AGE Concern Policy Response

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Treasury Committee's Inquiry into Budget Measures and Low-income Households

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Age Concern welcomes the opportunity to give evidence to the Committee's inquiry into Budget Measures and Low Income Households. This response mainly focuses on the impact for people aged 60 and over.

Age Concern is the UK's largest organisation working with and for older people. Four national Age Concerns in England, Northern Ireland, Scotland and Wales and a federation of over 400 local organisations work together to promote the well-being of all older people. Our work ranges from providing vital services to influencing public opinion and government. Every day we are in touch with thousands of older people from all kinds of backgrounds – enabling them to make more of life.

The Age Concern England Policy Unit develops public policy proposals on ageing and older people with respect to England and UK-wide policy. We influence Government, public bodies and professional organisations by commissioning and undertaking research, responding to consultations, liaising with decision makers, holding policy events and developing partnerships with other organisations.

Most of our policy responses and summaries are available to download on our website: www.ageconcern.org.uk.

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Key points and recommendations

The impact of the tax changes

- Age Concern welcomes the protection given to people aged 65 and over through increases in personal allowances and we are particular pleased that 580,000 older people have been taken out of the tax system altogether.
- We are concerned that many people on low incomes under the age of 65 have lost out due to abolition of the 10 pence rate.
- Some of those affected may also owe tax for 2007-08 and will have an increased liability for future years due to an HMRC error in taxing some small pensions.
- Problems due to the interaction between income tax and state benefits may be exacerbated due to the increased tax liability.
- A small number of pensioners will have to pay double the tax previously due on a lump sum payment gained from deferring their state pension.
- The 10 pence rate remains for savings so it will be important to ensure those who receive savings income net apply for any rebate due.

Measures to address concerns

- Compensation should be through the tax systems – increasing personal allowances is the fairest and most effective way to do this.
- For those aged 60 to 64 ideally we would like to see personal allowances increased to the level for people aged 65 and over although a more modest option would be to raise allowances to the level of the pension credit guarantee.
- Age Concern does not support using the winter fuel payment as a mechanism for compensating those aged 60 to 64.

Other budget measures – fuel poverty

- The Budget announcements on winter fuel payments and the role of energy companies, while welcome are an inadequate response to fuel poverty. There should be a co-ordinated cross government strategy to address fuel poverty through measures relating to energy efficiency, fuel prices and incomes.

1. The effects of the abolition of the 10 pence rate

Age Concern welcomes the protection given to people aged 65 and over through increases in personal allowances and we are particular pleased that 580,000 older people have been taken out of the tax system altogether.

People aged 65 and over

The abolition of the10 pence rate (for non-savings income) and related tax changes will generally have a positive or neutral impact on the incomes of people aged 65 and over. The higher age-related personal allowances for people aged 65 and over were increased by £1,800 more than inflation and, this combined with the reduction in the basic rate tax, has protected people aged 65 and over from the loss of the 10 pence rate. Some people are now better off and Age Concern particularly welcomes the fact that 580,000 people aged 65 and over have been taken out of the income tax system altogether. This not only increases their income but simplifies their financial affairs by limiting there need to come into contact with HMRC.

People approaching the age of 65

We are concerned that many people on low incomes under the age of 65 have lost out due to abolition of the 10 pence rate.

Age Concern has been contacted by older people concerned about the abolition of the 10 pence band ever since this was announced in the 2007 Budget. Of the 5.3 million households who will be worse off the Government estimates that 600,000 are women aged 60 to 64[1]. Most people who have contacted us are women in this age group. However we have also heard from men aged 60 to 64 and people approaching 60 who are either retired or on low earnings. In addition we have been approached by a number of people aged 65 and over who had not realised their position was protected and were worrying about increased tax liability.

In May 2007 we wrote to the then Chancellor Gordon Brown expressing our concerns about the people under the age of 65 with modest incomes who would lose out. We argued that it was unfair that this group should be worse off due to the abolition of the 10 pence starting rate. It is particularly difficult for those who are already retired, perhaps having been forced to stop working due to ill health or redundancy, and have little option of increasing their income.

Many of the women who have contacted us argue that the higher personal allowances should apply to them as they have reached state pension age and are therefore ‘pensioners’. Those with incomes just over the tax threshold who heard the Chancellor referring to ‘a fair system for pensioners’ in the 2007 Budget did not expect this to mean their tax liability would increase. Typical of the letters we have received is the woman who wrote:

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[1] *House of Commons Hansard* 18 Oct 2007, 1266W.

> *I cannot believe the Chancellor has chosen to target low paid people on an income of less than £17,000 pa by removing the 10% tax bracket…. I personally will be £180 pa worse off - just the same as the forthcoming rise in the state pension*.

Even before the abolition of the 10 pence tax rate we regularly heard from women aged 60 to 64 who argued the higher personal allowance should be linked to state pension age rather than age 65. While we understand why people feel this way this would then raise issues of gender inequality. Unequal state pension ages are allowed under European legislation but in other policy areas it has been ruled that men and women should be treated equally in terms of financial entitlements.

Increased tax liabilities for people with small pensions

Some of those affected may also owe tax for 2007-08 and will have an increased liability for future years due to an HMRC error in taxing some small pensions.

Some of the group affected will also be among the 420,000 pensioners who have small pensions to which PAYE has not been properly applied in recent years. While any tax debt accrued before the tax year 2007-08 will not be recovered the expectation is that HMRC will start to recover tax due in 2007-08 in the current tax year – even though these pensioners are not yet aware they have a tax debt. This issue was raised by the Public Accounts Committee in its report on Tax Credits and PAYE in January 2008.[2] The Committee criticised HMRC's previous failure to apply the correct procedures and recommended it should notify the pensioners affected of the change to their tax liability – this has not yet happened. Age Concern has argued that any tax debts accrued before an individual is informed of their tax liability should be written off. The impact of the withdrawal of the 10 pence rate adds to the arguments for doing this to prevent confusion and to avoid an additional tax burden on lower income pensioners.

The interaction between the income tax and income-related benefits

Problems due to the interaction between income tax and state benefits may be exacerbated due to the increased tax liability.

The Budget tax changes will increase the tax liability of some people aged 60 to 64 who are both due to pay income tax and entitled to the income-related benefits Pension Credit, Housing Benefit and Council Tax Benefit. It is highly inefficient that one Government department assesses liability and collects tax from some individuals while another carries out a complex assessment of income, savings and other circumstances in order to pay means-tested benefits to the same individual. In terms of the impact on the individual's overall income an increase in tax will reduce income therefore increasing benefit entitlement because benefits are based on net income.

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[2] *Tax Credits and PAYE*; Public Accounts Committee, Eighth Report of Session 2007/08, January 2008

However a particular problem arises when the individual's tax cannot be collected via PAYE, for example because their only source of income is the state pension. In this scenario the Pension Service or local authority will calculate benefit entitlement on current gross income because tax will not be paid under the self-assessment system until a later date. Procedures for backdating entitlement are unclear and often people do not understand the position. The likelihood is that pensioners in this position will end up with a lower income overall than people with the same income who are taxed under PAYE.

This is a complex issue and one that for some people aged 60 to 64 will be exacerbated by the abolition of the 10 pence rate because tax liability and therefore underpayments of benefit will be higher if entitlement has been calculated on gross income. There is a need for a co-ordinated approach by the DWP and HMRC to address this problem.

Tax liability on state pension lump sums

A small number of pensioners will have to pay double the tax previously due on a lump sum payment gained from deferring their state pension.

In our letter to the Chancellor in May 2007 we raised a concern about the impact of the abolition of the 10 pence rate on some people who choose to take a lump sum after deferring their state pension. Tax on this lump sum is paid at the pensioner's marginal tax rate so for people in certain income bands this could double the tax payable. Take the example of 'Ahmed' on the Pension Service website, who is entitled to £18,000 after deferring his £105 pension for three years. If his gross income is just below the tax threshold he will not be taxed on this payment. However if his income is just over the tax threshold he will be liable to pay £3,600 tax. While the nature of the system inevitably results in those just over certain income thresholds paying more than those with slightly lower incomes, the differences will be starker now there is no 10 pence tax band. Age Concern suggested that one option would be to treat the lump sum in the same way as savings income and only deduct 10% tax for those in the appropriate income bracket. In response the Government told us that this would only affect a small number of people and that any change would be disproportionate to the numbers affected.

Simplification

The 10 pence rate remains for savings so it will be important to ensure those who receive savings income net apply for any rebate due.

We recognise that the abolition of the 10 pence rate does in general simplify the system. However the 10 pence rate will remain for savings. We support the intention of limiting the tax liability on savings for people with non-savings taxable incomes of less than £2,320. However many people affected by this will have 20 per cent tax deducted from savings income at source so will need to claim back overpaid tax. It will be a considerable challenge for Government and the HMRC to ensure that all those eligible to pay 10 per cent tax on savings income are aware of this and receive any rebate due. This problem existed previously but it will be exacerbated because many people will not be aware that the 10 per cent rate continues for savings, and because people aged 65-plus who previously paid tax at 20 per cent on savings will now have moved into the nil-rate or 10 per cent bands. We would like HMRC to consider ways of addressing this such as reviving the Taxback campaign.

2. Measures to address concerns

Increasing personal allowances

Compensation should be through the tax systems – increasing personal allowances is the fairest and most effective way to do this.

We believe the best way to compensate those on low incomes who have lost out from the changes is through the tax system. Increasing personal allowances is the fairest and most straightforward way to do this. Indeed in 1999 when the 10 pence starting rate was announced Age Concern wrote to the Chancellor saying that while we recognised that the new rate would be of benefit to older taxpayers we believed increasing allowances was the most effective way of reducing the tax burden on those with low incomes. A lower starting rate does reduce the marginal deduction rate but it is questionable whether individuals are sufficiently knowledgeable about the tax system for marginal tax rates to have a significant impact on, for example, incentives to work and save.

The cost of increasing personal allowances could be reduced if higher levels of allowance were subject to an income limit (as with people over 65) although this would introduce additional complexity.

Protecting those aged 60 to 64

For those aged 60 to 64 ideally we would like to see personal allowances increased to the level for people aged 65 and over although a more modest option would be to raise allowances to the level of the pension credit guarantee

The Government has said that pensioners aged 60 to 64 are one of the groups that it intends to provide more help to. Looking specifically at this age group ideally we would like to see personal allowances increased to the level of allowances for people aged 65 and over. This would be the simplest approach and would produce fairness between all people who have reached state pension age. Because the higher allowances are subject to an income limit the measure would not benefit better off older people.

An alternative approach would be to increase the allowances for people aged 60 to 64 to the level of the standard Pension Credit guarantee rate for a single person - £124.05 a week or £6450 a year. As seen in the table below this would help protect people from the loss of the 10 pence tax rate and would have the added advantage that a single person aged 60 to 64 entitled to the standard rate of Pension Credit guarantee would not be liable to pay income tax. As with the current age-related personal allowances these could be subject to an income limit.

Tax paid by 60 to 64 year olds under different systems

Gross income	**Previous system** (personal allowance £5,435, Tax rates 10%/22%)	**Current system** (personal allowance £5435, tax rate 20%)	**Aligned with pension credit guarantee** (personal allowance £6,450, 20% basic rate tax)
£6,000	£56.50	£113	£0
£7,000	£156.50	£313	£110
£,8000	£286	£513	£310
£10,000	£726	£913	£710
£15,000	£1,826	£1,913	£1,170
£20,000	£2,926	£2,913	£2,710

We would favour any increases in allowances to be made on a permanent basis for all those affected to provide ongoing compensation for the loss of the 10 pence rate. However it would be possible to introduce measures specifically for 60 to 64 year olds linked to the higher age-related allowances on a transitional basis so any additional personal allowance targeted at 60 to 64 year olds could be linked to women's state pension age. In this case as state pension ages start to be equalised from 2010 onwards the age at which higher allowances are given would be gradually increased. This would also be in line with increases in the minimum age for receiving Pension Credit.

People under the age of 60

An increase in allowances for those over the age of 60 would still leave some of those who have contacted us, for example people in their late 50s who were forced to leave work due to ill health or retired early, perhaps to provide care or be with an older partner. These groups also feel aggrieved that having planned their finances tax rules have changed. For this group again we feel that an income tax based approach would be the best solution. Changes to the tax credit systems have been suggested as a way of providing compensation but this would only apply to those in paid work and for those who could benefit measures would need to be accompanied by effective administration, and a major effort to improve take-up. HMRC estimates indicate that the take-up of Working Tax Credits for people without children is only 22%[3].

Winter fuel payments

[3] *Child credit and working tax credit take-up rates 2005-06.* HMRC 2008.

Age Concern does not support using the winter fuel payment as a mechanism for compensating those aged 60 to 64.

Age Concern does not support the idea of using the winter fuel payment[4] mechanism to compensate people aged 60 to 64. Although these payments are a good way of providing help with heating costs and have the advantage of being made to virtually all older people over the age of 60, avoiding problems of take-up, we do not see this as an appropriate mechanism for compensating people for tax changes. Winter fuel payments (and other age-related payments that have been made) are not means-tested – they go to people who will gain from tax changes, and those who have no tax liability. As far as we know the Department for Work and Pensions would not be able to identify and pay additional amounts specifically to those who have lost out due to the tax changes. Furthermore winter fuel payments are linked to households so for example a single person aged 60 receives £200 while 2 people aged 60 sharing a household (whether a couple of not) receive £100 each (except if both receive pension credit). In contrast the tax system is based on individual's income.

For the above reasons we believe this is not a good mechanism for compensation. In any case there is no need to use the benefit systems when HMRC have information about people's taxable income and as set out above could address the issue in a more straightforward and targeted way through an increase in personal allowances.

3. The broader context of Budget Measures for Low Income Groups

The Budget announcements on winter fuel payments and the role of energy companies, while welcome are an inadequate response to fuel poverty. There should be a co-ordinated cross government strategy to address fuel poverty through measures relating to energy efficiency, fuel prices and incomes.

Another key area of policy for low income older people covered in the Budget was fuel poverty. We welcomed the announcement of an additional one off payment of £50 (£100 for over 80s) to 'help pensioners who are facing pressures such as higher energy bills' and the £225 million package of assistance from the energy companies announced recently. However, these measures alone are an inadequate response to the major problem of fuel poverty.

We welcome the various recent and current select committee inquiries addressing aspects of this issue.[5] This Committee is well placed to draw these different strands together and examine this issue from a poverty perspective. We therefore welcome

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[4] Although reference has been made to support through winter fuel payments in practice it is likely that compensation delivered in this way would be made through the age-related payments legislation and paid at the same time as winter fuel payments.

[5] These include the recent CLG Committee report on existing housing and climate change, the current BERR Committee inquiry into possible anti-competitive behaviour in the energy market and the forthcoming EFRA Committee inquiry into energy efficiency and fuel poverty.

the intention to examine the impact of measures to address fuel poverty in the Committee's inquiry into the 2008 Pre-Budget Report. However, with recent increases in energy prices biting hard and further price rises predicted, the plight of people in fuel poverty has become extremely pressing. We therefore hope the Committee will begin to examine this issue and make initial recommendations in this inquiry.

Older people are more at risk of fuel poverty than any other group, accounting for around 50 per cent of households affected. We estimate that the number of pensioner households living in fuel poverty in the UK has doubled in the last four years, and now stands at 2.25 million.

A recent summit hosted by Ofgem agreed some useful measures to help vulnerable households switch suppliers but, despite the presence of a number of senior ministers and energy company chief executives, failed to discuss the full range of measures needed to tackle fuel poverty. In light of this, and the admission by ministers that the Government will not meet its 2010 target to end fuel poverty among vulnerable households, it is clear that the Government's fuel poverty strategy should be urgently revised. We hope the Committee will press ministers on this and consider a range of measures to tackle fuel poverty including:

- Policy co-ordination: a range of departments have responsibility for tackling fuel poverty through measures related to energy efficiency, fuel prices and incomes. It is important that this is co-ordinated effectively across government. Our evidence suggests that this is not happening as effectively as it should be.
- Funding; all options should be considered including looking again at the financial commitment made by the energy industry, especially given the Fuel Poverty Advisory Group's estimate that 30 per cent of recent energy price rises may be accounted for by higher margins. FPAG also estimates that the Treasury is accruing £400 million a year in additional VAT receipts as a result of fuel price increases - this should be recycled to alleviate fuel poverty.
- Links between fuel poverty and energy efficiency: tackling fuel poverty and improving energy efficiency should be mutually reinforcing policy objectives; again our evidence is that more could be done to achieve this.
- Energy prices: mandatory social tariffs offering the lowest market rate should be made compulsory through the Energy Bill currently before Parliament.
- Warm Front: funding levels were cut in the last CSR. We have received many complaints about the operation of the programme, especially concerning the level of the maximum grant available under the scheme. Funding should be immediately increased by at least 25 per cent and the maximum grant under the scheme should be increased significantly.
- Income measures: This year's one off increase in winter fuel payments will not be adequate to meet the increases in fuel bills. The £100 increase announced in the Budget should be extended to all pensioners and made permanent. Fuel poverty could also be significantly reduced by increasing the take-up of income-related benefits. Currently between £3.1 and £4.6 billion is unclaimed by older people each year.

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