



## *Policy Paper:* *Tax and Benefits*

**The tax and benefit systems are a central part of the UK's economic life, providing funding for Government services and social security when times are tough. However, the systems are complex and have many details that can be hard to understand and navigate. The language used in communications about taxes and benefits needs to be simple and accessible. Changes to the tax and benefit systems should take account of the impact they are likely to have on people's ability to behave in financially capable ways.**

### **What are the issues?**

The tax and benefit systems affect us all. All UK residents pay some form of tax, whether direct or indirect,<sup>1</sup> and a majority of the adult population pays income tax. Most workers pay National Insurance. In August 2018, 6.7 million working age people received benefits. Housing benefit was received by 4 million people (of all

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<sup>1</sup> The main indirect tax is VAT (£132.2 billion budgeted in 2018/19), but there are also duties charged on a wide range of goods and services (fuel duty, customs duty, air passenger duty, insurance premium tax etc). See HMT, Budget 2018, p 96.

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ages) and 1.1 million received Universal Credit. Thirteen million people received the State Pension.<sup>2</sup> 7.33 million families received Child Benefit.

Benefits are paid for a range of reasons including (a) spreading income across the life course, (b) redistributing income to those who have insufficient market income to support themselves and their families, and (c) insuring against the risks of life.

One of the UK's challenges is that, even with tax relief and a benefits system, millions of people still have incomes below the contemporary UK poverty line.<sup>3</sup>

Tax and benefit systems are notorious for complexity. There are so many rules and interactions between different taxes and benefits that even experts find it hard to work out precise individual entitlements. It is easy for HMRC, DWP and consumers to make mistakes, often triggered by changes in circumstances. This can lead to tax underpayments or benefit overpayments that have to be remedied later, sometimes at considerable cost to the person affected.

Some benefits, such as Employment and Support Allowance and Jobseekers require the applicant to pass ability or behavioural tests, which can be subjective and inconsistent in the way they are administered.

Some benefits interact with each other to create a poverty trap<sup>4</sup> – which is where benefit tapering creates a high effective marginal tax rate, which can reach 100% (ie a person's extra income can be 100% offset by benefit reductions).<sup>5</sup>

Universal Credit was designed in part to address the poverty trap, but because it came with waiting times and benefit cuts it has created a range of additional challenges for consumers.

The design of a tax and benefit system raises many policy, ethical and political questions.

From a financial capability point of view, The Money Charity believes that clarity and simplicity are two guiding principles the system should strive to achieve.

DWP and other agencies need to signpost people better to sources of free advice, as these are often not well known. There need to be better tools available to assess whether it is better to be in work than on benefits, as assessing this is still for many people too complex.

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<sup>2</sup> The Money Charity February 2019, The Money Statistics, pages 12 and 16.

<sup>3</sup> ONS 2018, An expenditure-based approach to poverty in the UK: financial year ending 2017.

<sup>4</sup> [https://en.wikipedia.org/wiki/Welfare\\_trap](https://en.wikipedia.org/wiki/Welfare_trap)

<sup>5</sup> [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/48897/universal-credit-full-document.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/48897/universal-credit-full-document.pdf)

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## What needs to happen?

### Overall

- The tax and benefit systems should be designed to be as clear and simple as possible, so they are easy for users to understand and navigate.
- Non-digital or assisted-digital means of access should be available for all users who are not by themselves able to access systems digitally.
- Policy should be based on the real lives of people, for example not expecting people to live for weeks without an income.
- Policies that cause people to go into debt, such as benefit delays and sanctions, should be avoided.
- The language used in tax and benefit explanations, forms and other documentation should be tailored to the actual levels of financial and reading capability of the relevant population.
- The volume and timing of communications needs to be improved, to avoid people being confused by multiple and sometimes inconsistent messages from different agencies (DWP, Local Authority etc).
- Changes to the tax and benefit systems should be designed to make money management easier and enable people to behave in financially capable ways.
- Pension saving and other forms of long-term saving should be appropriately incentivised by tax relief, with a fair sharing of incentives by income level.<sup>6</sup>

### Administration, advice and guidance

- Good practitioner training should be available for all staff involved in the administration of the tax and benefits system and for those in the advice sector giving advice on tax and benefits.
- All users of the tax and benefit system should have access to quality free advice on how the tax and benefits system works, the taxes they are required to pay and the benefits they are entitled to receive. Free tax advice should be expanded.
- HMRC and DWP should work with other regulators and the Money and Pensions Service to develop a joined-up consumer environment favourable to the improvement of financial capability across the UK population.
- HMRC and DWP should continue consulting with consumer groups and charities to ensure that consumer views are taken fully into account in designing the tax and benefit system.

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<sup>6</sup> At present, tax incentives for pension saving are strongly skewed towards high income earners. See The Money Charity Sept 2015, Response to DWP consultation on strengthening the incentive to save. Available at: <https://themoneycharity.org.uk/media/The-Money-Charity-response-to-strengthening-the-incentive-to-save1.pdf>

## The Money Charity

- In our workshops for young people and adults we explain how the tax and benefit systems work, where the money comes from and where it goes.
- We raise awareness of tax rates, allowances and benefit entitlements.
- We alert people to the various sources of advice they can get, especially relating to benefits.
- We design workshops for the specific needs of particular communities and groups.
- We do the above in engaging and lively ways, using exercises and group participation.
- In our policy work we propose regulatory and other reforms to promote financial capability in relation to tax and benefits.

**The Money Charity** is the UK's financial capability charity providing education, information, advice and guidance to all.

We believe that everyone achieves financial wellbeing by managing money well. We empower people across the UK to build the skills, knowledge, attitudes and behaviours to make the most of their money throughout their lives, helping them achieve their goals and live a happier more positive life as a result.

We do this by developing and delivering products and services which provide education, information and advice on money matters for those in the workplace, in our communities, and in education, as well as through influencing and supporting others to promote financial capability and financial wellbeing through consultancy, policy, research and media work.

We have a 'can-do' attitude, finding solutions to meet the needs of our clients, partners, funders and stakeholders.

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