

SUPPLEMENTARY BENEFIT**Resources—treatment of payment under a Deed of Covenant**

The claimant was a student who had claimed benefit during the summer vacation from her course. The Department of Health and Social Security had awarded her a bursary under which approved fees were paid and the claimant's maintenance requirements were calculated as £1,904. This sum was to be made up of a contribution from her parents of £1,119 and a payment by the DHSS of £785. Her father chose to make his contribution by way of a Deed of Covenant executed 31 August 1983. He undertook to pay the gross sum of £540 each 1 September, 1 January, and 1 April for a period of up to 7 years. He made payments net of tax (the annual net amount exceeding £1,119). The adjudication officer decided that the difference between the gross amount paid by her father and the assessed contribution was an income resource to be taken into account at the weekly rate of £9.63, subject to a disregard of £4, and awarded a weekly allowance of £15.82. The claimant appealed against this decision. Before the appeal was heard, the adjudication officer reviewed his decision so that the annual gross figure of £1,620 was taken into account at a weekly rate subject to a £4 disregard, thereby removing her entitlement altogether. On appeal the tribunal confirmed the decision by a majority. The claimant appealed to the Commissioner.

Held that:

1. where a payment in respect of which tax may be payable was made net of tax, regulation 11(6)(a) of the Supplementary Benefit (Resources) Regulations 1981 provided that any reference in regulation 11 to such a payment was a reference to the net payment (paragraph 6);
2. whether or not her father actually made any contribution, by virtue of regulation 4(4) of the Supplementary Benefit (Resources) Regulations 1981 she had to be treated as possessing the assessed contribution of £1,119 (paragraph 7);
3. documents which may have to be acted on by persons not party to them have to be construed by reference to what they contain in the light of the surrounding circumstances. Account could be taken of the fact that the covenant was drawn up so as to benefit from the tax law relating to such covenants, but not of what was now said to have been the intention of the covenantor (paragraph 9);
4. the covenant provided for 3 separate annual payments of £540 each. One was payable on 1 September for 7 years from 1 September 1983, one payable on 1 January for 7 years from 1 January 1984 and one payable on 1 April for 7 years from 1 April 1984 (paragraph 9);

5. in August 1984, 1/52 of each of the net payments due on 1 September 1983, 1 January 1984 and 1 April 1984 was attributable to each week. In September 1984, the payment of September 1983 would have been exhausted but the payment due 1 September 1984 would have come into play (paragraph 11);

6. any repayment of income tax related to a period of one year. Under section 42(7) of the Taxes Management Act 1970 it was to be treated as repayable when it was repaid. Under regulation 11(5) of the Supplementary Benefit (Resources) Regulations 1981 the weekly amount (being 1/52 of the payment) would attract a £4 disregard unless that disregard had already been used up (paragraph 12);

7. regulation 4(4) of the Supplementary Benefit (Resources) Regulations 1981 did not make clear the period to which the notional income was to be appropriated. That did not matter in this case because the notional income was subsumed into the contribution actually made. There would only have been a notional income if the actual payment under the Deed of Covenant had been less than the assessed contribution (paragraph 13);

8. the covenanted income fell to be taken into account in full up to the extent of the assessed contribution. The excess including the tax recovered would have the benefit of the £4 disregard permissible under regulation 11(5) of the Supplementary Benefit (Resources) Regulations (paragraph 13);

The appeal was allowed.

1. My decision is that the decision of the social security appeal tribunal dated 18 January 1985 is erroneous in point of law. The matter must be remitted to another tribunal for determination in accordance with the principles deducible from this decision.

2. The claimant at the material time (the summer vacation in 1984) was on vacation from a course of occupational therapy at a training establishment near Oxford. In connection with this she was awarded by the Department of Health and Social Security in addition to the payment of approved fees, a maintenance grant or bursary of £785 making together with "parental contribution" of £1,119 a total of £1,904. There is a statement in the submission of the adjudication officer to the appeal tribunal that she also received a bank student sponsorship of £785. I am not clear whether this was additional to the £785 from the Department or not, but this can be investigated by the new tribunal. The parental contribution is not an amount to which the claimant had a legal right enforceable against her parents, who could pay it or not as they chose. In fact the claimant's father chose to provide the contribution under a Deed of Covenant dated 31 August 1983 in a form propounded by the Commissioners of Inland Revenue, under which he undertook to pay the sum of £540 (gross) on 1 September, 1 January and 1 April in each year for a period of seven years. On the assumption that the payments under the Deed of Covenant constituted "annual payments" in terms of sections 52 and 53 of the Income and Corporation Taxes Act 1970 (the Taxes Act) the father could fulfil his obligations under the Deed by paying the instalments less basic rate income tax (ie £378 per payment); and the three payments of £378 in a year would add up to £1,134, which would be sufficient to satisfy the "obligation" in relation to the parental contribution. Moreover so long as the transaction did not fall foul of one of the provisions of the Taxes Act designed to negative the tax advantages of a Deed of Covenant in certain circumstances, the claimant, if she had no other income sufficient to exhaust her personal allowances, would be in a position to reclaim the amount of the tax deducted by her father in whole or in part.

3. I understand that the claimant's father duly paid the amounts due under the Deed of Covenant, so far as relevant to the present appeal at least, deducting basic rate income tax therefrom; that is to say he paid £378

on each occasion deducting £162 by way of income tax from each £540 payment. When the claimant claimed a supplementary allowance during the summer vacation of 1984 her weekly requirements were assessed at £21.45 and her weekly resources at £5.63 being 1/52 of £501, the excess of the gross amount of her father's total annual covenanted sums over the amount of his assessed parental contribution less the disregard of £4 per week provided for by regulation 11(5) of the Supplementary Benefit (Resources) Regulations 1981 [SI 1981 No. 1527] (the Resources Regulations). The net effect of the decision was to award her a weekly allowance of £15.82.

4. The claimant appealed against this decision on the ground that the payments under the Deed of Covenant ought in her submission to be appropriated to term time. Before however the appeal could be heard Commissioner's Decision CSB 1153/1983 was published which suggested to the adjudication officer that the allowance had been wrongly awarded. And as I understand it, the adjudication officer, presumably by way of review, substituted a decision that no allowance was payable. This conclusion was reached on the basis that the claimant ought to be treated as having a weekly resource equal to 1/52 of the full gross amount of the covenant less the £4 disregard. This figure brought her resources above her requirements. And the claimant's appeal was treated as an appeal against this revised decision. The appeal tribunal confirmed the decision of the adjudication officer by a majority, one member wanting there to be an adjournment. The claimant now appeals to the Commissioner.

5. The matter turns on the interaction on the Deed of Covenant of a number of labyrinthine regulations, in particular regulation 3(2)(e), regulation 4(4), regulation 9(2)(a) and (b), and regulation 11(2)(1) (5) and (6)(a) of the Resources Regulations. I shall need to refer to all these provisions though not in the above order.

6. I start with regulation 11(6)(a) of the Resources Regulation, which is a defining provision in relation to regulation 11 as a whole, which relates to income resources not derived from any employment. So far as material it provides as follows:

“a reference to any payment in respect of which income tax may be payable—

- (i) where that tax is deducted before payment is made is a reference to the net payment,
- (ii)”

The tax so deducted, if recovered, becomes an income resource under regulation 3(2)(e), of the Resources Regulation, but, as will emerge when I come to the consideration of regulation 9(2) of those Regulations, it will almost certainly be an income resource for a different period. It may be recalled that the claimant's supplementary allowance (or lack of one) was worked out on the basis of the gross amount of the payments under her father's covenant; and the decision was erroneous in law on that ground. If that were the only matter in issue I might have contemplated giving myself the decision that the tribunal should have given. But there are other matters that in my judgment make it necessary that I should refer the matter to a new tribunal.

7. The real issue in the appeal centres on the question whether the payments under the Deed of Covenant can be appropriated to term time or to some period other than the summer vacation, so as to bring about the effect that the claimant did not have any income resource derived from the Deed of Covenant during that vacation. On this question it is necessary first to consider regulation 4(4) of the Resources Regulations, which so far as material provides as follows:

“Notwithstanding that it is not actually made, a student shall be treated as possessing any contribution in respect of the income of any other person which a Minister of the Crown or an education authority takes into account in assessing the amount the student’s grant or award unless . . . (not relevant. . . .)”

It follows that the claimant had an income resource of £1,119 for the year, whether or not her father paid her the parental contribution. The father was not under any legal obligation to pay it and if he chose to make the contribution he was free to do so in any way that he might choose. If he simply made a periodic allowance he could appropriate it to whatever period he chose and thus confine it to term time. It would appear that the claimant’s local authority grant and bank student sponsorship money (if any) were treated by the assessing authorities as so appropriated.

8. In the present case, however, the claimant’s father elected to make his parental contribution by means of a Deed of Covenant. The tax effect of a Deed of Covenant to make an annual payment to another individual is (subject to certain restrictive provisions of the Taxes Act) that the covenantor deducts tax from the payment, which, if the payment is made out of his taxed income, he retains, while the beneficiary can recover the tax so deducted to the extent that he or she has any unexhausted personal reliefs. This is a well recognised method of converting the income of A into that of B, which is evidently accepted by the Inland Revenue who have furnished a form of Deed of Covenant for the purpose. In order that the covenant shall have this effect it must however be a covenant for the payment of an “annual payment”. And under section 434 of the Taxes Act it must not be for a period which cannot exceed six years. Payments made at stated periods of less than a year can be annual payments if they can last beyond the year. But I do not think that payments for non-continuous periods of, say, nine months at a time can constitute annual payments; nor would payments for seven periods of nine months each in aggregate exceed six years. Indeed I am disposed to think that the covenant in this case, which provides for payments to be made at irregular intervals, is effective for tax purposes only because it can be treated as three separate covenants for annual payments.

9. I am not of course directly concerned with the question whether the covenant is effective for tax purposes. But I am invited to construe it as a covenant for payments for term time on the ground that, although the covenant does not say so, it was the intention of the covenantor that it should so operate. I consider that in construing the covenant I can take account of the fact that it was manifestly prepared to enable the parties to take advantage perfectly properly of the tax law relating to such covenants. And I cannot take account of what is now said to have been the intention of the covenantor. Documents, that may have to be acted on by persons not parties to them have to be construed by reference to what they contain in the light of the surrounding circumstances. In my judgment the covenant falls to be construed in accordance with its terms and provides for three separate annual payments of £540 each, one payable on 1 September for seven years starting 1 September 1983; one payable on 1 January for seven years starting on 1 January 1984 and one payable on 1 April for seven years starting with 1 April 1984.

10. The question to what periods payments under the covenant relate is governed by regulation 9(2)(a) (b) and (c) of the Resources Regulations which provide so far as material as follows:

“Earnings and other income shall be calculated on a weekly basis, and
.....shall be attributable as follows:

- (a) subject to the following sub-paragraphs, a payment of income shall be taken into account
 - (i) where it is payable in respect of a period, for a period equal to the length of that period, and
 - (ii) in any other case for the period to which it is fairly attributable;
- (b) a payment of income shall be treated as paid on—
 - (i) in the case of a payment which falls to be taken into account but which is payable before the first benefit week pursuant to the claim, the date on which it is payable,
 - (ii) in any other case, the first day of the benefit week in which it is payable or the earliest succeeding benefit week in which, having regard to the method by which pension or allowance is payable in the particular case, it would be practicable to take it into account;
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- (c) where a payment of income is payable in respect of a period which exceeds one week, it shall be attributable at a weekly rate.....beginning with the appropriate date ascertained in accordance with sub-paragraph (b);”

11. The foregoing is not straightforward. But it emerges from it that the length of the period to which a payment is to be attributed is to be ascertained in accordance with sub-paragraph (a)(i) or (ii), while the starting date for such period is ascertained in accordance with sub-paragraph (b) read together with sub-paragraph (c). And in my judgment it emerges that each Deed of Covenant payment is to be related to a period of a year starting on the date on which it was payable or in certain cases the slightly different date ascertained in accordance with sub-paragraph (b)(ii), thus in relation to August 1984 1/52 of the net payments that fell due on 1 September 1983, 1 January 1984 and 1 April 1984 will be attributable to each week. If time runs on into September the net payment due on 1 September 1983 will have spent its force but the net payment due on 1 September 1984 will have come into play.

12. I now turn to the recovery of income tax. This too relates to a period of one year. But under section 42(7) of the Taxes Management Act 1970 it must, I think, be treated as becoming payable when it is repaid and must be appropriate thus to the year from then. It will be for the new tribunal to find whether there had been any repayment that might affect the claimant's resources during the period in issue. If there has been any repayment the weekly amount of the resulting income resource will be 1/52 of the payment. Under regulation 11(5) of the Resources Regulations there will be a disregard of the first £4 of the amount except so far as that disregard may have been used up on any other income resource arising under regulation 11(5), such as the excess of the net covenanted payments over the parental contribution.

13. I have still to consider regulation 4(4) of the Resources Regulations under which a student is to be treated as having a notional income equivalent to the amount of the parent's allotted contribution, whether the parent makes the contribution or not. The regulations do not seem to me to be clear on the periods to which such notional income is to be appropriated. But this does not matter in the present case because I have

reached the conclusion that where the parent does make the contribution the notional income under regulation 4(4) is subsumed into the actual income contributed. The only alternative possibility (which I reject) is that the student has both the notional income and the contributed income. I therefore do not need to look beyond the actual income paid under the Deed of Covenant and the tax recovered, though if the net amount so paid has been less than the assessed contribution there would have been a notional income of the excess. The principal effect of regulation 4(4) is that to the extent of the assessed contribution the covenanted income falls to be taken into account under that regulation in full and not subject to the £4 disregard that would have been permissible if it had been income only under regulation 11(5) of the Resources Regulations. In the present case payments in excess of the contribution including tax recovered will have the benefit of the £4 disregard.

14. To sum the matter up a parent whose student child has an assessed parental contribution may no doubt arrange for that contribution to be provided in a variety of ways. Two possible ways are simply for the parent either to make periodical payments on account of the contribution without placing himself under any legal obligation to do so; or to enter into a Deed of Covenant to make periodical payments on account of the contribution. If he adopts the latter course, he will incidentally give his child the benefit of the tax advantages that go with covenanted payments. But there is the counter-balancing disadvantage that he is not free to apportion the covenanted payments over the term weeks to the exclusion of the vacation weeks without jeopardising the tax advantage. On the other hand he can apportion without risk if there is no deed of covenant. He can choose which course to adopt but he cannot have it both ways.

15. The claimant's appeal in form succeeds; but on the substantial issue she fails.

(Signed) J.G. Monroe
Commissioner

**NOTE ADDED WITH THE AUTHORITY OF THE CHIEF
COMMISSIONER**

The regulations relating to the treatment of a student's resources (including payments under a Deed of Covenant) were amended with effect from 3 November 1986 by the Supplementary Benefit (Requirements and Resources) Miscellaneous Amendments Regulation 1986 [SI 1986 No 1293]. The amended regulations include modification of the treatment, for supplementary benefit purposes, of student grants, contributions paid under Deeds of Covenant and associated tax refunds.