Tax and Marriage

Research Paper 95/87

13 July 1995

In 1990 a fundamental reform in personal taxes was implemented. Under the new system of independent taxation, all individuals became responsible for their own tax affairs, and married couples were assessed for income tax and capital gains tax as separate persons. This represented the reversal of a principle which had held good for almost two hundred years: namely, that a married woman's income was simply part of her husband's total earnings, and should be taxed as such. All individuals became entitled to the personal tax allowance to set against any type of taxable income they received. Married couples were entitled to an additional allowance called, appropriately, the married couple's allowance (MCA).

One reason for the introduction of the MCA was to compensate married men for the abolition of the personal allowance they had been entitled to as husbands, the married man's allowance. A further reason for its provision was the Government's wish that the tax system continue to 'recognise' marriage. The structure of personal tax allowances, and the recognition of marriage by the tax system, has come under some scrutiny recently, following a series of reductions made in the value of the MCA. This paper provides a short history of these changes, and discusses a number of issues in personal taxation related to one's married state.

Antony Seely
Business & Transport Section

House of Commons Library

CONTENTS

I Introduction

> "What [God's] chief end was of creating woman to be joined with man, his own instituting words declare ... "It is not good," saith he, "that man should be alone. I will make a helpmeet for him" (Genesis 2:18). From which words so plain, less cannot be concluded, nor is by any learned interpreter, than that in God's intention a meet and happy conversation is the chiefest and noblest end of marriage, for we find here no expression so necessarily implying carnal knowledge as this prevention of loneliness to the mind and the spirit of man."
> John Milton *Doctrine and Discipline of Divorce* 1643.

Since the introduction of income tax in this country in 1799, the prevention of loneliness to both mind and spirit has had fiscal implications for both man and wife, since a married woman's income has been taken to be but part of her husband's, and taxed accordingly. The *Income Tax Act 1806* directed that any profits earned by a married woman "shall be deemed to be the profits of the husband." The language used in section 279 of the *Income and Corporation Taxes Act (ICTA) 1988*, which codified this rule prior to the introduction of independent taxation, shows little change over the intervening years: "A woman's income chargeable to income tax shall ... during which [time] she is a married woman living with her husband, be deemed for income tax purposes to be his income and not her income."

A number of changes were made during this century mitigating the inequalities of this rule, three of particular importance. In 1918 an additional tax allowance was introduced - the so-called "wife" allowance - given to all married men; this was the first specific provision made by the income tax system for married couples. At the time, it was felt that recognition should be given to the additional financial burdens that marriage imposed. One usual consequence of a wedding was that two people became dependent on the one (husband's) salary, while sole responsibility for the care of children usually fell to a wife. The idea that child caring be shared between working parents, possibly supplemented by professional help, was rarely entertained. Indeed, in most occupations open to women before 1945, it was common practice that on marriage women should cease being employed. In 1920 the wife allowance was renamed the married man's allowance and increased substantially in value to about 1.5 times the single person's allowance (which it remained up to its abolition in 1990).

That same year, 1920, saw a second innovation in the provision of a new tax allowance for wives who worked outside the home: the wife's earned income relief. This was given to couples to set against any earned income of a wife; unearned income, from savings or investments, was not covered by this allowance. Initially it was set equal to the difference between the married man's allowance, and the sum of two single person allowances.

From 1914 spouses could elect to file their own tax return, being liable to pay tax on their own income. However this election had no effect on their aggregate tax liability. The two incomes were added together, tax due on the joint income was computed as if the joint income was the husband's, and the tax liability was then apportioned between the spouses roughly in the ratio of their incomes. The system was complicated and unpopular, both with taxpayers and the Revenue. In 1971 an election for separate taxation of a wife's earnings was introduced. Couples could elect to have their earned income assessed separately for tax, and a wife's earned income was taxed as if she were a single person. This election had to be made jointly, and any unearned income enjoyed by a wife continued to be aggregated with her husband's when assessed for tax. Although the wife claimed her own single person's allowance, neither spouse could claim either of the married allowances. Election for separate assessment was only attractive for couples with relatively high incomes, where the wife had significant earned income. Couples only benefited if the saving they made in higher rate tax, from the disaggregation of the wife's earned income, outweighed the loss of personal allowances (the gap between the single and married allowances). By 1989-90 spouses had to have a joint income of £30,511, of which the wife's earned income had to be at least £7,026, before the election would be beneficial.[1]

Despite these changes, the fact remained that on marriage a woman lost her rights to financial privacy and independence. Moreover the same principle applied in the taxation of capital gains as in the taxation of income, though, of course, this affected a relatively small number of people compared to the numbers paying income tax. Any capital gains realised by a married woman were assessed and charged for tax on her husband. Married couples were only entitled to the one annual exemption given to single persons. Clearly, then, independent taxation represented a major reform in the personal tax system. As the then Chancellor, Nigel Lawson, said in his 1988 Budget speech when first announcing its introduction, "the present system ... takes the income of a married woman as if it belonged to her husband. Quite simply, that is no longer acceptable."[2]

Although the separate assessment of all individuals dealt with this unacceptable anomaly, the structure of personal tax allowances and reliefs continues to make some distinctions between those who are married and those who are not. For those once married, but now divorced, the tax system has implications for the payment of maintenance, though this area of tax law was reformed in 1988 as well. In addition, although there are no universal tax allowances given to parents in the UK,[3] there exists one limited fiscal concession targeted at families, in the form of tax relief for workplace nurseries.

This Research Paper provides a description of the principal ways in which the personal tax system affects marriage, and the related matters of divorce, children and childcare. Its aim is to provide a brief outline of the most important tax allowances and reliefs, along with some of the background to recent debates on how these might be altered, amended or abolished. A detailed discussion of tax planning issues is well beyond its scope, and individuals considering such decisions are, as always, recommended to obtain professional advice.

---

[1] *Taxation of the Family* O.P.Wylie Butterworths 1993; p.2.

[2] HC Deb 15.3.88 c.997.

[3] Child tax allowances existed for most of this century, but were abolished in the late 1970s in favour of child benefit.

II A Short History of Independent Taxation

A. The 1980 Green Paper

> "The aggregation for Income Tax purposes of the income of husband and wife is not dependent upon any medieval conception of the subordination of women; nor is it a question of sex disability, since either partner can claim separate assessment and separate collection. The incomes are aggregated because the law of taxable capacity is the supreme law in matters of taxation, and taxable capacity is, in fact, found to depend on the amount of income that accrues to the married pair, and not upon the way in which that income happens fortuitously to be owned by the members of the union. It is beyond question that in the immense majority of cases where the wife has separate means she contributes to the common purse either by actual merger of her income with her husband's, or by bearing expenses which in less fortunate households fall upon the husband ... We therefore recommend that the aggregation of the incomes of wife and husband should continue to be the rule."[4]

This was the conclusion of the Royal Commission on the Income Tax, discussing the tax treatment of husband and wife, as part of its 1920 report on all aspects of income tax, its scope, rates, incidence, and those alterations of law and practice deemed necessary or desirable. For the next fifty years, the Royal Commission's conclusion was generally accepted. For example, in 1955 the Radcliffe Commission, appointed to examine the taxation of profits and income, endorsed this viewpoint:[5]

> "We see in the existing rule nothing that embodies an outmoded or unworthy conception of the relations of man and woman in marriage ... It does not appear to us ... that marriage creates a social unit which is not truly analogous with other associations involving some measure of joint living expenses and that to tax the incomes of two married people living together as if each income were equivalent to the income of a single individual would give a less satisfactory distribution than that which results from the present rule."

Despite the introduction of the wife's earning election in 1971, aggregation of spousal income came in for increasing criticism during that decade. An indication of the pervasive nature of the system was given when finally, in 1978, the Inland Revenue changed its practice of replying to any correspondence from married women by simply writing to their husbands.

---

4 *The Royal Commission on Income Tax* Cmd 615 1920; pp.58-9.

5 *Royal Commission on the Taxation of Profits and Income* Cmd 9474 June 1955. Cited in, *The Taxation of Husband and Wife* Cmnd.8093 December 1980; p.59.

Instead, tax offices were instructed to write directly to the person concerned.[6] That same year, 1978, the Equal Opportunities Commission published a highly critical report on the taxation of married couples.[7] The Commission argued that individuals who did the same work should expect to receive the same reward and be taxed on that reward in a like manner. Indeed, the taxation of men and women as individuals, irrespective of their married status, was the only approach consistent with the *Sex Discrimination Act 1975* and the *Equal Pay Act 1970*.

In December 1980 the Government published a Green Paper on the taxation of married persons. It proposed three possibilities for the unit of taxation in the taxation of families:[8]

> "The first is to treat the family (husband, wife, perhaps also other dependants) as the unit. The second approach takes the married couple (husband and wife) as the tax unit. The third is to look at each person as a separate individual regardless of whether they are single or married."

It conceded that substantial social change over the century had made certain aspects of the current arrangements deeply unpopular. Most important, the role of women in the national workforce had been transformed in scale and scope.

The Green Paper cited the *Report of the Committee on One Parent Families*,[9] published in 1974, on the situation before World War Two: "Before the last war, representative women workers were young and single. Working women in the older age groups were mostly lifelong spinsters drawn from the reservoir of unmarriageable women. The custom then both among the middle and the working classes was for work to cease on marriage and therefore the proportion of married women in paid jobs was less than 10 per cent." By comparison, the Green Paper noted, "today over half of all married women under pension age are working or actively looking for a job."[10]

Though the Green Paper made no strong recommendations itself, it prompted a large number of submissions, the majority of which favoured the radical solution of mandatory independent taxation. As one commentator has put it, there was an "unusually long gestation period" between the 1980 Green Paper, and amending legislation being introduced.[11] In Nigel Lawson's memoirs, *The View From No.11*, this delay is attributed to the inconclusive nature

---

6 *The Taxation of Husband and Wife* Cmnd 8093 December 1980; p.59.

7 *Income Tax and Sex Discrimination* December 1978.

8 *The Taxation of Husband and Wife* Cmnd 8093; p.21.

9 Cmnd 5629 July 1974.

10 *The Taxation of Husband and Wife* Cmnd 8093; p.10.

11 *Taxation of the Family* O.P.Wylie 1993; p3.

of the public response to the Paper, coupled with the personal antagonism of the then Prime Minister, Margaret Thatcher, to any reform:[12]

> "It was clear that, despite her oft-pronounced and no doubt deeply felt belief in the importance of the family, in practice she strongly identified with the two-earner couples, who (in financial terms) were the beneficiaries of the old system. I suggested that there was a long-term electoral bonus to be secured from being the party that emancipated married women so far as the tax system was concerned. She countered by claiming that all we would do was alienate working wives, on whose votes we depended ... She insisted that what I was proposing was the wrong kind of tax cut: the right way to help families with children was by reinstating the old child tax allowance - a proposal of singularly little merit which I knew to be a hobby-horse of hers (she was always proposing it)."

B. The Second Green Paper

The success of the Government's reform of corporate taxation in 1984 reinvigorated the debate on personal taxes - an opportunity seized by the Chancellor: "A Green Paper seemed to me the best means of getting the disadvantages as well as the advantages of these schemes into the public arena - which should then give me a freer hand to introduce those reforms I wished to bring about."[13]

In his 1985 Budget speech, Nigel Lawson set out the case for his preferred solution to the dilemma of taxing marriage:[14]

> "The present structure of personal income tax is far from satisfactory ... 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 husband were unable to make full use of their allowance, the unused portion could be transferred, if they so wished, to their partner."

---

12 *The View From No.11: Memoirs of a Tory Radical* Nigel Lawson 1992; p.882, 884.

13 *op.cit*; p.883.

14 HC Deb 19.3.85 cc.794-5.

It is notable that Mr Lawson used two distinct arguments for independent taxation, only one of which - privacy in marriage - could be seen as a matter of pure principle. The issue of privacy would appear to transcend questions of policy. Could one imagine it being argued now that the tax system should encourage **less** financial privacy? By comparison, the decision whether the tax system should encourage married women with children to join the job market, or stay in the home, obviously has a political dimension. Of course, changes in the tax system are not made in a vacuum, and choices about a particular social end in taxation will always be judged in light of other social implications, as well as the likely impact on tax revenues. In this respect, independent taxation proved no exception.

In his Budget speech Mr Lawson anticipated that the second Green Paper on personal taxation would be published later that year, so that it would be possible to legislate in 1987, and have the new system in operation by the end of the decade. In fact, the Paper was published in 1986,[15] following further opposition from the Prime Minister and others within the Cabinet. The Green Paper argued that an equal tax allowance should be given to both husband and wife, and that this new allowance would be fully transferable between partners.

At this point it may be helpful to take a closer look at how the provision of personal tax allowances operated. Single persons, both men and women, received the same single person's allowance to set against their income for tax. On marrying, a couple's joint income was taxed as the husband's, and both partners ceased to be eligible for the single person's allowance. In the case of the husband, his single allowance was replaced by the married man's allowance (MMA). In 1989-90 the MMA was worth £4,375, compared to the single person's allowance of £2,785. The MMA was 'transferable', in the sense that it was given to the husband, even if he did not work, who used it to claim against income earned by his spouse (income which was, of course, counted as his own, for the purposes of tax).

Married women who did not work did not receive any allowance. Those who did work received the wife's earned income relief (WEIR). When this was first introduced in 1920, it was equal to the difference between the MMA and two single person allowances. In 1942 the WEIR was increased to the level of the single person's allowance itself, putting working couples at a distinct advantage. This allowance would be added to their husband's MMA when calculating the total earnings a couple could receive tax-free (worth, in 1989-90, £7,160 in total). This would compare with a lower level of total personal allowances - worth £5,570 in 1989-90 - if the couple in question had not got married.

As its name suggests, the WEIR did not cover savings income. As a result, the tax system strongly penalised those married couples in which the wife had had to give up work to have, and look after, children, yet contributed to the household finances with savings of her own. However, the system encouraged marriage, being more generous to working married couples than to unmarried couples.

---

15 *The Reform of Personal Taxation* Cmnd 9756 March 1986.

The position for these three types of family situation is summarised below, using figures for 1989-90:

	Value of total personal allowances
• Two unmarried people	£5,570
• Couple in which husband only works	£4,375
• Couple where at least wife works	£7,160

Clearly taxing people as separate individuals, irrespective of whether they were husbands or wives, meant ending the MMA. Husband and wife would then receive the same personal allowance, to claim against tax charged on their own income. However, abolishing the MMA without compensation would have resulted in severe hardship for very many families. In particular, married couples in which the wife did not work, and had no earned income, would lose a great deal. The 1985 Green Paper argued that allowing individuals to transfer their personal allowance to their partner, when they themselves had no use for it, could overcome these problems at a stroke.

C. Transferable Allowances

In the event, the Government received representations on the 1985 Green Paper from around 70 organisations and 400 individuals.[16] Though the principle of independence set out in the Green Paper received much support, the principle of transferability was criticised on four grounds: for being too expensive, for being administratively complex, for discouraging women from working, and for compromising women's rights to financial privacy.

An objection on the grounds of cost was based on the assumption that reform would only be politically feasible if few taxpayers lost out from the change. The Green Paper had noted "it is most unlikely that the Government would 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."[17] If one assumed that all individuals were paid the single person's allowance - worth £2,785 in 1989-90 - then two earner couples would see a cut of £1,590 from their combined allowances (ie, a rise of over £375 in tax, if they were basic rate taxpayers). To avoid this, the Government would have to set the new single person's allowance, payable to all individuals, married or single, considerably higher than before. The Institute for Fiscal Studies estimated that this would cost in excess of £4 billion.[18]

---

16 HL Deb 3.2.94 c.104WA.

17 *The Reform of Personal Taxation* Cmnd 9756; Foreword.

18 *Taxation of Husband & Wife* IFS Commentary March 1986; p.1.

A second objection was that a transferable system would be administratively complex. It would require tax offices to keep track of relatively small incomes, of either husband or wife, should one partner have insufficient income to use their whole allowance, and choose to transfer part of it to their spouse. If both partners continued to be taxed under the PAYE system, then changes in the tax code of one spouse would have to be related directly to changes in the code of their partner. This is because PAYE works on a cumulative basis. The tax deducted by an employer at the end of each month is the exact sum required for that month, taking account of all earnings received and tax paid in the tax year up to that date. If these tax code adjustments were left to the end of the tax year, then the Revenue would have to collect quite large lump sums from husbands, typically, whose wives had started to work during the past twelve months. Though this might be less complex, undoubtedly it would be unpopular.

Furthermore transferable allowances would create a strong disincentive for women to work. Under the old system, should a woman decide to go out to work, she would receive the WEIR, and the first £2,785 of her income would be tax-free. Her decision to work did not affect her husband's net income. With transferable allowances, this is not the case. As soon as a wife decides to work, taking part, or all, of her own tax allowance back from her husband, her husband's tax liability rises. In effect, every pound contributed to household income by a wife's wages is taxed at the marginal rate of tax.

The final criticism made was that transferable allowances compromised the right to privacy which represented the very rationale for reform. As each person's net income was directly dependent on what their partner was earning, then a spouse whose partner claimed but a part of their allowance could easily calculate their partner's exact income. In addition, should a wife or husband go out to work, the use of their transferable allowance would automatically cut their partner's net income, an income which their partner might very well regard as their own. The potential for family discord, it was suggested, was significant, and should be avoided.

One related argument, put forward by the Equal Opportunities Commission among others, was that transferable allowances did not target real need. The old system 'recognised' marriage, assuming it came with real financial penalties. This was no longer the case. The sheer fact of getting married did not, in itself, lead to a fall in a couple's joint income; consequently, marriage should not be subsidised through the tax system:[19]

> "Where marriage in contemporary society does have a bearing on the tax system lies in the likelihood of the subsequent effect that marriage has on the earnings capacity, and therefore taxable capacity, of women because of the career interruption caused by childbirth and the care of young children. This is where the major burden of dependency in contemporary society falls, which it is legitimate for the tax system to recognise. The most convenient, direct,

---

[19] *Taxation Without Discrimination* Equal Opportunities Commission September 1986; p.7.

> and least costly way of doing so is, as the Commission has consistently argued, to use the revenue saved by the abolition of the Married Man's Allowance to provide increased Child Benefits."

The use of child benefits, rather than tax reliefs, to help families is touched on in the final part of this Research Paper.

Though transferable allowances were not introduced at the time, they remain an attractive solution to some. Indeed, it was reported in the *Times* in July this year that the introduction of transferable allowances is being reviewed by the Prime Minister's Downing Street policy unit, apparently in the wake of "mounting concern among Conservative analysts that the current system is weighted too heavily toward two-earner couples."[20] A recent written answer estimated the cost of implementing them now would be £3 billion.[21] There remain advantages and disadvantages to such a system. It is best at promoting certain policy goals: giving fiscal encouragement to marriage, recognising a legal duty of one partner to provide for the other, and, promoting a family situation where one partner stays in the home. That said, the system is relatively poor at promoting financial privacy between couples, encouraging both partners to work, and minimising administration costs, all things at which the current system excels.

D. The 1988 Reform

Apparently the then Chancellor was taken aback by the strength of opposition to transferable allowances:[22]

> "Some women, whose support I had hoped for, argued that transferable allowances would destroy all the gains to privacy they and I both sought, since husbands and wives would still have to reveal their incomes to each other to decide which of them should have the allowance. This surprised me, since the wife for whom privacy was important could always purchase it cheaply enough by letting her husband keep the transferable allowance."

Determined to have a scheme up and running before the next election, Nigel Lawson developed what was, in his own words, a 'half-way house', which he announced in the 1988 Budget.[23] From the start of the 1990-91 tax year, a husband and wife would be taxed independently on income of all kinds.

---

20 "Tories plan tax incentives for wives staying at home" *Times* 11 July 1995.

21 HC Deb 18.5.95 c.307W.

22 *The View From No.11*; p.884-5.

23 HC Deb 15.3.88 cc.997-8.

All taxpayers, male or female, married or single, would be entitled to the same personal allowance, available against all income, whether from earnings, pensions or savings. This was to be set at the same level as the single person's allowance. A new married couple's allowance (MCA) would be introduced, replacing the MMA, equivalent to the gap between the new single allowance and the MMA, and going - in the first instance - to the husband, to ensure that his tax threshold would not fall. The WEIR was to be abolished. In addition married persons would be taxed independently on their capital gains. Each would have their own annual exempt amount equal to that of a single person, set at £5,000 in 1990-91. However transfers of capital between husband and wife would continue to be entirely free of any liability to tax. It should be noted that since 1988-89 capital gains have been charged tax at the same rates as income: ie, at the three income tax rates of 20%, 25% or 40%. Capital gains are treated as if they constituted a taxpayer's marginal, or "top", slice of income. Married couples were penalised by the old system, since they had use of the one annual exemption, though this anomaly was less publicised, since relatively few people pay capital gains tax compared with the numbers who pay income tax.

The introduction of independent taxation received cross-party support, though some criticism was made of the way in which the new MCA was to be paid. At the Committee Stage of the *Finance Bill 1988* Nicholas Brown set out the Labour Party's position:[24]

> "The Labour Party is strongly committed to moving towards truly independent taxation. We favour creating a taxation system that treats married women as equals, not as dependants of their husbands ... [However] the changes do not represent truly independent taxation [since] the intention of the proposals is that the married couple's allowance should go automatically to the husband. The wife will have no automatic right to any excess allowance. It will be for the husband to allocate ... The Opposition will try to amend the Bill to remove that indefensible anomaly."

In *The View from No.11*, Mr Lawson declared himself satisfied at the outcome, though his intentions for the MCA were not well-publicised at the time:[25]

> "Although inferior to independent taxation with fully transferable allowances, it was so superior to the old system, and went so far towards remedying all the existing grievances, that it would have been folly not to go ahead ... there would be genuine independent taxation, with everyone, man or woman, married or single, having the same standard allowance ... on top of that, however, all married couples would have an additional married couple's allowance (equivalent, initially, to the difference between the single allowance and the married man's allowance, but which ideally should be allowed to wither on the vine.)"

---

[24] HC Deb 9.5.88 c.86, c.87.

[25] *The View From No.11*; pp.885-6, 885.

III The Married Couple's Allowance

A. The Rate and Provision of the MCA

Following the introduction of independent taxation, which came into effect on 6 April 1990, the main personal reliefs for the tax year 1990-91 were the following:

Personal Allowance (PA)			£3,035
Age-Related PA	:	For those age 65-74[1]	£3,670
	:	For those age 75 and over	£3,820
Married Couple's Allowance (MCA)			£1,720
Age-Related MCA[2]	:	For those age 65-74	£2,145
	:	For those age 75 and over	£2,185
Income Limit[3]			£12,300
Additional Personal Allowance[4]			£1,720
Widow's Bereavement Allowance[5]			£1,720
Blind Person's Allowance[6]			£1,080

Notes : [1]Higher personal allowances are given to those between 65 and 74, and those aged over 75. [2]Higher allowances are paid to couples in which one partner is aged between 65 and 74, and 75 or over. Only the basic MCA is transferable between couples, not the higher rates. [3]Extra age-allowances are reduced above a certain income limit, by £1 for every £2 an individual's income exceeds the limit. The reduction continues until the allowance is equal in value to that of the ordinary personal allowance, and the basic married couple's allowance. [4]Given to single or divorced parents responsible for the upkeep of at least one child (the allowance is discussed in more detail below). [5]Available to widows, but not widowers, from the date of death to the end of the following tax year. [6]Given to any person registered as blind. Can be transferred to spouse if not used. Further details on personal allowances generally are given in *Personal Tax Allowances & Reliefs 1995-96* Research Paper 94/123 30 November 1994.

When first introduced, the MCA was paid in the first instance to the husband. If his income was too small to benefit from it, it could be transferred to the wife. However, this system meant that a husband's tax allowances were almost always greater than those of his wife. Moreover, it penalised couples where the wife was a higher rate taxpayer, and her husband paid tax at the basic rate (over those couples where this situation was reversed). In the March 1992 Budget it was announced that from 6 April 1993, couples could elect for the MCA to go to the wife, or have it split 50-50 between them. Legislation to this effect was included in the *Finance Act 1992*. That said, the higher rates of the age-related MCAs continue to be paid in the first instance to a husband. The extra amount above £1,720 may only be transferred to a wife if her husband has insufficient income to use it. Of course, some husbands may find that their income so far exceeds the income limit, above which age-related allowances are clawed back, £1 for each £2 of income earned in excess of the limit, that the additional value of the allowance has been reduced to zero.

It is the married man who must make a claim for the MCA. The legislation is quite specific in this respect. Section 257A of *ICTA 1988* states "if the claimant proves that for the whole or any part of the year of assessment he is a married man whose wife is living with him, he shall be entitled to [the MCA]." A wife cannot make a claim for the MCA unilaterally. Wives may make an election, independently of their husbands, to have the allowance divided between them, if their husband has already claimed it. Couples must make a joint election to have the full allowance transferred. The phrase "living together" is used here in the legal sense of living as man and wife. A married couple are taken as living together unless they have signed a separation agreement, are separated by order of the Court, or are living in such circumstances that their separation is likely to be permanent. The allowance is scaled down where marriage takes place during the tax year, reduced by one-twelfth for every complete income tax month before the marriage.[26] The allowance is not reduced proportionately if, during the tax year, a couple cease to live together, or the marriage ends, by divorce, annulment or death.

B. Restricting the Allowance

Though the provision of the MCA is now fairer, its value has fallen in real terms. The basic MCA has remained unchanged at £1,720 since the year of its introduction. The age-related MCAs have been increased on the levels first set for 1990-91, though this has been to compensate for another reduction in the value of the allowance. In the March 1993 Budget it was announced that relief for the MCA would be restricted to 20 per cent from 6 April 1994, so that its money value should be the same for all taxpayers, whatever their marginal rate of tax. Personal allowances are worth more to higher rate taxpayers, since they represent a fixed sum of money exempted from tax at an individual's marginal tax rate. For those who pay tax at the marginal rate of 40 per cent, the MCA was then worth £688; while it was worth only £344 for those whose marginal rate is 20 per cent. In his Budget speech, the then Chancellor, Norman Lamont argued that this result was the opposite of what this allowance was meant to do:[27] "There is no good reason why an allowance intended to recognise the responsibilities of marriage should give least to those on low incomes and most to those right at the top of the income scale."

From 1994-95 those claiming the MCA have had their tax bill calculated as if the MCA did not exist, and then had their final bill cut by £344 (ie, the value of the MCA to bottom rate taxpayers). In effect, the allowance was been changed into a tax credit. These changes have meant that the Revenue has had to introduce a new item on tax codes, which has confused some taxpayers. This item is the allowance restriction - or "ALLCE RESTRICTION" as it appears on the notice of code. When working out someone's tax code, the Revenue adds all the allowances together, then subtracts any reductions it needs to make, before producing a final figure, which is the amount of money someone may receive tax-free. This deduction

---

[26] An income tax month begins on the sixth day of one calendar month and ends of the fifth day of the next.

[27] HC Deb 16.3.93 c.182.

has to be larger in the case of a higher rate taxpayer, compared to someone paying tax at 20%. It should be noted that the figure given on anyone's tax code as the "allce restriction" is an aid to the Revenue working out one's tax bill; it is not the final amount that one's tax bill will go up by, as some have feared.

In the November 1993 Budget the Chancellor Kenneth Clarke confirmed this change would go ahead, and stated that the MCA would be further restricted to 15 per cent for 1995-96: "Now that husbands and wives are taxed independently - one of the best taxation reforms in recent years - the married couple's allowance is a bit of an anomaly. As announced in March, from next April it will be limited to 20 per cent. Given the need to raise extra revenue, I propose to reduce the rate of relief further, to 15 per cent from April 1995."[28] The two age-related MCAs have both been increased in two stages: by £200 for 1994-95, and by an additional £330 for 1995-96. This has been done to ensure that pensioners only suffer the same cash loss from the allowance restriction as non-pensioners.

The levels for the personal allowance, married couple's allowance, additional personal allowance, and the income limit, are summarised below for the period 1991-92 to 1995-96:

	1991-92	**1992-93**	**1993-94**	**1994-95**	**1995-96**
PA (Basic)	£3,295	£3,445	£3,445	£3,445	£3,525
PA (65-74)	£4,020	£4,200	£4,200	£4,200	£4,630
PA (75 & +)	£4,180	£4,370	£4,370	£4,370	£4,800
MCA	£1,720	£1,720	£1,720	£1,720*	£1,720*
MCA (65-74)	£2,355	£2,465	£2,465	£2,665*	£2,995*
MCA (75 & +)	£2,355	£2,505	£2,505	£2,705*	£3,035*
APA	£1,720	£1,720	£1,720	£1,720*	£1,720*
Income limit	£13,500	£14,200	£14,200	£14,200	£14,600

* Relief to be restricted to 20 per cent in 1994-95 and 15 per cent in 1995-96.

Though this reform may have come as a shock to couples, Mr Clarke's decision was not unexpected by tax practitioners. In a *Sunday Times* article published just before the November 1993 Budget, all five of the accountancy firms interviewed predicted further

28 HC Deb 30.11.93 c.933.

restrictions in personal allowances.[29] In an article in *Taxation*, the author suggested that these measures presaged the complete abolition of the MCA:[30]

> "The purpose behind *Finance Act 1994* provisions on restrictions on allowances is clear. Despite protestations to the contrary by Government ministers, these allowances are on the path to extinction. Some of them certainly appear like dinosaurs in the modern age. For example, the MCA has never sat comfortably in the world of independent taxation."

The changes in the MCA were debated in Standing Committee on 22 February that year, and agreed without amendment. There was general support for the principle that the MCA should be worth the same amount to all taxpayers. Diana Maddock, for one, argued that the MCA should be abolished completely, since it "is a relic of the days when a husband was taxed on his wife's income as well as on his own. It contravenes the principle that marriage should be tax neutral. The allowance does not target need." The then Chief Secretary to the Treasury, Michael Portillo, concurred with this argument, though would not comment on the future of the allowance:[31]

> "[Mrs Maddock] is right, at least concerning the breadth of that allowance, because it is given to people whether or not they are in work or have children. However, it has a value for some people and it recognises the responsibilities of marriage. I do not want to make any commitment for the future or to give any impression that the Government are determined to continue the process of reducing the allowance. That is a decision to be taken from time to time according to the prevailing circumstances."

One aspect of the restrictions made in the MCA, as they affect pensioners, has received relatively little attention. Taxpayers qualifying for the age-related MCA, along with the personal age-related allowance, have these allowances reduced by £1 for every £2 their income exceeds the income limit (this is set at £14,600 for 1995-96). Under section 257A(5)(b) of the *Income and Corporation Taxes Act (ICTA) 1988*, the age-related personal allowance is reduced before the age-related MCA, when any individual's tax bill is calculated. This order penalises pensioners on incomes above the limit of £14,600, since the personal allowance provides tax relief at the individual's marginal rate - ie, the basic rate of 25% - and the MCA provides relief at just 15%.

The numbers of married couples with one or both partners benefiting from the MCA for 1994-95 was 10.5 million. This compares with 750,000 individuals who benefit from the additional

---

29 "First the bad news ... there is no good news" *Sunday Times* 28 November 1993.

30 "Curbing the allowance" *Taxation* 4 August 1994.

31 Standing Committee A 22.2.94 c.344, c.348.

personal allowance.[32] This allowance is commonly known as the single parent's allowance, as it goes to unmarried or divorced parents taking care of at least one child. The additional personal allowance is pegged to the value of the basic MCA, and has been restricted in exactly the same way - to 20 per cent in 1994-95, and 15 per cent in 1995-96 - though this change has attracted less comment in the press. The allowance is examined in more detail below.

C. Families and the MCA

At the time of the November 1993 Budget, some commentators argued that the reductions made in the MCA went some way to undermining marriage. One writer in the *Sunday Telegraph* put it bluntly: "Mr Clarke has produced what, in traditional terms, could be regarded as the most anti-family Budget in living memory ... the fascinating thing is the total lack of reaction from any political quarter."[33] Malcolm Wicks, writing in the *Guardian*, also argued that Mr Clarke's proposals were anti-family, though his position was on the other side of the political divide. He suggested that the cuts in the MCA were a "neglected feature" of the Budget, and the allowance, "though an imperfect instrument" for helping families, should be maintained. "If [the MCA] goes, there will be no part of our taxation system that recognises the costs of children."[34]

More recently, comments made by the Archbishop of York, Dr John Habgood in February this year, about the need to make marriage "fiscally more attractive" were widely reported:[35]

> "There has been such emphasis in legislation in recent years on the equality of partners and not disadvantaging the illegitimate, and on the whole treating cohabiting couples as if they were married. Those who are looking at the possibilities of different lifestyles see no particular advantage for themselves in actually getting married, and society seems to be saying through the tax system that it doesn't matter."

A detailed critique of the restrictions made to the MCA is provided in a recent paper by Patricia Morgan published by the Institute of Economic Affairs.[36] In an article summarising her case,[37] Ms Morgan argues that fiscal and social policy over the past decade or more has

---

32 HC Deb 9.3.95 c.265W.

33 "Why the Tories don't value the family" *Sunday Telegraph* 5 December 1993.

34 "The part of the family? You're joking" *Guardian* 10 December 1993.

35 "Archbishop calls on taxman to boost marriage" *Times* 14 February 1995.

36 *Farewell to the Family? Public Policy & Family Breakdown in Britain and the USA* Institute of Economic Affairs January 1995.

37 "The family under threat" *Sunday Times* 13 November 1994.

encouraged the growth in numbers of lone parent families, in part, by increasing the tax burden on married parents. She highlights the recent restrictions made in the MCA, which "undermine the middle-income family provider, let alone the marginal worker to whom a little extra tax relief may be crucial."

She goes on to assert that "the Government regards any fiscal recognition for marital responsibilities as an 'anomaly'. Couples are no longer deemed financially dependent on each other, despite the fact that husbands still contribute the lion's share where there are children." Ms Morgan does not argue that the tax system penalises married parents over single parents per se, rather that the provision of benefits to single parents acts as a disincentive for marriage.

In *Farewell to the Family?* Ms Morgan suggests "the marriage allowance - the last recognition of marriage left in taxation - is regarded as a 'pot of gold' from which other areas of public expenditure could be funded", the implication being that reductions in this tax relief have gone to fund increases in social security benefits to lone parents. Furthermore, "it is particularly important that the tax changes of the mid-1990s will have the biggest impact in the crucial middle-income group", crucial in terms of their ability to shape popular opinion, in terms of the widespread acceptance of single parenthood:[38]

> "Here it might have been possible for one main earner to sustain a family, given that the allowance provided relief for the imposition of the higher rate tax on solo incomes. That relief is now vanishing. A bit of extra tax relief also provided some hope for men on the margins who felt that, given some effort, there was a chance that marriage and the rewards of work were not quite out of their reach ... The state is making it abundantly clear that it is not prepared to support a man's efforts to provide for a family and does not recognise his costs when his wife cares for his children. Rather it is more willing to use the public assistance system to build up the wages of the lone mother [that is, through benefit payments]."

Clearly, it is arguable that the state does recognise the costs of child rearing, in the provision of child benefit, and that it should not use the tax system in this manner. It is undeniable that, should the Government choose to restore the value of the MCA, this would go some way to help married parents, though it might appear an inefficient way of doing so, rewarding richer parents more than poorer ones, and giving tax relief to couples, irrespective of whether they have children or not. Whether the MCA plays a symbolic role or not, shaping public attitudes to marriage, is unverifiable perhaps.

Even if this were the case, the tax relief given to single parents, the additional personal allowance, has been restricted in value in exactly the same way as the MCA (this is discussed below). Other changes made in the tax system over the last few years have, if anything,

---

[38] *Farewell to the Family?* IEA January 1995; p.82, 106-7.

removed those tax advantages which had existed for couples who remained unmarried. In the case of the additional personal allowance, single partners with two or more children used to be able to both claim this allowance. Since 1989-90 unmarried couples have been entitled to just one allowance. Three other measures have made the situation between married and unmarried couples more equitable:

Mortgages : Since 1 August 1988, the £30,000 limit on mortgage interest relief has been related to the house or flat, irrespective of the number of borrowers. Before this change, unmarried couples could both claim tax relief on interest on a mortgage up to £30,000, whereas a married couple could only claim relief on one loan.

Covenants : Deeds of covenant were abolished from 15 March 1988 (excepting those made out to charities). The child of an unmarried father could reclaim tax on covenanted payments made by his or her father. Married couples had not been able to use covenants in this way.

Maintenance : No tax relief has been available to those making maintenance payments under a court order since 15 March 1988. Before this, unmarried fathers could receive tax relief on such payments even if they were living with the children, whereas married fathers could not.

In this sense, Ms Morgan has chosen the evidence for a bias in the income tax system against marriage rather selectively. Looking beyond income tax, it should be pointed out that transfers between married couples do not attract capital gains tax or inheritance tax, whereas transfers between unmarried couples are taxed in the normal way.

IV The Additional Personal Allowance

A. The Allowance for Single Parents

Under section 259 of *ICTA 1988* an additional personal allowance is available in respect of individuals caring for children. The child may be the claimant's natural or adopted child, or simply a child maintained at the claimant's expense (eg, fostered) and has to be under 18 unless in full-time education or in an apprenticeship of at least two years' duration. Those eligible for this relief are:

- a woman who is not, throughout the tax year in question, married and living with her husband.

- a man who is not, for all or part of the tax year in question, married and living with his wife.[39]

- a man who is, for all or part of the tax year in question, living with his wife, if she is totally incapacitated by physical or mental infirmity throughout the tax year (of course, in this case, the allowance would be given in addition to the married couple's allowance).

Single or divorced women, as well as widows, widowers, and single men, may claim this allowance, provided they are taking care of at least one child (only one allowance is paid, irrespective of the number of children cared for by the claimant). If both parents, living apart, claim the allowance in respect of the same child, then they may elect to have it split between them. If they cannot agree, the allowance is split in proportion to the amount of time each spends with the child.[40]

In a recent press article, one tax practitioner commented that relatively few parents were aware of the allowance, and argued it should be given wider publicity.[41] Allowances unclaimed or not deducted from assessments may be claimed within six years of the end of the tax year for which the claim is made.[42] As a consequence, separated parents who have been caring for a child for some time may be in the situation where they may claim the additional personal allowance for the previous six years, and receive back a significant sum of money paid in tax, if, of course, they met the necessary conditions throughout that period. Unmarried couples who live together as man and wife remain eligible for the allowance, but in such cases, relief to the couple is restricted to one allowance.

---

[39] Provided he is not entitled to the transitional tax relief given to couples who separated before 6 April 1990.

[40] Under section 260 of *ICTA 1988*.

[41] "Easing the pain of child support after separation" *Guardian* 8 January 1994.

[42] Under section 43 of the *Taxes Management Act 1970*.

B. The Allowance and Incapacitated Spouses

Married men caring for children who also care for their incapacitated wife may claim the allowance, but married women caring for an incapacitated husband may not. About 10,000 married men were entitled to this allowance for 1994-95.[43] During the Committee Stage of the *Finance Bill 1991*, Chris Smith proposed a new clause to remove this anomaly, by extending the provision of the additional personal allowance to women in this situation.[44] In response, the then Minister of State at the Treasury, Gillian Shephard, explained why this anomaly existed:[45]

> "The difference in tax treatment has long been a feature of the tax system; in its present form, it dates from 1960. No doubt, it reflects a view from those days that it was usual for a wife to look after a home and bring up children. Therefore, when a mother was incapacitated, a case was seen for additional help; that did not seem appropriate when the husband was incapacitated."

The Minister promised to look at the issue, and Mr Smith withdrew the clause.

Indeed, the history of this anomaly is a good illustration of how the structure of the current tax system is rooted in the past. The provision of some form of tax relief for widowed parents was first announced by Derick Heathcoat Amory, the then Chancellor, in his 1960 Budget speech.[46] He noted that the existing housekeeper allowance went only to widows and widowers employing a resident housekeeper to care for their children. In addition to increasing the level of this allowance, from £60 to £75, he proposed to introduce a new allowance of £40, to go to a widow or widower with care of a child who had no resident housekeeper.

It was the Chancellor's intention that the new allowance should also be given to any single parents who would have qualified for a housekeeper allowance under the existing rules for its provision, if they had decided to employ a housekeeper; so, the new allowance was extended to cover those married men caring for incapacitated wives, who also cared for their children. However, housekeeper allowance was not given to wives caring for incapacitated husbands, who employed a housekeeper to take care of their children, and this anomaly was carried over into the provision of the new allowance.

---

43 HC Deb 14.6.95 c.516W.

44 Standing Committee B 20.6.91 c.477-80.

45 Standing Committee B 20.6.91 c.479.

46 HC Deb 4.4.60 cc.61-2.

When this provision was debated in Committee, Dame Irene Ward was among those who argued that this was discriminatory and unfair:[47]

> "I want to know whether a married woman who has a totally incapacitated husband whom she has to look after as well as her children will be able to get the benefit of this concession, or has the tax structure got so involved that there is no possible way of including her?"

Sir Edward Boyle, the then Financial Secretary to the Treasury, argued that extending the new allowance to wives would change the basis on which the allowance was given:[48]

> "To give an allowance where a man is incapacitated would be to give an allowance not for the care of the children, but in respect of the husband's disability. This is a point which we have often discussed in Committee - whether or not there should be a disability allowance. Ministers on both sides ... whenever this point has been raised, have always felt obliged to resist that suggestion."

Clearly the underlying assumption was that married mothers would not enter the workforce, even if their husbands were incapacitated, and would not, in any case, require financial aid to care for their own children. Douglas Houghton pointed out this deficiency in Sir Edward's argument, which gives some indication of the Government's thinking on this matter:[49]

> "The Financial Secretary says that if we gave relief for a totally incapacitated husband whose wife is able to look after the children, it could not be for the purpose of employing a housekeeper, because in fact she was physically able to take care of the children. But that overlooks the possibility that she may have to become the breadwinner, and therefore a housekeeper is necessary to look after the children while she goes out to earn the money for the support of the family."

The housekeeper's allowance itself, which had been set at £75 in 1960, was only increased to £100 in 1973. It was allowed to diminish substantially in real terms over the next fifteen years, and was finally abolished in 1988, when it was still set at £100.[50] When this was discussed in Committee, the then Chief Secretary to the Treasury, John Major, suggested that the allowance was an anachronism, going on to argue that "it has been accepted on both sides of the House in recent years that the best way of helping to support elderly or infirm people

---

47 HC Deb 19.5.60 c.1555.

48 HC Deb 19.5.60 cc.1558-9.

49 HC Deb 19.5.60 c.1560.

50 Under section 25(3) of the *Finance Act 1988*.

is not through the tax system but through the social security system."[51] The rules for the provision of the additional personal allowance have stayed unchanged since 1960, though its value has been substantially increased. At present, it is pegged to the value of the basic married couple's allowance (MCA), though, as mentioned above, it has been restricted to 20 per cent for 1994-95, and to 15 per cent for 1995-96.

The way the additional personal allowance discriminated against women was discussed during the Committee stage of the *Finance Act 1992*, when Paul Boateng proposed a similar clause to Chris Smith's the year before.[52] The then Financial Secretary, Stephen Dorrell, opposed the clause, arguing that although the provision was an anomaly, extending this type of tax relief was an inefficient way of helping those wives caring for incapacitated husbands:[53]

> "It is not right to seek to mould the tax system to help small groups of people in the way that the additional personal allowance does for men and the amendment would do for women ... We believe that the way to help the disabled is not through the tax system, but by targeted social security benefits ... There are choices, none of which is attractive. The option of withdrawing the existing additional allowance does not seem attractive, nor does the option of extending it to women. Given the options available, the least bad road forward is to stay as we are."

As a result of the Government's opposition, the clause was negatived.

According to a written answer in January 1995, the information required to estimate the cost of extending the provision of the allowance to women is not available.[54] The Government's position was reiterated in June 1995, though the future of the allowance itself was left open:[55]

> **Mrs. Maddock:** To ask the Chancellor of the Exchequer what plans he has to review the operation of the additional personal allowance for married men with an incapacitated wife.
>
> **Sir George Young:** All personal allowances will be kept under review in the run-up to the Budget. In general, the Government believe that it is better to help both men and women with incapacitated spouses through the social security systems rather than through tax reliefs.

---

51 Standing Committee A 24.5.88 c.228.

52 Standing Committee B 1.7.92 cc.511-9.

53 Standing Committee B 1.7.92 cc.516-7.

54 HC Deb 26.1.95 c.304W.

55 HC Deb 13.6.95 c.433W.

V Divorce & Maintenance

Generally, all maintenance payments made under a court order, a Child Support Agency (CSA) assessment, or other type of legally binding agreement, are transacted **outside** the tax system. However separated or divorced individuals who pay maintenance direct to their ex-spouse do qualify for a limited form of tax relief, sometimes called a "maintenance allowance." This relief is not extended to those making maintenance payments to an ex-partner, rather than to an ex-spouse, and it does not cover maintenance paid to children. Individuals may claim relief for payments made to more than one ex-spouse, but however many people they make paymnets to, the total amount of relief given in any one tax year is the same. Tax relief is withdrawn if the ex-spouse who receives maintenance remarries.

The tax treatment of maintenance was substantially changed by provisions in the *Finance Act 1988*, with the aim that all maintenance payments might be transacted outside the tax system. Previously, those providing maintenance could apply for tax relief at their marginal rate of tax on these payments. The person receiving maintenance - ex-spouse or child - would then be taxed on this income. This reform was announced by the then Chancellor, Nigel Lawson, in his 1988 Budget speech:[56]

> "Most of the financial transfers that take place within families are rightly and properly outside the scope of the tax system altogether. I propose, as far as is practicable, to take covenants and maintenance out as well ... [With maintenance] we tax the recipient, only to give tax relief to the payer. The present rules can be complex and confusing for people going through separation and divorce. The tax system ought to intrude as little as possible, though it is reasonable that there should be some recognition of the fact that an ex-husband is continuing to support his ex-wife, or indeed vice-versa."

Legislation to this effect was introduced that year.[57] Those making payments under agreements made after 15 March 1988 (the "new system"), no longer claim these against tax, while those who receive maintenance are not taxed on this income.

Transitional arrangements were made to cover ex-couples who continued to give, and receive, maintenance under agreements made **before** 15 March 1988 (the "old system"). Those making payments may continue to claim these against tax, but they may only claim a sum equal to the maintenance they paid in 1988-89. For example, if an individual paid maintenance of £8,000 in 1988-89 on which they received tax relief, he or she continued to receive tax relief on £8,000 the following year, even if the actual maintenance payments they made had increased.

---

[56] HC Deb 15.3.88 cc.1001-2.

[57] Sections 37-40 of the *Finance Act 1988*, which amended sections 347A-B of *ICTA 1988* accordingly.

The value of this relief has been restricted in value, under section 79 of the *Finance Act 1994*. In effect, tax relief on the first £1,720 of maintenance paid has been restricted to 20 per cent for 1994-95, and to 15 per cent for 1995-96. Tax relief on maintenance paid in excess of £1,720 - up to the 1988-89 limit - continues to be given at the individual's marginal rate of tax. One writer, in *Taxation*, argued that it was quite unfair to link the two types of relief, as they served different purposes:[58] "This penny-pinching change is apparently in the interests of conformity with the restrictions of allowances for 1994-95 and after." Those who **receive** maintenance under the old system receive it gross. Though generally it is taxable, those receiving it will be able to use their personal allowance, and any other allowances for which they are eligible, to set against tax. The one exception to this is where payments are being made direct to an ex-spouse. In this case the first £1,720 of maintenance may be received tax-free. This allowance is unchanged by the provisions in the *Finance Act 1994*.

Those making payments under the "new system" may qualify for a limited form of tax relief - a "maintenance allowance" - for payments they make **direct** to their ex-spouse. This relief is equivalent to the MCA, and has been restricted in the same way, possibly as a prelude to its gradual abolition. During the debate in Committee on the restriction of the MCA, the then Chief Secretary to the Treasury, Michael Portillo, mentioned the restriction of tax relief on maintenance payments (though the clause itself was not debated separately):[59]

> "Parents who are not married, separated or divorced should be treated in exactly the same way as others. The amount of tax reduction for those making maintenance payments should be the same as the amount of tax reduction that comes into place for the married couple's allowance."

This restriction was not cause for much press comment; an article in the *Independent* cited practitioners who argued this might reduce the incentive to keep up maintenance payments, and others who suggested the allowance was an anomaly anyway, and should be done away with.[60]

Only "qualifying maintenance payments" attract this allowance; in short, payments must satisfy the following criteria:[61]

- They are made under a UK or EC-country court order, CSA assessment, or other legally binding agreement (voluntary payments, or capital payments are excluded).

---

58 "Jostling with a juggernaut" *Taxation* 20 January 1994.

59 Standing Committee A 22.2.94 c.344; c.348.

60 "Clarke deals new blow to maintenance tax relief" *Independent* 4 December 1993.

61 Under section 347B(1) of *ICTA 1988*, as amended.

• They are made direct to a divorced or separated husband or wife, who has not remarried. Payments may be made through the CSA, or direct to the person concerned. If the ex-spouse remarries, tax relief stops from the date of marriage. The provision of this relief is not affected if the person paying maintenance remarries, unless they remarry their ex-spouse.

• They are made for the maintenance of the ex-spouse themselves, or for the maintenance of a child under 21, who is part of the family.

However, this tax relief does not cover those situations where a parent is legally obliged to pay maintenance for the care of their child, if they have never been married to the other parent. This applies either if the parent is required to pay maintenance under a court order, or they are obliged to pay maintenance under a CSA assessment. It is important to note that in such cases, the court order, or CSA assessment, deals with payments made to a child, not to the child's parent. Relief does not cover those cases where a child has applied for a CSA assessment unilaterally (a situation that only pertains to Scotland).[62]

As mentioned, until 1988 tax relief was available on maintenance paid under a court order either to an ex-spouse, or to a child. In his 1988 Budget speech, Nigel Lawson referred to the fact that the operation of this relief discriminated against parents who were married:[63]

> "The reform of the tax treatment of marriage that I am proposing today will also remove one of the lesser known tax penalties on marriage. At present, an unmarried couple can make large payments either between themselves or to their young children, and get tax relief that would not have been available had they been married. My proposed reform will put an end to that."

In addition, the Government's decision to reform the system, and provide a limited relief just for payments to an ex-spouse, was possibly influenced by a legal case in 1987.[64] A divorced father applied to obtain a court order against himself to pay his own children maintenance (to finance their school fees). In doing so, he intended to claim the maintenance he paid against tax, while having his children use their own personal allowances to set against the income tax they were liable to pay.[65] The Court of Appeal refused to make such a court order on the basis that its sole purpose was tax avoidance. However, this decision was overturned by the House of Lords.

---

62 Under section 7 of the *Child Support Act 1991*.

63 HC Deb 15.3.88 c.1002.

64 *Sherdley v Sherdley* [1987] BTC 273.

65 Generally, a child's income is assessable on him/her, with full entitlement to personal allowances and reliefs.

Lord Brandon, delivering the leading speech in the Lords, argued that if the Court of Appeal's decision was right, "the law practises a strange form of fiscal discrimination in the way it treats two different but comparable situations arising out of the breakdown of a marriage of which there are children for whose maintenance and education the father has to provide." He discussed the situation of a divorced couple, living apart, with children: in the first case, the mother applied for a court order against the father to have maintenance paid direct to the children, who lived with her; in the second, the father applied for an order against himself, as the children lived with him:[66]

> "The sole reason why the court will make the order [in the first case] in that form is to enable the two tax advantages ... [which] is greatly for the benefit of the children in that they increase the amount of income available for their maintenance and education. If on the other hand, the children live with the father then, if the decision of the Court of Appeal is right, the same order may not be made, with the result that the children are denied a similar benefit."

The introduction of the new system, removing maintenance from the tax system, overcame this problem. At the time, it was commonly argued that significant tax relief should not be given to those maintaining children or ex-spouses, if similar relief was not available to those who were married, and had stayed married, who had the same family responsibilities. The provision of the "maintenance allowance" represented a limited concession, recognition of the fact that divorced or separated parents paying maintenance often supported two homes.

Even so, court orders are now often couched in such terms that maintenance payments are made to the children, at the cost of losing this tax relief. This is to ensure that payments continue to be made until the child reaches a certain age, regardless of either parent's marital state. This practice gives some indication that the value of the maintenance allowance is relatively small. Following the establishment of the CSA under the *Child Support Act 1991*, amending legislation was introduced so that maintenance assessed by the CSA qualified for tax relief in the same way as maintenance paid under a court order.[67] As a result, payments that pass between unmarried parents for the maintenance of their child, whether under a court order or a CSA assessment, do not qualify for any tax relief.

---

66 Cited in: *Taxation on Divorce and Separation* J.Gray 1987; p.54.

67 Section 62 of the *Finance Act (No.2) 1992*; contained in section 347B(8)-(12) of *ICTA 1988*, as amended.

VI Tax & Children

A. Tax Relief for Workplace Nurseries

One issue related to the way in which marriage is taxed is the provision of tax relief to alleviate the costs of childcare. Though this issue has been debated a good deal in the past few years, there exists just one type of tax relief: parents are not taxed when their employers provide a workplace nursery as a fringe benefit. Before the introduction of this tax relief, the provision of a workplace nursery would have been taxed as a benefit in kind.

For tax purposes, fringe benefits can be divided into two groups: those in cash (or which can be converted into cash quite easily), and those that cannot be converted into cash ("benefits in kind"). Since 1948 the general rule has been that most cash payments and benefits rank as taxable renumeration. Benefits in kind are taxed in the hands of all directors and any individual earning £8,500 or more.[68] A distinction has always been made between directors and employees, because of the power many directors have to determine their own level of pay and benefits. The £8,500 threshold was introduced in 1979; not so as to be more generous to the lower paid in terms of their perks, but to determine a threshold that would make tax collection administratively feasible. An individual is taxed on their benefits in kind at the same rate as the rest of their income (ie, 25% or 40% depending on their circumstances). Certain benefits are not taxed; for example, in 1988 the then Chancellor, Nigel Lawson, ruled out taxing the provision of free parking because it would be an "administrative nightmare".[69]

Since 1985 the Inland Revenue has been more rigorous in applying the law on the taxation of fringe benefits, to enforce the general principle that individuals should be able to deduct such benefits from their taxable income only if they represent expenses incurred **wholly, necessarily and exclusively** in performing the duties of their employment. Consequently the provision of workplace nurseries was treated as a benefit in kind, and the cash equivalent of the service taxed as part of an individual's income. If an employee's earnings - nursery provision included - exceeded £8,500, the employee had to pay tax at their marginal rate on the whole of that benefit. This remains true for cases where an employer pays an employee's fees for childcare.

The introduction of tax relief on the benefits enjoyed from a workplace nursery was announced by John Major, when Chancellor, in his Budget speech in March 1990:[70]

> "I have a small supply side measure to announce that will help the labour market to work better. We have always made it clear that it is not for the Government to encourage or discourage women with children to go out to

---

68 The general provision to tax benefits in kind is set out in section 154 of *ICTA 1988*.

69 HC Deb 15.3.88 c.1009.

70 HC Deb 20.3.90 cc.1020-1.

> work. That is rightly a decision for them to take, and one in which the Government would be wise not to interfere. However, it is undeniable that an increasing number of mothers do want to return to work, and many employers, in private industry and in public services such as health and education, are keen to encourage them to do so ... I have decided to exempt the value of workplace nurseries and playgroups from taxation as a benefit in kind."

This measure was implemented under section 21 of the *Finance Act 1990*.[71] Tax relief is given for the provision of a workplace nursery or playscheme only, and not for childcare that is mainly educational in content. Care facilities must meet local authority registration standards. The employer must be "wholly or partly responsible for financing or managing the provision of the care." This means that childcare provision can be subcontracted by an employer without losing its tax-exempt status, and a workplace nursery may be located anywhere to suit those who use it. The one exception to this rule is that care does not qualify for relief if it is given in a private house. All other types of childcare provision are taxed in the hands of the employee.

Turning from employees to employers, those who provide workplace nurseries can claim tax relief for the day-to-day costs of providing or subsidising childcare (these costs are deductible when working out corporate profits for tax purposes). These costs include, giving an employee a cash allowance for childcare; paying the fees - on behalf of an employee - for a nursery, child minder or nanny; and, the running costs of a workplace nursery or playscheme for employees' children. In addition, the cost of equipment for a nursery or play scheme may qualify for capital allowances. Similar rules apply to the self-employed. They may claim tax relief on the provision of childcare for an employee, such as a secretary, though they may not deduct expenses incurred for "private or domestic purposes."

There are two reasons for believing that tax relief to employees for workplace nurseries has had a rather limited impact. First, the cost of the relief has not grown significantly. A written answer in January 1993 stated the revenue cost of this relief had been £10 million for the three tax years 1990-91, 1991-92 and 1992-93.[72] This remains the Inland Revenue's own best estimate for the annual cost of this relief.[73] Second, on the limited information that exists, there does not appear to have been a significant increase in the number of nursery places offered by employers. Precise estimates for the current numbers of workplace nurseries are not produced by the Department of Employment; statistics cited relate to 1990-91 only. In an answer given in March 1994, it was estimated that about 20,000 employees had a full-time or part-time place for their children in a workplace nursery in 1991.[74]

---

71 Incorporated in section 155A of *ICTA 1988*.

72 HC Deb 20.1.93 c.257W.

73 Source : Inland Revenue July 1995.

74 HC Deb 30.3.94 c.881W.

In March 1995, in response to the same question, the Government stated that an estimated 5% of employees were offered this provision by their employer in 1990.[75] In January 1992 a survey by the Working for Childcare pressure group found that there were 425 workplace nurseries in the UK, offering 12,000 places for children under five - ie, one place for every 300 children.[76] The CBI cited this survey in giving evidence to the Employment Select Committee in April 1994, to support their contention that there had been little development in workplace nurseries over the past five years.[77]

The restriction of tax relief to workplace nursery provision has been criticised by some as being unfair and unduly restrictive.[78] Employees may find it hard to transport their children to their own workplace where a nursery has been set up; for example, if the parent commutes into London. Small businesses with widely dispersed workforces may consider it impractical to set up a nursery, and much prefer to subsidise childcare costs by supporting playschemes in a private house, or by paying employees with vouchers for childcare, though neither practice attracts tax relief for the parent.

These other types of employer benefit do not prevent parents choosing a local nursery - rather than one located at their place of work. Local nurseries may be attractive for those who wish to have their children grow up in the local community, and for the fact that their use is not dependent on working for the same employer. A number of witnesses to the Employment Select Committee raised all of these criticisms.[79]

The Employment Select Committee itself recommended, in its report *Mothers In Employment* published in May 1995, that tax relief should be extended to all forms of employer-provided childcare:[80]

> "The Treasury estimated the costs of extending tax relief on workplace nurseries to all forms of employer-provided childcare at about £5 million. However, this figure does not take into account the likelihood that employers will take advantage of this tax incentive to offer childcare support to employees currently making their own arrangements or to employers moving their provision of childcare to the most tax-efficient option, which could increase the cost significantly; although neither does it take into account the

---

75 HC Deb 7.3.95 c.139W.

76 "Nurseries appeal" *Times* 30 January 1992.

77 *Mothers In Employment* HC 227 1994/95 First Report of the Employment Select Committee 14 February 1995; p.xxiv.

78 "Complicated courtship rituals for a mythical creature" *Financial Times* 28 February 1992.

79 *Mothers In Employment* HC 227 Employment Select Committee 14 February 1995; p.xxv.

80 *op.cit*; pp.xxv-xxvi.

> increased return to the Treasury resulting from an increase in the number of mothers at work and paying tax ...
>
> The major advantage of allowing tax relief on employer provision is that the benefit is more likely to be targeted at those employees who otherwise would not be able to afford childcare costs without employer assistance. Employees who choose to pay for their own childcare by employing a nanny, a mother's help, or an au pair would be free to continue to make that choice. At worst their position would remain unchanged; at best they would be offered an additional option of employer-provided assistance ...
>
> Extending the tax relief currently available to employers on workplace nurseries, to other forms of employer-assisted childcare would help a number of women immediately. In increasing the amount of overall provision that exists, it may help others as well. **The Committee recommends that the tax relief currently available to employers on workplace nurseries be extended to cover all forms of employer-assisted childcare in order to provide the necessary flexibility to suit a greater variety of circumstances.**"

In response to the Committee's recommendations, the Government firmly refused to extend tax relief at all, though the cost cited by the Government - £300 million - referred to the cost of allowing all employees to write off against tax any costs of childcare purchased, something the Committee itself had ruled out as being both inefficient and expensive:[81]

> "Wider tax reliefs for employees for the benefit of employer-provided childcare would be: potentially expensive (up to £300 million); difficult to defend as fair to those who pay for their own childcare out of taxed income; give most help to those who can afford childcare, and do so now, and no help to those who do not pay tax. The 1990 exemption for workplace nurseries was never intended as a step towards more general relief for childcare costs."

Though nursery education is a separate issue to childcare, it should be pointed out that in July this year, the Secretary of State for Education and Employment, Gillian Shephard, announced the Government's proposals for a voucher scheme for pre-school education. Under the scheme, parents of all four year old children would receive a voucher worth around £1,100 exchangeable for pre-school education. The value of the voucher would not be taxable. It is intended to lauch a pilot scheme by April 1996.[82]

B. Recent Legislative Initiatives for Tax Relief

---

81 *Mothers In Employment : Government Reply to the First Report of the Committee in Session* HC 457 1994-95 Second Special Report of the Employment Select Committee 23 May 1995; p.vii.

82 HC Deb 6.7.95 cc.517-32.

During the proceedings on the *Finance Act 1990* the then Chief Secretary to the Treasury, Norman Lamont, set out the reasons why the Government had introduced tax relief for workplace nurseries, while ruling out the provision of tax relief for any other form of childcare:[83]

> "First, it was put to us repeatedly that employers found it troublesome to continue assessing and reporting to the Inland Revenue the value of day nurseries. Secondly, it was argued that the burden on industry was an effective deterrent to the development of workplace nurseries. It was also argued repeatedly in the House that there was a degree of resentment about the tax treatment of workplace nurseries. We have made a limited change, putting the tax treatment of workplace nurseries very much in line with that of other benefits in kind. For example, there is a tax exemption for workplace canteens that are provided on the premises. The treatment of workplace nurseries is broadly analogous to those limited concessions."

At the Report Stage of the Bill, two months later, the Liberal Democrats put down a new clause to give tax relief for childcare vouchers given by employers, and similar provisions to cover the self-employed. Opposing these initiatives, the then Financial Secretary to the Treasury, Peter Lilley, stated that the new relief introduced by the Government "is simply a supply-side measure. It is not meant to be a relief for childcare as such. It is designed to remove an obstacle to the provision of such facilities and allow greater supply."[84]

A number of attempts from various quarters have been made to introduce further tax relief to cover childcare costs in succeeding years, though none have met with success. The Liberal Democrat Party proposed tax relief for employer vouchers, and for costs incurred by the self employed during the proceedings of both the *Finance Act 1991* and *Finance Act 1992*.[85] In March 1990 Theresa Gorman presented the *Tax Relief for Household Employers Bill*. The Bill would have allowed tax relief on earned income for the employment of any worker essential for the earner's availability for work, including home helps and child minders. Mrs Gorman wanted these costs to be treated as a business expense.[86] The Government

---

83 HC Deb 16.5.90 c.938.

84 HC Deb 16.7.90 c.764.

85 HC Deb 18.6.91 c.370; 30.6.92 c.479.

86 HC Deb 6.3.90 cc.732-50.

consistently opposed both relief for childcare vouchers,[87] and tax relief for home help,[88] though speculation that it might extend tax relief has continued.[89]

The general argument for wider tax relief is that childcare represents a necessary expense incurred when parents go out to work; as such, it should be deductible from tax, like other costs of earning. By allowing parents to join the labour market, relief would boost tax revenues from present earnings. In the long term, by minimising the time that parents were isolated from the job market, losing knowledge and skills, tax relief would go some way to prevent the problem faced by many trying to find employment having spent a number of years in the home.

This argument received some support from a paper published in the *National Institute Economic Review* in November 1993.[90] This suggested that the lifetime earnings of a woman using childcare facilities were so much higher as a result of her being able to work as to totally compensate the Exchequer for subsidising childcare provision. Of course, predicting a path of lifetime income ignores any restraints on the demand for labour, and it says nothing about the way in which childcare should be subsidised.

One study which has attempted to discriminate between methods of subsidy has been carried out by the Institute for Fiscal Studies, commissioned by the Equal Opportunities Commission and published in June 1995.[91] Four strategies for childcare were compared in terms of the predicted impact on childcare use, on employment, and on Exchequer costs. These were:

- allowable deductions for Family Credit assessment (benefit 'disregard'),
- cash-limited childcare vouchers,
- direct subsidy of childcare places, and,
- tax relief for childcare costs.

The authors admit there are serious limitations in modelling household behaviour in this detail, and those interested in the wider issue of childcare provision are encouraged to read the report closely. In particular, the figures given as estimates should be treated as a guide to the effects of a particular policy, not its an actual outcome.

In terms of this discussion, the report's most striking conclusion is that tax relief is costly, and has relatively little effect on labour supply. The authors give the example of allowing weekly costs of up to £50 per week allowable against income tax at the lower rate of 20 per cent (ie,

---

87 In October 1991, for example, in answer to a written question put down by Sir David Steel [HC Deb 22.10.91 c.498W].

88 Most recently : HC Deb 2.3.95 c.665W.

89 Including the November 1994 Budget : "Childcare tax relief expected in Budget" *Times* 17 November 1994.

90 "Mothers' Human Capital and Childcare in Britain" H.Joshi, H.Davies; *National Institute Economic Review* 4/1993; pp.50-63.

91 *The Impact of Subsidising Childcare* Equal Opportunities Commission June 1995.

restricted in value in the same way as the married couple's allowance). They predict that this would cost £160 million per year, benefit mainly better off two-earner families, and encourage only 10,000 people to join the labour market, with 15,000 other persons working extra hours. The policy of benefit disregard - allowing lone parents or women with working husbands to offset £40 per week when means tested for benefit - was implemented by the Government in October 1994. The authors suggest this has the same order of effect on labour supply as tax relief, but saves the Exchequer an estimated £8 million over the long term. A wholesale subsidy of childcare costs has an annual cost of £900 million, but has 70,000 women entering paid employment and another 130,000 working longer hours.[92]

Certainly the principal disadvantage of a wider form of tax relief is that it is an untargeted subsidy. There is no guarantee that it will go to those who need it most, and the experience in countries where tax relief has been introduced, such as in the United States, would suggest that a disproportionate share of the tax credits go to high income families. In its report on working mothers cited above, the Employment Select Committee argued that "tax relief for employees would ... have very limited effects. Above all, the 2.25 million women earning less than £57 a week who pay no tax or NI would not benefit from an employee-based tax break."[93]

The case against was put strongly in an article in the *Financial Times* in March 1992. The author noted that without capping tax relief, higher earners would benefit most, being rewarded for employing the most expensive type of care. Even if relief were restricted, it would still be unfair:[94]

> "At present, parents without earned income cannot use their non-transferable personal allowances, unless they have investments. On the other hand, the benefits of their unpaid labour are not taxed. The current system is, therefore, probably as fiscally neutral as possible. To introduce tax relief for childcare expenditure, without assistance for parents at home, would upset this balance. A much better way than a standard deduction for all parents is to increase child benefit, which has the added advantage of being of value to non-taxpayers."

The issue of child benefit, and the possibility of taxing it, is discussed below.

During the Report Stage of the *Finance Bill 1994*, new clauses similar to those proposed in the last few years were put forward (ie, covering child care vouchers, and the self employed),

---

92 Summarised in : "Childcare subsidies and mothers' labour market decisions" *Institute for Fiscal Studies press notice* 16 June 1995.

93 *Mothers In Employment* HC 227 Employment Select Committee 14 February 1995; p.xxiv.

94 "The wrong type of relief" *Financial Times* 6 March 1992.

and, in the event, negatived.[95] Summarising the Government's position, the then Financial Secretary to the Treasury, Stephen Dorrell, stated the following:[96]

> "The Government's approach to the problem is to target assistance where there is a real problem, where there are real anti-work incentives and real difficulties for people in finding their way off benefit and into work. By using money in that way we shall be able to achieve a substantial social advance rather than a blanket subsidy which is ill targeted and delivers the lion's share of the benefit to people who do not need it and are comfortably off with their present arrangements."

That same year, the Labour Party proposed extending the existing system of capital allowances for businesses, so as to provide additional tax relief for the construction of workplace nurseries. In proposing this measure, Harriet Harman argued that there existed a "genuine anomaly in the tax treatment of employers who provide nurseries for their employees."[97] Under the current system of capital allowances, employers may write down against tax the cost of constructing a workplace nursery, but only if that nursery is located within an industrial building or a hotel. A similar relief covers expenditure on the construction of sports pavilions, for example, but not on workplace nurseries located in other types of building. Ms Harman suggested that if tax relief was being provided for all employers who built sports pavilions for the benefit of their employees, then it should cover all employers who built workplace nurseries as well. At this point it may be helpful to explain what capital allowances are.

Although the purchase of a capital asset is not a deductible expense in calculating taxable profits, the tax system provides a general relief for the cost of the depreciation of that asset's value over its lifetime, through the system of capital allowances. When a company buys a new asset, it can write off a fixed proportion of the price against tax. Further writing-down allowances may be made in following years, mirroring the gradual decline in value of that asset, until the entire cost of the asset has been offset against tax. Of course, given that not all capital assets will have the same lifespan, the date when an asset is finally written off against tax will not necessarily coincide with that asset being worthless and thrown away. Allowances are available for certain classes of assets only; notably, machinery and plant, along with industrial and agricultural buildings. Most expenditure on machinery and plant qualifies for an annual writing-down allowance of 25% (ie, companies can write down against tax 25% of the present value of a given asset each year). An allowance of 4% covers expenditure on industrial and agricultural buildings, and hotels.

---

[95] HC Deb 19.4.94 cc.765-822.

[96] HC Deb 19.4.94 c.816.

[97] HC Deb 19.4.94 c.766.

Many items used in a workplace nursery or playscheme would qualify as machinery for these purposes: furniture, equipment used for heating, washing and cooking, and play equipment that was relatively durable. In addition, if a nursery were to be located in an industrial building or a hotel, then its construction would qualify for the 4% writing-down allowance. The definition of both types of qualifying building is set out in sections 18 and 19 of the *Capital Allowances Act 1990*; nurseries, and other structures built for the welfare of employees, are covered explicitly.[98] Section 14 of the Act extends this relief to sports pavilions provided for employees' welfare, even if these facilities are not located in an industrial building. Relief covers sports pavilions only, not sports facilities within any type of building.

The Labour Party's proposal was to amend Section 14 of the *Capital Allowances Act 1990*, so that employers who provided childcare facilities could write off the cost of this building against tax, as if it were an industrial building, irrespective of their trade. In the event, it was negatived, both in 1994, and again, during the proceedings of the *Finance Act 1995*, when it was re-introduced. On the latter occasion, the Economic Secretary to the Treasury, Anthony Nelson, set out the reasons for the Government's opposition to the measure:[99]

> "The clause ... is presumably aimed at facilities within shops, offices and other buildings. They do not generally qualify for relief on the footing that such buildings tend not to depreciate, at least over the medium to long term. An extension of capital allowances for childcare facilities would therefore run counter to our policy of keeping to a minimum the number of special reliefs within the tax system. It might also open the door to claims for special treatment for other types of currently non-allowable capital expenditure."

C. Taxing Child Benefit

In an article published in the *Financial Times* in 1991, journalist Joe Rogaly argued that the tax system had no useful role to play in the provision of childcare;[100] rather, child benefit provided "the best child care voucher [and] the best kind of family policy" since it did not discriminate between those women who work outside the home, and those who do not. Mr Rogaly made a distinction between the living arrangements that a couple may make - whether they get married, both work, stay married despite their differences - and the protection of children; clearly, the fiscal system could play an important part by sponsoring the latter, without assuming any role in the private behaviour of adult men and women.

---

98 Section 18(1) and section 19(5)(a) of the *Capital Allowances Act 1990*, respectively.

99 HC Deb 3.4.95 cc.1482-3.

100 "Keeping government out of the bedroom" *Financial Times* 15 February 1991.

Child benefit is not taxed. The cost of increasing it could be mitigated by making it taxable. This was one of the recommendations by the Social Justice Commission in its report, *Social Justice*, published in October 1994.[101] The Commission suggested that to improve the targeting of child benefit, it should be taxed as transferable joint family income, for families where at least one partner was a higher rate taxpayer.[102] This rather complicated solution was forced on the Commission by three factors:

- Many people support the idea of taxing child benefit when it goes to richer families.[103]

- Since the introduction of independent taxation in 1990, husband and wife are no longer taxed as a single unit.

- Child benefit is usually paid to the mother, though in wealthy families usually it is only the father who is a higher rate taxpayer.

The Commission ruled out taxing mothers on this income: taxing all mothers would hit many low income families; taxing wealthier mothers would not raise much revenue, as the earnings of married women tend to be much lower than that of their husbands'. The Commission also ruled out taxing all fathers on their wife's receipt of child benefit, arguing this would be costly, complex, and deeply unpopular. The taxation of child benefit has been ruled out by the Government, reportedly, for the quite severe technical difficulties there exist in taxing it in its present form.[104] In a recent written answer on the possible revenue receipts from doing so - which were estimated at £320 million - the then Financial Secretary to the Treasury, Sir George Younger, noted, "now that husbands and wives are taxed independently, it would be administratively complex to tax child benefit in a way which fairly reflected family circumstances."[105]

Indeed, the Cambridge Microsimulation Unit published a short response on the Commission's proposals for child benefit, which was keenly critical of the Commission's solution:[106]

> In order to tax child benefit in the manner suggested, the authorities will need to know the following:
> (i) how many children for whom a person is receiving child benefit,

---

101 "Labour told to tax child benefit" *Independent* 24 October 1994.

102 *Social Justice: Strategies for National Renewal* Social Justice Commission October 1994; pp.316-7.

103 As reported in: "Poll backs cut in child benefit for the well-off" *Independent* 11 October 1994.

104 "Taxation of child benefit ruled out" *Financial Times* 23 November 1992.

105 HC Deb 25.4.95 c.405W.

106 *The Commission on Social Justice's Proposals for Child Benefit* Cambridge Microsimulation Unit October 1994; p.3.

> (ii) whether they are a higher rate taxpayer or would be if child benefit were added to their taxable income
> (iii) whether they are married and if so, to whom,
> (iv) how much untaxed child benefit should be transferred to this person's taxable income.
>
> Only item (ii) is something that the Inland Revenue can calculate with the information it currently collects routinely. This proposal means that a far greater number of people than at present will have to fill in tax forms of one sort or another, if the new tax is to fall on the people for whom it is intended.
>
> Furthermore, we have assumed in our simulations that only married couples living together who are both parents of the child(ren) concerned, will be subject to this joint element of taxation. Many families with children are not in this situation. If only the 'straightforward' cases are to be effectively liable for tax, then not only will there be problems of horizontal equity between fathers in different situations, there will also be built in incentives to avoid particular living arrangements. What about co-habiting (as opposed to legally married) parents? Will stepfathers be liable for the tax or will it fall on absent fathers? How will the new arrangements integrate into the rules for Child Support? One can imagine the nightmare scenario of the tax transferring from mother to stepfather, to absent father, to the absent father's new partner, and so on in search of a higher rate taxpayer on whose income to stake a claim!

These appear quite fair criticisms. The revenue raised is relatively small, when set beside the Commission's proposal to restrict the MCA to couples aged 55 or over. One might add that a key difference in the MCA is that it does not target a clearly defined need, as child benefit does. It is surprising that the Commission has proposed a solution which does not recognise that many families now do not remain stable: the incidence of divorce, separation, remarriage and cohabitation all pose serious methodological problems for trying to combine independent taxation with a notion of child benefit as family income.

That said, with the advent of self assessment for the tax year 1996-97, the numbers of individuals required to submit detailed annual tax returns will increase considerably. The majority of employees are taxed under the PAYE system. They are likely to contact their tax office only when their status changes in some major way - marriage, divorce, retirement - or if they receive the occasional tax return to fill in. Those who are self-employed and individuals with more complicated tax arrangements are required to submit an annual tax return.

At present, filling in a tax return is a relatively simple operation, partly because it is the Revenue's responsibility to find out certain aspects of someone's income, such as contacting an employer for details on the value of an individual's fringe benefits. Much as the name implies, self assessment means that the taxpayer himself or herself has the **primary** responsibility for organising their tax affairs, and for paying the right amount of tax at the right time.

The system does not require individuals to calculate their own tax bill, but it does require that they themselves provide all the relevant information for the Revenue to do so. Automatic penalties apply should one fail to file a return, or fail to pay the tax one owes, by the specified deadlines. It is anticipated that self assessment be extended to the 8 million taxpayers who currently submit an annual return to the Revenue; leaving 16 million still under PAYE. Obviously, there will be a good deal of cross over between wealthy families, whose child benefit payments the Commission proposes to tax, and the individuals who will come under self assessment.

D. Child Tax Allowances

One further problem in taxing child benefit is highlighted if one compares the proposal with the current operation of the married couple's allowance. It remains true that the provision of this allowance gives individuals a clear motive to signal their married status to the taxman. In the case of taxing child benefit for richer families, no incentive is provided for either partner to reveal that they have children, or collect benefit, beyond - one assumes - a rather harsh penalty for not doing so. This raises the issue as to whether the re-establishment of a tax allowance tied to the number of children one has, rather than the fact that one is married, might not overcome some of these problems. Part of this allowance might then be clawed back, dependent on the individual's marginal rate of tax.

Child tax allowances were phased out over a two year period, until being abolished completely for 1979-80. Previously, parents had been given an allowance of £365 for each dependent child over 16, £335 for each child aged 11 to 16, and £300 for each child under 11, for 1976-77. The abolition of tax allowances was part and parcel of the introduction of child benefit, which at the time received support on both sides of the House.

The then Secretary of State for Social Services, Barbara Castle, discussed the abolition of tax relief in the Second Reading of the legislation implemented as the *Child Benefit Act 1975*:[107]

> "[The Bill] achieves a long overdue merger between child tax allowances and family allowances into a new universal, non-means tested, tax-free cash benefit for all children, including the first, payable to the mother. In this way it ensures that the nation's provision for family support is concentrated first and foremost where it is needed most - on the poorest families; and that it goes to the person responsible for caring for the children and managing the budget for their food, clothing and other necessities ... What will the child benefit scheme achieve? ... most important, the poorer families who have not been able to take advantage of child tax allowance in full, if at all, because of their low incomes, will in future do so, as the new benefit extends the cash advantage of the allowance to all those families."

This remains the most telling criticism of using tax reliefs to provide help to those at the lower end of the income scale. As Samuel Brittan in the *Financial Times* noted in an article

---

[107] HC Deb 13.5.75 c.330, c.334.

in 1990,[108] - when the possibility of child tax allowances had been raised by some right-wing commentators - "child tax allowances were replaced by child benefit precisely because they were worth nothing to those who paid no tax and little to those who paid low tax."

During the proceedings of the *Finance Act 1989*, Frank Field put down a new clause to reintroduce child tax allowances. Mr Field argued that the clause provided the Government with a choice: either accede to the introduction of this tax relief, or ensure that child benefit was fully up-rated in line with inflation, restoring the reductions in real terms made since 1980. If implemented, the benefit from allowances could easily be transferred into increases in child benefit, if that proved more effective. "That is not a change in direction, but it is one of seeking immediate ways to improve the living standards of families and also to have the option at a later stage of moving those resources over to the child benefit scheme."[109]

Jeff Rooker supported the clause, arguing that the Government's attitude to child benefit had changed significantly, given its refusal to index-link the benefit as it had index-linked personal tax allowances:[110]

> "In 1977, child benefit was being phased in with all-party support, with increasing commitments from right hon. and hon. Members in all parts of the House, including the then Tory Opposition that child benefit would be viewed just as though it was a tax allowance - which it was, in part - and in terms both of its value and spending power ... It is consistent and logical for hon. Members to say that the idea of child benefit as a universal benefit loses its validity ... if its spending power was not maintained."

Mr Field's proposal received support from Sir Ian Gilmour, as well as from Sir George Young, then on the backbenches:[111]

> "Child tax allowances endorsed a basic principle of taxation, which is that an individual should be taxed only on his surplus income once his unavoidable expenditure has been met ... the burden of taxation has shifted progressively during the past 10 years from taxpayers without children on to the shoulders of taxpayers with children ... It is true that part of the money saved by not uprating child benefit has been ploughed back to help people on low incomes, but that has meant only that the cost of tackling family poverty has not been borne by taxpayers as a whole but by taxpayers who happen to have children, and there is no sense of justice or logic in that."

---

108 "Family package for a budget" *Financial Times* 11 January 1990.

109 HC Deb 11.7.89 c.919.

110 *op.cit*; c.921.

111 *op.cit*; c.923.

In response, the then Financial Secretary to the Treasury, Norman Lamont, argued that the system of family credit had compensated poorer families for the real reductions in child benefit. In answer to the point that individuals with children had not benefited as much from recent changes in the tax system as those without, Mr Lamont said the following:[112]

> "It is, of course, perfectly true that reductions in the basic rate of income tax have benefited single people more than married couples with children. The reason is that single people pay a higher proportion of their income in tax to start with. However, the tax cuts have benefited everyone, including families with children ... Although it may be true that take-home pay after tax cuts has increased somewhat more for those without children, when one takes account of what has been achieved by the increases in family credit, it is not true at the bottom end of the scale ... I believe that the redeployment of resources to the direct relief of poverty is more valuable than, and should come before, the principle of horizontal equity ... I believe there should be a recognition of children in the system, but I do not believe that my right hon. Friend is right in saying that those whose incomes take them well above the family credit network - those on average earnings and above - have really had a significant degree of hardship inflicted on them by our decision."

112 *op.cit*; c.928, c.929-30.

E. Tax Allowances and Reliefs Abroad

The following details on the basic tax allowances given in relation to marriage and parenthood in ten countries in 1993 are taken from a study on the taxation of production workers, published by the Organisation for Economic Co-operation and Development.[113]

Australia

Tax unit : Members of the family are taxed separately.

Standard marital status reliefs : A taxpayer may claim a tax credit where he or she contributes to the maintenance of a dependent spouse (legal or defacto). The credit is A$ 1,188 (£539) for a dependent spouse and A$1,425 (£646) where there are dependent children. The credit is reduced by A$1 for every A$4 by which the spouse's separate net income exceeds A$282 (£128). A tax credit of A$1,116 (£506) is available to a resident, single, widowed or divorced taxpayer who has the sole care of a dependent child.

Reliefs for children : There are no tax credits for the maintenance of children.

Belgium

Tax unit : The tax unit is the couple. If both spouses benefit from professional income, they are taxed separately. If one partner does not have any professional income, they are taxed on a quotient basis, assessed on a given fraction of their spouse's income (30% of net income) which is treated as their own. This quotient is capped at FB297,000 (£6,493).

Standard marital status reliefs : The basic tax allowance for a married person is FB146,000 (£3,192), compared to the single person's tax allowance of FB186,000 (£4,066).

Reliefs for children : Tax allowances are given for the maintenance of dependent children as follows:

• 1 child	BF39,000	(£853)
• 2 children	BF101,000	(£2,208)
• 3 children	BF228,000	(£4,985)
• 4 children	BF369,000	(£8,067)
• 5 children	BF501,000	(£10,953)

Canada

Tax unit : Tax is levied on individuals separately. In cases where a spouse's income falls below C$5,918 (£2,751), they report their income on their partner's tax return.

Standard marital status reliefs : In cases where a spouse files a joint tax return for both partners, they receive a tax credit of C$915 (£425), reduced by 17 cents for each C$ accruing to the spouse in excess of C$538 (£250).

Reliefs for children : There are no tax credits for the maintenance of children, though there is provision for a parent to set childcare costs against taxable income.

---

113 *The Tax/Benefit Position of Production Workers Annual Report 1990-1993* Organisation for Economic Co-operation and Development 1994; pp.107-229. Current exchange rates are used for conversion to £ sterling.

France

Tax unit : Tax is levied on total family income; children are included if they are dependent. Married couples are always taxed together. Children and other members of the family have the choice to be taxed separately

Standard marital status reliefs & reliefs for children : The family quotient system recognises the married state and the numbers of family dependents. Family income is divided up into a number of parts, relating to the husband (one part), wife (one part), children and dependents (one half part each); ie, a married couple with three children would have a quotient of 3½. The total tax charge is calculated by multiplying the tax due on but one part of total family income by the family quotient.

Germany

Tax unit : Spouses are normally assessed jointly, though they have the option of separate assessment.

Standard marital status reliefs : In the case of joint assessment, specific allowances are doubled.

Reliefs for children : DM4,104 (£1,843) tax allowance per child.

Ireland

Tax unit : Tax is levied on the combined income of both spouses. Either spouse may opt for separate assessment, in which case the tax payable by both spouses must be the same as would be payable under joint taxation. Spouses may opt for assessment as single persons, and be taxed as separate individuals.

Standard marital status reliefs : The married person's allowane is Ir£4,350 (£4,471), which is twice the single person's basic tax allowance.

*Reliefs for children :*There are no tax allowances for the maintenance of children.

Italy

Tax unit : Spouses are taxed separately. Spouses may file joint returns, under which they are taxed separately. In addition, tax credits which one spouse is entitled to are transferable to their partner.

Standard marital status reliefs : A tax credit of L757,000 (£294) is given for a dependent spouse, if their income does not exceed L5,100,000 (£1,983).

Reliefs for children : Both husband and wife are given a tax credit according to the number of children they have, worth L87,500 (£34) per child. Under certain conditions the credit is doubled in value and given to just the one parent; for example, if the children are dependent on one parent only, or if one parent's income does not exceed L5,100,000.

Netherlands

Tax unit : Husband and wife are taxed separately.

Standard marital status reliefs : If one spouse's income is too low to make full use of the basic personal allowance, the entire allowance of Gld5,769 (£2,314) may be transferred to their partner.

Reliefs for children : There are no tax allowances for the maintenance of children.

Spain

Tax unit : Families are taxed as a single unit, or as separate individuals.

Standard marital status reliefs : If the family is taxed as a unit, a tax allowance of Pta25,200 (£132) is allowed for each member of the family unit who works.

Reliefs for children : Pta20,000 (£104) tax allowance per child.

United States of America

Tax unit : Families are taxed in one of three ways :

- As married couples filing jointly on the combined income of both spouses.
- As married individuals filing separately and reporting actual income of each spouse.
- As heads of households (only unmarried or separated individuals with dependents).

Standard marital status reliefs : Married couples generally benefit from a more favourable schedule of tax rates for joint returns of spouses. There are no other general tax reliefs for marriage.

Reliefs for children : For each child and other person claimed as a dependent of a taxpayer's return, the taxpayer is entitled to a dependency exemption of US$2,350 (£1,479). Further provision is made for low income workers with dependables.

VII Further Reading

A chronological list of the principal sources used in writing this Research Paper is given below:

The Royal Commission on Income Tax Cmd 615 1920.

Royal Commission on the Taxation of Profits and Income (Radcliffe Committee) Final Report Cmd 9474 June 1955.

Income Tax and Sex Discrimination Equal Opportunities Commission December 1978.

The Taxation of Husband and Wife Cmnd 8093 December 1980.

Income Tax : Problems & Possibilities Library Background Paper 178 Timothy Edmonds 5 February 1986.

The Reform of Personal Taxation Cmnd 9756 March 1986.

Taxation of Husband & Wife Institute for Fiscal Studies Commentary March 1986.

Taxation Without Discrimination Equal Opportunities Commission September 1986

Taxation on Divorce and Separation J.Gray 1987.

Independent Taxation Library Research Note 90/9 Fiona Poole 5 February 1990.

Taxation and Childcare Library Research Note 90/17 Fiona Poole 5 March 1990.

Child Benefit Library Research Note 91/24 Kim Greener & Robert Twigger 20 March 1991.

The View From No.11: Memoirs of a Tory Radical Nigel Lawson 1992.

The Married Couple's Allowance Library Research Note 92/62 Fiona Poole 17 June 1992.

Taxation of the Family O.P.Wylie Butterworths 1993.

"Mothers' Human Capital and Childcare in Britain" H.Joshi, H.Davies; *National Institute Economic Review* 4/1993.

Social Justice: Strategies for National Renewal Social Justice Commission October 1994.

The Commission on Social Justice's Proposals for Child Benefit: A Comment Holly Sutherland Paper No. MU/RN/8 Cambridge Microsimulation Unit October 1994.

Personal Tax Allowances & Reliefs Library Research Paper 94/123 Antony Seely 30 November 1994.

The Tax/Benefit Position of Production Workers Annual Report 1990-1993 Organisation for Economic Co-operation and Development 1994.

Farewell to the Family? Public Policy & Family Breakdown in Britain and the USA Patricia Morgan Institute of Economic Affairs January 1995.

Mothers In Employment HC 227 1994/95 First Report of the Employment Select Committee 14 February 1995.

The Impact of Subsidising Childcare : Research Discussion Series No.13 Equal Opportunities Commission June 1995.

The Allied Dunbar Tax Handbook 1995-96 A Foreman 1995.

Recent papers on related subjects have been :

Economic policy & taxation

Research Paper

95/82	Economic indicators: July 1995	03.07.95
95/75	Unemployment by constituency: May 1995	14.06.95
95/53	Building Societies (Joint Account Holders) Bill (Bill 104 1994/95)	26.04.95
95/46	The Pensions Bill (HL): pension fund regulation (Bill 87 1994/95)	24.04.95
95/35	Commonwealth Development Corporation Bill (Bill 66 1994/95)	15.03.95
95/10	Pension Fund Regulation	23.01.95