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MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

BRINGING UNEMPLOYMENT BENEFIT WITHIN THE TAX CHARGE

Memorandum by the Secretary of State for Employment

I strongly favour the subsequent method of taxation (Method B) for the following reasons.

2. It is essential to bring supplementary benefit within the reckoning for tax. It would not be consistent with our policy on work incentives if we were to tax the NI benefits paid to the involuntarily unemployed, while leaving untaxed the supplementary benefit which may be paid to those who have been disqualified from NI benefit because they have caused their own unemployment.
3. However, any of the Method A (current) systems of taxation discussed in the Inland Revenue paper, if applied to supplementary benefits, would mean that the amount payable in a particular week might be reduced below the minimum entitlement considered necessary to avoid hardship. Either the deduction would have to be restored, which is a nonsense, or we should have to introduce legislation restricting supplementary benefit entitlement in such cases. This would be extremely controversial and very difficult to defend in Parliament.
4. The advantages of adopting Method B are:-
  - (1) There would be no question of reducing the weekly income of any claimant below the supplementary benefit level.
  - (2) ERS (as well as UB and supplementary benefit) could be taxed at the rate appropriate to the tax position of each claimant. This would be fairer than applying the rough justice of the "compounding" method (suggested in paragraph 15 of the Chancellor's paper and para 15 of the paper by the Inland Revenue). This would be seen by the claimant not as taxation but as an arbitrary cut in a benefit to which he is entitled by reason of past payment of earnings-related NI contributions.
  - (3) Under a current system (Method A) tax refunds, where due, would be payable automatically during unemployment, instead of being paid only on application after a delay, as happens now. Under the subsequent

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system (Method B) they would be payable only on return to work or at the end of a tax year. This would provide an extra incentive to return to work.

5. I favour, therefore, the adoption of Option 1B, ie taxation of flat-rate UB, ERS, and Supplementary Benefit up to the standard rate of UB by the subsequent method. This option would bring in the same revenue (£200 million) as would the option favoured by the Chancellor, at a similar staff cost.

Department of Employment

J P

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