10 DOWNING STREET

Prime Minister

If you have time, though there is a slot at 17.30 but this will also have to cover the speech.

AT

13/3

I agree – this is not queer – it is unilaterally pronouncing a change which has not even been discussed in E or in Cabinet

MG

PRIME MINISTER

Draft Green Paper on Personal Income Tax

You are due to discuss this with the Chancellor on Thursday, at 18.30 ~~before Cabinet~~. The following points struck me:

(i) The tone is not very "Green". In the introduction the Chancellor launches into his proposals and sets the context, i.e. the opportunities afforded by computerisation, at the end. Without saying very much different in substance, the tone would be better if he said:

"Approaching computerisation - opens up new options for reform of personal tax - my preference is for transferable allowances. What do you the public think?"

At a couple of points - paras. 3.1 and 4.5, the Chancellor gives the impression that he is pressing on with the preparatory work even before there is any public reaction. A "Greener" tone would give the Government the option of retreating if the reaction were adverse.

(ii) Annex 2 sets out the international comparisons. In general the UK has

- a low ratio for single: married, one earner thresholds;
- a high ratio for single: married two earner thresholds;
- a high ratio for married, one earner to married two earner.

/ (iii) The Chancellor's

(iii) The Chancellor's proposal increases the single threshold by 20%, £575, worth £3.32 per week; 680,000 out of tax. It raises the married one earner threshold by 63%, £2,005, worth £11.57 per week. 620,000 out of tax.

(iv) Annex 4 spells out the gainers and those who stand still - there are no losers. The gainers are single people including widows; one earner couples; two earner couples where one spouse is very part-time; two earner couples paying higher rate tax. The only group to stand still are two earner couples where both pay at basic rate. These represent only 3.3 million out of 17.7 million taxpaying units.

(v) The synopsis does not provide details of the treatment of investment income, though it hints at independent taxation. There must be quite a lot of revenue at stake if husband and wife are allowed to distribute investment income between them to best advantage. Measures against artificial schemes are hinted at, but would these turn out to make the system more, not less complex?

(vi) The synopsis does not cover mortgage interest. Several options, including allowing husband and wife their own ration of mortgage interest are still being looked at.

There is still some work to be done before any publication in the summer. At this stage the Chancellor seeks agreement to canvassing the basic principle of transferable allowances.

13 March, 1985

ANDREW TURNBULL

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

12 March 1985

Andrew Turnbull Esq
10 Downing Street
LONDON
SW1

Dear Andrew

DRAFT GREEN PAPER ON PERSONAL INCOME TAX

As promised I attach two copies of the draft synopsis of the proposed Green Paper on personal income taxation, for discussion at the Prime Minister's bilateral with the Chancellor on Thursday morning.

Yours ever
Rachel.

MRS R LOMAX
Principal Private Secretary

(1) Too white, too much impression of I'm getting on with this unless you stop me. Too little genuine consultation
(2) Gainers & losers set out in Annex. Single people; widows; two earner couples where wife is very part time when they elect for separate taxation. Only group [illegible] [illegible] are two earner families where both paying at standard rate 3,300 out of 17,660 thousand taxpayer units.
(8) Annex 2 sets out international comparisons. In general UK has low scores for S/MOE and high for S/MTE and M/MTE

DRAFT MINISTERIAL FOREWORD/INTRODUCTION

1. Last year I reformed the system of business taxation, setting the pattern for the next three years and beyond. In this year's Budget, I foreshadowed a programme for the reform of personal taxation.

2. My objective in both reforms is to create a tax structure that reflects the changing needs of the modern world and encourages the creation of wealth and jobs.

3. The Government is committed to reducing the burden of income tax. But changes in income tax are expensive and the money can only be found to the extent that it is not pre-empted by increases in public expenditure. It costs £1 billion to put the main personal allowances up by 5 per cent or to reduce the basic rate by 1 per cent. So it is vital to ensure that any resources that are available for reducing the burden of tax are put to the best possible use.

4. We need a tax system which is fair, comprehensible, and makes economic sense.

5. Measured against these criteria, the present system has a number of drawbacks:

- it discriminates in favour of two-earner families, at the expense of those where the wife stays at home to look after the children

- married women have no separate tax status; both their investment income and, normally, their earned income is aggregated with their husbands'

- low tax thresholds contribute to the poverty and unemployment traps - which are a disincentive to work

- it is complex and difficult for taxpayers to understand.

wishes to explore?

6. The Government can see considerable advantages in adopting a new system of personal taxation, based on a single transferable allowance for each taxpayer.

7. Under such a system everybody, man or woman, married or single, in or out of paid employment, would have the same standard tax allowance. Where one partner to a marriage is unable to make a full use of his or her tax allowance he or she would have the right (if they wish) to transfer the unused allowance to the other partner.

8. This reform would mean that all taxpayers would have exactly the same allowance. All married couples, whether one partner or both is earning, would have the equivalent of two allowances. The existing married man's allowance would disappear. The aggregation of husband and wife's income would go.

9. The single transferable allowance system offers three main advantages.

- it ends the present discrimination against the family where the wife works at home, which nowadays increasingly means discrimination against the family with young children

- unused allowances can be transferred within a marriage, ensuring that each taxpaying couple can take full advantage of them

- it gives married women equality and the right to privacy in their tax affairs, removing the anomalies created by the existing aggregation system.

10. It would, furthermore, enable the Government to raise tax thresholds both for families where the wife works at home and for young people and other low earners to a level that would be prohibitively expensive under the present system. For a given amount of tax relief it would take far more people out of the poverty and unemployment traps -and out of the tax net altogether - than is possible under the present system.

11. Transferable allowances would require changes to the way the tax system is run. These will be made possible by the computerisation of PAYE which is well under way; this is due to be largely completed by the end of 1987. It is essential to plan now for the tax structure that will be operated under a fully computerised system. The change to a new system can take place as soon as all the new facilities are available.

12. While this preparatory work is proceeding we are publishing this Green Paper to explain our proposals for reform in more detail. Subject to the outcome of the consultation period which will follow this Green paper, the Government propose to introduce the necessary legislation for a change in the system in 1987. New arrangements could be fully operational from April 1990.

13. Computerisation also opens up the possibility of other changes in the tax and benefit systems, which are discussed in the paper, and its Annexes.

<u>REVISED OUTLINE OF GREEN PAPER</u>

<u>Chapter 1: The Objectives of Reform</u>

<u>Background: Reform of the Tax System</u>

1.1 Government committed to tax reform.

1.2 1984 Budget achieved major reform of corporate tax system including substantial reduction in corporation tax rates; and dealt with distorting effects of capital allowances and stock relief.

1.3 1985 Budget sets in hand reform of personal income tax to reduce the tax burden and bring tax structure into line with reality of modern society. Green Paper outlines objectives and describes a system Government believes compatible with them. Outside comments welcome.

<u>Objectives of Reform</u>

1.4 Reform will have three specific aims

1.5 First: to provide a fairer system. To remove discrimination against couples with only one breadwinner. To remedy anachronistic treatment of married women (following 1980 Green Paper).

1.6 Second: <u>simplification</u>. Structure of system should be as simple as possible.

1.7 Third: <u>to find cost effective answers to the problems caused by low tax thresholds</u>. Consistent objective has been to increase income tax threshold. But very costly within present system. Reform needed so that, within limit of what can be afforded more can be done to reduce the burden of tax on the young and low paid, and to tackle the problems of the poverty trap and the unemployment trap.

1.8 Under the new system everyone would have a tax allowance in their own right; man or woman, married or single, in or out of paid employment. But tax system should continue to recognise the status of marriage, so unused allowances would be fully transferable within a marriage. Aggregation of husband and wife's income (investment as well as earned) would go. So structure will recognise each individual's right to independence and privacy in tax matters.

Chapter 2: The Case for Change and Proposals for Reform

Background

2.1 Structure of personal allowances has remained the same since the Second World War. Some of most important features of personal income tax system go back much further.

2.2 In brief:

Present structure

Single people: 1 personal allowance

Married men: approx 1½ the single person's allowance

Married women: wife's earned income allowance, equal to single personal allowance

Thus: single person: 1 allowance

one-earner couple: approx 1½ single allowance

two-earner couple: approx 2½ single allowance.

Wife's income aggregated with husband's income. Fuller details in Annex 1.

How the present structure originated

2.3 Before the War, there was an allowance for a single person, and an allowance of at least half as much again for a married man, who was expected to support his wife.

2.4 It was then unusual for a married woman to be in paid employment - only 10 per cent were in 1931 - but where she was in paid work, her husband got a small allowance to set against her earnings. This brought couple's total allowances up to roughly twice the single allowance.

2.5 In 1942 as part of the drive to encourage women to contribute to the war effort, the wife's earned income allowance was increased to the level of the single allowance. Wife's earned income allowance has remained at same level as single allowance ever since.

2.6 Married man has continued to get a higher allowance whether or not his wife is in paid employment. This gives the UK a system which, by international standards, discriminates in favour of two earner couples and against most one-earner couples. (See Annex 2 for international comparisons.)

<u>**Social aspects**</u>

2.7 Under present system:

- A married woman has no tax allowance of her own to set against her own income (wife's earned income allowance only available if she has earned income of her own, and even then theallowance belongs in strict law to the husband).

- Where wife has investment income of her own, couple may pay more in tax than two single people - a tax penalty on marriage.

- Because husband is nominally responsible for returning all couple's income and paying all the couple's tax, wife cannot have privacy in her financial affairs.

2.8 Major social and economic changes since the structure of allowances was fixed during the War. Very large proportion of women in paid employment. Now the rule rather than the exception for married women to go out to work except when they have young children. The great majority of women will be working at some point in their married lives; half of all married women already work outside the home, and the proportion is likely to go on rising.

2.9 It is right that everyone should have same tax allowance. All married women should have their own tax allowance - not just those who work outside the home. There is no reason to discriminate in favour of the married man whose wife goes out to work, as against single people and married couples where the wife works at home.

Traps

2.10 Low tax thresholds are one of the main causes of the poverty and unemployment traps. People most affected by these traps are married men on low earnings supporting families.* Traps wrong in themselves and bad for the economy.

2.11 Government has made progress, raising tax thresholds by [16] per cent in real terms, taking almost 1 million people** out of tax since 1978-79 (compared with indexation). But still too many people paying tax and in traps. New system will be more accurately targetted at those worst affected by low tax thresholds.

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* By historical accident, the present system does give relatively high tax thresholds already to married women supporting families: see Annex 1.

** Pre-Budget figures.

Proposals for reform

2.12 Government therefore proposing the system of single transferable allowances, which should correct many of the drawbacks of existing scheme.

2.13 Government's intention would be to phase in the new system over two years with no couples losing out in cash terms. The new allowance will be set at the level at which two such combined allowances currently given to a two-earner couple. Effects will be as follows.

- Single people will gain from increase in allowance. Helps young people looking for their first job. Unemployment worst among single youngsters.

- Married man who is sole earner will see a substantial increase in his tax threshold. This will reduce numbers of those most affected by poverty and unemployment traps.

- Two-earner married couples and married couples where the wife is the sole earner will keep the same total allowances in cash terms.

2.14 Phasing in such a change over 2 years would cost around £4.5 billion. But the effect would be to lift about 200,000 more tax units (mainly married couples) out of tax than would be the case if allowances were raised under the present system at a similar cost to the Exchequer. (Annex 3 shows how the change might be phased in; Annex 4 gives more details of the effects on couples in different circumstances.)

Aggregation of husbands' and wives' income

2.15 New system will also deal with widespread and justified criticism of present tax system among women. Aggregation of both earned income and investment income will be ended; and both partners in a marriage will have right to refuse transfer of any unused allowance. The rule which says that the income of a married woman living with her husband is deemed for income tax purposes to be his income and not her income will be ended. Husband and wife can have equal privacy and independence in tax matters.

2.16 Annex 5 gives more details of the treatment of investment income and discusses possible implications for other aspects of the income tax and for the capital taxes.

Particular groups

2.17 Annex 6 discusses how the new system will affect the elderly; Annex 7 looks at the position of single parents.

How the system will work

2.18 When it is fully phased in system will run broadly as follows:

(a) Before the start of the tax year a partner in a married couple who thinks he/she will have no income during that year may arrange for the tax office to give the whole of the unused allowance to the other partner, who will benefit through the PAYE code.

(b) If one partner thinks that he/she will only have modest earnings - eg from a part-time job - they may arrange for the tax office to transfer only part of the allowance.

(c) Otherwise each partner will get a single allowance.

(d) The position will be reviewed after the end of the tax year to ensure that the couple have received the right allowances.

Chapter 3: Practical implications of the change

pre-empting consultation?

3.1 Introduction of fully transferable allowances represents a major change in the tax system. Government have set in hand the planning for this change and, subject to the response to this Green Paper, intend to legislate during the life of this Parliament. Change will directly concern something like 1 million employers, 600 Tax Offices and [12] million married couples. Will also affect indirectly a further [9] million single people.

Computer support

3.2 To run smoothly, system of fully transferable allowances requires new administrative infrastructure in the Inland Revenue.

3.3 Government has already authorised the Revenue to go ahead with two major computer projects. A pilot system for computerisation of PAYE (COP) has been running live in the West Midlands for well over a year. COP system is now being extended across the whole country, region by region, and its installation beginning this year will be complete by late 1987 or early 1988. Procedures for taxing self employment income under Schedule D are also being computerised (CODA). This new system also will be in place by 1989.

3.4 Government has now authorised Inland Revenue to enhance this basic computer system by two further developments: an efficient data transmission network, enabling the 600 Tax Offices to exchange information quickly and economically with each other, and with the offices responsible for collection and enforcement; and also a computer based national index, which will maintain up to date records of each taxpayer, his or her employer (or self employment), together with the necessary information to connect the tax records of married couples.

3.5 This development will provide Inland Revenue with computer support it needs to run a fully transferable allowance system. The link can be created and maintained between the tax records of husbands and wives who (because they may have different employers) may be dealt with by Tax Offices hundreds of miles apart. For the great majority of couples these records are not linked at present. Computer system will also enable tax offices to handle the many more cases which will need to be reviewed after the end of the year.

3.6 Without these added facilities it would be almost impossible to run fully transferable allowances. First requirement is therefore that necessary computer support should be in place in the Revenue before the administrative action to change to the system of fully transferable allowances can begin.

3.7 The Revenue will be using the computer facilities in the COP and CODA systems, and the new integrated data network, to set up the new national index; and the index cannot therefore be completed until after the other facilities are in place (1989). This explains why changeover to the new system cannot begin until then.

3.8 Annex 8 looks in more detail at the administrative consequences of the change.

Chapter 4: Next Steps

4.1 This Green Paper outlines main features of the proposed reform to a system of fully transferable allowances.

4.2 In the long run computerisation in the Inland Revenue will open up wider possibilities for change. Government will be considering the case for changing from present cumulative PAYE to a system of non-cumulation and 100 per cent end year review, of the kind used by the USA and many other countries. This would imply major changes for employers, taxpayers and Revenue administration.

4.3 With wider computerisation of DHSS, Government will also be considering the case for closer integration between data bases for tax and social security, and the systems themselves.

4.4 Government not bringing forward any proposals for change in these wider areas at present. But implications need to be studied. Annexes 9 and 10 set out some of the issues for consideration. Full consultation before any decision is made. Important to note that move to fully transferable allowances does not prejudice any of these possible changes.

4.5 In shorter term, over the coming months Government will be working up the necessary detailed procedures to operate fully transferable allowances. Will want to discuss with, in particular, employers' representatives, what the reform would imply for changes in employers' payroll procedures.

4.6 The Government will welcome comments, both on the proposed reform itself and, in due course, on the detailed procedures.

4.7 Subject to that, the Government intend to legislate in this Parliament [1987?]. During [1988 and 1989] Tax Offices will be asking married couples for the information necessary to link their tax records, set up the national index, and to give them the appropriate allowances. The new system could come into operation in the 1990-91 tax year.

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Summary of Annexes

Annex 1 **The present structure of personal income tax**

Explanation of the present system and personal allowances, including those for elderly people.

Annex 2 **International Comparisons**

Comparison of levels of personal allowances available to single people and married couples in [15] other countries. The UK is exceptionally generous in the scale of allowances given to two-earner couples but relatively much less generous to one-earner couples.

Annex 3 **Phasing in the new structure**

Text and tables to show how the new structure could be phased in, the consequences for different couples, and the costs to the Exchequer. A two-year phasing-in period could avoid losers in cash terms, at a total cost of £4.5 billion for the non-elderly.

Annex 4 **Distributional effects**

Text and tables to show the effects of the new system on different families at various income levels

Annex 5 **Consequences for investment income, other aspects of income tax and capital taxes**

Consequences of independent taxation for wives with investment income. Possible measures to counter artificial income splitting.

- Treatment of mortgage interest ceiling for married couples.
- Treatment of other limits for husband and wife.
- Implications for capital taxes.

Annex 6 **<u>The Elderly</u>**

To what extent should transferability extend to the age allowance; might age allowance be phased out as part of the change; and the distributional consequences of the options.

Annex 7 **<u>Single parents</u>**

Single parents currently receive an additional allowance equal to about half the single allowance; should this extra allowance be phased out as part of the change and/or converted into increased One Parent Benefit.

Annex 8 **<u>Administrative consequences of fully transferable allowances</u>**

- Staff costs of running the new system: would depend on the detail, but much less than under a manual system.

- Setting up costs.

  Capital costs of integrated data network national index - necessary in any event for efficient working of Revenue in 1990s.

Annex 9 **<u>Administration in the longer term</u>**

Computerisation opens up possibility of moving to taxation on a non-cumulative basis as in US. Would be attractive for small business.

Annex 10 **<u>Integration of tax and social security</u>**

Raises wider issues. Clarify possible objectives and how far they would be met by different schemes proposed. Explain administrative consequences.

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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 treated as the husband's and taxed at his marginal rate. He is formally responsible for handling the couple's tax affairs, claiming the allowances, and paying the tax.

2. The personal allowances are as follows:

- the married man's allowance (£3155 in 1984/85) can be set against any income of the couple;

- the wife's earned income allowance (£2005 in 1984/85) is technically an allowance available to the husband to set against his wife's earnings only; in practice, it is usually given against the wife's earnings directly 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	(3155 + 2005)	5160
Husband only working		3155
Wife only working	(2005 + 3155)	5160

The Elderly

4. People over 65 have higher tax allowances, if their income is below a certain limit (see paragraph 5 below):

single age allowance	£2490
married man's age allowance	£3955

The wife's earned income allowance for married women over 65 is the same as for younger people, £2005.

5. Age allowance is given in full up to income of £8100 - this 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 basic allowance.

Wife's earnings election

6. Where husband and wife both have substantial earnings they may elect to have their earnings taxed separately. Each partner then gets a single allowance and his/her own set of tax rate bands. The election does not affect the investment income of the wife which remains aggregated with her husband's income.

Annex 2.

International Comparisons (DETAILS ARE SUBJECT TO CONFIRMATION).

1. Comparisons are very difficult to make, especially in such a confined area as the level of allowances available to single people and married couples. In many instances a comparison is impossible because the system provides allowances which vary with the size of earnings.

2. The comparisons which follow, so far as possible, give an indication of the ratio of allowances in three cases. These are:

	Col 1		Col 2		Col 3		
	Single:	Married One Earner	Single:	Married Two Earner	Married: One Earner	Married Two Earner	
[UK	1 :	1·5	1 :	2·5	1 :	1·66	]

[It has been assumed for a one earnier married couple that

a. the husband is the earner and

b. the wife has no income.

For all cases it is assumed the taxpayers have no children or other dependents.]

3. Denmark

1:2	1:2	1:1

Since 1983 a system of fully transferable allowances and independent taxation has applied. This does not extend to investment income which is aggregated with the income of the spouse with the highest earned income.

4. Ireland

1:2	1:2	1:1

Married couples can be taxed separately or jointly. The ratios given above are based on joint taxation which most married couples opt for. In addition to extra allowances with joint taxation a married couple also enjoy a special scale of rates with bands double that for single taxpayers so they usually pay less tax than a single person with the same size income.

5. Germany

1:2	1:2	1:1

In addition to allowances, married couples have the choice of separate assessment, where each are taxed as individuals, or income splitting. In the latter case the total income is divided by 2 and the tax calculated on that part. This is then multiplied by two to get the total tax due. This gives married couples an added advantage particularly where the incomes vary. Effectively any higher income which may be taxed at a higher rate is transferred to the lower income and taxed at a lower rate.

6. France

1:2	1:2	1:1

The French have a family quotent system under which income of the family (including children) is aggregated and then divided by a certain coefficient. The tax is calculated on that reduced 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 splitting system. The ratios above are not based on allowances but on the effect of this system on the zero rate band only. Allowances, or expense deductions, have maximum or minimum values, but vary with a. the size of income and b. the type of job. So a comparison of allowances alone is not possible.

7. Italy

Taxpayers are allowed tax deductions as opposed to personal allowances. A husband and wife are assessed separately, although an additional tax deduction is available to them if one spouse has taxable income not exceeding a specific level. Tax deductions vary with income levels so a comparison is not possible.

8. Luxembourg

1:1.78	1:2	1:1.12

A husband and wife are assessed jointly. One tax scale applies to all taxpayers but a married couple's tax is calculated by applying the table to only half their income and then multiplying the result by 2. As the table includes a zero rate band, this is effectively doubled for married taxpayers. (This same method also applies to a single taxpayer who has been divorced less than 5 years at the start of the tax year - so in the ratios shown such a person is equivalent to a one earner married couple.)

Broadly, allowances to set against income are doubled for two earner married couples. The ratios given include minimum special expenses and employment income allowance.

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. Netherlands

Allowances vary and are broadly dependent upon 1. age, 2. size of income and 3. whether or not the taxpayer lives with someone (not necessarily a spouse). A comparison is not therefore possible.

11. USA

1:1.6	1:>1:6 (2.5 max)	1:>1 (1.55 max)

Married couples can be taxed separately but in practice most opt for joint taxation. This is generally more beneficial, a different scale of tax rates then applies with wider bands, which includes a larger zero rate band than available to single taxpayers and marrieds 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. (Hence the variation in rates.)

12. 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, there are basic allowances which vary with the level of income, so a comparison is not possible.

13. Sweden

1:1	1:2	1:2

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 can only be set against local income tax. Husband and wife are taxed separately although the unearned income of both is aggregated with that of the spouse with the highest earned income. The tax calculated on the unearned income is then split between the spouses in proportion to the amounts of their respective unearned income.

All taxpayers benefit from a zero rate band on National income tax upon which the above ratios are based. There is no special treatment for a dependent spouse.

14. Greece

1:1.24	1:2	1:1.6

Spouses are taxed separately although a husband is entitled to an allowance for a wife provided her income is less than a specified level. He is also entitled to a tax reduction for his wife but only if she has no taxable income. If allowances or tax reductions cannot be used in full by the husband, they are transferred to the wife.

The ratios provided take into account the basic personal allowance, the maximum value of the general employee's allowance, (this allowance will vary with income) the zero rate band effect and converting the tax reduction for a one earner family into an allowance taking the lowest rate of tax only. (11 per cent.)

15. Canada

1:1.87	1:2	1:1.07

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 spouses income exceeds a set level.

16. Australia

1:1.6	1:2	1:1.25

Husband and wife are taxed separately. A spouse is entitled to a tax rebate only where he/she maintains the other spouse.

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 tax scale of rates includes a zero rate band. The first tax rate above this is 30 per cent. The ratios therefore take into account the maximum value of the tax rebate at the 30 per cent rate to a one earner couple.

17. New Zealand

1:1	1:2	1:2

A husband and wife are taxed separately. The only basic allowance given for all taxpayers is a standard deduction for employment expenses. Otherwise taxpayers receive tax rebates against income. The 'principal income earner' rebate is available to most individuals and varies with income.

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

The ratios given above are based on the entitlement to the 'principal income earner' rebate and will only hold good if it is assumed that the income of the single taxpayer and that of each married taxpayer is identical.

18. It would be wrong to attempt to draw any worthwhile conclusions from a limited comparison of this kind. In the majority of cases, the effect of any one country's tax system on married or single people is far more complex than the outline above demonstrates.

Where comparisons of this sort are made, it may well be the case that other features of the tax system provide additional tax advantages to married couples which are not reflected within the narrow confines of the allowances given.

but UK in general has a low figure in col 1, a high figure in col 2 and col 3.

ANNEX 3: PHASING IN THE NEW STRUCTURE

1. Aim will be to phase in fully transferable allowances over [two year] period avoiding cash losers amongst two-earner couples.

2. But this will involve substantial forward commitment of resources (£4.5 billion at current prices and income levels). Precise way in which system would be phased in would therefore need to be considered in light of economic circumstances at the time.

3. Phasing in over two years enables the cost to be spread.

4. For illustration, at 1984-85 allowance levels, a possible two-year phasing in scheme would be

Year 1

(i) Reduce married man's allowance to £2,855. -300

(ii) Raise single allowance and wife's earned income allowance to £2,305. +300

(iii) Introduce transferable component of £1,200 within wife's earned income allowance. (The married man's allowance is, under present rules, already available to set against a wife's income if the husband has insufficient income of his own.)

Year 2

(i) Raise single allowance to £2,580. +275

(ii) Convert wife's earned income allowances into a single allowance. at £2,580

(iii) Replace married man's allowance by single allowance of £2,580. −275

(iv) Make single allowance fully transferable between spouses.

[5. Position of elderly would need special consideration in light of decision about future of age allowance.]

Annex 4

FULLY TRANSFERABLE ALLOWANCES: DISTRIBUTIONAL EFFECTS

1. The attached tables show the detailed effect of introducing fully transferable allowances.

TABLE 1

EFFECT OF FULLY TRANSFERABLE ALLOWANCES

After transition with no cash losers

Non-elderly

	Amount of Allowance Before	Amount of Allowance After	Numbers (thousands)		Amount of cash gain
Single (7.8 million)	2,005	2,580	680 (9%)	taken out of tax	up to £3.32 per week
	20% +575		7,000 (90%)	currently liable at basic rate	£3.32 per week
			100 (1%)	currently liable at higher rates	over £3.32 per week
One-earner couples (4.4 million)	3,155	5,160	620 (14%)	taken out of tax	up to £11.57 per week
	63% +£2,005		3,580 (81%)	currently liable at basic rate	£11.57 per week
			220 (5%)	current liable at higher rates	over £11.57 per week
Two-earner couples (5.5 million)					
gains for v.. part time — wife earns less than £2,005	3,155 to 5,160	5,160	1,800 (33%)		up to £11.57 per week
no gain here — wife earns over £2,005					
- couple do not elect	5,160	5,160	3,300 (60%)		no gain
- couple liable at higher rates but do not elect	5,160	5,160	200 (4%)		gain depends on split of income between husband and wife.
i.e. gains for professional women — couple elects	4,010	5,160	160 (3%)		at least £6.63 per week

TABLE 2

Distribution of gains after transition with no cash losers

(1984-85 allowance levels)

Size of gain	Number of taxpayers (thousands)	Per cent
No gain/loss	3,300	19
Taken out of tax	1,300	7
Total gainers remaining in tax	13,060	74
	17,660	100

Annex 5 — <u>Consequences for investment income, other aspects of income tax and capital taxes</u>

Annex 6 — <u>The Elderly</u>

Annex 7 — <u>Single parents</u>

Annex 8 — <u>Administrative consequences of fully transferable allowances</u>

Annex 10 — <u>Integration of tax and social security</u>

Still in preparation; dependent on decisions.

Annex 9 Administration in the Longer Term

1. Chapter 4 of the Green Paper explained that work is in hand on a study of how the tax system might be run in the longer term. This annex sets out some of the possibilities under consideration.

2. There are basically three stages in the work of calculating and settling tax bills:

   (a) Before the year - coding, to give taxpayers their personal allowances and to make other adjustments;

   (b) During the year - taking account of changes in personal circumstances, job changes, and fluctuating income;

   (c) At the end of the year - calculation of any repayment due or tax still owed, and settling the balance.

3. Changes could be made to any or all of these stages. Some could be made independently; others only make sense in conjunction with changes to other parts of the tax system.

Before the year

4. The most likely change here would be a move from Revenue-coding to self-coding by taxpayers.

5. This would save work for the Revenue. By the same token, it would impose a burden on taxpayers, and would make life more difficult for employers who would receive coding notices piecemeal from their employees instead of in a batch from the tax office.

6. The first question to consider is how well taxpayers could cope with self-coding under the present system. Some simplification would certainly be desirable and perhaps essential. And particularly if coupled with a change to non-cumulation (see paragraphs 8 to 10), self-coding would mean that many taxpayers would have paid too little or, typically, too much tax by the end of the year.

7. Self-coding would inevitably mean more work for the Revenue in reviewing cases at the end of the year. It would be for consideration whether this would require returns from all taxpayers or whether, as information technology develops, the information provided by income payers would be enough in many cases (see 13 below).

<u>During the year</u>

8. The key question here is whether to retain the present system of cumulation or to move to non-cumulation.

9. A change to non-cumulation would have these advantages.

(a) Some employers, particularly those whose payrolls were not computerised, might find non-cumulation simpler to operate during the year, but this could be offset by any extra work from self-coding (see paragraph 5 above).

(b) Non-cumulation for IT could help to make it easier to integrate tax and NIC deductions into a single set of tables.

(c) Non-cumulation could mean an end to the current staff-intensive system for handling taxpayers moving from one employer to another.

10. The central disadvantage of non-cumulation is that it will not produce the right result for a high proportion of taxpayers. Of itself, non-cumulation would tend to mean that taxpayers would overpay tax - the person with breaks in employment will lose the benefit of some of his personal allowances, and the person who receives a bonus may find himself paying higher rates for the week in question.

After the end of the year

11. Either of the preceding changes would inevitably mean more work in sorting out cases after the end of the year. This extra work could either be done entirely by the Revenue, as happens at the moment, or there could be a move to self-assessment.

12. The Revenue could assess all taxpayers on the basis of information provided by the taxpayer. All taxpayers would therefore have to fill in returns, which the Revenue would process. There would be perhaps 20 million returns to handle, and millions of assessments and repayments to follow.

13. The paper mountain which that would generate would be reduced sharply, as technology develops, by an alternative approach. Information could be provided by income payers - employers, banks, companies paying dividends etc - on electronic tape. The Revenue would assess on the basis of this information, and fewer taxpayers would have to fill in returns.

14. Self-assessment would take a good deal of work from the Revenue, at the cost of putting the work on the taxpayer. A number of important changes would have to be made before self-assessment could be introduced. Some

simplification to the tax system would be needed, to ease the actual process of self-assessing. In particular, the basis of assessment for Schedule D would have to be brought into line with that for income from employment.

15. Under a non-cumulative system, and a fortiori under self-assessment, a compliance regime with more effective and automatic penalties would be required, to ensure that taxpayers met their obligiations.

16. A switch to the sort of system described in this Annex would have four main advantages.

(a) The new system might be run by fewer staff.

(b) The marginal extra staff cost of running transferable allowances within such a system might be small.

(c) Small (non-computerised) employers might be able to calculate the deductions for tax and NIC from one table.

(d) The way might be opened to further policy options.

The main possible disadvantages are that there would be extra compliance requirements for taxpayers and on balance possibly, for some employers. Taxpayers could also often pay too much tax during the year, though in expectation of an eventual repayment.