

Department for Work and Pensions

ADJUDICATION AND CONSTITUTIONAL ISSUES DIVISION

DMG Letter 04/05

February 2005

Dear Decision Maker

IS and JSA(IB) – Income disregard concerning tax paid

This letter gives guidance about the effects of a recent Commissioner's Decision¹ that deals with the meaning of the word "paid" when considering the disregard relating to tax for income other than earnings.

1 CIS/1067/2004

DMs should note that this guidance expands on that given at DMG 28007. As a result of this decision where it says "any amount paid by way of tax" in the IS/JSA(IB) disregard¹, this now means tax, which either has been paid or is to be paid.

1 JSA Regs, Sch 7, para 1; IS (Gen) Regs, Sch 9, para 1

Background

The claimant made a claim for IS, which was rejected because her RP exceeded her applicable amount.

The RP although taxable, was paid to the claimant gross. Any tax due would be payable by the claimant in a lump sum following the end of the tax year. The claimant produced a forecast from the IR, which showed what her tax was likely to be for the current year. The claimant argued that this amount should be disregarded from the amount of RP being paid to her, to allow for the tax she would eventually have to pay.

Commissioner's Decision CIS/1067/2004

The Commissioner decided that the disregard,¹ is not concerned with the time at which tax is paid. The disregard applies to tax, which at the date of the benefit decision, either has been paid or is to be paid, the only condition being that it is tax on income, which is taken into account in the calculation of income other than earnings.

1 JSA Regs, Sch 7, para 1; IS (Gen) Regs, Sch 9, para 1

This meant that the amount of tax forecast for the current year was disregarded from the claimant's RP. As a result the claimant was entitled to IS.

Action for DMs to take

A claimant may provide evidence, such as a forecast from the IR, which shows tax due on income other than earnings paid to them for the current year. In such circumstances DMs should disregard the amount of estimated tax from the gross income being paid to the claimant. The net result is the amount of that income which should be taken into account for IS/JSA(IB) purposes.

Example

Jack makes a claim for IS on 5 June due to his incapacity for work.

His partner has been receiving RP of £106.50 since April.

Jack provides a forecast from the IR which estimates that his partner will be liable for £79 tax on this year's RP paid to her.

The DM calculates the amount of RP to be taken into account as follows:

£106.50 a week RP being paid

less £1.52 a week tax [£79 divided by 52]

= £104.98

The DM takes £ 104.98 RP a week into account

When to refer cases for further guidance

Individual cases should be referred to ACI Leeds for further guidance if a claimant declares

- they may have a future tax liability on income other than earnings - but no other details are provided
- a future tax liability exists but they are unable to provide an estimate **or**
- tax paid differs from an estimate previously used.

Annotations

The number of this letter should be noted against DMG paragraph 28007.

Contacts

If you have any queries about this letter, please write to ACI Division, Room GS36, Quarry House, Leeds. Existing arrangements for such referrals should be followed, as set out in DMG Letter 05/04.

Yours faithfully

Marilyn Stephens

DECISION OF THE SOCIAL SECURITY COMMISSIONER

1. I allow this appeal. The decision of the Appeal Tribunal was erroneous in law. I give the decision that the Appeal Tribunal ought to have given, which is that the claimant was entitled on 6 April 2003 to income support of £0.06 per week.

REASONS

2. The claimant is a woman born in 1941. She claimed income support with effect from 6 April 2003. Her applicable amount was £102.10. Her claim was rejected by a decision of 25 April 2003 on the grounds that she had income of £103.52, which exceeded her applicable amount.
3. Though the amount of benefit at issue is very small, the appeal raises an issue of law of some significance. The claimant also explains in the papers that an award of income support would have the additional benefit for her of entitling to certain other benefits and advantages, some – but not all – of which she had been able to obtain independently of an award of income support.
4. The issue of law is as follows. The claimant's income consisted of a state pension which was payable gross of tax but on which the claimant was liable for a small amount of tax. She has produced (page 3) a letter from the Inland Revenue to herself dated 3 April 2003, which contains a calculation of her tax liability as amounting to tax at 10% on the £768 by which her annual state pension in 2003/2004 exceeded her personal allowance. The claimant contends that her income for income support purposes should be computed after tax. If her income is computed in that way, then her weekly income is £102.04, which falls short of her applicable amount by 6 pence.
5. In her notice of appeal of May 2003 (page 2) the claimant set out these calculations and contended that she was entitled to income support of 6 pence per week. The decision was reconsidered but not changed.
6. For the purposes of her appeal the claimant supplied further estimates of her tax liability in earlier years. On the basis of those, the Secretary of State submitted additionally (page 25) that the claimant's tax liability due on 31 January 2004 (relating to the tax year 2002/2003) was £64.30. If that was deducted from her gross pension payable from April 2003, her income would still be above her applicable amount. The claimant produced some notes to the Appeal Tribunal (page 26) in which she drew attention to regulation 40 of the Income Support (General) Regulations 1987 and paragraph 1 of schedule 9 to those Regulations. She also submitted that the tax to be taken into account was the £76.80 of tax due on her pension received in 2003/2004, not the tax due on her pension in an earlier year.
7. Regulation 40 provides, so far as material

- (1) For the purposes of regulation 29 (calculation of income other than earnings) the income of a claimant which does not consist of earnings to be taken into account shall, subject to paragraphs 2 to 3B, be his gross income
 - (2) There shall be disregarded from the calculation of a claimant's gross income under paragraph (1) any sum, where applicable, specified in schedule 9.
8. Paragraph 1 of schedule 9 specifies
 1. Any amount paid by way of tax on income which is taken into account under regulation 40
9. The appeal was heard by a chairman sitting alone on 5 November 2003, and was dismissed. The decision notice (page 31) gives the Tribunal's reason as being that retirement pension does not appear in schedule 9 to the Income Support (General) Regulations and therefore tax cannot be deducted when calculating income. In the fuller statement of reasons (pages 33 and 34) the Tribunal states the issue as being 'whether a Retirement Pension falls within the disregard under schedule 9'. It goes on to find that on a strict construction of schedule 9 it does not do so, explaining that the retirement pension 'does not include any amount paid by way of tax on income taken into account under regulation 40. No income tax is deducted from that income at the point of receipt. Although a liability may arise at some future date, it may be nil, or below the tolerance level [apparently a reference to the Inland Revenue's practice of not collecting very small amounts of tax] or below a level that even when deducted from the gross (which is not permissible in any case) still disentitles her to Income Support'.
10. The claimant appeals with the leave of a district chairman. On 5 April 2004 (page 47) a Commissioner directed the Secretary of State to make a written submission. In that submission (page 49) the Secretary of State submitted that in order to fall within paragraph 1 of schedule 9 tax would actually have to have been paid to the taxing authority, not potentially be payable at some future time; the submission referred to the deduction of tax through PAYE on occupational pensions as illustrating that it was the act of actually paying the tax that rendered it susceptible to disregard under the paragraph. The claimant made a written submission in reply (pages 53-55); this made some relevant points but I do not need to refer to it.
11. On 2 July 2004 (page 61) I directed the Secretary of State to make a further written submission on certain issues, particularly whether the Regulations could be intended to produce the difference in treatment the Secretary of State appeared to contend for between recipients of occupational pension taxed under PAYE and recipients of state pension paid gross. I also questioned whether tax deducted under PAYE in a week was in fact paid over to the Inland Revenue in that week.
12. In response the Secretary of State submitted (pages 63 and 64) that the word 'paid' in paragraph 1 referred to the past and so supported the contention that the tax has actually to have been paid. The Secretary of State referred to CIS/1931/2003 in support of the distinction between what is 'paid' and 'payable'. The Secretary of State went on to explain that, in order to fall within paragraph 1, the tax did not have to have been paid in the same benefit week as the income that was taken into account in that

week, explaining ‘rather, my submission was that the tax had already to have been paid. Where it is clear to the Decision Maker at the time of deciding how much income is to be taken into account, that an amount has been paid by way [of] tax, then I submit that that amount falls to be disregarded under paragraph 1’. He further explained that he was not contending that enquiry had to be made of the payer as to whether they had yet paid to the Inland Revenue the deductions they had collected.

13. The Secretary of State also drew attention to the contrast between paragraph 1 of schedule 9 and regulation 17(10) of the State Pension Credit Regulations 2002, which provides that ‘there shall be disregarded any amount payable by way of tax’. In response to that the claimant said (page 76) that she was putting this to the test by claiming state pension credit; she later reported (page 77) that she had been refused state pension credit on the grounds that her gross income exceeded her applicable amount, and produced a letter to that effect from the Department.

My decision

14. Paragraph 1 of schedule 9 is one of three sets of provisions in the Income Support (General) Regulations 1987 dealing with the deduction of tax from income. The relevant provisions are in part V of the Regulations. Regulation 29 applies to earnings derived from employed earner’s employment and income other than earnings; regulation 29(5) provides that earnings are to be calculated in accordance with chapter III of part V and income other than earnings in accordance with chapter V. Within chapter III, regulation 36 provides that the earnings of an *employed earner* shall be his net earnings, which are to be

calculated by taking into account the gross earnings of the claimant from that employment less
 - (a) any amount deducted from those earnings by way of
 - (i) income tax;
 - (ii) primary Class I contributions under the Social Security Act; and
 - (b) one half of any sum paid by the claimant in respect of a pay period by way of a contribution towards an occupational or personal pension scheme.
15. Regulation 30 provides for the earnings of *self-employed earners* to be calculated in accordance with part IV of the Regulations. Within part IV, regulation 38 provides for the income of a self-employed earner to be the net profit derived from self-employment; the net profit is the earnings less *inter alia* ‘an amount in respect of (i) income tax and (ii) social security contributions ... calculated in accordance with regulation 39’; regulation 39 then contain rules for calculating the tax.
16. Finally, income other than earnings is dealt with in regulation 40 and paragraph 1 of schedule 9, which I have set out above.
17. The Regulations accordingly provide, for each type of income, for the deduction of tax. For employment income, the deduction is of ‘any amount *deducted* from those

earnings by way of tax'; this recognises that employment income is normally paid under PAYE. In the case of self-employment income, it was necessary to provide rules for determining what the amount of tax is to be taken to be, and these are contained in regulation 39. For other income, there is simply a deduction of 'any amount paid by way of tax' under paragraph 1 of schedule 9.

18. It is against this background that I have to decide between the opposing contentions as to the meaning of an 'amount paid by way of tax' in paragraph 1 of schedule 9. The Secretary of State contends that the tax has to have 'already been paid' or been 'paid in the past', though not necessarily in the same benefit week as the income to which it relates – 'the past' here meaning prior to the decision on entitlement to benefit: see the submission in paragraph 3 on page 63. The claimant contends that it is sufficient that the tax is to be paid in the future. I reject the Secretary of State's construction for the following reasons.
19. First, it would produce the result that certain types of income other than earnings were to be calculated gross of tax, whereas all other income is calculated net of tax, which I do not consider that the draftsman can have intended.
20. Secondly, it would produce a difference in treatment between income support claimants who are in receipt of pension income, depending purely on whether the income was subject to deduction of tax at source. One can illustrate that by positing, as I did in the Direction of July, two claimants who receive identical amounts of pension, one being a state pension and the other an occupational pension taxable under PAYE. On the Secretary of State's construction, the first claimant never has the tax which she in fact pays taken into account. Even in the week in which it is paid, it cannot be taken into account so as to make the claimant eligible for income support, since it is not tax on the claimant's income of that week but of earlier weeks. The recipient of an occupational pension, by contrast, has the net figure taken into account. This cannot in my view be the intended outcome, given that the two claimants' level of financial need is in principle the same.
21. Thirdly, if the Secretary of State's construction is right, then it seems to me that the only circumstances in which paragraph 1 of schedule 9 will apply at all is where tax is deducted by the payer (which is what the Secretary of State submitted to the Appeal Tribunal on page 1C) – and that at the expense of some straining of its language. I know of no other circumstance in which tax is paid before the end of the tax year in which the income arises (and I do not consider that the draftsman of the Regulations can have had payments on account of tax in mind). The benefit decision will invariably be taken before then. If the draftsman had intended paragraph 1 of schedule 9 to apply only to tax deducted by the payer, I would have expected him to use the words 'amount deducted by way of income tax' which he did use in regulation 36 but *not* in paragraph 1 of schedule 9.
22. Fourthly, deduction of tax by the payer is not the same thing as payment of tax to the Inland Revenue. Paragraph 4 of his submission on page 64 shows that the Secretary of State regards it as 'impractical' to check that the deducted tax has been remitted to the Inland Revenue prior to the benefit decision. On this approach, the words 'amount paid' in paragraph 1 of schedule 9 are taken as meaning 'amount deducted (but not yet necessarily paid to the Inland Revenue)'; that is a straining of the language used in

paragraph 1 of schedule 9 – and, moreover, one which gives it a meaning identical to the language used in regulation 36 but eschewed in paragraph 1 of schedule 9.

23. I also reject the Secretary of State's implicit submission to the Tribunal (page 1C) that the Regulations are only concerned with tax suffered in the benefit week in question; that is clearly not the case with self-employment income (which, like this claimant's income, is taxed by way of assessment after the tax year); regulation 38 requires the amount calculated under regulation 39 to be deducted despite that.
24. These considerations lead me to the conclusion that paragraph 1 is not concerned with the time at which tax is paid. It applies to tax which, at the date of the benefit decision, either has been paid or is to be paid. The only condition is that specified in paragraph 1 itself, namely that the tax must be 'on income which is taken into account under regulation 40'.
25. For the same reason, the relevant amount of tax is that paid on the pension income attributable to the benefit weeks in question, not the tax payable in respect of earlier tax years. Where, as in the present case, that tax is an annual sum, I agree with the claimant that regulation 32(1) provides for calculating the weekly amount of the payment. While that regulation may principally envisage payments of income, nothing in its wording prevents it applying to a payment of tax where that tax is to be disregarded under paragraph 1 of schedule 9.
26. As mentioned above, the Tribunal made the point that, as at the time of the benefit decision, the amount of tax to be paid may be unpredictable. As to that, it seems to me that the amount of tax will be capable of a fairly simple calculation. It is true that in the case of income support recipients the amount of tax will be small and the Inland Revenue may in some cases choose to waive collection. Where that occurs, I accept that there may not be any scope for revising or superseding the award decision with retrospective effect. But I do not consider that the possible absence of any such mechanism can affect the construction of the Income Support (General) Regulations.

(signed on the original)

Nicholas Paines QC

Deputy Commissioner

19 November 2004