Strengthening the self-employment test for working tax credit

Employment Tax | Personal tax | Technical

01 June 2015

At Autumn Statement 2014, it was announced that the government would be looking to strengthen the eligibility conditions for those claiming Working Tax Credit (WTC) on the basis of being self-employed by introducing a 'genuine and effective' test, in a bid to prevent bogus self-employment and abuse of the tax credit system. This new 'genuine and effective' test was proposed to take effect from 6 April 2015, along with the legal requirement that a WTC claimant must also register for self-assessment and obtain a unique taxpayer reference (UTR) before making a claim to WTC.

The idea of strengthening the test was not really surprising, given that for Universal Credit (UC), self-employed claimants are also subject to similar conditionality tests; albeit newly self-employed claimants under the UC system are granted a period of grace in which conditionality does not apply, known as the Start-Up period – something which does not seem to apply to the new test for WTC.

At Budget 2015, the test had been somewhat revised. The new test would now be based on the principles of whether the self-employment was being carried out on a commercial basis with a view to realising a profit. The new test did come into effect on
6 April 2015 and applies to new claimants. Existing claimants will be transitioned to the new test from 6 April 2015 onwards, although the exact timetable has not yet been advised. The legal requirement to obtain a UTR before claiming WTC has now been deferred until 6 April 2016, although self-employed claimants making a claim to WTC for the first time after 6 April 2015 will be advised that they should register with HMRC for self-assessment.

HMRC held a teleconference on 20 March 2015 with members of the Benefits & Credits Consultation Group (BCCG), which includes representatives from the ATT and

LITRG, to discuss the draft guidance and required updates to the HMRC manuals to advise claimants of the new test.

Following this teleconference, the ATT provided a written response to HMRC, setting out our concerns with the new test. Our full responses can be read on the ATT website.

In summary, our concerns were as follows:

- The lack of publicity surrounding the change to forewarn claimants;
- The very short timescale in which to make the finalised guidance available;
- The lack of time in which to appropriately train HMRC Tax Credits staff who are going to be taking on the role of key decision makers when reviewing whether an individual is trading commercially, with a view to realising a profit;
- The number of claimants who will not have the necessary evidence, such as business plans, with which to prove to HMRC that they are trading commercially; and
- The number of unanswered questions arising from the teleconference regarding specific issues. For example, foster carers are considered to be self-employed for WTC, but they would not meet the new test of trading commercially with a view to realising a profit. HMRC were unable to comment on the treatment of foster carers during the teleconference.

As we were concerned that both the guidance and HMRC staff would not be ready for the new test to take effect from the 6 April 2015, we suggested a delay in its implementation.

The ATT did receive a reply from HMRC. Due to pre-election purdah, the reply was somewhat limited; but it did say that it was not possible to provide advance notice to potentially affected claimants, due to the new test being subject to some revisions following its initial announcement at Autumn Statement 2014, resulting in the finalised test only being reported at Budget 2015. Whilst the ATT accepts this as the logical reason for the lack of publicity surrounding the new test, we believe that this only strengthens our point that the legislating of the new test should have been delayed, as was the case with a number of other measures previously announced at Autumn Statement 2014 but then deferred from being included in Finance Bill 2015 (such as the trust changes and the trivial benefits exemption).

The finalised revisions to the Tax Credits Technical Manual, including details of the new test, are now available on GOV.UK.

Since the teleconference HMRC has been able to confirm that foster carers who opt to use the simplified method to calculate how much tax they must pay will be considered to have met the new test, even if they do not make a taxable profit. However, foster carers who exceed the qualifying amount for tax relief and opt to use the profit method may be asked to demonstrate that they are trading on a commercial basis with a view to making a profit. HMRC are currently updating the content of the Tax Credits Technical Manual that relates to foster carers. This will be shared with members of BCCG for comment before being published on GOV.UK.

HMRC assure us that staff are receiving the appropriate ongoing training and that operational guidance is continuing to be updated. HMRC intend to involve BCCG members in the development of this guidance.

In the final paragraph of the ATT submission, we pointed out that the rush to bring in the new test from 6 April 2015 could lead to much ‘muddling along’ by HMRC to begin with, while it figures out the answers to some of the, as yet, unanswered and perhaps unknown questions. We still believe that this could well be the case. However, with continued communication between HMRC and BCCG, the ATT hopes to be able to assist with resolving any issues that arise as soon as possible.

We would be interested to hear of any issues our members experience with their clients and this new strengthened self-employment test for WTC.