.

2.13 The present tax system takes no account of this life cycle. Couples have high tax allowances ($2\frac{1}{2}$ times the single allowance) when both are in paid work, but see a sharp reduction (to $1\frac{1}{2}$ times the single allowance) if the wife leaves paid work. This is likely to be the time when the couple are under greatest

CHART 2.1 AVERAGE RATES OF TAX FOR MARRIED COUPLES
AT VARIOUS LEVELS OF GROSS INCOME
(TAXPAYERS OF WORKING AGE)

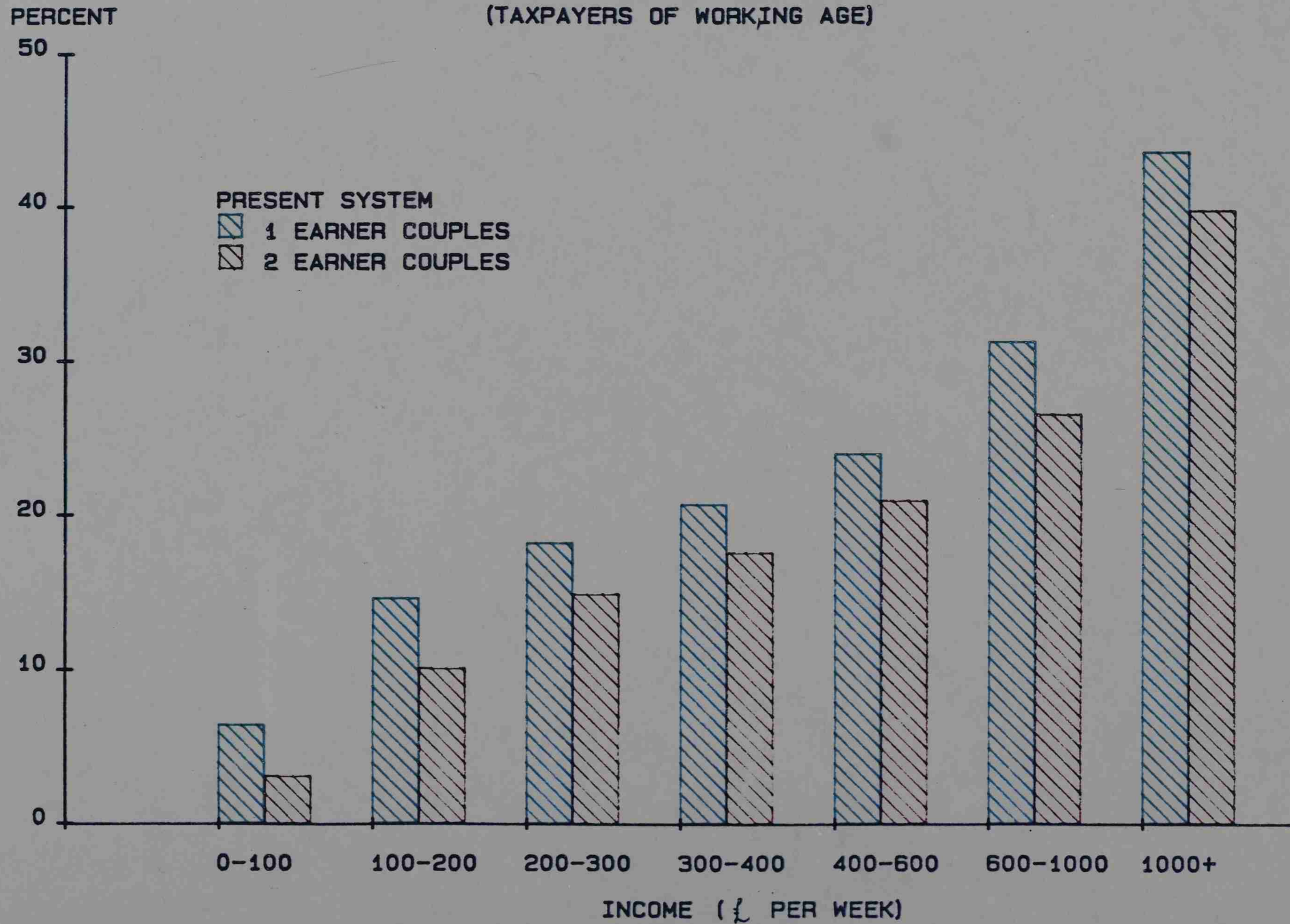
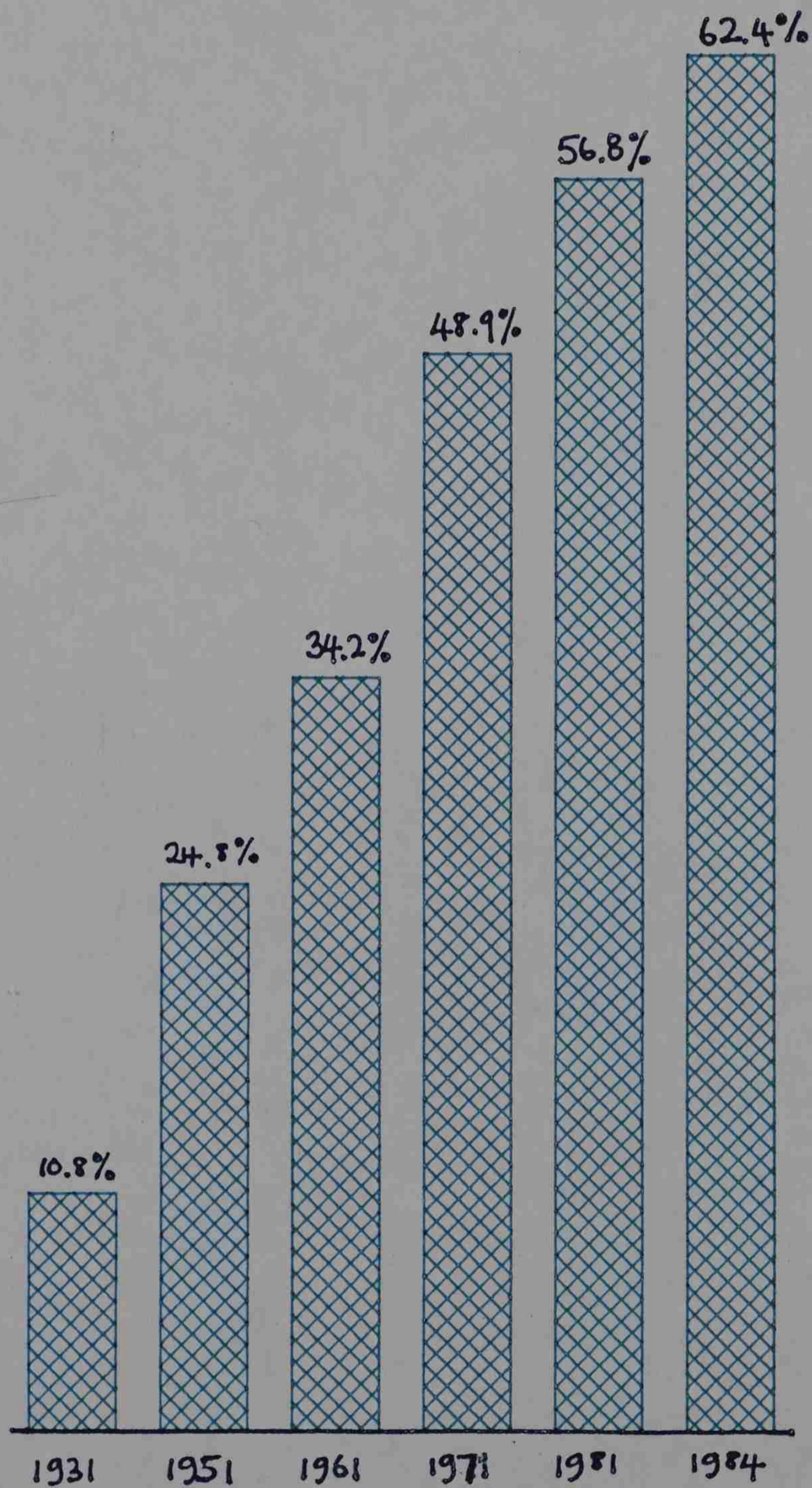


CHART 2.2 : THE PROPORTION OF MARRIED WOMEN WORKING OR LOOKING FOR WORK HAS BEEN GROWING SINCE THE 1930's.



SOURCE : CENSUSES OF POPULATION AND LABOUR FORCE SURVEY 1984

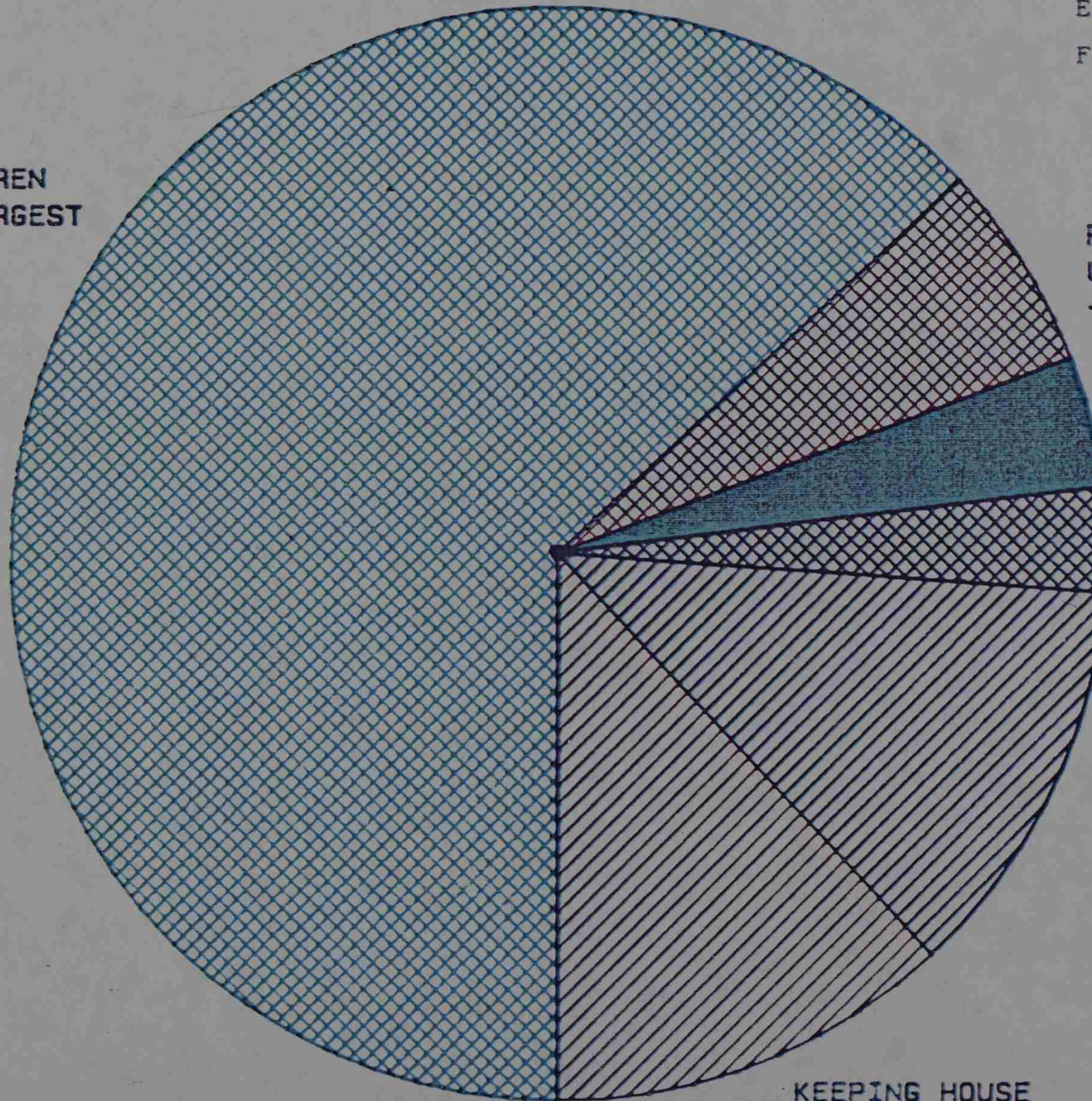
FOR DETAILED FIGURES SEE ANNEX 6 TABLE 1.

CHART 2.3 : REASONS GIVEN BY MARRIED WOMEN FOR BEING ECONOMICALLY INACTIVE

Source: DE/OPCS 1980 Women and Employment Survey

For detailed figures see Annexe 6, Table 3

LOOKING AFTER CHILDREN
ACCOUNTS FOR THE LARGEST
NUMBER OF WOMEN
NOT WORKING - - 63%



PERMANENTLY
UNABLE TO WORK
- - 5%

OTHER REASONS
- - 4%

LOOKING AFTER
RELATIVES - - 3%

KEEPING HOUSE
AGED UNDER 50 - - 12%

KEEPING HOUSE
AGED OVER 50 - - 12%

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financial pressure - they lose the wife's earnings, and may be taking on new family responsibilities, usually with the birth of the first child.

2.14 The present structure of allowances, giving two-earner couples 2½ times the single allowance, originated in the circumstances of war in 1942, when there was a need to give specific encouragement to married women to go out to work. Today, for most married women, it is the rule rather than the exception to be in employment, and the system needs to be changed to remove discrimination against couples where only the husband is in paid employment. The present tax system bears hardest on couples at precisely the point when most of them can least afford it.

RAISING THRESHOLDS

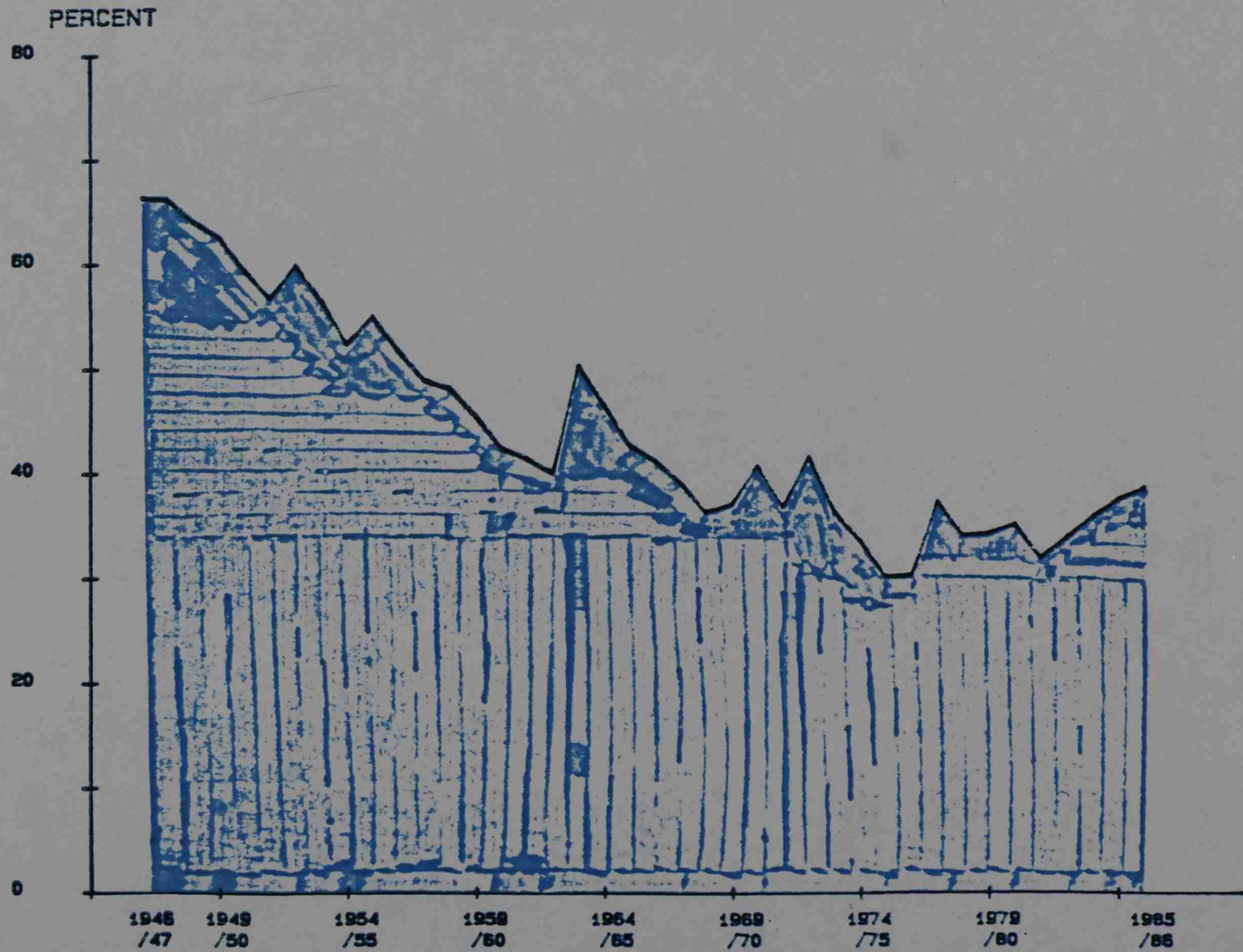
Thresholds for Different Couples

2.15 Tax thresholds are too low. Chart 2.4 shows how the married man's tax threshold has fallen as a proportion of average manual earnings since the late 1940s.

2.16 In spite of the 20 per cent real increase in thresholds since 1979, too many people still come into tax at too low a level of income. Further progress must be made. But raising tax thresholds is expensive - it costs around £1 billion in revenue to increase personal allowances by 5 per cent. So it is vital that thresholds are increased in the most cost-effective way.

2.17 Low tax thresholds weaken incentives. The group worst affected are married men on low earnings with families to support. Not only is their tax threshold (at £3,455, or £66 a week) a good deal lower than for families where both husband and wife are in paid work (where it is £5,660 or £108 a week), but they are often at a stage in life when their family commitments are high. Thus it is mostly one-earner families that are caught in the unemployment and poverty traps that arise where the tax and social security systems overlap.

CHART 2.4 : MARRIED MANS TAX THRESHOLD AS A PERCENTAGE OF MANUAL WORKERS AVERAGE EARNINGS 1946-47 TO 1985-86



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The Unemployment Trap

2.18 People find themselves in the unemployment trap when their income out of work is almost as high as their disposable income when they are in work. Indeed, it may actually be higher on occasion. An important reason for this is that people entering work start paying tax at levels of income well below half average earnings.

2.19 It is reckoned that one in every 16 working families - 900,000 - would have at least 80 per cent of their present income if they did not work at all.

The Poverty Trap

2.20 People who are in work find themselves in the poverty trap when, because of the combination of income tax, national insurance contributions, and the withdrawal of income-related benefits, they are little or no better off if their earnings increase. Indeed they may sometimes be worse off.

2.21 The amount that people in the poverty trap lose out of each extra pound of earnings is known as their marginal rate. At present, in the extreme case, it is possible for the marginal rate to be as high as 110 per cent.

2.22 It is estimated that some [210,000] low income families with children have marginal rates of 75 per cent or more; [165,000] of these are people receiving family income supplement who also pay tax. A further [90,000] families have marginal rates between 50 and 75 per cent.

Changes in Social Security

2.23 The Government's proposals for the reform of social security³ will help to alleviate these traps.

(3) "Reform of Social Security", December 1985, Cmnd 9691. This is referred to from now on as "the Social Security White Paper".

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2.24 They will align the structure of the benefits paid to people who are out of work with those for people in work, with the aim of ensuring that people in work are better off than they would be if they were not working. Family income supplement is to be replaced by a new income-related benefit for low income families in work, called family credit.

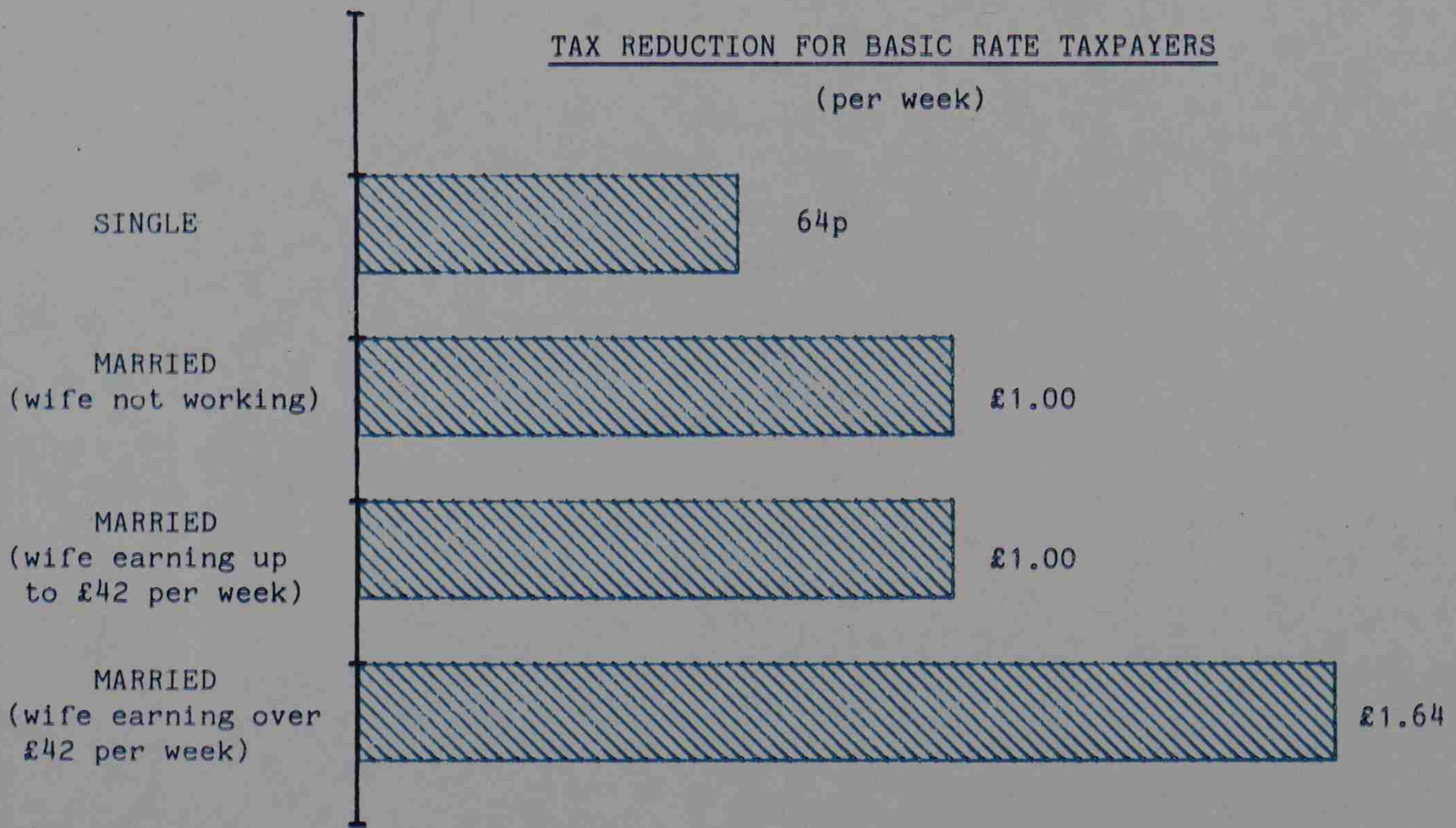
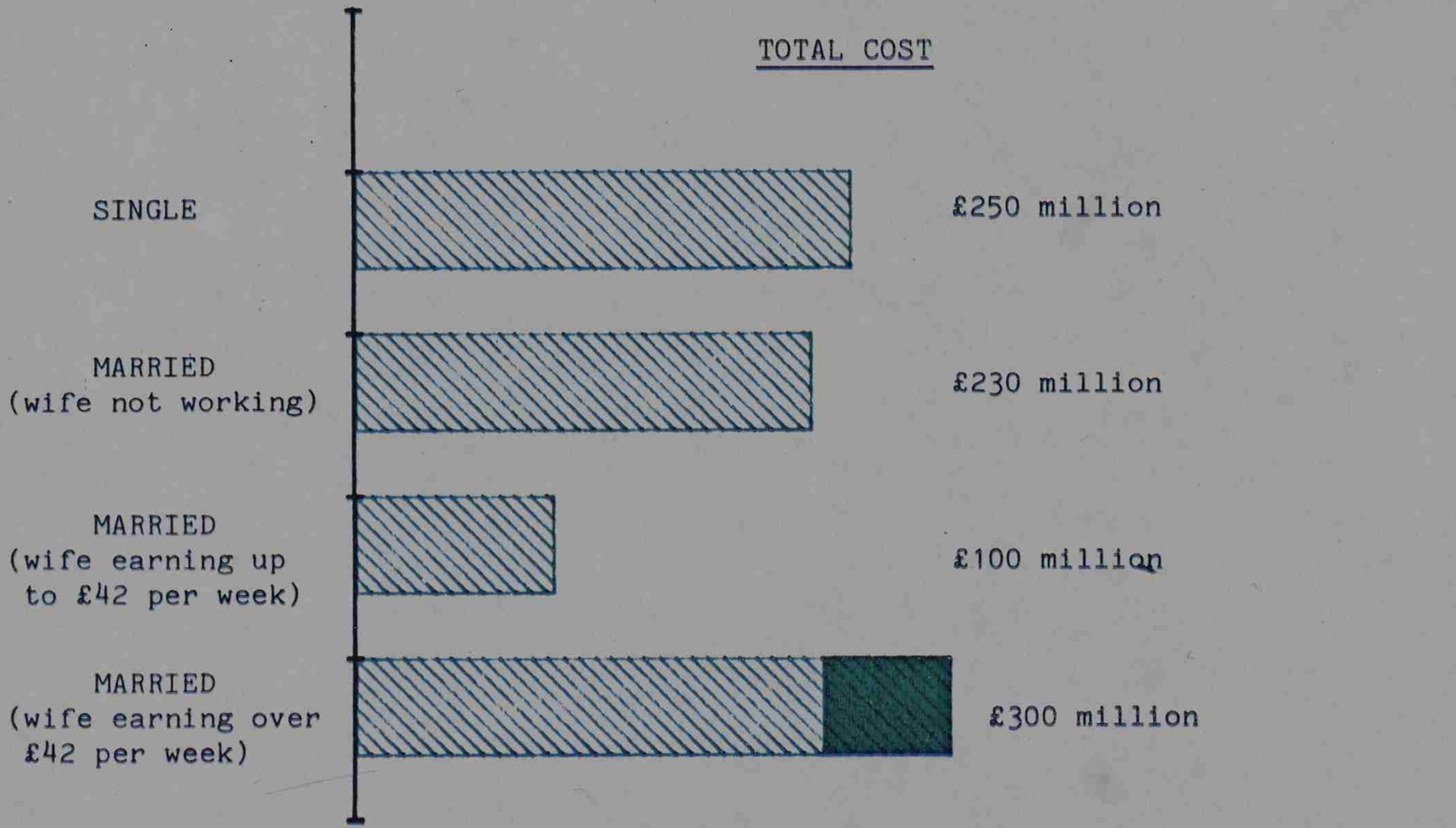
2.25 The amount of family credit a person receives will depend on his net income, after tax and national insurance contributions, rather than on his gross income. Similarly, the entitlement to housing benefit will depend on net income, after tax, national insurance contributions and family credit.

2.26 The social security reforms will reduce the level of marginal rates that people can face: marginal rates of 100 per cent or more will be eliminated. However, further changes are needed to reduce the number of people who find that their incomes are low enough to make them eligible for income-related benefits but high enough for them to have to pay income tax.

2.27 This can be achieved by raising tax thresholds. But with the present system of personal allowances it is very expensive to increase thresholds for married couples where the wife is not in paid employment, who are the largest group affected by the traps. The table below and Chart 2.5 show how a rise of 5 per cent in personal allowances, costing about £1 billion in revenue, would be distributed among different groups of the population. Because the married man supporting his family gets $1\frac{1}{2}$ times the allowance for a single person, whereas the couple who are both in paid employment get up to $2\frac{1}{2}$ times, some 45 per cent of the increase in tax relief for those of working age goes to two-earner couples, though these form only 30 per cent of taxpaying families.

2.28 So when tax thresholds are increased in the Budget, two-earner couples benefit much more than one-earner couples. If allowances are increased by 5 per cent, families with one-earner will be £1.00 a week better off, whereas families with similar incomes but with two-earners will gain by £1.64 a week.

CHART 2.5 : EFFECT OF 5 PERCENT INCREASE IN PERSONAL ALLOWANCES
(Taxpayers of working age)



Extra cost (£65 million) due to these couples having about 2½ times, rather than twice, the single persons allowance

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2.29 The present system therefore does not target effectively the benefit of threshold increases where it is most needed and where it can do most to ease the poverty and unemployment traps.

THE CASE FOR REFORM

2.30 In short, we need to move to a new system that will be better for incentives, that taxes married women on the same basis as their husbands, and that does not discriminate against marriage and the family.

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Chapter 3: Transferable Allowances

3.1 Taken separately each of the objectives discussed in Chapter 2 could be met in various ways. A way of meeting all of them, however, would be by a new system of independent taxation with transferable allowances.

3.2 Under this system everyone - man or woman, married or single - would have a tax allowance in their own right, whether or not they were in paid employment. To recognise the shared responsibilities of a married couple, spouses who did not have enough income to use up their own tax allowance would be able, if they wished, to transfer the balance to their partner. A husband and wife's income would no longer be added together for tax purposes, and all taxpayers would have independence and privacy in their tax affairs.

3.3 Were a system of this kind to be introduced, the Government would aim to do it in such a way that no couple would suffer a reduction in cash terms in their total tax allowances during the change. The ultimate aim would be to get to a position where two new-style allowances amounted to the same as the total allowances available to a two-earner couple before the change.

3.4 On 1985-86 figures this would mean:

- Single people would have their allowance raised from £2,205 to £2,830.

- The married man who is the only earner in the family would have his tax threshold raised from £3,455 to £5,660 (assuming that his wife transferred her allowance to him).

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- Two-earner married couples and married couples where the wife is the sole earner would keep the same total allowances in cash terms, £5,660.

3.5 The loss of revenue from reducing the tax burden in this way would depend on developments during the period before the change is made. It would, for example, be affected by movements in prices and wages and by changes in tax rates and allowances in the years leading up to the change.

3.6 The change itself could theoretically be made in one year, or, more realistically, it could be phased in over a number of years. The sums that in any event would have been set aside for indexation of personal allowances - whose size would depend on the rate of inflation - could contribute to financing the change. The longer the period of phasing, the smaller the revenue forgone by way of tax reductions in addition to what would have been required for this indexation. At the extreme the change could be phased in over a period long enough to ensure that there was no loss of revenue beyond what would have been required for that purpose.

3.7 The table below illustrates what the average annual loss of revenue (at today's prices) would be if the move to this new structure of allowances were phased in over periods varying from two to five years. These revenue losses in effect indicate the cost of the change to the 'fiscal adjustment' - which measures the scope for reducing the overall tax burden.

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Phasing in Transferable Allowances

Loss of revenue: Average annual cost,
£ billion (at 1985-86 prices)

Two Year Transition

		Basic Rate of Income Tax		
		25%	27½%	30%
	0	2.3	2.5	2.7
Inflation (% pa)	2½	1.9	2.0	2.1
	5	1.4	1.5	1.6

Three Year Transition

		Basic Rate of Income Tax		
		25%	27½%	30%
	0	1.6	1.7	1.8
Inflation (% pa)	2½	1.1	1.2	1.3
	5	0.6	0.6	0.7

Five Year Transition

		Basic Rate of Income Tax		
		25%	27½%	30%
	0	0.9	1.0	1.1
Inflation (% pa)	2½	0.5	0.5	0.5
	5	0	0	0

3.8 The phasing would also have implications for the distributional effects of the change. During the transitional period, the cash allowances for single people and one-earner married couples would be increased in stages to the levels indicated in paragraph 3.4 and so would the amount of those allowances that would be transferable between spouses (see Annex 2). While the new systems was being phased in some taxpayers would find that their allowances remained unchanged in cash terms over a period of a year or more. The value of these allowances would therefore fall in real terms, with inflation. The extent of these possible real losses

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would depend upon the length of the transitional period and how any fiscal adjustment for overall tax cuts was being used during that period.

3.9 The decision about the length of the period of phasing cannot be taken now. It would be taken much nearer the introduction of the new system, in the light of economic circumstances at the time and in particular the scope for tax reductions. And the length of phasing could be altered while it was in progress if circumstances changed. The Government will make reductions in taxation only as and when it is prudent to do so. But their firm objective is to reduce the total burden of taxation, for all the reasons given in Chapter 1, and a move to transferable allowances should be seen as part of that process.

HUSBAND AND WIFE

3.10 If transferable allowances were introduced, married women would be treated as independent taxpayers: they would be responsible for their own tax affairs, be able to fill in their own tax returns, and to pay their own tax. It follows that the legislation which deems a married woman's income to be her husband's for tax purposes would be abolished.

3.11 Transferable allowances would give married women an opportunity for complete privacy in tax matters. Couples where the husband and wife both had income above the tax threshold would be treated, in effect, wholly independently. For other couples, any transfer of allowances would be wholly voluntary: people would not have to make any transfer, or they could transfer an amount less than the whole of their unused allowances if they so chose (accepting that their partner would be entitled to less tax relief in consequence of their choice).

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3.12 Annex 3 explains in more detail how transferable allowances would work in practice.

THE FAMILY

3.13 Transferable allowances would provide a means for recognising through the tax system that, at different times and for different reasons, one partner in a marriage may be financially dependent on the other. The Government reject the view that the tax system should pay no regard to the special relationship and responsibilities that exist within marriage. The aim is to recognise these in a way that is straightforward, flexible, and does not seek to make invidious distinctions between couples in different circumstances.

3.14 With transferable allowances there would no longer be discrimination against couples where, for whatever reason, the wife was not in paid employment. And since transferability could operate both ways between a husband and wife, the system would give equal recognition to circumstances where the husband did not have income but his wife did.

3.15 Transferable allowances would ensure that a couple's total allowances remained the same, and did not fall when one partner left paid work. This is often at a time when the couple may be under financial pressure, for example when they start a family.

3.16 The Government has already announced major proposals to strengthen and rationalise the support it provides for families with children through the social security system. Details were set out in the White Paper on the Reform of Social Security in December (Cmd 9691). General support will continue to be provided through the universal, flat rate child benefit. A new family credit scheme will be introduced to give substantial and well targeted extra help for low income

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families in work. And a new income support scheme will replace Supplementary Benefit with a family premium paid on top of the basic rate and in addition to the rates for individual children. Legislation is currently before Parliament to implement these changes.

3.17 The Government believe that the tax system should not discriminate against families where the wife wishes to remain at home to care for young children. Transferable allowances would direct more tax relief to such families.

3.18 The effect of transferable allowances on the willingness of married women to go out to work would need to be carefully considered. Since it would give everybody the same tax allowance, the system would treat married men and married women in exactly the same way. What it would remove is the present special incentive for two-earner couples, introduced in the war-time conditions of 1942. Such positive discrimination is neither necessary nor economically desirable at a time of high unemployment, particularly among the young (of both sexes). In principle, transferable allowances are neither an incentive nor a deterrent for married women seeking work.

3.19 It is sometimes argued that they would deter married women from seeking work, because they would suffer tax on every pound that they earned. That would not be the position. As already explained, married women would be entitled to the single person's allowance against their earnings or other income, in precisely the same way as any man or single woman. A variant of this argument is that, in practice, the husband would regard both allowances as a married man's allowance, and would not want his wife to go back to work because he would lose the benefit of her tax allowance. There can be no direct evidence for or against these views.

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But the experience of countries such as Canada, Sweden and Denmark, that operate a form of transferable tax allowance, does not suggest that this system discourages married women from going out to work. Denmark, for example, has the highest proportion of married women working of any country in the European Community.

3.20 By taxing a husband and wife separately and giving a married woman her own allowance and tax rate bands in the same way as any other taxpayer, transferable allowances could remove the tax penalty which arises for married couples where the wife has more than a modest amount of savings income. Paragraph 2.24 above lists the other main tax penalties on marriage. Chapters 4 and 5 below show how these penalties could be removed by a system of transferable allowances and also discuss other ways in which such a system would give married women privacy, and equal treatment, in their tax affairs.

RAISING THRESHOLDS

3.21 The introduction of transferable allowances in the way described in the opening section of this chapter would entail a substantial increase in tax allowances for married couples where the husband alone was in paid employment. Couples where the wife, too, had a paid job but earned less than the wife's earned income allowance (currently £2,205) and single people would also have increased allowances. Other couples where both partners had a paid job would have the same total allowances as before.

3.22 A change to transferable allowances would enhance the benefits of raising tax thresholds in two ways:

- The change itself would reduce the tax burden on couples at the time when only one partner has a paid job.

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- Once the new structure was in place, thresholds could be raised more cost-effectively than under the present system.

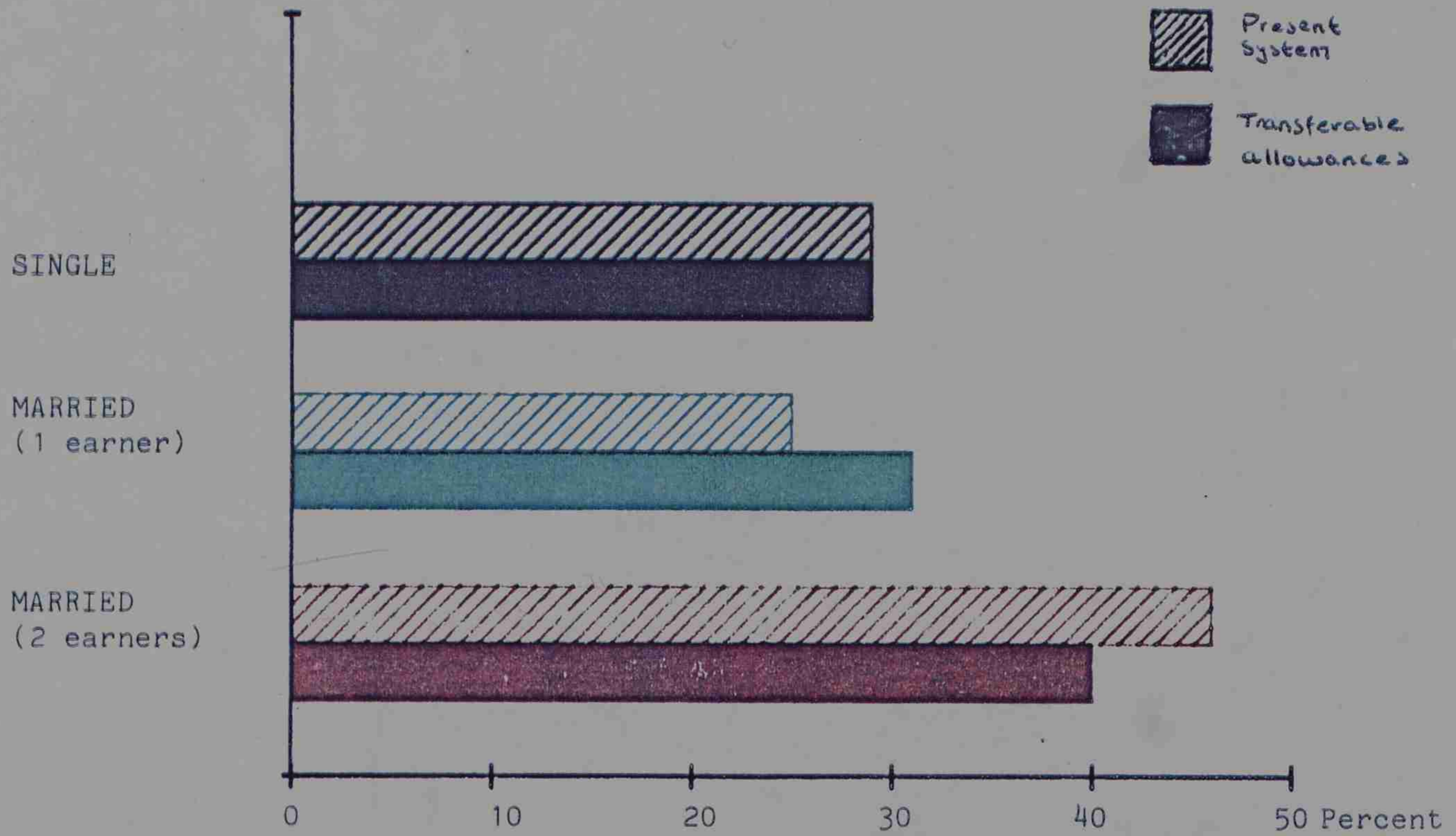
As can be seen from chart 3.1, the extra allowances for one-earner couples would mean that a higher proportion of the total amount of tax relief would go to these couples.

3.23 Chapter 2 explained why the Government wish to remove the discrimination in the tax system against one-earner couples. Their present tax allowances are much lower than those for two-earner couples. Couples generally have only one earner precisely at the stage in life when their family commitments are high - but under the present tax system that is when their allowances are low. Later, as both partners go back to work their allowances are higher. This is illustrated in the table below.

LIFE CYCLE STAGE	INCOME		% OF INCOME PAID IN TAX	
	Husband £	Wife £	Present System	Transferable Allowances
Young two-earner couple	8,000	4,000	15.9	15.9
Wife gives up work to have child	8,000	0	17.0	8.8
Husband works extra overtime	10,000	0	19.6	13.0
Wife resumes work part-time	10,000	2,000	16.4	15.9

3.24 Thus the present tax system takes no account of the changing needs of couples over their life cycle. Moreover, a particularly high proportion of the couples caught in the poverty and unemployment traps have only

CHART 3.1 : PERCENTAGE OF TAX RELIEF GOING TO
DIFFERENT FAMILIES
(Taxpayers of working age)



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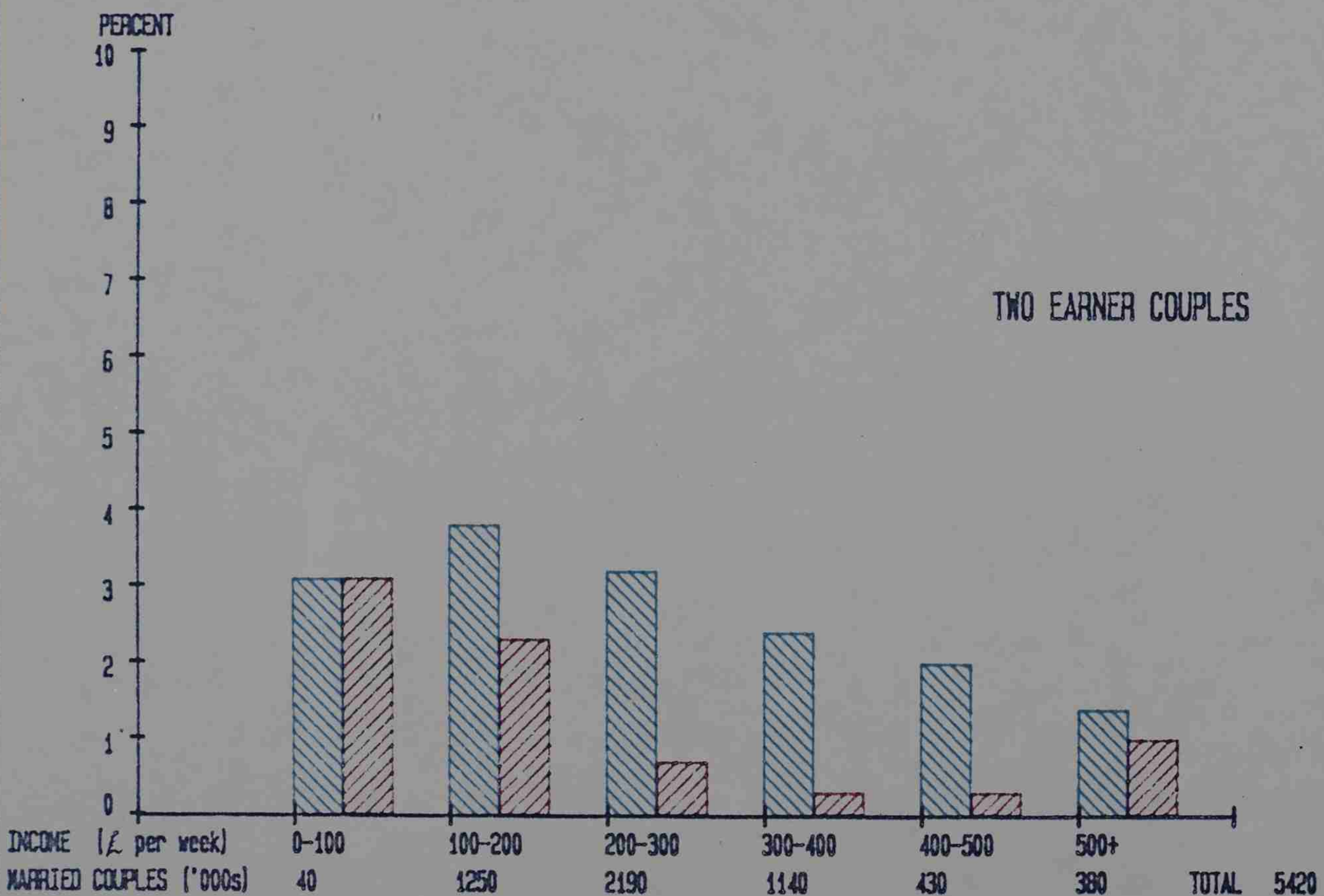
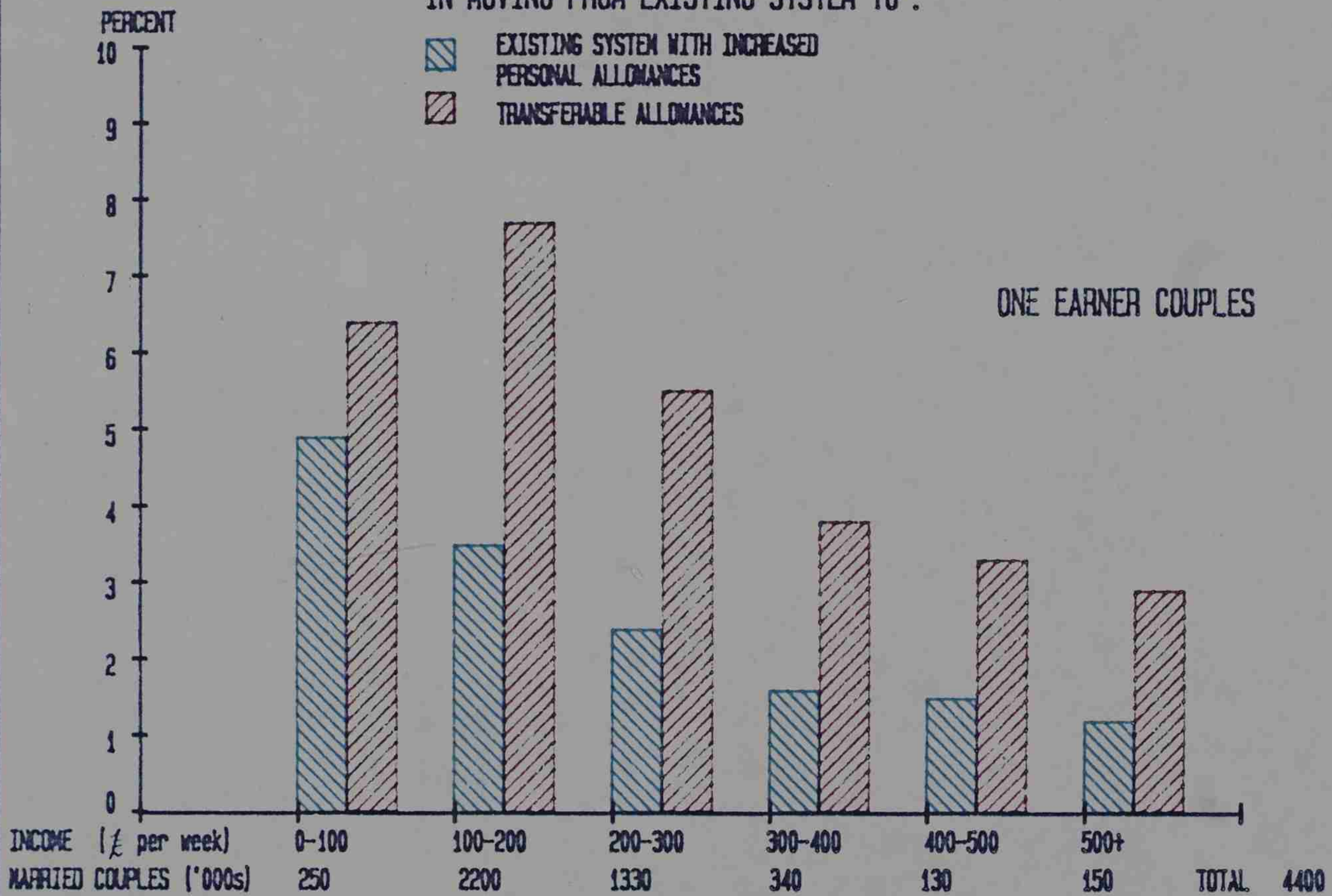
one earner. The introduction of transferable allowances would reinforce the benefits of the changes in social security proposed in the Social Security White Paper.

3.25 The effect of the change on people's tax payments would depend both on the structure of the new system and on what happened to the total tax burden when it was introduced. To isolate the structural effects the following paragraphs compare the effects of introducing the new system with what would happen if the same amount of revenue were spent on raising the present structure of allowances. In both cases the simplifying assumption is made that the changes are made in one step.

3.26 Chart 3.2 compares the effect of these alternatives on the proportion of income that would be paid in tax - the average rate of tax - by one-earner and two-earner couples at different income levels.

3.27 The red-shaded bars show the reduction in the average rate of tax if transferable allowances were introduced in the way assumed.. One-earner couples at all income levels would see their tax burden fall substantially. The fall would be most marked at lower incomes. Most two-earner couples would see no change in their average tax rate. However, as the chart shows, there would be some fall in the rate for two-earner couples as a whole. This would arise partly from the disaggregation of their incomes. More importantly it would reflect the fact that two groups among the two-earner couples would have their total allowances raised by the change. The first would be those couples where the wife was earning less than the wife's earned income allowance and the husband, with her agreement, would be able to set the unused portion of her personal allowance against his own income. The second group would be those couples who under the present system had already made a "wife's earnings election" (see Annex 1): these couples do not receive the married man's

CHART 3.2: REDUCTION IN AVERAGE RATE OF TAX (PERCENTAGE POINTS)
IN MOVING FROM EXISTING SYSTEM TO :



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allowance, and so for them the increase in the basic single allowance would not be offset by the withdrawal of the married man's allowance.

3.28 The blue-shaded bars in chart 3.2 show what the effect on average tax rates would be if, at the same loss of revenue, personal allowances were increased under the present structure. This would imply an across-the-board rise of 27 per cent in basic personal allowances. As will be seen, one-earner couples, at all income levels, would benefit more from transferable allowances than they would from this alternative way of reducing the tax burden. The improvement is particularly important for the lowest two income brackets, which include the couples caught in the poverty and unemployment traps. Transferable allowances would take one-earner couples with incomes below £109 a week out of tax; but the alternative measure would only take those with incomes below £84 a week out of tax.

3.29 In addition, the proportion of income paid in tax by those one-earner couples earning between £100 and £200 per week would drop substantially with transferable allowances on this illustrative basis.

3.30 The improvement in the relative position of one-earner couples means that transferable allowances would be more effective in helping couples in the poverty and unemployment traps than an increase in existing allowances involving the same revenue loss. Some two-thirds of married couples of working age with incomes below half average earnings are couples where the wife is not in paid employment.

3.31 Married men on low incomes with families to support are the group most likely to be in the unemployment trap. A rise in their tax allowances increases their net income when they are in work. This increases the incentive for all married men supporting families to

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take a job (though for some, under the proposed new structure for social security benefits, the increase in income would be offset in part by a fall in the income-related benefits they would receive). Transferable allowances could therefore ease the unemployment trap more than a straight increase, involving equal revenue loss, in personal allowances under the present system.

3.32 Very much the same factors mean that transferable allowances could be more effective in taking people out of the poverty trap, where again most of those in the trap are one-earner families.

3.33 Single people, who are particularly heavily represented among the 16-24 age group, where unemployment is highest, would also gain from the increase in the single allowance if transferable allowances were introduced on this basis. The increase would be roughly the same as would occur with an equal revenue-loss increase in allowances under the present system. Thus under transferable allowances, they would pay the same proportion of the total tax burden as they do now.

Threshold Increases under the New Structure

3.34 If transferable allowances were introduced, one-earner and two-earner couples would subsequently gain equally from any threshold increases. More of the benefit of increases in the allowances would go where they could be more effective. Transferable allowances could thus provide a more sensible - as well as a more straightforward - basis on which the Government could carry forward its long-term objective of further raising tax thresholds.

CONCLUSION

3.35 The Government will study the response to the Green Paper very carefully before deciding how to take

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these issues forward. If it is decided to proceed, legislation would then be introduced to permit transferable allowances. Annex 5 sets out a possible timetable for change, though it is stressed that, as with all other tax changes, transferable allowances could only be introduced as far and as fast as economic circumstances permitted.

CONFIDENTIAL**PART II - IMPLICATIONS FOR OTHER ALLOWANCES AND TAXES**Chapter 4: Treatment of Particular Groups

4.1 If transferable allowances were to be introduced, their effect on particular groups of people who are currently entitled to personal tax allowances other than the basic allowances would have to be considered.

ELDERLY PEOPLE

4.2 Most taxpayers over 65 are entitled to the age allowance. For a single person over 65 this is £2,690 for 1985-86 (compared with £2,205 for the basic single allowance). Where one partner in a marriage is over 65 the husband may claim an allowance of £4,255. The full benefit of the age allowance is obtained by those with taxable income (before deducting the allowance) of up to £8,800. For those with higher incomes the extra amount of the age allowance over the corresponding basic allowance is gradually withdrawn by reducing the allowance by £2 for every £3 of additional income. The benefit of the age allowance therefore runs out at an income of £9,528 for a single person and £10,000 for a married couple. If a married woman aged 65 or over has earned income (either from a job or in the form of her own pension) the wife's earned income allowance (£2,205) is available against it. Table 3 in Annex 4 gives details of the number of elderly taxpayers.

Age allowance

4.3 When it was introduced, the age allowance (and the similar provisions which preceded it) had two linked objectives - to recognise in a broad way, the additional expenses which the elderly might incur and to ensure that a high proportion of elderly people were kept out of income tax altogether. Accordingly, entitlement to age allowance was linked to reaching a particular age - 65. Qualification for the allowance is not tied either to payment of the national insurance retirement pension or to retirement itself. About 60 per cent of the total of 6½ million elderly households are not liable to income tax.

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4.4 While it is true that in some respects, taxpayers find that their living costs and expenses rise with the onset of old age, there is no evidence to suggest that this is true for taxpayers generally at age 65. And in other respects, there is evidence that people who pay tax find that their living costs fall at around this time. Those over 65 who are still in work no longer have to pay National Insurance Contributions; those who are owner-occupiers will usually have paid off the mortgage on their home; and those who retire no longer have to bear the cost of travelling to work.

4.5 The Select Committee on the Social Services in 1982⁽¹⁾ expressed doubts about the justification for the age allowance in its present form. The Committee questioned the rationale for an allowance based on attainment of a particular age and recommended that the Government should review the justification for continuing with the age allowance.

Transferable allowances and the elderly

4.6 A move to transferable allowances would tend to benefit elderly taxpayers through the general increase in their tax allowances. On the basis set out in Chapter 3, the basic single allowance would rise to £2,830, at 1985/86 levels - £140 above the present single age allowance. For a married couple where the wife has no earnings or occupational pension, the total allowances available would be £5,660, compared with the present married age allowance or £4,255.

4.7 There are also two special reasons why elderly taxpayers would benefit from such a change:

- First, a higher proportion of elderly couples are one-earner couples who stand to gain from transferable allowances. In over 70 per cent of taxpaying elderly couples, the wife has no earned income of her own (compared with 45 per cent of wives in younger couples).

⁽¹⁾ Report on the Age of Retirement Session 1981-82 HC 26-1 Paragraphs 131-132.

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- Second, a number of elderly married women do have savings income, and would benefit from having their own tax allowance to set against this.

4.8 Thus transferable allowances would raise the question of whether a separate tax threshold for the elderly was any longer necessary. If age allowance were subsumed in the change, this would be achieved in such a way no elderly single person or married couple would suffer a reduction in their total allowances in cash terms. This would bring about a simplification of the tax system, particularly for elderly taxpayers themselves. It would mean that taxpayers would be subject to the same tax rules throughout their lives.

SINGLE PARENTS

4.9 Under the present system, single parents with dependent children receive the Additional Personal Allowance (APA), of £1,250 in 1985-86, in addition to the single person's allowance. This means that single parents get allowances equal in total to the married man's allowance.

Support for single parents

4.10 Some 450,000 single parents, including 70-100,000 widows, will claim APA in 1985-86. An estimated 590,000 single parents claim One Parent Benefit (OPB) through the Social Security System. This is a flat-rate benefit of £4.55 per week paid for the first child of a one parent family in addition to child benefit. Widows with children receive widowed mother's allowance of £38.50 per week, plus a child dependency addition of £8.05 per week for each child, rather than OPB.

4.11 The case for rationalising provision for single parents by converting the APA into increased rates of benefit, in particular One Parent Benefit, was discussed in the Green Paper "The Taxation of Husband and Wife"⁽¹⁾ published in 1980. This

(1) Cmnd 8093

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approach would have a number of advantages. First, it would mean that financial support (from the State) for single parent families would be provided entirely through the social security system.

4.12 Second, the change would simplify the tax system by removing the one remaining tax allowance for children.

4.13 Third, like the conversion of child tax allowances into Child Benefit, the change would give more help to single parents who do not pay tax.

4.14 Fourth, the change would reduce the tax penalty on marriage. At present couples who are not legally married but who live together as man and wife can each claim APA (on top of their basic single allowances) if they have two or more children. Thus between them the couple get the equivalent of two married allowances. This is a widely resented element of the so-called tax penalty on marriage. Converting the allowance into a social security benefit would deal with this problem since the relevant benefits are, by law, not available to people living together as man and wife, and DHSS ensure that only those with single handed responsibility for children receive the benefits.

4.15 The vast majority of organisations and individuals who responded to the 1980 Green Paper favoured the option of converting the APA into increased social security provision and a change to a system of transferable allowances could provide an opportunity to make this change. As the 1980 Green Paper pointed out, however, this approach would have some disadvantages. The conversion would lower the tax threshold for lone parents: they would pay more tax and begin to pay it earlier. For them the overlap between payment of tax and receipt of benefits would be increased - precisely the opposite effect to that which the other proposals in this paper are designed to achieve. There would also be considerable practical problems in adjusting benefit provision for those lone parents, in particular widows, who receive support for their children through child dependency additions to their national insurance benefits rather than through OPB

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itself.

4.16 An alternative approach, which would avoid some of these difficulties, but which would remove the present tax penalty on marriage created by the APA would be to change the qualifying conditions for the allowance so that entitlement was linked to the receipt of OPB and other appropriate benefits (in particular child dependency additions to national insurance benefits). By this means it would be possible to ensure that only people who had single-handed responsibility for children received the allowance without the need for the Revenue to make a separate check on eligibility. It would be for consideration, how the necessary liaison between the DHSS and the Inland Revenue could be organised in order to ensure that the treatment of individuals was aligned. Once both departments were fully computerised in the early 1990s, one possibility might be that DHSS could notify the Inland Revenue automatically about those benefit recipients who would be entitled to the revised APA. If it proved practicable this would avoid the need for single parents to make a separate claim to the Inland Revenue for the allowance.

4.17 The APA is also available to a married man with a dependent child, if his wife is wholly incapacitated. Between 5,000 and 10,000 men currently qualify. Their total allowances in 1985/86 are £4,705 (married man's allowance of £3,455 plus APA of £1,250). One of the main aims of transferable allowances would be to recognise the situation where one partner in the marriage is - for whatever reason - dependent on the other and has insufficient income to use up their own tax allowance. This is precisely the position of the married man whose wife is incapacitated, and, on the illustrative levels of allowances in Chapter 3, such a person would get allowances of £5,660 under transferable allowances, compared to £4,705 at present. There would therefore no longer be a need for the APA in these cases, and it could be phased out in the event of a move to transferable allowances.

WIDOW'S BEREAVEMENT ALLOWANCE

4.18 The widow's bereavement allowance (which is set at £1,250 for 1985-86) is available to a widow in the tax year in which her husband dies and for the following year.

Tax treatment in year of bereavement

4.19 At present the tax year in which a married man dies is split into two parts for the purposes of calculating liability to tax. The married man's allowance is available against the couple's joint income in the period up to the husband's death and the wife's earned income allowance is also available against any earned income of the wife up to the same date. For the period after the date of death the widow is entitled to the basic single allowance and the widow's bereavement allowance against her income for this period.

4.20 Under transferable allowances both partners would be treated independently for tax purposes; there would be no need to separate the periods before and after the date of a husband's death. The year of death would be treated in the same way as any other tax year. Thus, if a partner in a married died before he or she had received sufficient income to use up his or her allowances, the unused balance would be available to set against the income of the surviving spouse. Where one partner had transferred allowances during the tax year to another who subsequently died there would normally be an increased repayment due to the estate of the deceased partner.

4.21 Under transferable allowances the widow's bereavement allowance could continue to be available in both the year of bereavement and the following year to help all widows with the difficult period of adjustment following a husband's death. There would be a case for increasing the allowance so that it was equal in size to the basic single allowance. An increase in the

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allowance would ensure that in the year of bereavement any entitlement to widow's pension or widowed mother's allowance would not of itself give rise to a liability to tax, even if the whole of a widow's own allowance had already been used against her own or her husband's income.

MINOR PERSONAL ALLOWANCES

4.22 The minor personal allowances are:

Dependent relative allowance (£145 for a single woman; £100 for others);

Housekeeper allowance (£100);

Son's or daughter's services allowance (£55);

Blind person's allowance (£360).

4.23 The first three of these allowances originated at a time when arrangements for the care of elderly or infirm people were very different from today.

4.24 Dependent relative allowance is given to people who supported a widowed mother or another relative who is unable to work because of old age or ill health. It was introduced in 1920 when many widows and elderly people had little or no income of their own, and hence relied largely on a relative for their maintenance and support. In the past 65 years there has been a significant trend away from this, as pensions have improved and elderly people have become more independent. Similarly housekeeper allowance, and son's or daughter's services allowance, were important at a time when many taxpayers employed a housekeeper, or had one of their children living with them to look after them. Such arrangements are now much less common. The development of the social security system has led to resources being concentrated on helping elderly people themselves rather than those who support them, and specific needs and disabilities have been recognised, for example by paying a cash benefit, attendance allowance, to

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people who are in need of frequent attention.

4.25 Successive Governments have taken the view, explicitly or implicitly, that these allowances have outlived their usefulness. Their cash values have not been increased for many years. A change to transferable allowances would provide an appropriate opportunity to subsume these allowances. If this were done, it would further simplify the personal tax system.

4.26 Different considerations apply to the Blind Person's Allowance, which is currently £360. The Government regard this as an important measure of help to working blind people. They believe it should be retained.

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Chapter 5: Other implications for the tax system

5.1 This Chapter considers the implications of a system of transferable allowances for other aspects of income tax and for the capital taxes.

Treatment of investment income

5.2 Many married couples - and elderly couples in particular - have some income from investments. The single most common type is building society interest. It represents about 40 per cent of investment income and two-thirds of couples with investment income receive it. The available information⁽¹⁾ suggests that perhaps 20 per cent or more of investment income belongs to wives (treating income jointly owned as split 50/50 between husband and wife) and so might therefore be affected by a change to independent taxation. Over half of all wives receive some investment income either in their own right or jointly with their husbands.

5.3 Under the present system a wife's investment income is added to her husband's for tax purposes and the combined amount is taxed as if it all belonged to the husband at his marginal rate. A wife has no allowance of her own to set against her investment income. As a result, some married couples find that between them they pay more tax than two single people in the same circumstances.

(1) See "Investment Income of Husbands and Wives" issued by the Inland Revenue in January 1981 as a Background Paper for the Green Paper "The Taxation of Husband and Wife", (Cmnd 8093). The Paper sets out the results of a special survey of the distribution of investment income between husband and wife. As the Paper explains, data about the investment income received by couples is subject to a number of limitations.

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5.4 If a system of transferable allowances were introduced this further tax penalty on marriage could be ended. A married woman would have a full personal allowance in her own right to set against her income, whether it is earned or from investments. And husband and wife would each have their own set of income tax rate bands available against their individual incomes.

5.5 Transferability of allowances would in itself go far to remove the present tax penalty on a wife's investment income. Where a wife has investment income but no earned income, transferable allowances would give the couple upto two single allowances against their incomes, compared with the equivalent of only $1\frac{1}{2}$ times the single allowance at present. Thus if the wife had only a small amount of investment income, she would pay no tax and would be able to transfer unused allowances to her husband, if she wished, so that the couple between them made full use of their new higher allowances.

5.6 For most couples, there would be no financial benefit from the extra set of rate bands, because all the income above the personal allowances would be taxed at the basic rate, both before and after the change. In the 10 per cent of cases where the couple currently pay tax at higher rates, ending aggregation would mean that the wife's investment income would be taxed at her own marginal rate, instead of at her husband's marginal rate; in most cases the husband's marginal rate would be the higher of the two.

5.7 Independent taxation would also give both husband and wife the opportunity for privacy in all of their tax affairs. In the present system there is no privacy for most married women, only for husbands. Under transferable allowances a wife could make a return of her own income and would no longer have to disclose details of the amount and source of her investment income to her husband.

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5.8 Overall the additional cost of allowing independent taxation of a wife's investment income compared with a transferable allowance system which retained aggregation of investment income would be about [£100 million]. This is the measure of the tax penalty the present aggregation rule imposes on marriage. The case for ending the present discrimination in the tax system against a married woman's investment income applies to incomes at all levels.

Rearrangement of investment income between husband and wife

5.9 If a married woman's income were taxed separately from her husband's, there would in some cases be an incentive for couples to rearrange the ownership of their income-producing assets between them. For example, if a husband with investment income was liable to tax at 60 per cent, whereas his wife was liable only at the basic rate of 30 per cent, the couple's combined tax bill would be reduced if the husband transferred some of his investments to his wife. This process of rearrangement is sometimes known as income splitting.

5.10 It is very unlikely that all couples would seek to rearrange the ownership of their income-bearing assets in order to take maximum advantage of separate tax rate bands. Many would not be able, or would not want, to make the necessary transfers of assets. But if, for example, those affected were to transfer assets yielding half the relevant investment income there could be a revenue cost of around £100 million.

5.11 The Government do not consider that there would be a case for special measures to prevent rearrangement of investment income between husbands and wives where this resulted from an outright gift or other complete and irrevocable transfer of the right to the underlying capital. There would be great practical difficulties enforcing such special provisions - for example, trying to determine how for a married couple's joint bank deposit derived from the married woman's own savings, as distinct from any money contributed by her husband. In any event, under a system of independent taxation, there is no reason in principle

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why couples where, say, the wife derives all or part of her capital from her husband should pay more income tax than a couple - in otherwise similar circumstances - where she derives her capital, say, from an inheritance. If one partner in a marriage made a genuine transfer of assets to the other, there would be no reason to impose a tax penalty on the income from those assets.

5.12 Different considerations would arise, however, where, for example, a husband might seek to transfer income to his wife (or vice versa), in order to enjoy a reduction in their joint income tax liability, without genuinely transferring the right to the underlying capital. It would be necessary to consider whether steps would need to be taken to prevent tax avoidance by this means.

Mortgage Interest Relief

5.13 One of the aims of independent taxation with transferable allowances would be to remove the tax penalties that can arise on marriage.

5.14 Under the present system, a married couple are entitled to mortgage interest relief on up to £30,000 of the loan to buy their main home. Single people are entitled to relief on up to £30,000 each. But where two or more single people borrow in order to buy the same home to live in, each can get relief on borrowing of up to £30,000, so that relief on £60,000 - and more - may be available for the same home. The fact that this opportunity is open to unmarried couples sharing the same home is widely seen as yet another tax penalty on marriage.

5.15 The case for removing this anomaly arises independently of the case for reforming personal allowances. But the inequity of the present rules would be accentuated under a system of independent taxation with transferable allowances.

5.16 One approach might therefore be to apply mortgage interest relief to the residence rather than to the individual taxpayer. Thus two or more people borrowing to buy a house as their main residence would share the £30,000 ration between them, whether they were married or unmarried. This would end the present advantage to unmarried couples.

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THE CAPITAL TAXES

5.17 The Government's approach to personal income tax is founded on two principles: that the tax system should recognise the fact of marriage and the responsibilities that go with it; and that the system should recognise the independence and equal standing of the husband and the wife within marriage. These same principles should apply to the capital taxes.

5.18 It will already be clear that the Government do not accept the view that the income tax system should, as a matter of principle, disregard the fact of marriage and, for income taxation purposes, treat husband and wife in precisely the same way as two quite separate people. By the same token, they reject the view that capital transfers between husband and wife should, in principle, be taxed in the same way as other capital transfers. And they believe that the practical effect would be quite unacceptable, most obviously in the case of the family home, the most important asset for most people.

Capital Transfer Tax (CTT)

5.19 Capital Transfer Tax is in general charged independently on each taxpayer, without differentiation by sex or marital status (with the important exception of transfers between spouses) marital status. Each spouse has his or her own threshold and set of ratebands. Each has a set of exemptions, such as the annual exemption for lifetime gifts. Chargeable transfers made by one spouse are not cumulated with those made by the other. Each spouse is responsible for delivery of accounts in respect of his or her lifetime transfers and is liable for the tax on them. Only in special circumstances may one spouse become liable to CTT on a transfer to a third party by the other spouse. Transfers between spouses domiciled in the UK - whether in lifetime or on death - are fully exempt from CTT.

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5.20 The Government see these provisions as wholly consistent with the objectives of transferable allowances. They would therefore see no need to change the present CTT provisions if transferable allowances were introduced.

Capital Gains Tax (CGT)

5.21 Under present arrangements, the gains of a wife living with her husband are generally assessed on the husband:

- the gains and losses of each spouse are aggregated⁽¹⁾ and the couple are entitled only to one annual exempt amount (currently £5,900);
- the husband is responsible for making a return of chargeable gains and assets acquired by both spouses, and the assessment is issued to him;
- transfers of assets between the spouses do not give rise to any liability at the time, but the partner to whom the assets are transferred takes over the acquisition costs of the transferor.

5.22 These arrangements are open to the same criticisms - on grounds of lack of independence and privacy - as the present arrangements for income tax. Here too there is a case for reform.

5.23 If transferable allowances were introduced there would be a case for reforming the capital gains provisions so that:

- capital gains would be separately chargeable on each of husband and wife;
- each would be entitled to an annual exempt amount (currently £5,900), any unused part of which would be transferable to the other spouse.

(1) Spouses can however elect instead to carry forward their own losses against their own future gains.

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- the present relief from capital gains tax for transfers of assets between husband and wife would be retained but the provisions which allow the losses of one spouse to be set against the gains of the other would be withdrawn.

5.24 The Government see no reason to change the present capital gains tax relief that is available on the disposal of a private residence. Where a married couple living together have only one house, whether it is owned by the husband or wife or jointly, the relief would continue to apply. Where such a couple have more than one residence, they could, as at present, designate one as their main residence for the purpose of relief.

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PART III - THE TAX SYSTEM IN THE LONGER TERM

CHAPTER 6: TAXES AND BENEFITS

6.1 There is a wide overlap between the tax and social security systems. Originally income tax was paid by only the richest in the land and the social security system was concerned with the very poorest. Now, some 20 million families or single people pay income tax, and there are also 18 million receiving social security benefits. Often the same people are both paying income tax and drawing benefits. Chart 6.1 shows the extent of the overlap for each benefit.

6.2 This overlap has led many people to argue that the relationship between tax and benefits should be rationalised. This Chapter considers the possibilities for such rationalisation. It looks first at the proposals made in the early 1970s for a closer link between tax and benefits, and then at the case for moving in this direction today.

The Tax Credit System

6.3 Improving the relationship between tax and social security was the main object of the tax credit proposals put forward in a Green Paper in 1972⁽¹⁾. The scheme would have introduced a new tax credit that for most people would have taken the place of the main income tax personal allowances and family allowances. When paying wages the employer would deduct tax at the basic rate (30 per cent) from the whole of those wages. Against this tax, the employer would set the amount of credit to which the taxpayer was entitled. If credit exceeded tax, the difference would be paid to the taxpayer; if tax exceeded credit, the difference would stand as a tax deduction.

6.4 The tax credit scheme would have applied to people in regular employment earning above a certain amount, to retirement pensioners and people receiving other national insurance benefits, and to certain others. The self-employed were not within it nor were married women, though the coverage was to be kept under review.

(1) "Proposals for a Tax Credit System" Cmnd 5116; October 1972

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6.5 The scheme was expected to achieve a major administrative simplification. Computerisation, simplification of tax allowances and deduction of tax at source from bank interest would have made the tax system less complex and less expensive to run. Family Income Supplement would have been abolished. The other social security benefits would have continued, but there would have been less need to "top up" national insurance benefits with supplementary benefit.

6.6 Work on the tax credit scheme stopped in 1974 with the change in Government. But since then there have been many other changes in both the tax and benefit systems. Many ideas originally part of the tax credit scheme have since been implemented independently; including the replacement of child tax allowances and family allowances by child benefit, the taxation of unemployment benefit, and the introduction of statutory sick pay which means that most payments for short-term sickness are taxable.

6.7 Many of the administrative savings that would have flowed from the tax credit scheme have also been realised, in particular from changes in the treatment of mortgage interest relief and life assurance premium relief, and the introduction of a composite rate of tax on bank deposit interest. Others are in prospect, as a result of the computerisation of PAYE. In the form originally proposed, the 1972 tax credit scheme was expected to produce possible net staff savings of the order of 10-15,000. The administrative changes already implemented or in prospect will have produced staff savings of around 13,000 by 1988.

6.8 The illustrative rates of tax credit used in the 1972 Green Paper were those necessary to finance the abolition of the FIS for employees, at a net Exchequer cost of £1.3 billion. The cost would be much larger now, largely because since 1972 FIS income limits have risen faster than earnings, while tax thresholds have fallen as a percentage of earnings. Whereas in 1974-75 80 per cent of FIS recipients were below the tax threshold, now around two-thirds of recipients are above it. The cost of a tax credit scheme now, at a rate sufficient to enable FIS to be abolished would be some £8 billion. A scheme large enough to achieve the objectives of the new family credit scheme would involve a further large cost.

Looking to the future

6.9 There could be advantage in greater integration of the tax and benefit systems, where this would produce a more coherent and logical pattern of payments, simplify the systems and help to deal with the poverty and unemployment traps. The Government have taken a number of important steps in this direction, and will take others as opportunity offers.

6.10 But the Government do not regard integration as an overriding objective in its own right. Bringing together the mechanics of the two systems is not an end in itself. The Government believe it philosophically important not to blur the distinction between reward for effort and support for need, between what individuals gain for themselves and what they receive from the State. Moreover, the fact that taxes and benefits have different functions leads to big differences in the way the two systems work. There are also variations between benefits, with sharp distinctions, for instance, between income related and contribution-based benefits.

6.11 Suggestions have been put forward from time to time for the integration of all social security benefits with the tax system, or at least for the integration of the income related benefits with tax. The details and likely effects of such schemes differ considerably. However proposals tend to be based on two broad alternative approaches:

- entitlement to benefit should depend simply on income, as assessed for tax purposes. Under this approach, total integration would imply that benefits paid on the basis of contributions (eg retirement pension) or to reflect particular circumstances (eg child benefit) would be withdrawn from people with higher incomes;
- a basic benefit or credit should be provided to everyone, pitched at a level sufficiently generous to remove the need for separate benefits; and earnings and other income should be taxed more heavily in order to recoup the cost.

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There are many variants of these approaches, and particular schemes may incorporate elements from both. With such schemes, it is suggested, the need for two separate administrative systems would largely or completely disappear.

6.12 In spite of the superficial attractions of such all-embracing schemes, the Government has serious reservations about either approach. The first would conflict with the principle - reaffirmed in the White Paper "Reform of Social Security" - that eligibility for National Insurance benefits should be based on contributions. Income-testing all pensioners, for example, and paying the retirement pension only to those on low incomes would not be acceptable, however sensitively carried out. Conversely, to pay a substantial basic benefit to everyone, irrespective of their financial circumstances, would imply quite unacceptable increases in public expenditure and in the level and burden of taxation on earnings. This in turn would worsen work incentives. Unless the basic benefit were pitched at a very generous level for everyone, there would be a continued need for fall-back income-related benefits to cope, for example, with high housing or other costs. Moreover, total integration could not be achieved without a good deal of upheaval and this in itself has costs.

6.13 The Government's approach, therefore, is to promote closer integration between tax and benefits where this is consistent with the primary objectives of the systems, is practicable and offers greater efficiency, but not to pursue all-embracing, "big-bang" solutions which put administrative tidiness before fundamental social and economic objectives.

6.14 The proposals in Part I of this paper and others already announced will produce a more coherent relationship between the tax and social security systems:

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- Transferable allowances would reduce the numbers of people who are both paying tax and receiving income-related benefits. They would reduce the present overlap between the two systems.
- Paying the new family credit and housing benefit on the basis of net income will end marginal rates of 100% or more as a result of the interaction of the tax and social security systems.
- Introducing the new Statutory Maternity Allowance will carry forward the programme of bringing the main earnings-replacement benefits into tax, building on the progress already made with unemployment benefit and Statutory Sick Pay;
- Paying family credit through the pay packet will reduce "churning" by eliminating the present arrangement under which one member of a family may be paying tax and contributions to the State while another member is in receipt of FIS from that State.
- It will also make much clearer the net family income in work for those families receiving support.
- Moving the uprating date for social security benefits to April will enable changes in benefits to be synchronised with changes in tax.

Together, these changes will mark a major step in streamlining the systems. Moreover, by simplifying and computerising both the tax and benefit systems, the Government will have created a better basis for further steps in the future. In developing the two systems the Government will seek further opportunities for improvements of this sort. The Government is therefore taking steps to ensure that the computer systems of the Inland Revenue and DHSS are compatible, so that opportunities for integration can be exploited. This in itself may widen the range of these opportunities.

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6.15 Closer integration between taxes and benefits could take either or both of two forms. Under the first, the tax system could be used to assess the eligibility of people for income-related benefits. Under the second, a single system of payments could be introduced, setting off benefits against tax, so that only one net payment is made to or from each individual or family. These possibilities are discussed in the following sections of this chapter.

Assessment of benefits through the tax system

6.16 One of the aims of closer integration between the tax and benefit systems would be to make greater use of common information both for tax purposes and to assess entitlement to benefits. Such an approach might reduce administrative overlaps. It could also make claiming a more acceptable, more automatic process and help more people to receive their full benefit entitlement.

6.17 Of course, the argument is relevant primarily for those benefits that are assessed mainly on the basis of income. Entitlement to other classes of benefits, such as those assessed on the basis of past contributions, or on the grounds of medical factors such as disability, could not be assessed readily through the tax system. Where entitlement is based primarily on income, however, there may be a case for closer integration.

6.18 How appropriate such integration would actually be in practice varies, however, even from one income-related benefit to another. One question is the degree of overlap between the particular benefit and tax. At one extreme the overlap between supplementary benefit (and the new income support) and tax is minimal. On the other hand, around two-thirds of those receiving FIS are taxpayers, and the proportion is likely to increase for the new family credit. About a quarter of housing benefit recipients are taxpayers. But only a small proportion of taxpayers are eligible for any of those benefits (see Chart 6).

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6.19 Assessing benefit entitlement through the tax system would require a good deal of information which is not currently needed for tax purposes and is therefore not collected. At present, the Inland Revenue do not need detailed information on the family circumstances and total family income of vast majority of taxpayers: less than one-third of taxpayers fill in an annual return, and most of these are people on higher levels of income. There are also a number of significant practical differences between income-related benefits and tax which would have to be taken into account in considering the possibility of further integration. They include:

- differences in the unit of assessment. Most income-related benefits have regard to the income and needs, not only of the individual making the claim, but of the family as a whole. By contrast, husbands and wives can have their earnings treated wholly independently for tax purposes, and there are strong arguments, on grounds of independence and privacy, for treating husbands and wives even more independently on tax matters. Unmarried couples have always been treated independently for tax purposes.
- differences in the way resources are measured. For example, entitlement to income-related benefits depends amongst other things on the capital resources of the claimant. The tax system, by contrast, does not generally need to collect information about capital resources.
- differences in the timescale of measuring income and needs for assessment purposes. Supplementary benefit is based on current income or other means. This is because, in the last resort, the social security system has to ensure that families can manage from day to day. Family income supplement, housing benefit and the planning family credit are also assessed on the basis of - broadly speaking - current income, but rates of payment change much less frequently. FIS continues

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in payment at the same rate for a year, irrespective of changes of circumstances, and Family Credit will generally do so for 6 months. There are thus differences between the benefits in the timescale over which income is measured for assessment purposes and in the required responsiveness of the assessment system to changes in circumstances. Liability for tax, by contrast, is measured over a period of not less than 12 months and the family's total taxable income cannot be known until after the end of the year.

6.20 Clearly it would be necessary to overcome such differences in order to bring benefit assessment into the tax system. How easy, and how appropriate, it would be to do so varies from benefit to benefit. The case appears strongest for the new family credit. The position is less favourable for Housing Benefit, which is related not just to levels of income but also to individual, and widely varying, housing characteristics and costs. Supplementary benefit and income support have little overlap with tax and have to be quickly responsive to varied and sometimes rapidly changing circumstances, so they could not fit within the present tax structure.

6.21 The new family credit is designed specially to help low-income working families with children, and does not require the immediate responsiveness of income support. This is the area which the Government regards as the most promising longer-term possibility. The Government will therefore consider particularly closely the case for further integration of the assessment of tax and family credit in the light of responses to this Green Paper and eventual decisions on the long-term shape of the tax system. In the meantime, the DHSS and Inland Revenue will ensure that their computer developments are compatible so that information could be exchanged (subject to the need to protect privacy) and so as to provide a technical infrastructure more readily able to handle such a system.

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Delivery of benefits through the tax system

6.22 Integration of the payment of tax and benefits raises many of the same issues as those raised by integration of assessment. In both cases, integration seems likely to make practical sense only where there is significant overlap between those receiving the benefit and those paying the tax. In both cases, it is least likely to be desirable for benefits which, like Supplementary Benefit, are aimed at meeting needs which may vary frequently. But some further integration of payment, as opposed to assessment, could make sense for National Insurance as well as income-related benefits.

6.23 The Government has already made a major step towards integration of payment with its proposals for the new family credit. The White Paper on the Reform of Social Security has proposed that the credit should be paid through the wage packet. For most recipients this means that it will in practice appear as an offset to their national insurance and tax payments. This will reduce the present degree of churning and make the system clearer and simpler to the beneficiary. The Government will keep under review the possibility of making similar arrangements for other benefits when computerisation of the Inland Revenue and DHSS is complete.

6.24 One important area which the Government intends to examine further is the method of taxing National Insurance benefits. At present it is not always possible to take advantage of the Government's dual role in paying and taxing these benefits. In particular, the Government will explore further the scope for applying PAYE to the National Insurance retirement pension, so that so far as possible a pensioner would receive his pension from the Government, after any tax due to the Government had been deducted. This would not be cost-effective at the moment, but the balance of advantage may change when computerisation is complete. They will also explore the possibility of bringing some other benefits, such as sickness and maternity benefits, and into tax.

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Conclusion

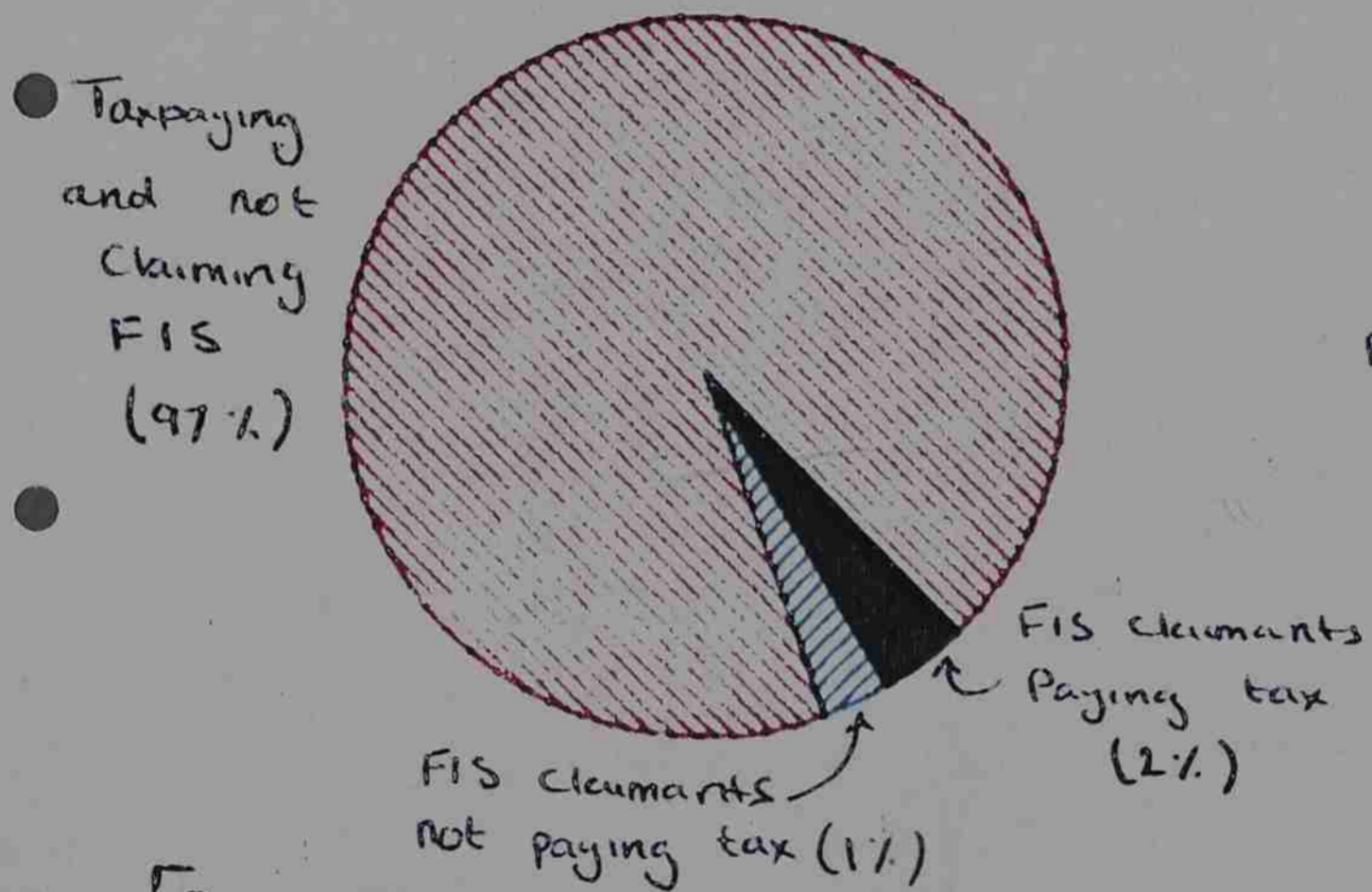
6.25 This analysis suggests that, although full integration of all benefits with tax is never likely to be either desirable or practical, some partial or further steps towards integration may become both. The Government would welcome comments on the longer-term possibilities and will ensure that opportunities for closer working of the systems are taken where they make practical sense and do not confuse the real differences of function between tax and benefits.

6.26 There remains the question whether the two revenue-raising systems - income tax and national insurance contributions - might usefully be brought together. This is the subject of the next chapter.

CHART 6.1 : EXAMPLES OF OVERLAP BETWEEN TAX & BENEFITS

INCOME RELATED BENEFITS

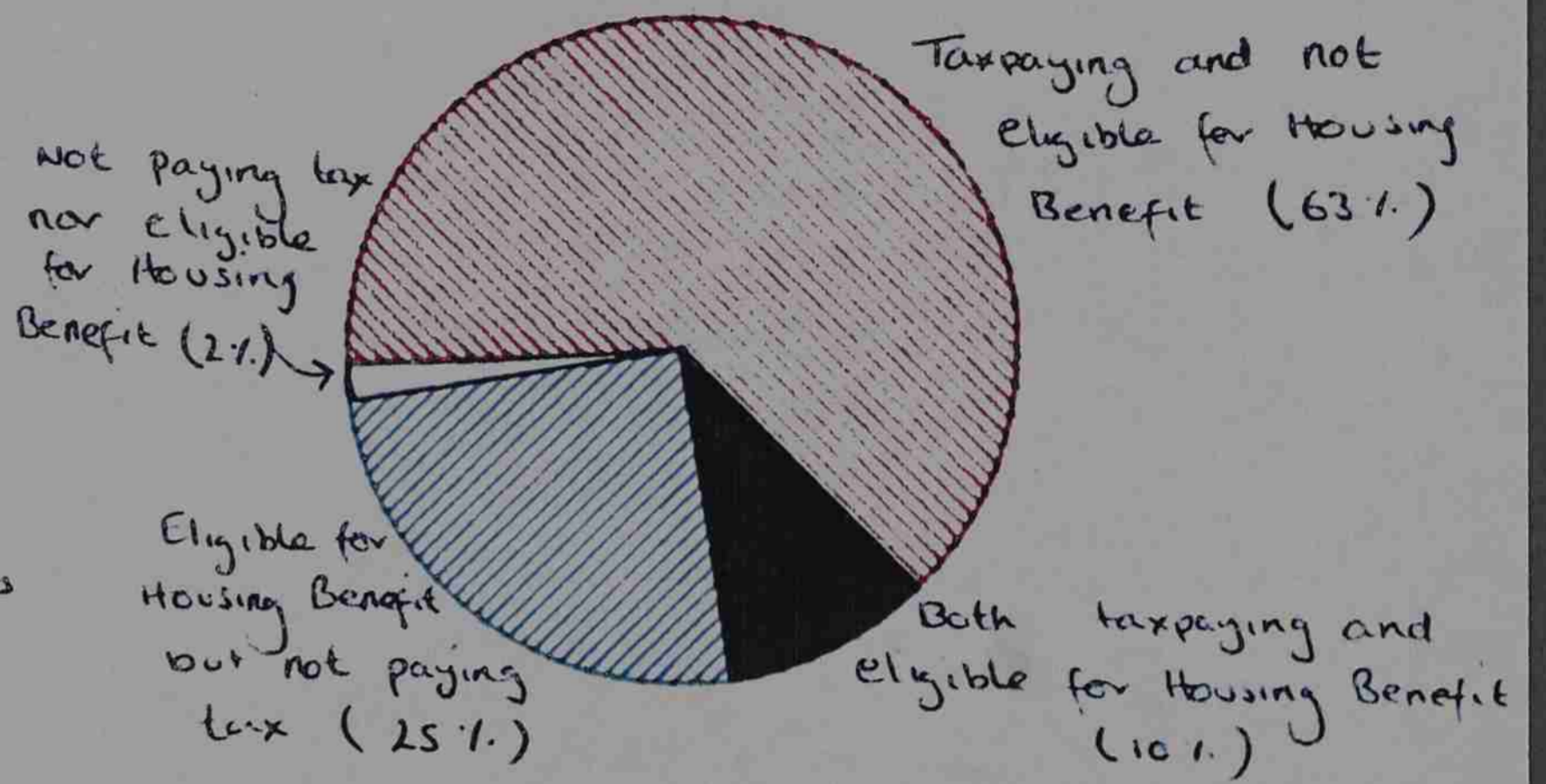
FAMILY INCOME SUPPLEMENT



Base for percentages: Employed families with children

Source: Survey of Personal Incomes & DSS administrative data

HOUSING BENEFIT

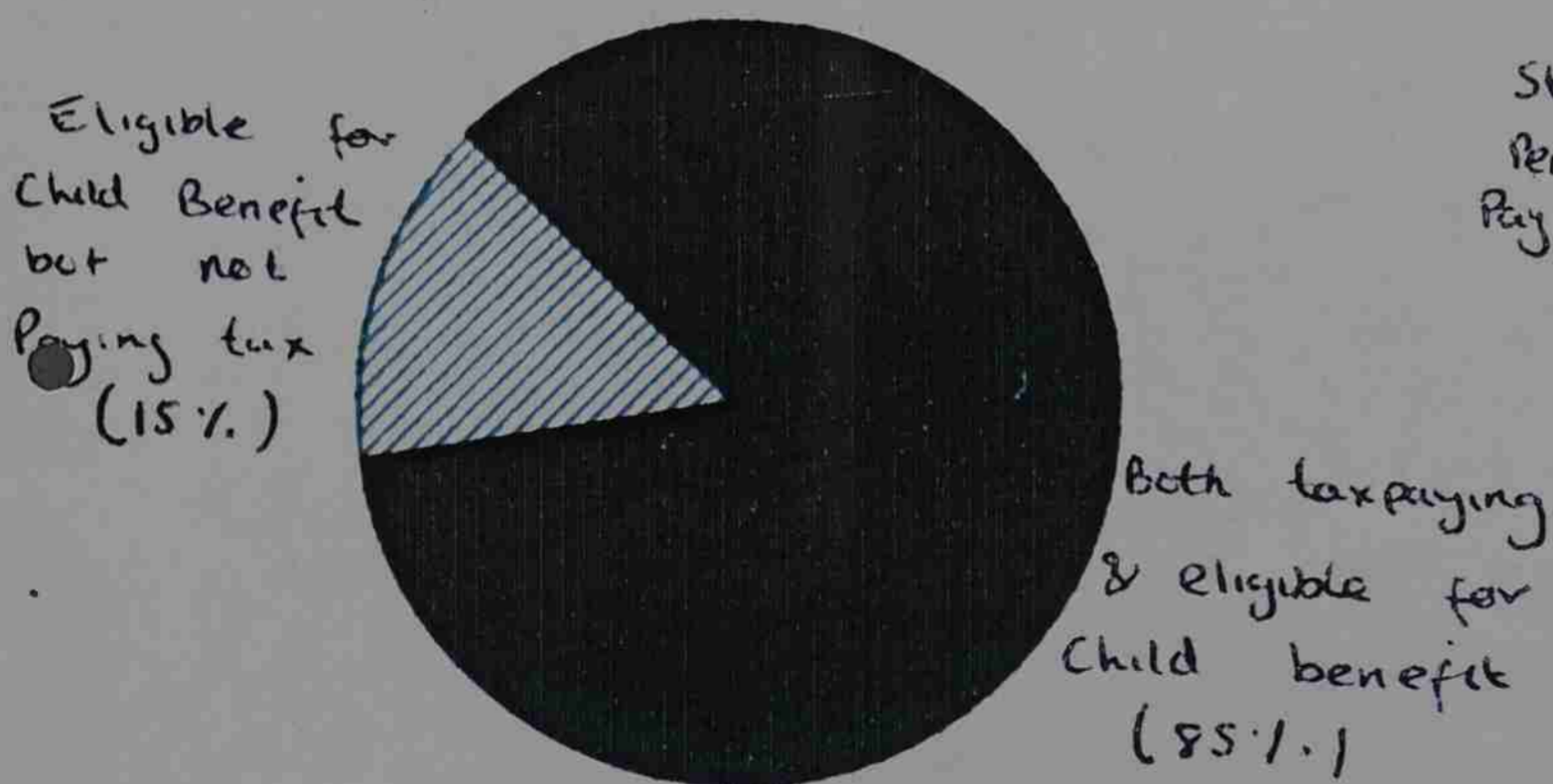


Base for percentages: all households

Source: 1983 Family Expenditure Survey

NON-INCOME RELATED BENEFITS

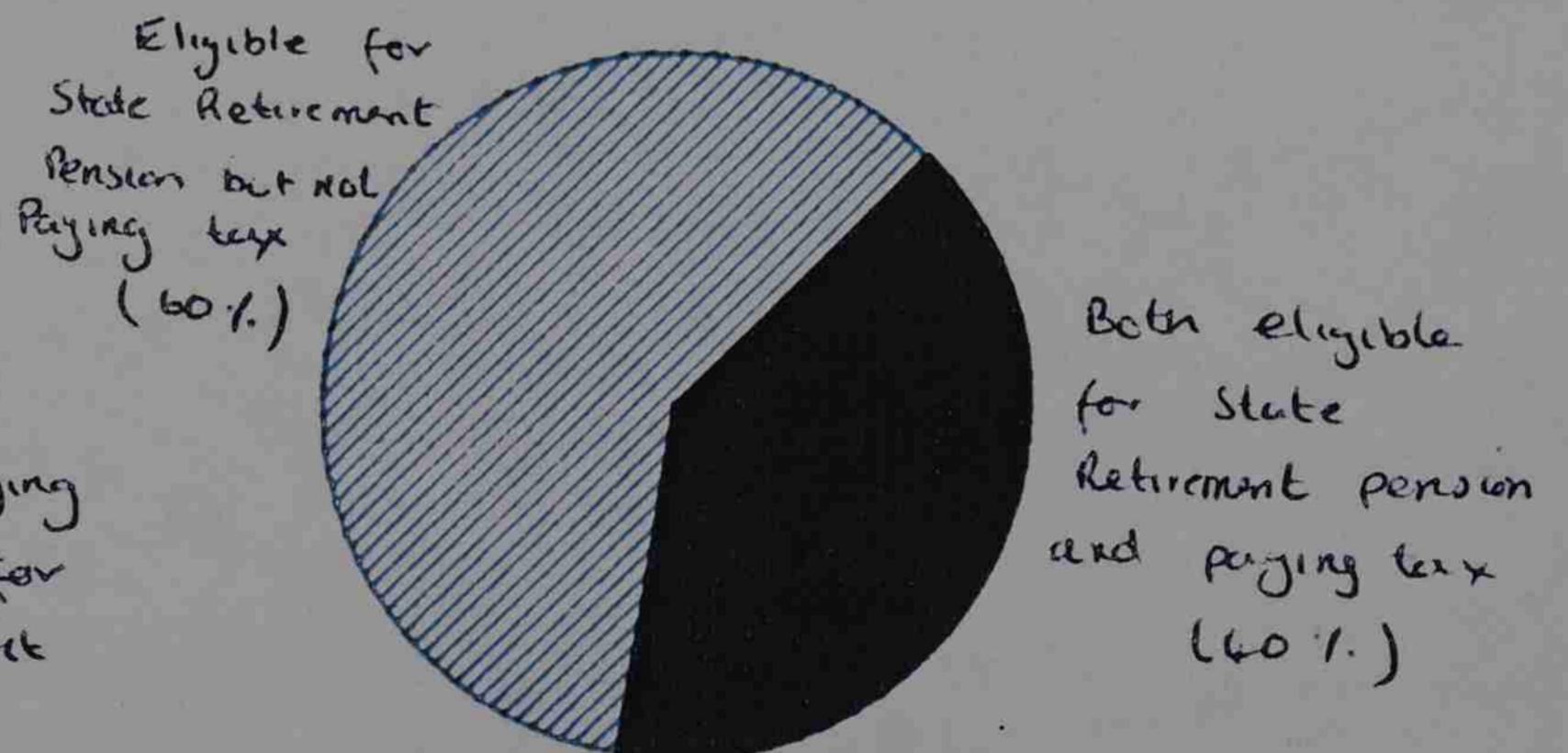
CHILD BENEFIT



Base for percentages: Families with children

Source: 1983 Family Expenditure Survey

STATE RETIREMENT PENSION



Base for percentages: Families entitled to State Retirement Pension

Source: Survey of Personal Incomes and Population estimates

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Chapter 7: Integration of National Insurance Contributions
And Income Tax

7.1 Earnings are subject to two charges: income tax and employees' National Insurance Contributions (NICs). Other forms of income, such as pensions, investment income and some social security benefits, are subject to income tax, but not NICs.

7.2 It has frequently been suggested that it would be more efficient if the existing two charges on earnings - income tax and employees' NICs - with their different but overlapping bases were replaced with one combined charge to replace income tax and employee NICs. The main argument for a single charge is that it would simplify the overall structure of the administrative system, and reduce the compliance burdens which employers currently face in dealing with two separate systems. (Employers' NICs could remain as a separate charge; the Green Paper on Social Security reaffirmed the continuing need for some form of employers' contribution to the National Insurance fund.)

7.3 It has already been possible for the collection arrangements to be substantially integrated. Employers deduct both income tax and NICs from their employees' earnings, record those deductions on the same document and pay both over to the Inland Revenue in a single payment. The Inland Revenue divide the payment into an income tax component, which is paid into the Consolidated Fund, and a NIC component, which is paid mainly to the National Insurance Fund.⁽¹⁾ The Inland Revenue also collects Class 4 contributions from the self-employed at the same time as it collects Schedule D income tax.

7.4 In order to consider the arguments for and against a combined charge, it is necessary to look at the present differences between the two charges:

(1) A small amount of the income from contributions goes to the Maternity Pay Fund, the Redundancy Pay Fund and the National Health Service.

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Differences between Income Tax and National Insurance Contributions

a. Base for charge. NICs are charged on earnings, and only earnings, of all employees and the self-employed with the exception of those over pensionable age. They are not charged on pensions, investment income and social security benefits. Income tax is charged on all income, including investment income, pensions, certain lump sums, and certain income replacement benefits such as unemployment benefit. NICs paid by employees and the self-employed raise about £12 billion per year, while income tax raises about £35 billion.

b. Structure of charge. Everyone earning at or above the Lower Earnings Limit (LEL) (currently £35.50 per week) pays employee national insurance contributions on all their earnings up to the Upper Earnings Limit (UEL) (currently £265 per week). The employee rates build up in a graduated structure from 5 per cent to a flat 9 per cent. The self-employed pay a flat rate (Class 2) contribution plus a percentage of their profits between certain limits (Class 4). In the case of income tax, there are personal allowances which exempt the first slice of income from tax; tax is charged at graduated rates on the amount by which income exceeds the tax-free allowance, but there is no ceiling on the amount of income charged.

c. Reliefs and Rebates. There are no reliefs that can be set against NICs. Once the LEL is reached contributions are charged without regard to individual circumstances, though married women, and certain special categories of people, such as those in the Forces, pay lower

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contribution rates, reflecting differing benefit entitlements. For income tax, as well as the personal allowances, there is a wide range of reliefs reflecting individual circumstances, eg for mortgage interest and superannuation contributions, which reduce the amount of income on which tax is chargeable.

d. Period of Assessment. NICs are due in each pay period (a week or a month for most employees) on earnings in the pay period. Each pay period is assessed individually and without regard to the previous earnings record of the employee. So an employee is liable to NICs in any period when earnings reach the LEL. Liability to income tax is measured by reference to income over the year from 6 April to 5 April. A person is not liable to income tax unless his total income for the year exceeds his allowances.

e. Basis of Deduction from Pay. For employees NICs are deducted on a non-cumulative basis. Each pay period is treated separately. Income tax is deducted on a cumulative basis so that deductions in each pay period take account of earnings and allowances that have accrued from the start of the year.

Implications of Full Integration

7.5 Levying a new combined charge on the same basis as income tax would in effect mean that tax allowances would be deducted from earnings before calculating NICs, but that all income above the tax allowance would become liable to NICs. In addition, tax reliefs would be available against the combined charge; they are not, of course, available against NICs. Since the revenue loss from these changes would exceed the revenue

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gain from the extension to all income, at present rates of allowances, the combined charge would have to be set at 40 per cent to remain revenue neutral. Those with low earnings would tend to gain overall because the tax allowance would reduce their liability. But this would be at the expense of taxpayers with income not currently subject to employee NICs, such as State and occupational pensions, investment income and earnings above the UEL.

7.6 Applying the new combined charge to all income would result in significant shifts in the tax burden between different sections of the community. Elderly taxpayers and other pensioners would probably be the largest group to suffer disadvantage, since they do not currently pay NICs. Other groups who would be adversely affected would be many basic rate taxpayers with earnings above the UEL (currently £265 per week), and all higher rate taxpayers.

7.7 As noted earlier in this Green Paper, distributional effects are not in themselves a conclusive argument against tax changes; otherwise nothing would ever be changed. But wide-ranging shifts on the lines described above would be hard to justify on either economic or social grounds.

7.8 Moreover, there is an important principle enshrined in the present arrangements, namely that eligibility for National Insurance benefits should be related to the contributions paid. This would be seriously weakened by a combined charge applied to all income.

7.9 Entitlement to National Insurance benefits depends upon payment of the appropriate amount of NICs. Those who have made sufficient qualifying payments are entitled to such benefits, without means-testing, if they experience one of the contingencies that the benefits

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cover. People who do not have an adequate payments record are in some cases not entitled to benefit; or in others, merely entitled to part-benefit. They may of course then be eligible for other state benefits subject to a means test, but this would normally be at a lower rate. If employee and self-employed NICs were abolished as a separate charge the form of the contributory principle would have to be reconsidered; it could not continue on its existing basis.

7.10 The Government's commitment to the contributory principle was made clear in the Green Paper, "Reform of Social Security":

"The principle that entitlement to benefits should be related to contributions paid is an important one to which the Government is firmly committed. The Government believe that it is right to retain a link between contributions paid in and benefits received".⁽¹⁾

7.11 There are several reasons for retaining a direct link between payments and entitlement to benefit. People value the unqualified right to benefit which their payments confer upon them. Contributors in effect insure themselves both against temporary loss of earnings and to provide themselves with income support when their working lives are over. Such arrangements bring home the cost of NI benefits. If benefits were paid to everyone, regardless of their contribution record, there would be substantial extra costs which would have to be borne by the general body of taxpayers. At the extreme, the absence of a qualifying test would open contributory benefits, such as the full state pension, to people who had just arrived in the country. Other safety net arrangements exist to deal with such cases where there is hardship. It would destroy the rationale of contributory benefits to make them available

(1) Reform of Social Security. Volume 1 (Cmnd 9517)
Chapter 11.1

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without regard to contributions. The Government does not consider that this would be acceptable.

7.12 It would be very difficult to sustain the contributory principle with a combined charge applied to all income. In the case of people solely or mainly dependent on investment income, they would be paying for benefits, such as unemployment benefit, to which they were not entitled. Tax-paying pensioners would in a sense be asked to pay twice: after a lifetime of paying NICs, they would then have to pay contributions towards benefits which they thought they had earned as of right on the basis of their earlier contributions record. This kind of anomaly would tend to weaken the link between contributions and entitlement and thus undermine the contributory principle.

7.13 Problems would also arise as a result of setting a tax-free allowance against liability to the combined charge. Some people who currently pay NICs would find themselves taken out of charge altogether. Should they be entitled to National Insurance benefits to which they would not have contributed? The problem could become significant as tax allowances increase, for example, as a result of transferable allowances. A further question would arise in the case of an individual whose earnings just exceeded the tax allowance. Should he be entitled to National Insurance benefits on the basis of minimal contributions? These examples illustrate the problems of reconciling a combined charge with the contributory principle.

A Combined Charge with Limited Coverage

7.14 Because the distributional consequences of applying the new combined charge to all income are recognised, it is sometimes suggested that exceptions should be made to the coverage of any combined charge. The elderly, for example, could be exempted from it,

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while investment income could be treated differently from earnings and taxed at a separate rate. The groups who currently pay their own lower employee NICs could have a special rate of combined charge. All these arrangements would mean that those who paid the combined charge were in essence those who pay income tax and employees NICs now. But to pay for these exemptions the tax rate of the combined charge would have to be increased to compensate for the lost revenue. This would increase the extra tax paid by those above the UEL and also mean that some of those earning below the UEL would pay more tax. The loss would be proportionately greatest for those towards the top end of the current basic rate band, but the higher marginal tax rates would have adverse consequences for incentives throughout the income range on which they were levied.

7.15 A combined charge limited more or less to those who now pay employee NICs would probably do less damage to the contributory principle than one applied to all income. But the difficulties mentioned in paragraph 7.13 above would remain).

7.16 Perhaps the strongest objection to trying to restrict the base of a new combined charge in the way suggested above would be that simplicity, the main aim of the new combined charge, would be lost. There would no longer be a single tax on all income. Earners would be subjected to the new combined charge, tax-paying pensioners would pay some different rate, which might or might not be the same as that paid on unearned income. Even the combined charge itself would have to have more than one rate. This would be necessary if the special groups were not to find themselves worse off. It would also arise as a result of the rebate for those contracted out of the State Earnings Related Pension Scheme. At this point the whole rationale for introducing a combined charge becomes very questionable.

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Conclusions

7.17 A combined charge replacing both income tax and employees' NICs could lead to reductions in administrative costs. The size of these would depend on the precise scope and nature of the new charge, and on the form taken by any new qualifying entitlements test. To the extent that the new charge was not extended to all income and/or differentiation was introduced into it the benefits of administrative simplification would be reduced.

7.18 A combined charge would have benefits for employers, especially small employers. It would simplify the calculations which have to be made separately at present. The increasing use of computers and hand calculators for payroll work, however, and their declining cost may well mean that the complexity of the present arrangements will increasingly impose less and less of a burden even on small employers.

7.19 Against those benefits must be weighed the major distributional effects of such a change and the need to find a satisfactory way of upholding the contributory principle. The Government's view is that the benefits of a combined charge would be unlikely to justify the ensuing upheaval.

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Chapter 8: Administration of Personal Tax In The Longer Term

8.1 The administration of income tax rests largely on PAYE, which has remained broadly the same since it was introduced over 40 years ago. With the PAYE system being computerised, it is clearly time to ask whether the mechanics of PAYE are likely to be the best ones for the 1990s. In particular, it is important to recognise the compliance costs which PAYE places on employers - especially small businesses. As the White Paper, "Lifting the Burden"⁽¹⁾, makes clear, the Government attaches a high priority to reducing the burdens on employers. This chapter looks at the PAYE system and at possible changes to it.

PAYE as it stands at present

8.2 Under PAYE, each employee is given a code, which reflects the personal tax allowances and reliefs to which he is entitled. In the normal case, the Inland Revenue send the employee his notice of coding, and also inform his employer what the code is.

8.3 The employer uses the employee's code - in conjunction with tax tables that the Revenue provide - to deduct the appropriate amount of tax from his weekly or monthly earnings. The deduction system works cumulatively. In other words, the deductions which an employer makes from his employee's earnings under PAYE in any given week (or month) normally take account of the employee's cumulative pay and tax payments for each previous week (or month) of the current tax year. The aim is that - at any point in the tax year - the amount of tax the employee has paid should be the appropriate proportion of the likely tax liability for the year as a whole.

(1) Cmnd 9571

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8.4 If an employee's circumstances change during the tax year - for example if he gets married - his tax code is normally changed to reflect this. If he changes jobs, in order to maintain cumulation his new employer needs to know the total of his pay and tax during the current tax year. To achieve this, his previous employer fills in a form (the P45) including these details, which the employee gives to his new employer. The procedures associated with the P45 also allow the employee's tax record to be moved to the correct tax office when he changes jobs. This is necessary because the Revenue keeps an employee's records at the office which deals with his employer (all the employees of one employer are therefore dealt with in the same tax office).

8.5 At the end of the tax year, the employer sends the Revenue the information about his employees' pay and the tax deducted; the Revenue then make any adjustments or assessments (and repay or collect tax) where this is necessary. Under-payments of tax are normally collected over the succeeding year or two through adjustment of the employee's code number.

Main Effects of the Present System

8.6 Coding by the Revenue and cumulative deduction operate so far as possible to avoid the need to make adjustments after the end of the year to the employee's tax payment. For more than five out of six employees paying tax under PAYE no adjustment is required to the amount of tax they have paid.

8.7 Changes of policy which would require extra end-of-year adjustments impose an additional cost. In this respect, the present system is less flexible than a system under which it is the norm to adjust and finalise the employee's liability after the end of the tax year.

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8.8 The ordinary taxpayer is very little involved with the running of the system. From time to time he may have to provide information about his personal circumstances; but otherwise he is not really directly concerned in the PAYE process itself. In fact, many people could now go through the whole of their working life without being sent a tax return - or a tax demand.

8.9 A corollary of this is that the work of running the PAYE system falls largely on the employer and the Government.

An Alternative System

8.10 Apart from the United Kingdom and the Republic of Ireland, no other country operates its tax deduction system cumulatively. An alternative system for this country would be based on non-cumulation.

8.11 An inevitable feature of a non-cumulative system is that for many employees it will not result in the right amount of tax being deducted from earnings during the year. An adjustment - either a repayment of tax or a demand for it - frequently has to be made after the end of the year. In the United States and Canada, for example, this is at present done through the self-assessment system; all employees send in a tax return, with details of their complete tax position for the year, and either a cheque or a claim for repayment of tax. In most other countries the assessment is made by the Revenue authorities.

8.12 In a system where adjustments after the end of the year are the norm, it is neither necessary nor cost-effective⁽¹⁾ for the Revenue authorities to try to ensure

(1) As a rough rule of thumb, to spend an additional 10 minutes on each taxpayer's affairs would cost a total of over 2,500 Inland Revenue staff or perhaps 2800 if a standard loading for administrative overheads such as typing, handling post etc is added.

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that an employee's code reflects precisely the personal reliefs to which he is entitled. Most countries with non-cumulative systems therefore use some form of "self-coding" - that is to say, the employee (and not the tax authority) determines his code.⁽¹⁾

8.13 It may be helpful to describe in outline how a system of this sort might work.

8.14 The employee starting a new job would collect a self-coding form from his employer, fill it in, calculate his code and hand the code back to his employer. If the employee's circumstances changed during the course of the year, he would be responsible for setting, and giving his employer, his new code. Depending on how the self-coding system was designed, it might be feasible for employers to give effect to Budget increases in personal allowances without altering codes. (In the United States, such increases are given effect by a new issue of tax deduction tables to employers.) In that case, a person's code would simply run on unchanged from one year to the next unless altered by a change in his circumstances. The Inland Revenue's part in a coding system of this sort would be restricted to providing any advice and guidance to employers and employees that was needed, subject, possibly, to some form of random check. On the United States pattern, the Inland Revenue might also have to give prior clearance if the taxpayer wished to claim more than a given total of deductions in his coding.

(1) A possible compromise was floated in the Tax Credit Green Paper under which a form of official coding card would be issued by the Inland Revenue to the employee; the employee would hand it to his employer when taking up a job, and collect it back when leaving (Cmnd 5116, paragraph 36). However it was argued in evidence to the Select Committee that this would impose an unacceptable burden on employers (evidence from the Confederation of British Industry, the Association of British Chambers of Commerce and the British Computer Society, HC 341-II, pages 280-1 and 430-438, and HC 341-II, Appendix 24). The Select Committee recommended against the proposal and it was abandoned (HC 341, page 5 and paragraphs 242-3).

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8.15 During the course of the year, the employer would deduct tax non-cumulatively from the employee's earnings. This weekly or monthly calculation of tax would depend simply on the employee's tax code and his earnings in that particular week or month; there would be no need to involve in the calculation the employee's previous earnings and tax for that year. For this reason, there would be no necessity for the employee changing jobs to take with him details of his previous earnings and tax. Under a self-coding, non-cumulative system it might turn out to be more efficient to abandon the system of keeping an employee's tax record in the tax office dealing with his employer. If that proved to be the case, employers could be relieved of all of the present information procedures associated with employees' job changes.

8.16 If the system were based on self-assessment all employees would be required to send in a tax return within a specified period after the end of the tax year. The tax returns, with the accompanying cheques or repayment claims, would normally be accepted by the Inland Revenue without detailed enquiries to the taxpayer; but there might be a check to ensure that the calculations were arithmetically correct; and United States experience suggests that with improvements in technology it is becoming feasible and cost effective to check taxpayers' returns against returns made in machine readable form by employers and other payers of income. Under a system based on self-coding and non-cumulation it might be necessary for the Inland Revenue to have more effective powers to enforce compliance (and to ensure that returns were sent in promptly). In the United States, for example, the tax authorities are able to make random audits of taxpayers' affairs.

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Effects of an Alternative System

8.17 A change from our present system to a non-cumulative, and possibly a self-assessment, system would obviously have major implications for employers, employees and the Government. It is important to be as clear as possible what these would be.

8.18 For employers, the main implications would be as follows.

8.19 First, coding. As suggested above, coding alterations arising from Budget changes might become unnecessary. On the other hand, more work would be involved for many employers in receiving coding notices separately from individual employees rather than (as at present) in a batch or list from the Revenue.⁽¹⁾ (This applies less to smaller employers and more to larger ones: in particular, it is possible that some of the larger employers whose payroll records are on computers may be able to receive batches of coding information highly efficiently from the Revenue once the computerisation of PAYE is complete.)

8.20 Second, non-cumulation. The effects of non-cumulation for employers are likely to be either helpful (to smaller employers) or broadly neutral (to larger ones). They will depend on whether the employer operates PAYE manually or as part of a computer-assisted payrolling system. At present almost all larger employers, but probably only a minority of other employers, have computer-assisted payrolls or use a computer bureau (though the proportion of employers with access to computer assistance is likely to rise each year.) For this category of employer, the costs of operating PAYE cumulatively or doing so non-cumulatively would probably not on the whole be very different (though the transition from one type of system to the other would itself involve a substantial once-for-all cost).

(1) This was one of the points made in discussion of the 1972 Tax Credit proposals.

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8.21 For those employers who operate PAYE manually - mainly smaller employers - a non-cumulative system should mean less work in making the weekly PAYE calculations, because these no longer have to take account of the previous weeks' pay and tax, but rather more work (in totalling figures up) after the end of the year.

8.22 If the Government were to merge income tax and NIC, the resulting system could be run either cumulatively or non-cumulatively. However, if the present separate and distinct PAYE and NIC deduction systems are maintained, non-cumulation could make it possible to put the appropriate PAYE and NIC deduction figures, for any given amount of earnings, side by side on the same line in one deduction table. The employer would still have to read off the table, and enter on his record sheet, three separate figures for the employer's NIC, the employee's NIC and the employee's tax for the week or month in question. But if the Inland Revenue and DHSS were able to combine their existing deduction tables, this would be helpful to employers who operate PAYE manually.

8.23 Third, a self-coding and non-cumulative system would save employers some work over employees' job changes. This would be particularly so if the Inland Revenue's present system of keeping the records of employees was changed, though employers would then lose the convenience of being able to deal with only one tax office for all their employees.

8.24 For employees, a new system for the type described would have three main consequences.

8.25 First, self-coding would obviously mean for most people more active involvement in, and responsibility for, determining their tax liabilities. How much extra

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work this involved would depend on their particular circumstances. In many cases, it might be relatively little. A lot has been done to simplify PAYE coding in recent years, and the latest figures suggest that (apart from pensioners) somewhere between 60 and 70 per cent of taxpayers have codes reflecting the basic (single or married) personal allowance only.

8.26 Were transferable allowances to be introduced, some form of self-coding system would not be inappropriate: deciding the allocation (or transfer) of allowances between husband and wife will depend in many cases on the couple's own knowledge and prediction of their particular circumstances.

8.27 Second, running the system non-cumulatively would have a cash-flow effect for some employees. Provided that a person's earnings in each week or month stay within the wide band covered by the basic rate of tax (or indeed within any one tax band), and provided that his code is correct and does not change, a non-cumulative system produces the same result as a cumulative system. If earnings fluctuate from week to week (or month to month) above and below the tax threshold or between different tax bands, it does not: other things being equal, the employee pays more tax during the year than his strict liability because he does not get the full benefit of his personal allowances or of the basic rate band.

8.28 This effect is likely to be relevant mainly for three groups of people:

- a. Many people move during the year between employment and unemployment or between employment and self-employment. Others have irregular or occasional earnings - or have earnings which are regular but relatively low, and fluctuate around the level of the tax threshold. (In

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practice around 4½ million people move in and out of employment during an average year; and well over ½ million have earnings exceeding the tax threshold by less than 10 per cent). People whose incomes were just below the tax threshold for the year, but who had tax deducted in certain weeks, would be within this group. And:

b. There are a significant number of people who leave employment in the course of a year and effectively leave the labour market either temporarily or permanently. These include those retiring from work, women leaving work to raise children and people giving up work because of ill-health.

c. There is a smaller, but still significant, number of people whose earnings fluctuate between the levels of the basic and higher rates of tax, or between different higher rates - as can commonly happen with (say) payment of a bonus in one particular month of the year.

8.29 Third, self-assessment, if that was considered desirable, would require every taxpayer to submit a return of his income every year and calculate the tax due on it. Many taxpayers have income from both employment and self-employment (as well as investment income) and may also move from one to the other during the year. Self-assessment would therefore extend also to self-employment income chargeable under Schedule D and all other sources of income.

8.30 For the Government, the change to an alternative system has two main consequences.

8.31 First, the Inland Revenue's work before and during the tax year would decrease (in relation to coding, job changes etc); and its work in processing tax returns

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after the tax year would increase. Taking the balance of these two effects, a system of self-coding, non-cumulation and self-assessment should be significantly cheaper for the Government to run than the present system (though the work of running it would be spread less evenly over the course of the year). In particular, the extra costs of running transferable allowances should be smaller under an alternative system of the sort described than under the present system. All this depends, of course, on the Inland Revenue being able to handle the increase in end-of-year work economically. This implies that a large part of the job of processing tax returns would be done by computer and that there would be appropriate provisions to encourage compliance.

8.32 Second, if the system required all taxpayers to send in tax returns as a matter of course, this should make it less costly - by comparison with the present PAYE system - to introduce policy changes which imply more end-year adjustments to people's tax payments.

A Possible Development

8.33 The preceding paragraphs in this Chapter have been written on the assumption that a change of system might involve self-assessment. In fact, a non-cumulative system does not necessarily imply that all taxpayers should send in tax returns or assess themselves. Indeed, as computer technology develops, it may be more efficient to run a system in which only some taxpayers - those with relatively complicated circumstances - send in returns, and in which for many, or most, people the tax continues to be Revenue-assessed rather than self-assessed.

8.34 The essential choice for the tax authority is either to rely on the recipient of income to provide information about it or to rely on the payer of the income.

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8.35 Under the emerging new technology, it is likely to be relatively expensive - even with the benefit of more advanced facilities for optical character recognition - to process tens of millions of paper forms completed in manuscript. At the same time, it is likely to become increasingly feasible, and relatively cheap, to process information provided in machine readable form by the payers of wages and other income. Thus, for example, the United States has announced its intention of moving away from its present system (under which all taxpayers are required to submit a tax return) to one in which, by the early 1990s, more than 50 per cent of all taxpayers would be absolved from the need to submit a return. The United States Internal Revenue Service could receive most of the necessary information about their annual income (with the appropriate social security reference number) in machine readable form from the payers of income; and would make any necessary refund of tax or demand for tax accordingly.⁽¹⁾

8.36 As one would expect, the taxpayers whom the American proposals would exempt from the need to submit a tax return would in the first place be single wage earners who have no complicated financial transactions. But the proposal is to extend the approach, after a pilot programme and further study, to some further categories of taxpayers.

8.37 It is an important element in these developments that the US administration is at the same time proposing to simplify the personal tax system: to limit the number and range of tax deductions; and in particular to extend the Zero Bracket Amount.⁽²⁾ The President's tax proposals

⁽¹⁾ The President's tax proposals to the Congress for fairness, growth and simplicity, May 1985, Chapter 5.01. The proposals are currently under consideration in Congress and may of course be subject to modification.

⁽²⁾ A flat rate relief that can be claimed as an alternative to itemising specific deductions and allowances.

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to the Congress envisage that the number of taxpayers needing to itemise claims for tax relief, in returns made to the Internal Revenue Service, will be reduced to a little over a quarter.

Conclusions

8.38 This Chapter does not seek to do more than outline some of the main issues for discussion. Nevertheless, there are some general points worth drawing out.

8.39 First, a new system of the sort described above would mean major changes for the ordinary taxpayer: more active responsibility for his tax affairs, including perhaps the need to seek advice and guidance; a more widespread incidence of overpayments and subsequent repayments of tax; and a less elastic set of rules for meeting underpayments of tax.

8.40 Second, non-cumulation could provide advantages for many smaller employers (though the numbers benefiting will fall as more employers make use of computer-assisted payrolling arrangements). However, self-coding could be more expensive for larger employers than the present system.

8.41 Third, a system where the emphasis falls more on end-of-year action should be able to accommodate at less cost policy changes which require more end-of-year adjustments. However this would in practice depend on the nature of the change; and there could still be substantial marginal costs in a policy option that required individual taxpayers (for example) to claim a new relief and for that purpose to make a return of total income which would not otherwise be needed.

8.42 Fourth, - and depending very much on the development of new technology - basing a non-cumulative system on universal self-assessment may in future not necessarily be the most efficient way to run it.

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8.43 Finally, a general move to a new system involving self-coding, non-cumulation and increased reliance on assessing or self-assessing would disengage the Inland Revenue from some substantial parts of its current involvement with the deduction system. Provided that the resulting additional end-of-year work could be handled economically, a new system should be capable of being run with fewer staff - and therefore at less cost.

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Chapter 9: Conclusion

9.1 The Government would welcome comments from organisations, representative bodies, and members of the public on the ideas discussed in this Green Paper.

9.2 The main proposals are for a new structure for income tax, based on independent taxation. Everybody would have a tax allowance in their own right. Married people who could not use up all their tax allowance would be able to transfer the balance to their partner. This system would concentrate the benefits of tax allowance increases where they are most needed and would ease the unemployment and poverty traps. It would give married women the opportunity for privacy and independence in their tax affairs; would remove the present discrimination against families where only the husband is in paid employment; and would put an end to the present tax penalties on marriage.

9.3 Changing the structure of the personal taxation in this way would complement the Government's proposals for a reform of the social security system.

9.4 The Green Paper also opens up discussion on some important issues concerning the relationship between the tax and social security systems. Finally, it reviews the administration of personal taxes and examines the implications of moving to a non-cumulative basis for PAYE, and - a separate question - to some form of self-assessment.

9.5 The Government would be grateful if comments by [30 September 1986] could be sent to Inland Revenue Policy Division, Room F11, West Wing, Somerset House, Strand, WC2R 1LB.

ANNEX 1 : THE PRESENT STRUCTURE OF PERSONAL INCOME TAX

1. The basis of the present system of taxing married couples is that the incomes of a husband and wife are added together and taxed as if all the income belonged to the husband. He is formally responsible for handling the couple's tax affairs, claiming the allowances, and paying the tax.

2. The main personal allowances are as follows:

- the Married Man's Allowance (£3,455 in 1985-86) can be set against any income of the couple;
- the Wife's Earned Income Allowance (£2,205 in 1985-86) is technically an allowance available to the husband to set against his wife's earnings only; in practice, it is usually given directly against the wife's earnings under PAYE.

Because the Married Man's Allowance can be set against any income of the couple, it is available against the wife's earnings if the husband has no income of his own. But the reverse does not apply: if the wife has no earnings, the husband cannot claim the benefit of the Wife's Earned Income Allowance.

3. Thus the total allowances available to couples in different circumstances are:

Both working	(£3,455 + £2,205)	£5,660
Husband only working		£3,455
Wife only working	(£2,205 + £3,455)	£5,660

4. The Single Person's Allowance is £2,205 in 1985-86.

5. Income above the personal allowances is charged to tax at the following rates - the rates are the same for the joint income of a married couple as for a single person.

		£	
Basic rate	30%	0	- 16,200
Higher rates	40%	16,201	- 19,200
	45%	19,201	- 24,400
	50%	24,401	- 32,300
	55%	32,301	- 40,200
	60%	40,201	and over

Alternative methods of taxing married couples

6. There are two alternatives to the basic system of taxing married couples, which have different purposes.

a. Separate Assessment was introduced in 1914. It enables each partner to be responsible for handling his or her own tax affairs independently of the other. Either partner may apply for this - the other does not have to agree. This option does not affect the total amount of tax the couple have to pay - the partners' incomes are still added together in order to work out their tax bill - but the couple can fill in separate tax returns. The Inland Revenue put the information together, work out the joint tax bill, and divide it up between the couple broadly in proportion to their incomes. Each partner is then responsible for paying his or her own share of the bill.

b. By contrast, the Wife's Earnings Election, introduced in 1971, is designed to reduce a couple's tax bill. A couple have to elect jointly for this option. The effect is that the wife's earnings are taxed as though she were a single woman, with her own set of tax rate bands while the husband loses the

Married Man's Allowance and becomes entitled to the Single Person's Allowance instead. The election is only worthwhile where their incomes are such that the savings of higher rate tax from having the wife's earnings taxed separately outweigh the loss of the Married Man's Allowance. In 1985-86, the joint income needs to be over £25,360 and the lower earner's share at least £6,596 for the election to be beneficial. This election does not affect the investment income of the wife which remains aggregated with her husband's income.

The Elderly

7. People over 65 have higher tax allowances, currently £2,690 for a single person and £4,255 for a married man, provided their income is below a certain limit. This Age Allowance is given in full up to income of £8,800 - the limit applies to single people and to the joint income of a married couple. The allowance is then withdrawn by £2 for every £3 of income over that limit, until it is reduced to the same level as the corresponding main personal allowance.

8. The Wife's Earned Income Allowance for married women over 65 is the same as for younger people, £2,205.

Single parents

9. Single parents can get the Additional Personal Allowance (APA) in addition to the Single Person's Allowance. This allowance equals the difference between the Single Person's Allowance and the Married Man's Allowance, £1,250 in 1985-86. So a single parent gets total allowances of £3,455 in 1985-86, the same as the Married Man's Allowance.

10. The APA is also available to a married man with a dependent child, if his wife is wholly incapacitated.

Other Allowances

11. Widows get the Widow's Bereavement Allowance in the tax year in which their husband dies and in the following year. The allowance is at the same level as the Additional Personal Allowance, £1,250 in 1985-86.

12. Blind People get the Blind Person's Allowance, which is £360 in 1985-86.

13. People looking after their widowed mother, or after relatives who are too old or too ill to maintain themselves, can claim the Dependent Relative Allowance, which is £145 for single women and £100 for all other claimants.

14. Widows or widowers who have a resident housekeeper can claim the Housekeeper Allowance of £100.

15. Certain people can claim the Son's or Daughter's Services Allowance of £55 if they support a son or daughter and are dependent on that person to look after them.

How PAYE works

16. Of the 24 million people paying income tax, some 22 million pay tax under Pay-As-You-Earn (PAYE).

17. Chapter 8 gives more details about the way PAYE works. This Annex draws out some of the key features, which underlie some of the arguments in the Green Paper.

18. The fundamental principle of PAYE - and one which distinguishes it from deduction-at-source systems in most other countries - is that in normal circumstances tax deductions are made on a cumulative basis throughout the year. The aim is to ensure that, so far as possible, the amount of tax deducted from the employee's earnings, however they may vary within the tax year, is correct by the end of

the year. This is achieved for five taxpayers out of six. By contrast, the work of Revenue departments in other countries is concentrated in establishing the correct tax liabilities after the end of the tax year, and making any necessary adjustments to the tax which has been deducted at source.

19. PAYE can also be used to deduct tax from income other than earnings. Where a taxpayer has some income from which tax is not deducted at source, part of his personal allowances (equal to the estimated amount of the income) can be allocated against this source of income, leaving only what is left of the allowances (represented by his PAYE "code") to be set against his earnings. The most common example now concerns pensioners: tax is not deducted at source from the National Insurance pensions, but adjustments can be made in their PAYE code to deduct all their tax liability from their occupational pensions. It is not then generally necessary to make a formal assessment for tax on the other income; the PAYE system will deduct the right amount of tax to cover both sources of income. It is not, however, possible to deal with large amounts of other income in this way or with income received at irregular intervals.

20. Outside PAYE, tax is also deducted at source from other sorts of income. The basic rate tax due on building society interest and, from April 1985, on bank interest is collected at source through the so called "composite rate" arrangements. And recipients of company dividends are entitled to a tax credit which covers their liability to tax at the basic rate.

21. The operation of the tax system has been simplified in recent years. The most important changes have been the replacement of Child Tax Allowances by Child Benefit, and the introduction of arrangements for giving tax relief on life assurance premiums and mortgage interest payments by deduction at source.

22. Thus for most employees, the tax system is very simple: the only allowance or relief making up the PAYE code is the personal allowance; and the long basic rate band (up to £16,200 of taxable income in 1985-86) means that 95% of taxpayers pay all their tax at the single rate of 30%.

23. These features have three consequences for administration.

a. The system works without the need for most employees to complete a tax return each year - indeed a person whose affairs are straightforward may never be sent one until he or she retires.

b. In many instances there is no need for the Revenue to bring together information about the total income of a single person or the incomes of husbands and wives in most cases. The combination of deduction at source arrangements and the long basic rate band ensure that the right tax is collected from each source of income separately.

c. The Revenue does not need - and therefore does not hold - information about, for example, whether or not a taxpayer has children or what his or her housing costs are.

ANNEX 2 : PHASING IN THE NEW SYSTEM

1. Chapter 3 explains that a change to a system of transferable allowances could be phased in over a number of years. This would be achieved by having a transitional period during which only part of the wife's allowance would be transferable to her husband. (Under the present system the Married Man's Allowance is already transferable in full from the husband to the wife if the husband has insufficient income of his own to use it up, so couples where the wife is working but the husband is not already have the same allowances as a two-earner couple.)

2. As Chapter 3 also explains, the details of how the phasing arrangements could not be decided until much nearer the time. This Annex therefore shows, for illustration, broadly how the phasing in might be achieved. It takes 1985-86 allowance levels as the starting point, and shows how phasing might work over periods of 2, 3, or 5 years.

3. Whatever the length of the phasing-in period, the approach would be the same. From the start, the incomes of husband and wife would be disaggregated, and the wife would be able to set the former wife's earned income allowance against any of her income. Gradually, the married man's allowance would be reduced and the wife's allowance and single allowance would be increased in parallel, so that the total allowances for a two-earner couple would remain the same in cash terms. A transferable component would be introduced gradually into the wife's allowance, so that the allowances for a one-earner couple increased. The phasing-in process would be complete at the point when the married man's allowance and the wife's allowance and single allowance reached the same level, and the wife's allowance was made transferable in full. The examples show how this process would work.

4. This approach to phasing-in would be very flexible. The length of the phasing-in period would not need to be fixed in advance, and the phasing-in need not be at the same rate throughout the period. The increase in the transferable component could be determined by the resources available. The first three examples below show phasing in equal steps, but Example 4 shows a possible scheme for phasing-in over two years with most of the increase in the first year.

5. Example 1 - Phasing-in over 2 years

Year 1 (partial implementation)

- (i) Disaggregate incomes of husband and wife and allow Wife's Earned Income Allowance to be set against any income of the wife.
- (ii) Raise single allowance and wife's allowance to £2,525.
- (iii) Reduce Married Man's Allowance to £3,135.
- (iv) Introduce transferable component of £1,400 within wife's allowance.

Year 2 (full implementation)

- (i) Raise single allowance to £2,830.
- (ii) Convert wife's allowance into a single allowance.
- (iii) Replace Married Man's Allowance by single allowance of £2,830.
- (iv) Make single allowance fully transferable between spouses.

Illustrative allowance levels during two year phasing-in

		£ One-earner couple	£ Two-earner couple
Present system	Husband	3,455	3,455
	Wife	-	2,205
	Total	<u>3,455</u>	<u>5,660</u>
Year 1 (partial implementation)	Husband	3,135	3,135
	Transferred from wife	<u>1,400</u>	-
	Total for husband	4,535	3,135
	Wife	-	<u>2,525</u>
	Total for couple	<u>4,535</u>	<u>5,660</u>
Year 2 (full implementation)	Husband	2,830	2,830
	Transferred from wife	<u>2,830</u>	-
	Total for husband	5,660	2,830
	Wife	-	<u>2,830</u>
	Total for couple	<u>5,660</u>	<u>5,660</u>

6. Example 2 - Phasing-in over 3 years

The principle here would be exactly the same as in the previous example: in the years of partial implementation, a certain proportion of the wife's allowance would be transferable to the husband. The resulting levels of allowances are set out in the table below.

	Single person	Husband	Working wife	Transfer available from non-working wife	One-earner couple	Two-earner couple
Present system	2205	3455	2205	0	3455	5660
Year 1	2405	3255	2405	1000	4255	5660
Year 2	2605	3055	2605	1900	4955	5660
Year 3	2830	2830	2830	2830	5660	5660

7. Example 3 - Phasing-in over 5 years

	Single person	Husband	Working wife	Transfer available from non-working wife	One-earner couple	Two-earner couple
Present system	2205	3455	2205	0	3455	5660
Year 1	2330	3330	2330	560	3890	5660
Year 2	2455	3205	2455	1120	4325	5660
Year 3	2580	3080	2580	1680	4760	5660
Year 4	2705	2955	2705	2240	5195	5660
Year 5	2830	2830	2830	2830	5660	5660

8. Example 4 - Phasing-in over 2 years (unequal steps)

	Single person	Husband	Working wife	Transfer available from non-working wife	One-earner couple	Two-earner couple
Present system	2205	3455	2205	0	3455	5660
Year 1	2655	3005	2655	2000	5005	5660
Year 2	2830	2830	2830	2830	5660	5660

ANNEX 3 : HOW TRANSFERABLE ALLOWANCES WOULD WORK

1. Under a system of transferable allowances, husbands and wives would be treated independently. They would each be responsible for making their own returns (when those are required) and for paying their own tax.
2. Husbands and wives would also be more closely involved in the calculation of their code numbers for PAYE purposes.
3. Before the start of the tax year, a married man or a married woman would need to decide whether to transfer any or all of their allowance. Normally a husband or wife expecting to have income for the coming year which would exceed the level of the personal allowance (say £2,830) would not elect to make any transfer to their partner. If, however, they expected to have less income than £2,830, they would normally wish to keep enough of their own allowance to set against their expected income and transfer the balance. If one partner expected to have no income, then he or she would normally elect to transfer the whole of the allowance to the other. Examples 1, 2 and 3 below illustrate these cases.

Example 1

	£	£
A earns	8,000	
B earns	15,000	
No transfer		
	Allowance to A	2,830
	Allowance to B	2,830
	Total	<u>5,660</u>
		<u><u> </u></u>
		No transfer

Example 2

£

A earns	1,500		
B earns	15,000		
- A transfers	1,330		
		Allowance to A	1,500
		Allowance to B	2,830
		<u>plus transferred</u>	<u>1,330</u>
		Total	<u><u>5,660</u></u>

Example 3

A has no income			
B earns	15,000		
- A transfers full	2,830		
		Allowance to A	-
		Allowance to B	2,830
		<u>plus transferred</u>	<u>2,830</u>
		Total	<u><u>5,660</u></u>

4. If a husband or wife decided to transfer part or all of the allowance, they would tell the tax office. The tax office would then set the PAYE code numbers of both the husband and wife in accordance with that decision. It would not be necessary for all married couples to make fresh elections each year. An election once made could run on from year to year until the husband or wife decided to change it.

5. During the course of the tax year, husbands and wives would have the right to revoke or vary any election they had made previously. In this way the system would be able to respond flexibly and quickly to changes of circumstances. For example, if a wife stopped work to have a baby, she would be able to transfer any unused balance of her allowance to her husband so that he could benefit as soon as possible from the extra allowance. Example 4 below illustrates this.

Example 4

- i. At the start of the year a husband and wife are both in paid work, and there is no transfer of allowances between them.
- ii. After three months the wife leaves employment to have a baby. Up to that time she has earned £1,500. On giving up work she asks her tax office to transfer the balance of her allowances to her husband.
- iii. The tax office makes a repayment to the wife of any tax deducted from her earnings and arranges for the balance of her allowances (£2,830 - £1,500 = £1,330) to be transferred to her husband.
- iv. Over the year as a whole, the position of the partners is then:

Allowances to wife (equal to her income)	£1,500
Allowance to husband	£2,830
plus transferred	£1,330
	<hr/>
Total	£5,660

6. If, on the other hand a husband or wife who had not been in paid work at the start of the year (and who had transferred their allowance to their partner) began a new job they could ask the tax office to end the transfer and give their own full tax allowance in their own PAYE code. Their partner's allowance would then be reduced correspondingly. Example 5 below shows how this would work.

Example 5

- i. At the start of the year only the husband is in paid work and his wife has transferred her allowance to him.
- ii. After three months the wife takes up paid employment. On doing so she asks the tax office to end the transfer of her allowance to her husband.
- iii. The wife's tax office gives her the benefit of her full allowance in her PAYE code. The husband's tax office adjust his PAYE code so that he has only his own allowance. The husband's new code is introduced on a non-cumulative basis so that the husband does not suffer a large tax deduction in the week or month when the change is made.
- iv. After the end of the year the tax office reviews the husband's position and checks the amount of tax deducted. Any underpayment of tax would be collected (as at present) by adjusting the husband's PAYE code for a succeeding year (or years).
- v. Over the year as a whole the position of the partners would be:

Allowance to husband	£2,830*
Allowance to wife	£2,830
	<hr/>
Total	£5,660

*after non-cumulative reduction in his PAYE code from month 4.

7. After the end of the tax year, the tax office would review a couple's tax position

For the purpose of calculating tax liabilities at the higher rates, however, a transfer of allowances would only have effect to the extent that the transferring partner's allowance exceeded his or her own income; if, for example, a wife's income was only £1,000, the transferred amount could not exceed £1,830 (£2,830 - £1,000). These arrangements would ensure that where a transfer of allowances was made, the right amount of tax was collected in total from the couple.

ANNEX 4 : ILLUSTRATIONS OF THE EFFECTS OF TRANSFERABLE
ALLOWANCES

1. Chapter 3 made it clear that the Government would only introduce transferable allowance, if and when it could do so, in such a way that no taxpayers would suffer a cash loss.

2. Table 1 shows the cash effects on different family types of introducing the new system in this way. The comparison is against the 1985-86 level of allowances, and is at 1985-86 prices. Table 2 shows the cash effects by income range and Table 3 gives a more detailed analysis.

3. Chapter 3 also pointed out that the change could be made in one year, or, more realistically, phased in over a number of years. If the change were made in one year the real effects on families, taking account of inflation, would be the same as the cash effects. On this assumption, therefore, the real effects also would be as shown in Tables 1-3.

4. If, however, the change were phased in over a number of years, some taxpayers would find that their allowances remained unchanged over this period and therefore fell in real terms, with inflation. The extent of these possible real losses would depend on the length of the transitional period and on how any scope for real reductions in tax was used during that period.

5. At the extreme the change could be phased in over a period long enough to ensure that there was no loss of revenue beyond what would have been required for indexation of allowances. The cash effects of a change made in this way would still of course be as shown in Table 1. The real effects would be as shown in Tables 4 and 5.

6. As Chapter 3 makes clear, the assumption about phasing on which Tables 4 and 5 are based is an extreme one. A move to transferable allowances should be seen as part of the process of tax reduction, in line with the Government's declared objective of reducing the total burden of taxation. To the extent that tax reductions were made during the period of transition, the phasing would be shorter than assumed in Tables 4 and 5 and the position in real terms for taxpayers better than is shown there.

7. The annex now goes on to discuss in more detail the effect of the change on different types of taxpayer as summarised in Table 6. All the detailed calculations are in cash terms, again with the comparison against the 1985-86 level of allowances and at 1985-86 prices. The annex also shows how the proposed reform of social security will affect the net income of taxpayers (Tables 10 and 11).

IMPACT FOR PARTICULAR GROUPS

Taxpayers of working age - single people

8. In 1985-86, the allowance for a single person is £2,205. Under the illustrative transferable allowance system, it would be £2,830: that is £625 higher. At this level of allowance, there would be 750,000 fewer single people of working age paying tax and the tax bills of the seven million who would be liable at the basic rate would be £187.50 (£3.60 per week) lower. The change for the 120,000 single people currently liable at higher rates would be correspondingly greater.

- One earner couples

9. The allowance available in 1985-86 to a married couple where the husband is the sole earner is £3,455. Under the illustrative system it would be £2,205 higher at £5,660, twice the amount of the single transferable allowance. At this level of allowance, there would be 600,000 fewer one earner couples paying tax and the tax bills of the 3.6 million who would be liable at the basic rate would be £661.50 (£12.72 per week) lower. The change for the 245,000 couples currently liable at higher rates would be correspondingly greater.

10. Under the present tax system, couples where the wife is the sole earner, in general, receive the same allowances as couples where both spouses are earning, since they receive both the married man's allowance and the wife's earned income allowance. Under the illustrative system of transferable allowance, the amount of allowances available to such couples would be the same as in 1985-86. The husband would, however, be able to transfer to his wife any allowance unused against his investment income.

- Two earner couples

11. The effect of the illustrative system on two earner couples depends in part on the amount of the wife's earnings. At present, the total allowances available to a two earner couple are £5,660; but £2,205 of this can be set only against the wife's earnings. Under the illustrative arrangements, the whole of the £5,660 would be available to the couple whatever the split of their income. The 1.8 million couples where the wife's earnings are below £2,205 would therefore pay less tax under the illustrative arrangements than at present. The difference would depend on the amount of the wife's earnings and table 3 shows that it would average about £5.80 per week. Under the transferable allowance system, most two earner couples where the wife earns more than £2,205 would have available between them the same allowance as at present and their combined tax bill would not change. Since the allowances would be split equally between them, however, in practice, the wife would find a reduction in the amount of tax deducted under PAYE and her husband a corresponding increase.

12. Under the present rules, some 180,000 two earner couples find it beneficial to elect to have the wife's earnings taxed separately. These couples are, in effect, taxed as two single people on their earned income with a single allowance each. Under the system of transferable allowances, therefore, each spouse would have an increase in allowance of £625. Where both spouses were liable at the basic rate, the couple's combined tax bill would be £375 (£7.21 per week) lower.

13. Finally, there are at present some 250,000 two earner couples liable to tax at higher rates where the wife's earnings are over £2,205 but who do not find it beneficial to elect. Under the illustrative system, they would receive the same amount of allowances in total. Where the wife's

earnings were between £2,205 and the illustrative transferable allowance of £2,830, the couple's combined tax bill would not change. Where the wife's earnings were greater than this, their combined tax bill might be reduced under the illustrative system, since income taxed at present at a marginal rate above 30 per cent might become liable at a lower rate of tax as a result of the disaggregation of each spouse's income and the operation of the separate set of rate bands to which each of them would be entitled.

Elderly taxpayers

14. Under the present arrangements, age allowance is income limited. Single people aged 65 and over, and married couples where one of the spouses is aged 65 or over, are entitled to age allowance in full if their total income does not exceed £8,800. Above this level, the allowance is withdrawn by £2 for every £3 increase in income, so that elderly single people become entitled only to the basic allowance at an income of £9,528, and elderly married couples at £10,000. Table 7 shows the numbers of elderly taxpayers in 1985-86 in the various categories. The illustrative transferable allowance system does not include a higher level of allowance for elderly taxpayers.

- Elderly single people

15. At present, 1.1 million elderly single taxpayers receive the full age allowance of £2,690. Under the illustrative system, they would receive £2,830. At this level of allowance there would be 60,000 fewer elderly single taxpayers and the tax bills of the remainder would be £42 (81p per week) lower. Allowances for the 30,000 elderly single people who now receive an abated age allowance would be between £140 and £625 higher under the illustrative system, depending on the amount of the abatement. The effect of the system on the remaining 190,000 - who are entitled only to the basic allowance - would be the same as for single taxpayers of working age.

- Elderly married couples where the wife is not at work⁽¹⁾

16. At present, the allowance available to the 550,000 taxpaying elderly married couples with total incomes below £8,800 where only the husband has earned income (earnings or pension) is £4,255. Under the illustrative system of transferable allowances, it would be £5,660. An allowance at this level would remove 330,000 couples from tax and the tax bills of the rest would be £421.50 (£8.10 per week) lower. The effect of the illustrative system on the 45,000 elderly couples with total incomes above £10,000 would be the same as for one earner couples of working age.

⁽¹⁾ This group includes couples where the wife has a category B NI pension on the basis of her husband's contributions. Category B pensions are treated as earned income of the husband and cannot be set against the wife's earned income allowance.

- Elderly married couples where the wife is still at work

17. At present, an elderly married couple with total income below £8,800 where the wife has earned income of at least £2,205 has available allowances of £4,255 (married age allowance) plus £2,205 (wife's earned income allowance), a total of £6,460. Under the illustrative system of transferable allowances, the allowances available to the 70,000 taxpayers in this position would be £5,660; that is £800 lower. With allowances at this level, some 30,000 couples would be brought into tax. A further 50,000 couples who have wife's earned income of between £1,405 and £2,205 would also receive a lower level of allowances than at present as would some 25,000 couples whose total income was between £8,800 and £10,000. There are, therefore, at present up to 175,000 elderly couples who, under the illustrative system of transferable allowances, would receive a lower amount (up to £800) of allowances than at present.

To prevent this, if a system of transferable allowances were to be introduced the Government would make special arrangement, so that couples in this position would not experience a reduction in the combined cash amount of their main personal allowances compared with the year before transition to the transferable allowance system began. In the illustrative system, the revenue cost of this protection would be about £30 million. The effect of this protection has been included in the tables, so that the couples concerned have allowances unchanged from 1985-86 levels. Under the illustrative system, allowances available to the remaining 130,000 elderly couples with wife's earned income, who receive age allowance in full or in part, would be higher than at present. The position of the 285,000 elderly married couples with total income of over £10,000 would correspond to that of a couple of working age with a similar split of income between husband and wife. About 160,000 -

those with wife's earned income of less than £2,205 - would have a higher level of allowance under the illustrative system; the rest would have the same level of allowances in total under the present and the illustrative arrangements.

Higher rate tax

18. The total number of single people and married couples liable to higher rate tax in 1985-86 is estimated at about a million. Under the illustrative system of transferable allowances 750,000 individuals would be liable at higher rates. 150,000 of these would be single people (10,000 fewer than at present), 560,000 would be married with a spouse who was not liable at higher rates and a further 40,000 would be married to a spouse who was also a higher rate taxpayer. About $\frac{1}{4}$ million couples who are liable to higher rate tax at present would not be liable at higher rates under the illustrative system. About two-thirds of these couples would be two earner couples who do not make a wife's earnings election under the present arrangement. Table 8 gives more detail on the effect of the illustrative system on married couples. No couple not currently liable to higher rate tax would be liable under the illustrative system of transferable allowances.

Disaggregation of investment income

19. Under a system of transferable allowances, the investment income belonging to a wife would be taxed as hers and not, as now, aggregated with her husband's income and taxed as his. For the 92 per cent of taxpaying married couples who are currently liable only at the basic rate, this disaggregation of investment income - as distinct from transferable allowances - would not, by itself, have any effect on their combined tax bill. However, married couples who are liable at higher rates would in general benefit from disaggregation (if the wife has investment income not covered by her tax allowance and her marginal tax rate is lower than her husband's). If in the illustrative system of transferable allowances, a wife's investment income was treated as her husband's for tax purposes instead of being disaggregated, the revenue yield would be about £85 million. Table 9 shows an analysis of the 170,000 couples who would have lower tax bills within the illustrative system as a result of disaggregation and the extent of the reduction. These estimates are based on the current recorded distribution of investment income between husband and wife, allocating joint income equally between the spouses.

EFFECTS OF THE NEW SOCIAL SECURITY PROPOSALS

20. Under the proposals in the White Paper on Social Security, due to be introduced in 1987 and 1988, some taxpayers who also receive social security benefits will find that their entitlement to benefit will change when their tax decreases or increases under transferable allowances. This is because the benefits will be based on net income, not as at present on gross income. It is expected that about 2 million taxpayers might also be entitled to income-related benefits such as family credit and housing benefit.

21. Those who gain in real terms through lower tax bills will lose some of the gain in reduced benefit entitlement. The tax changes would however substitute income as of right for these benefits. On the other hand if the tax changes are phased in over several years at no real reduction in the tax burden, some taxpayers with income-related benefits will have their tax liabilities increased in real terms. For these people, their real net income will fall and thus their benefits will increase to offset the loss.

22. After allowing for the changes in benefit caused by the Social Security proposals, the effects of introducing transferable allowances are shown in Tables 10 and 11 for different family types. Table 10 shows the changes in cash terms and Table 11 shows the changes in real terms if no real reduction in tax burden were possible during the implementation.

23. This annex only summarises the effects of introducing transferable allowances. As explained in Chapter 3, once in place they would allow changes in levels of allowances to be undertaken more effectively than under the present structure of personal allowances.

TABLE 1 Taxpayers: Cash changes in tax if transferable allowances introduced with no cash losers: By Family Type

(thousands)

FAMILY TYPE	ALL TAXPAYERS	Change in tax (£ per week)									AVERAGE CHANGE (£ per week)
		OVER £10	£5-£10	GAIN £2-£5	UNDER £2	NO CHANGE	UNDER £2	LOSS £2-£5	£5-£10	OVER £10	
NON-AGED											
Single	7,550	10	70	7,020	440	-	-	-	-	-	3.45
Married couple											
: Wife not working	4,090	3,440	220	160	90	170	-	-	-	-	11.66
: Wife Working	5,600	350	840	580	450	3,400	-	-	-	-	2.32
Lone Parent	360	*	10	330	20	-	-	-	-	-	3.52
ALL NON-AGED	17,600	3,800	1,140	8,090	1,000	3,570	-	-	-	-	5.00
AGED											
Single pensioner	1,580	*	40	180	1,130	240	-	-	-	-	1.15
Pensioner couple	1,400	220	480	190	160	340	-	-	-	-	5.51
ALL AGED	2,980	220	520	370	1,290	580	-	-	-	-	3.19
TOTAL	20,580	4,020	1,660	8,460	2,290	4,150	-	-	-	-	4.74

TABLE 2 Taxpayers: Cash changes in tax if transferable allowances introduced with no cash losers: By Income

(thousands)

INCOME £ PER WEEK	ALL TAXPAYERS	Change in tax (£ per week)									AVERAGE CHANGE (£ per week)
		OVER £10	£5-£10	GAIN £2-£5	UNDER £2	NO CHANGE	UNDER £2	LOSS £2-£5	£5-£10	OVER £10	
0-60	1,200	-	-	420	530	240	-	-	-	-	1.49
60-100	3,340	-	120	2,290	840	90	-	-	-	-	2.91
100-150	4,680	820	510	2,600	390	360	-	-	-	-	5.04
150-200	3,530	1,030	290	1,500	180	530	-	-	-	-	5.77
200-300	4,590	1,350	300	1,140	180	1,630	-	-	-	-	5.10
300-400	1,800	380	90	310	40	980	-	-	-	-	3.68
400+	1,440	440	350	200	130	320	-	-	-	-	8.27
TOTAL	20,580	4,020	1,660	8,460	2,290	4,150	-	-	-	-	4.74

TABLE 3 Taxpayers: Cash changes in tax if transferable allowances introduced with no cash losers: By income and family type

Income (£ per week)	Taxpayers	Amount of reduction	Average reduction		Taxpayers	Amount of reduction	Average reduction	
	(thousand)	(£ million)	(£ per week)	(% of gross income)	(thousand)	(£ million)	(£ per week)	(% of gross income)
NON-AGED		<u>Single</u> ⁽¹⁾				<u>Married couple: wife not working</u>		
0-60	840	90	2.05	4.1	10	-	0.32	0.6
60-100	2,110	390	3.55	4.5	320	70	3.92	4.8
100-150	2,500	470	3.61	3.0	950	540	10.93	8.8
150-200	1,300	240	3.60	2.2	1,040	630	11.68	6.9
200-300	860	160	3.61	1.6	1,160	750	12.40	5.4
300-400	180	40	3.67	1.1	320	210	12.53	3.8
400+	120	30	5.33	0.9	290	280	18.87	2.9
TOTAL	7,910	1,420	3.45	2.6	4,090	2,480	11.66	5.4
NON-AGED		<u>Married couple wife working earning £2,205 or below</u>				<u>Married couple wife working earnings above £2,205</u> ⁽²⁾		
0-60	-	-	-	-	-	-	-	-
60-100	40	-	2.08	2.3	20	-	-	-
100-150	250	80	6.12	4.9	170	-	-	-
150-200	450	140	5.79	3.4	380	-	-	-
200-300	730	210	5.67	2.4	1,540	-	-	-
300-400	200	60	5.36	1.6	950	-	-	-
400+	180	70	7.26	1.3	700	120	3.31	0.6
TOTAL	1,850	560	5.81	2.4	3,760	120	0.61	0.2

TABLE 3 (cont)

		<u>Elderly single</u>			<u>Elderly married couples</u>			
0-60	350	4	.21	0.4	-	-	-	-
60-100	630	30	.81	1.1	230	20	1.76	2.0
100-150	320	20	1.06	0.9	500	130	4.86	4.1
150-200	110	10	1.69	1.0	240	40	2.81	1.7
200-300	90	20	3.58	1.5	210	80	7.20	3.1
300-400	50	10	3.85	1.2	100	30	6.59	2.0
400+	40	10	5.92	0.9	120	100	17.11	2.8
TOTAL	1,590	104	1.15	1.0	1,400	400	5.51	2.8

(1) including single parents

(2) about 100,000 couples in this group would have increased tax bills as a result of withdrawal of minor personal allowances.

TABLE 4 Taxpayers: Real effects of changes in tax if transferable allowances financed by provision for indexation of personal allowances only: By family type

(thousands)

FAMILY TYPE	ALL TAXPAYERS	Change in tax (£ per week)									AVERAGE CHANGE (£ per week)
		OVER £10	£5-£10	GAIN £2-£5	UNDER £2	NO CHANGE	UNDER £2	LOSS £2-£5	£5-£10	OVER £10	
NON-AGED											
Single	7,550	-	20	10	7,370	-	140	-	-	-	0.32
Married couple											
: Wife not working	4,090	100	3,560	170	90	-	10	160	*	*	5.77
: Wife Working	5,600	10	150	380	360	-	390	630	3,670	20	-4.29
Lone Parent	360	-	*	-	350	-	10	0	0	0	0.38
ALL NON AGED	17,600	110	3,730	560	8,170	-	550	790	3,670	20	0.12
AGED											
Single pensioner	1,580	-	*	10	190	-	210	1,180	-	-	-1.90
Pensioner couple	1,400	40	160	60	640	-	60	110	320	-	-0.41
ALL AGED	2,980	40	160	70	830	-	270	1,290	320	-	-0.82
TOTAL	20,580	150	3,890	630	9,000	-	820	2,080	3,990	20	0.0

TABLE 5 Taxpayers: Real effects of changes in tax if transferable allowances financed by provision for indexation of personal allowances only: By Income

(thousands)

INCOME £ PER WEEK	ALL TAXPAYERS	Change in tax (£ per week)									AVERAGE CHANGE (£ per week)
		OVER £10	£5-£10	GAIN £2-£5	UNDER £2	NO CHANGE	UNDER £2	LOSS £2-£5	£5-£10	OVER £10	
0-60	1,200	-	-	-	830	-	190	180	-	-	-0.31
60-100	3,340	-	120	140	2,350	-	70	660	-	-	0.13
100-150	4,680	-	880	110	2,810	-	110	500	260	*	0.83
150-200	3,530	-	1,010	140	1,420	-	170	260	530	*	0.80
200-300	4,590	-	1,280	140	1,050	-	150	240	1,720	-	-0.78
300-400	1,800	-	360	60	250	-	30	80	1,020	-	-2.49
400+	1,440	150	240	40	290	-	100	160	460	10	0.65
TOTAL	20,580	150	3,890	630	9,000	-	820	2,080	3,990	10	0.0

TABLE 6 Taxpayers in 1985-86: By family type and liability at higher rate of tax

(thousands)

Family Type	All	Liable at Higher Rates
NON-AGED		
Single	7,520	120
Married couple		
: Husband only earning	4,090	245
: Wife only earning	300	-
: Husband and wife earning		
- wife earning less than £2,205	1,810	120
- wife earning over £2,205		
- without earnings election	3,190	250
- with earnings election	180	125
Lone Parents	380	-
ALL NON-AGED	17,470	860
AGED		
Single Pensioner	1,360	40
Pensioner couple	1,310	100
ALL AGED	2,670	140
TOTAL	20,140	1,000

TABLE 7: Aged taxpayers in 1985/86: By use of age allowance and wife's earnings

(thousands)

Use of Age Allowance	Single	No wife's earned income	Wife's earned income:			Total married couples
			below £1,405	£1,406- £2,205	£2,205+	
Age allowance in full	1,140	550	130	50	70	800
Reduced age allowance	30	35	10	10	25	80
Basic allowance only						
- liable at basic rate	150	100	90	40	100	330
- liable at higher rates	40	45	20	10	25	100
TOTAL	1,360	730	250	110	220	1,310

TABLE 8: Married couple taxpayers: liability at higher rate tax if transferable allowances introduced with no cash losers

	One earner couples	Two earner couples		Total
		Non-electing	electing	
Neither spouse liable	70	180	10	260
One spouse liable	220	230	110	560
Both spouses liable	-	-	20	20
TOTAL	290	410	140	840

TABLE 9: Married couples benefiting and reductions in tax from disaggregating investment income if transferable allowances introduced with no cash losers:
By income and family type

(married couples (thousands), tax reduction (£'m))

	Reduction in tax (per annum)									
	less than £250		£250-£500		£500-£1000		Over £1000		Total	
	couples	tax	couples	tax	couples	tax	couples	tax	couples	tax
1 earner: Annual income										
: below £50,000	11	1.2	5	1.9	6	4.0	10	18.2	32	25.3
: above £50,000	1	0.1	-	-	1	0.5	4	12.1	6	12.7
2 earner: Annual income										
: below £50,000	84	5.3	15	5.3	8	5.9	9	13.6	116	30.1
: above £50,000	9	0.8	2	0.8	3	1.9	5	13.7	19	17.2
TOTAL	105	7.4	22	8.0	18	12.3	28	57.6	173	85.3

TABLE 10: All Tax Units: Cash changes in net income if transferable allowances introduced with no cash losers: By family type

(thousands)

FAMILY TYPE	TAX UNITS WITH NO LIABILITY	TAX-PAYERS	Change in net income (£ per week)								AVERAGE CHANGE (£ per week)	
			OVER £10	£5-£10	GAIN £2-£5	UNDER £2	NO CHANGE	UNDER £2	LOSS £2-£5	£5-£10		OVER £10
NON-AGED												
Single	4,200	7,550	10	70	6,910	550	-	-	-	-	-	3.40
Married couple												
: Wife not working	1,110	4,090	3,050	230	450	180	170	-	-	-	-	10.72
: Wife Working	600	5,600	300	820	630	470	3,400	-	-	-	-	2.21
Lone Parent	640	360	*	10	210	140	-	-	-	-	-	2.69
ALL NON AGED	6,550	17,600	3,360	1,130	8,200	1,340	3,570	-	-	-	-	4.71
AGED												
Single pensioner	2,520	1,580	*	40	180	1,130	240	-	-	-	-	1.10
Pensioner couple	1,100	1,400	200	470	180	170	350	-	-	-	-	5.87
ALL AGED	3,620	2,980	220	510	360	1,300	590	-	-	-	-	3.36
TOTAL	10,170	20,580	3,580	1,640	8,560	2,640	4,160	-	-	-	-	4.51

TABLE 11: All Tax Units: Real effects of changes in net income if transferable allowances financed by provision for indexation of personal allowances only:
By family type

FAMILY TYPE	TAX UNITS WITH NO LIABILITY	TAX- PAYERS	(thousands)								AVERAGE CHANGE (£ per week)	
			Change in net income (£ per week)									
			OVER £10	£5-£10	GAIN £2-£5	UNDER £2	NO CHANGE	UNDER £2	LOSS £2-£5	£5-£10		OVER £10
NON-AGED												
Single	4,200	7,550	-	20	10	7,360	10	140	-	-	-	0.31
Married couple												
: Wife not working	1,110	4,090	100	2,980	270	570	-	10	160	*	*	5.19
: Wife Working	600	5,600	10	90	370	430	-	430	620	3,640	20	-4.30
Lone Parent	640	360	-	*	-	350	-	10	0	-	-	0.30
ALL NON AGED	6,550	17,600	110	3,090	650	8,710	10	590	780	3,640	20	-0.03
AGED												
Single pensioner	2,520	1,580	-	*	10	190	60	440	890	-	-	-1.56
Pensioner couple	1,100	1,400	40	160	60	630	10	60	110	320	-	0.39
ALL AGED	3,620	2,980	40	160	70	820	70	500	1,000	320	-	-0.65
TOTAL	10,170	20,580	150	3,250	720	9,530	80	1,090	1,780	3,960	20	-0.10

ANNEX 5 : TIMETABLE FOR CHANGE

1. The introduction of transferable allowances and the end of aggregation of husbands' and wives' incomes would affect 11 million married couples, about 1 million employers, and some 600 Tax Offices. By any standards it would be a major change.

2. A system of transferable allowances would require information from taxpayers which is not held in many cases at present, and would have two major consequences for personal tax administration.

3. First, tax offices would need to be geared to making more adjustments, assessments, or repayments of tax, because many people's allowances would change during the tax year as their circumstances changed (see Examples in Annex 3). At present, such adjustments are needed for only one PAYE taxpayer in six. Handling the extra end-of-year work economically would require full computer support.

4. Second, there would need to be an efficient mechanism for linking the tax records of a husband and wife. For the great majority of couples, these records are not linked at the moment. It is not necessary under the present system: although a married couple's tax liability depends upon their joint income, the long basic rate band means that over 90 per cent of couples pay tax at that rate only. So PAYE will collect the right amount of tax in the majority of cases without needing to link a husband and wife's records.

5. The new links would require two new facilities:

- An index and tracing facility, so that information about a change in, say, a husband's employment position could be directed quickly and economically not only to his own tax office, but also, where appropriate, to his wife's tax office.

(A PAYE taxpayer's records are kept in the office dealing with his employer's affairs, so when a husband and wife have different employers, they are quite likely to have different tax offices.)

- Facilities to transfer such information electronically between the tax offices concerned. Relying on written correspondence would be too slow, and would give rise to substantial over-payments and underpayments of tax.

6. The Inland Revenue are already engaged on two major computer projects. A pilot system for the computerisation of PAYE (referred to as "COP") has been running in the West Midlands for some time. It is now being extended across the country, region by region, and will be complete by late 1987 or early 1988. When fully implemented, COP is likely to be the biggest on-line computer project in Europe. Staff in the 600 Tax Offices will have access to 17,000 terminals for COP, linked to mainframe computers in 11 regional processing centres.

7. The procedures for taxing self-employment income under Schedule D are also being computerised (CODA). This further development, which will be in place by 1989, will use the same mainframe computers as COP, but will increase the number of terminals to 25,000.

8. The Revenue plan to enhance this basic computer system by two further developments:

- a nationwide data transmission network. The network, which will use over 900 British Telecom circuits, will link the 600 tax offices into the computing facilities and will connect them with each other and with the offices responsible for collection and enforcement.

- a computer-based index. This will maintain up to date records of each taxpayer, his or her employer (or self-employment), and will be able to hold the necessary information to connect the tax records of married couples. The index, which is already running on an experimental basis in Scotland, will provide rapid access to vast amounts of stored data.

These facilities will be introduced as soon as possible after COP and CODA are complete.

9. If transferable allowances were introduced, the Revenue would also need to ask married couples for the information necessary to establish links between their records, and to give the appropriate allowances.

10. Transferable allowance would mean considerable additional work for tax offices. In particular, they would be handling separately the tax affairs of many millions of married women, whereas at present a married woman's tax affairs are handled along with her husband's. The new computer facilities described earlier would be an essential requirement to undertake this extra work efficiently, but there would also be a need for additional staff - possibly in the region of 5,000. In the event of a change to transferable allowances, there would be full consultation with the staff and departmental unions in the Revenue.

ANNEX 6 : MARRIED WOMEN IN THE LABOUR FORCE

Introduction

1. This Annex gives some detailed information about the increasing participation of married women in the labour force over the past 50 years. It also sets out some recent evidence on the reasons why married women do not seek paid work at particular times.

Participation in the Labour Force

2. Chart 2.4 in Chapter 2 illustrates the steady rise in the proportion of married women with paid jobs.

3. Table 1 provides the detailed information on which the chart is based, and also gives information about men in the labour force. The table shows that while the size of the total workforce has continued to show an increase for each year that figures are presented, the number of economically active men - that is, those who are working or looking for work - has recently declined from the number counted in the 1971 census. The number of females has on the other hand continued to show a steady rise, almost entirely due to the increasing participation of married women.

4. Table 2 shows more clearly how the share of married women in the labour force has expanded.

TABLE 1

Number and activity rate of people of working age, by sex and marital status (for women), 1921-1984, Great Britain (numbers in thousands)

<u>Males and females</u>	<u>People of working age*</u>		
	<u>Number</u>	<u>Number EA</u>	<u>AR</u>
1921	30750	18559	60.4
1931	30416	20057	65.9
1951	31250	21564	69.0
1961	31885	22736	71.3
1966	32014	23579	73.7
1971	32361	23947	74.0
1981	32228	24560	76.2
.....
1981	32425	25048	77.2
1983	32801	24980	76.2
1984	33043	25484	77.1
 <u>Males</u>			
1921	14575	13006	89.2
1931	14917	14107	94.6
1951	15674	14968	95.5
1961	16427	15506	94.4
1966	16589	15418	92.9
1971	16939	15495	91.5
1981	16790	15188	90.5
.....
1981	16895	15232	90.2
1983	17147	15072	87.9
1984	17327	15202	87.7
 <u>All Females</u>			
1921	16175	5553	34.3
1931	15499	5950	38.4
1951	15576	6596	42.3
1961	15458	7230	46.8
1966	15425	8161	52.9
1971	15422	8452	54.8
1981	15438	9372	60.7
.....
1981	15530	9817	63.2
1983	15654	9908	63.3
1984	15716	10282	65.4
 <u>Married Females</u>			
1921	7949	713	9.0
1931	8355	904	10.8
1951	10388	2574	24.8
1961	10904	3727	34.2
1966	10916	4776	43.8
1971	11134	5444	48.9
1981	10536	5988	56.8
.....
1981	10685	6338	59.3
1983	10731	6433	59.9
1984	10788	6727	62.4
 <u>Other Females</u>			
1921	8226	4840	58.8
1931	7144	5046	70.6
1951	5188	4022	77.5
1961	4554	3503	76.9
1966	4509	3385	75.1
1971	4288	3008	70.1
1981	4902	3384	69.0
.....
1981	4845	3478	71.8
1983	4923	3475	70.6
1984	4928	3556	72.2

Sources: Censuses of Population 1921-1981, Labour Force Surveys 1981-84

* upper limit: males 64 years
females 59 years except for 1921 (64 years)

lower limit: 1921 12 years
1931 14 years
1951-71 15 years
1981-84 16 years

TABLE 2: Shares in the labour force 1921-1984, Great Britain

	Men*		All Females*		Married Women*		Total*	
	No. 000's	% of total	No. 000's	% of total	No. 000's	% of total	No. 000's	% of total
1921	13656	70.5	5701	29.5	733	3.8	19357	100
1951	15649	69.2	6961	30.8	2658	11.8	22610	100
1971	16029	63.5	9205	36.5	5815	23.1	25234	100
1981	15527	61.1	9879	38.9	6286	24.7	25406	100
.....								
1981	15645	60.0	10432	40.0	6663	25.6	26077	100
1984	15416	58.9	10764	41.1	7046	26.9	26179	100

* Includes persons of all ages above minimum school leaving age.

Sources: Censuses 1921-1981; 1981 and 1984 Labour Force Surveys

In the 1920s very few married women worked or sought paid employment; they represented less than 4 per cent of the labour force and only about one seventh of all women who worked. By 1951, married women's share of the labour force had grown to nearly 12 per cent - slightly over one-third of all women who worked. In 1984, the latest year for which figures are available, nearly $\frac{2}{3}$ of all women in paid work (or looking for work) were married, and married women's share of the labour force had doubled to 27 per cent.

Reasons for not working

5. The reasons given by married women for not working or seeking paid employment were one of the topics covered in a representative survey of women aged 16-59 carried out in Great Britain by the Department of Employment and OPCS in 1980(*). These reasons are summarised in Chart 2.5 of Chapter 2; the detailed information is set out in Table 3.

(*) J Martin and C Roberts (1984) Women and Employment: a Lifetime perspective HMSO London.

TABLE 3

REASONS GIVEN BY MARRIED WOMEN FOR NOT BEING IN PAID EMPLOYMENT

This table sets out the reasons given by married women, aged 16-59, (excluding full-time students), for not being in paid employment or seeking paid work, according to their stage in the life cycle.

	<u>Life cycle stage</u>							All women not in paid employment or seeking paid work	Base for row %s
	Childless, aged:		Youngest child aged:			No child under 16, aged:			
	Under 30	30 or over	0-4	5-10	11-15	Under 50	50-59		
Permanently unable to work	%	%	%	%	%	%	%	%	
	*	26	1	2	7	17	15	5	
	%	-	4	5	10	15	53	100	79
Looking after children	%	%	%	%	%	%	%	%	
	*	3	96	78	44	8	2	63	
	%	1	71	21	6	1	1	100	906
Looking after other relatives	%	%	%	%	%	%	%	%	
	*	13	0	3	6	4	9	3	
	%	-	2	17	15	6	50	100	48
Keeping house	%	%	%	%	%	%	%	%	
	*	51	2	14	35	63	64	24	
	%	4	5	10	12	13	50	100	344
Other reasons	%	%	%	%	%	%	%	%	
	*	8	1	3	8	8	10	4	
	%	2	13	13	14	10	43	100	62
All women not in paid employment or seeking paid work	%	%	%	%	%	%	%	%	
	*	100	100	100	100	100	100	100	
	%	1	47	17	8	5	19	100	1439
Base for column %s		23	39	671	247	115	73	271	1439

0 (Less than 0.5%)

* (Base too small to show percentages)

Source: DE/OPCS 1980 Women and Employment Survey.

Note: The percentage figures may not always total 100 because of rounding.

6. Over 60 per cent of married women who are not in paid work are looking after dependent children, and over 70 per cent are either looking after children or other relatives, or are prevented from working by ill health. Moreover, of the women who have no children under 16 and do not give one of these specific reasons for being economically inactive, at least 50 per cent* are aged 50 to 59 and therefore at an age when finding employment would be very difficult. Moreover, women aged over 50 in 1980 are of a generation which was less likely than married women now are to work when they were younger. Women who did not go out to work when younger are less likely to be able to enter the labour market in their fifties than those who did. This group also includes women who were unable to enter the labour market earlier because of responsibility for young children, relatives or other dependants. Women in this position similarly find it difficult to enter the labour market in their fifties, even though their earlier domestic responsibilities may now have ended.

7. This age group also understandably accounts for the largest percentage (53 per cent)* of women who are permanently unable to work.

* There will be some women aged 50-59 who have never had children and who will therefore appear in the column headed "Childless, aged 30 or over".

ANNEX 7 : PERSONAL ALLOWANCES FOR MARRIED COUPLES IN OTHER
COUNTRIES

Introduction

1. This annex looks at the relative level of personal allowances available to single people and married couples in most of the EEC countries, Australia, New Zealand, Canada, Sweden, Japan and the USA. It also provides some information about the basic systems of taxing married couples in those countries.

2. It should be recognised that difficult problems arise in making any sort of international comparison. Comparisons can rarely be of like with like, or show the whole picture. So conclusions drawn from some of the material in this annex could be misleading unless its limitations are appreciated.

3. The information provided may be subject to change, although it is as up to date as possible.

4. The first purpose of this annex is a specific one: to look at the ratios of allowances between single and married taxpayers, in different countries. The comparisons are complicated by the fact that not all countries provide basic personal allowances for everyone of the kind applying in the UK system. The term 'allowances' is therefore used here to refer to whatever system of giving relief for personal circumstances applies in each country.

5. Some assumptions have been made to simplify the comparisons:

- a. for a one earner married couple it is assumed that the husband is the sole wage earner and the wife has no income.

b. No account has been taken of 'allowances' given for children or other dependants or because of age, disability or the status of the taxpayer (for example widowed, divorced, single parent)

c. The comparisons assume that income is from employment.

6. The table below shows the ratio of 'allowances' in the different countries in three cases:

Country Details

7. United Kingdom

Married couples are taxed jointly on their combined incomes. A married man receives a Married Man's Allowance, which is about 1½ times the Single Person's Allowance, to set against any income of the couple. If his wife is working she has the Wife's Earned Income Allowance which is equivalent in size to the Single Person's Allowance, but can only be set against her earned income. More details are given in Annex 1.

8. Australia

Husband and wife are taxed separately. A spouse is entitled to a tax 'rebate' where he/she maintains the other spouse. The 'rebate' operates by reducing the tax payable by the amount of the rebate. If the rebate exceeds the amount of tax due there is no refund or carry forward of any 'excess' rebate.

Where the supported spouse has income above a specified amount the rebate is reduced by \$1 for every \$4 by which the spouse's net income exceeds that amount.

The schedule of tax rates includes a zero rate band. The first tax rate above this is 25 per cent. The ratios therefore take into account the maximum value of the tax rebate at the 25 per cent rate to a one earner couple.

9. Belgium

A comparison cannot usefully be made because allowances for employment income vary with income up to a maximum level. Furthermore the tax position of married couples varies depending upon the size of their total net income.

10. Canada

Husband and wife are taxed on an individual basis, but a married person supporting a spouse is entitled to a further allowance over and above that available to single taxpayers. This further allowance is reduced \$ for \$ if the supported spouse's income exceeds a set level.

11. Denmark

A system of fully transferable allowances and independent taxation applies. This does not extend to investment income which is aggregated with the income of the spouse with the highest earned income.

12. France

The French have a family quotient system under which income of the family (including children) is aggregated and then divided by a certain coefficient. The tax is calculated on

the resulting amount and then multiplied by the same coefficient to get the total tax due. For a husband and wife only, the coefficient is 2 and the effect is therefore similar to the German system. The ratios in the table are not based on allowances but on the effect of this system on the zero rate band only.

13. Germany

Married couples have the option of individual or joint taxation. There is effectively a zero rate on an initial portion of taxable income: that portion is doubled for married couples who are jointly assessed and is the basis of the ratios given above. Where the couple opt to be taxed jointly their total income is divided by two and the tax calculated on that part. The result is then multiplied by two to arrive at the total tax due. This gives married couples an added advantage particularly where their incomes are of different sizes: the effect is that part of the larger income, which would otherwise be taxed at a higher rate, is aggregated with the smaller income and taxed at a lower rate.

14. Ireland

Married couples can choose to be taxed separately or jointly. The allowance for a married couple taxed jointly is double the single allowance. Joint taxation is usually of greater benefit to a married couple, especially where one spouse has little or no income, because they enjoy tax bands which are twice the width of those for single people.

15. Italy

Taxpayers are allowed credits (as opposed to personal allowances) which operate as a deduction from the total tax due. A husband and wife are assessed separately, although

an additional tax credit is available to them if one spouse has taxable income not exceeding a specific level. One tax credit varies with income so a simple comparison is not possible.

16. Japan

Individuals are taxed separately but a special exemption is available for a spouse who has no income, or income which does not exceed a specified level. In addition, an 'employment income deduction' is available but as this varies with the level of income, a comparison is not possible. Investment income can also be taxed separately but it may be aggregated if the income of the 'household' exceeds a specified level. The 'household' can include children, parents and grandparents if they live together.

17. Netherlands

Allowances vary and are broadly dependent upon age, size of income and whether or not the taxpayer lives with someone (not necessarily a spouse). A comparison is not therefore possible.

18. New Zealand

A husband and wife are taxed separately. Taxpayers receive tax 'rebates' against income. (These 'rebates' operate in a similar way to Australian rebates.) The 'principal income earner' rebate is available to most individuals with below average earnings and varies with income. In the case of a married couple this rebate is given to the spouse with the higher income or, where incomes are equal, to whichever spouse opts for it.

A special rebate was also available for a dependent spouse but this was abolished with effect from 1 April 1983.

The ratios given in the table are only based on the entitlement to the 'principal income earner' rebate and will apply only on the assumption that the income of the single taxpayer and of the partner in the married couple claiming the rebate is identical.

19. Sweden

Individuals pay both National Income Tax (at progressive rates) and Local Income Tax (at a flat rate which can vary from area to area). A personal deduction is given to all taxpayers but only for local income tax. Husband and wife are taxed separately on their earned income. All taxpayers benefit from a zero rate band on National income tax upon which the ratios are based. In addition a married couple where one spouse has no income, or income below a specified level, is entitled to a tax credit of 30 per cent of the difference between that spouse's income and the specified level. The maximum credit will therefore go to a one earner couple.

The investment income of a married couple is aggregated with that of the spouse with the highest earned income. Liability for the tax due on the investment income is then split between the spouses in proportion to the amounts of their respective investment income.

20. USA

Married couples can be taxed separately but in practice most opt for joint taxation. This is generally more beneficial, because a different scale of tax rates applies with wider

bands, which includes a larger zero rate band, than is available to single taxpayers and married couples who are taxed separately. One and two earner couples filing joint returns both receive double the exemption given to a single taxpayer. In addition, two earner couples, taxed jointly, get an extra exemption equivalent to 10 per cent of the lesser of \$30,000 or the amount of the lower earning spouse's earned income. The benefit of this exemption will vary according to the size of the lower income but has a maximum value of \$3,000. This is reflected in the ratios set out in the table.

Personal Allowances in other Countries

	Single: One Earner Married Couple	Single: Two Earner Married Couple	One Earner Married Couple	Two Earner Married Couple
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United Kingdom:

a. Present System	1:1.57	1:2.57	1:1.64
b. Transferable Allowances	1:2	1:2	1:1
Australia	1:1.72	1:2	1:1.16
Canada	1:1.87	1:2	1:1.07
Denmark	1:2	1:2	1:1
France	1:2	1:2	1:1
Germany	1:2	1:2	1:1
Ireland	1:2	1:2	1:1
New Zealand	1:1	1:1	1:1
Sweden	1:1	1:2	1:2
USA	1:1.6	1:1.6 (2.5 max)	1:1 (1.55 max)

A comparison of allowances is not possible for all the countries included in the annex. (See text for details.)