

The Government has already taken action to help people through the current global economic difficulties. Building on this, the Government announces further packages of targeted support, providing additional help to those who need it most now.

To provide additional support for low- and middle-income taxpayers, the Government will:

- **make permanent the £600 increase in the income tax personal allowance announced in May 2008 with a further increase of £130, meaning basic rate taxpayers pay £145 less tax a year in 2009-10.** The Government is also taking measures to consolidate the public finances. The combined effect of all its reforms should mean that taxpayers with incomes below £40,000 will pay less tax and national insurance contributions in April 2011 compared to April 2008;
- **bring forward April's increase in Child Benefit to January**, worth an additional £22 on average to families; and **bring forward its commitment to increase the child element of the Child Tax Credit by £25 above indexation in April 2010 to April 2009** meaning it will increase by £75 above indexation to £2,235 in April 2009; and
- **pay £60 to all pensioners in the New Year** which is equivalent to bringing forward the April increase in the basic State Pension for a single pensioner to January.

This, alongside other measures announced in the Pre-Budget Report, will focus support on those who need it most.

The Government is committed to supporting householders facing financial difficulties. **A new Lending Panel** will improve monitoring of lending to households and businesses, as well as drive up best practice across the mortgage market and promote awareness of initiatives to support households against repossession. Individuals can also expect:

- **help through mortgage rescue and Support for Mortgage Interest schemes for eligible homeowners in difficulty;**
- **a commitment from major mortgage lenders on the Panel not to initiate repossession action within at least three months of an owner-occupier going into arrears; and**
- **free and impartial debt advice through increased Government funding.**

The UK's dynamic labour market leaves it well placed to deal with rising unemployment, with 1.2 million people finding new jobs in the three months to September. To ensure that those facing redundancy and those seeking employment are helped back into work as quickly as possible, the Government announces:

- **an additional £1.3 billion to continue delivering effective support for the unemployed to find a new job;**
- **a National Employment Partnership**, bringing together the Government and major employers to tackle rising unemployment; and
- **refocusing Train to Gain to provide support in pre-redundancy situations, expanding the Rapid Response Service to target small and large scale redundancies and extending Local Employment Partnerships to focus on the short-term unemployed.**

The 2008 Pre-Budget Report also announces further measures to continue the Government's established fairness agenda, including **contributing 50 pence for every pound saved in the Saving Gateway** and **reforms to modernise tax administration and protect tax revenues.**

**5.1** The Government has made significant progress in ensuring that the tax and benefit systems are fair and help people find and stay in work. Central to this strategy is providing the right incentives for individuals to work and save, and reducing child and pensioner poverty. The reforms to date provide a solid foundation for helping individuals and families to get through the current global economic difficulties.

**5.2** However, the Government is determined to provide further help to those most affected now. The Government expects that, over time, the majority of the VAT reduction will be passed on to consumers in the form of lower prices. For those families in most need of support, this temporary reduction is expected to support their finances in the short term in the form of increased purchasing power. For others, where it is saved or used to pay off debt, it will help households to adjust their finances enabling them to fund future spending.

**5.3** Lower commodity prices and easing inflation are set to support real incomes in 2009, while monetary and fiscal policy is responding to support the economy and provide help for people now. This Chapter sets out the Government's plans to support households during these challenging times while also continuing to pursue its established fairness agenda.

#### Supporting motorists

**5.4** The Government is also taking action to support motorists. The 2008 Pre-Budget Report confirms the Government's commitment to reform of vehicle excise duty (VED), including the introduction of new bands in 2009. However, to reduce pressures on motorists during the current economic downturn, no driver will pay more than £5 extra in any given band in 2009, and there will be no significant rate changes until 2010, when no driver will pay more than £30 extra in any given band, and many will see a reduction in tax paid of up to £30. Further details on VED rates and bands are set out in Chapter 7.

### Supporting low and middle income taxpayers

**5.5** Budget 2007 continued the Government's reforms of the tax and benefit system by reducing the basic rate of income tax and increasing support for many low-income households. To provide further support for low- and middle-income households, the Government announced in May an additional £600 increase in the personal tax allowance for 2008-09, providing up to £120 to around 22 million basic rate taxpayers aged under 65. These measures helped those affected by the removal of the 10p tax rate.

#### Further support for basic rate taxpayers

**5.6** The 2008 Pre-Budget Report makes permanent the £600 increase in the personal allowance and the £1,200 reduction in the basic rate limit announced in May, and announces further reforms to personal tax. These changes will provide additional help for low- and middle-income families next year. **In April 2009, the Government will increase the personal allowance by £130 above indexation.** This goes further than the announcement in May, and is on top of the £600 increase for 2008-09. It means 22 million basic rate taxpayers under 65 will pay £145 less tax in real terms in 2009-10.

**5.7** The Government will also maintain the additional £130 of personal allowance in April 2010, continuing this extra support for a further year. The real terms benefit will increase in 2010-11, when the Retail Price Index (RPI) measure of inflation is projected to be negative, as described in box 5.1. To reduce the gain for higher rate tax payers from the real terms benefit of negative inflation on tax allowances and limits, **the basic rate limit will be held at its 2010-11 value in 2011-12.**

## Income tax and NICs changes from 2010-11 onwards

**5.8** As set out in Chapter 2, this Pre-Budget Report sets out measures which put the public finances on a path to achieve cyclically-adjusted current balance and a declining debt to GDP ratio by 2015-16. These measures are a combination of adjustments to both taxation and spending, including reforms to income tax and national insurance contributions (NICs):

- **the income tax personal allowance will be restricted for those with incomes over £100,000 – the two per cent of people with the highest incomes – from April 2010, when the economy is forecast to be growing.** From that level of income, the personal allowance will be reduced at a rate of £1 of allowance lost for every £2 of income over that level until it is halved in value. At this value, the personal allowance will be worth the same as for a basic rate taxpayer. **From £140,000 of income, the remaining allowance will be completely withdrawn at the same withdrawal rate**, so that people with the very highest incomes do not benefit from the personal allowance;
- **a new additional higher rate of income tax of 45 per cent (and 37.5 per cent for dividend income) for those with incomes above £150,000 from April 2011.** This will ensure that people with the very highest individual incomes pay a greater share of their income in tax; and
- **a 0.5 per cent increase in the employee, employer and self-employed rates of NICs from April 2011, alongside an increase above indexation in the point at which individuals start to pay NICs – known as the primary threshold –** so that it is aligned with the personal allowance. This will ensure that the fiscal consolidation is broad based, without affecting those over state pension age, who do not pay NICs. These changes will be introduced from 2011, when the economy is forecast to be growing above trend rates and real incomes are growing strongly.

### Effect of personal tax changes from 2010-12

**5.9** The measures above mean that people with incomes below £40,000 will not pay more income tax and NICs in April 2011 than in April 2008. People with incomes between £40,000 and £100,000 a year will pay slightly more income tax and NICs, around £3 a week on average. Those with incomes between £100,000 and £140,000 will pay around £22 a week more on average in income tax and NICs, while those between £140,000 and £200,000 will pay on average £61 a week, and progressively more as income rises.

**5.10** These reforms, and the measures announced in May, will permanently reduce the number of households paying more net tax as a result of Budget 2007 personal tax changes from 5.3 million originally to 500,000 by 2011-12. As a result of all the measures taken since Budget 2008, in April 2011, 23 million taxpayers with incomes below £40,000 will pay less tax and NICs than in April 2008 in real terms. The increase in the NICs primary threshold and the 0.5 per cent NICs rate rise in April 2011 will reduce the amount of NICs payable by those earning less than £20,000.

**Box 5.1: The effect of negative RPI inflation on the value of tax and benefits**

The Government's economic projections show RPI inflation as negative in September 2009. This means general prices using this measure of inflation are expected to fall. RPI inflation for that month is used to index income tax, tax credits and national insurance allowances, thresholds and limits for 2010-11. September measures of inflation are also used to index social security benefits.

With projected negative RPI inflation, the Government would maintain the cash value of tax allowances and thresholds, and the RPI-indexed social security benefits, consistent with statute. Holding these constant with lower prices means that in 2010-11, their real terms value would rise in relation to RPI, and that people would be better off in real terms. Analysis in real terms shows the effect on tax and benefit changes in terms of people's purchasing power.

The basic State Pension is indexed by RPI inflation or 2.5 per cent, whichever is greater. This means that there will be an even larger real terms benefit for pensioners in 2010-11. Some benefits are uprated by earnings, and negative RPI inflation increases the real terms value of those increases. For 2011-12, when RPI inflation is projected to be positive, allowances, thresholds and benefit levels will be increased from their 2010-11 levels in line with standard indexation. This will maintain the real terms gain from 2010-11 for future years.

## Giving everyone the best start in life

### Tackling child poverty

**5.11** The consequences of child poverty are far reaching and extend beyond the individual, impacting on families, communities, the taxpayer and the economy. This is why the Government remains committed to eradicating child poverty. Since 1998-99 substantial progress has already been made, with 600,000 children lifted out of relative poverty and absolute poverty halved. Measures announced since Budget 2007 will lift around a further 500,000 children out of relative poverty.

### Financial support

**5.12** Especially in these difficult times for the global economy, the Government will continue to increase financial support for children. The tax credits system is already providing an average of £3,400 a year to six million families, benefiting ten million children. The spending increases announced in previous Budgets and Pre-Budget Reports will build on this foundation.

#### From April 2009:

- **the child element of the Child Tax Credit will increase by £75 above indexation to £2,235**, providing additional support to families with low or moderate incomes. This builds on the Government's commitment to increase by £50 above indexation in April 2009 by **bringing forward the Government's commitment to increase the child element by £25 above indexation in April 2010 to April 2009**;
- **Child Benefit will increase from £18.80 to £20 a week for the first child, and from £12.55 to £13.20 a week for subsequent children**, providing further support to all families with the costs of raising children. To provide additional support, **these increases will be brought forward from April 2009 to January 2009**; and
- **the Health in Pregnancy Grant will be introduced at a value of £190 for all women after the 25th week of pregnancy.**

**5.13** Low-income families and children will also benefit from the wider measures on personal taxation and VAT, as well as the uprating of benefits and tax credits above earnings this year and the real terms gains from projected inflation next year. In the light of the wide

range of changes coming into effect in the coming months, the Government will take stock of progress towards its 2010 and 2020 child poverty target in the Budget.

**5.14** Take-up of tax credits is higher than for any previous system of income-related support, with 82 per cent of eligible families claiming what they are entitled to, rising to 96 per cent for those on the lowest incomes. The Government will ensure that as many families as possible take up the available help. **The Government is setting up a taskforce of experts from local authorities and the third sector which will report in spring 2009. It will assist local authorities in further improving take up of tax credits and benefits.**

**5.15** HM Revenue and Customs (HMRC) has rolled out four new services nationally over the last twelve months to assist customers to claim, renew and manage their tax credit awards. These initiatives will help up to 400,000 customers each year get the right tax credits award, and by the beginning of next year around 100 Children's Centres will offer tax credits advice.

**5.16** In May the Government invited views on proposals to further improve the tax credit system,<sup>1</sup> including a series of options to simplify the childcare element of the Working Tax Credit. The Government welcomes the engagement of interested parties. Following input from stakeholders, as part of the Childcare Affordability Pilot **the Government intends to trial making childcare payments that more closely reflect childcare costs at the time they were incurred. Further proposals for childcare reform, updating the Government's ten year framework for childcare policy, will be brought forward in the New Year.**

**Public services** **5.17** The family environment in which children are raised is important and public services play a key role in providing disadvantaged families with opportunities to enhance their life chances and break cycles of deprivation. Looking towards 2020, public services will play an increasingly central role in achieving this sustainable eradication of child poverty. Budget 2008 announced an additional £125 million across the UK for pilots to develop new methods of tackling child poverty. Two have been rolled out already in 18 local authorities including Birmingham, Blackpool and Nottingham, testing the value of having HMRC and Jobcentre Plus advisors based in Children's Centres. Others will begin in January 2009:

- trialling innovative local approaches proposed by local authorities to tackle child poverty in their communities;
- testing whether helping families financially with a Child Development Grant will help them to engage with local services and improve children's outcomes in their early years;
- extending Family Intervention Projects to support an additional 500 families with complex needs; and
- developing new ideas around accommodating teenage parents.

**5.18** The Government is now well on the way to delivering a nationwide network of 3,500 Sure Start Children's Centres by 2010. These centres deliver coordinated, comprehensive family, childcare, health and employment support to all families, particularly reaching out to those families most in need of support.

**Improving the quality of children's housing** **5.19** Eradicating child poverty requires a sustainable strategy that focuses on improving children's life chances as well as tackling material deprivation. Improvements in housing quality will help children achieve their potential in later life. Living in poor quality, overcrowded or temporary accommodation has been shown to have detrimental effects on the physical

<sup>1</sup> *Tax Credits: improving delivery and choice - a discussion document*, HM Treasury, May 2008.

and mental health of children. It has therefore been a key aim of the Government to reduce the number of children living in such conditions.

**5.20** Since 1997 the Government has already reduced the number of children living in bad housing (non-decent or overcrowded homes and temporary accommodation) by over 1.4 million. By 2010 the Government will increase this figure to over two million. Measures announced in the Pre-Budget Report to bring forward spending will accelerate progress in lifting children out of poor quality housing. The £250 million for Decent Homes and £150 million spend for new social housing will help an estimated 9,000 more households with children move into high quality accommodation more quickly. In addition, the £150 million spend for Warm Front programmes will benefit 60,000 households more quickly.

**Child poverty bill** **5.21** Eradicating child poverty requires a renewed approach that makes sustainable progress in improving children's life chances for the longer term. Demonstrating its commitment to this approach, **the Government will introduce a child poverty bill in 2009.** As Budget 2008 set out, the Government is committed to working with stakeholders to develop its strategy and **the Government will launch a consultation asking stakeholders how legislation can best reflect its long-term ambition to eradicate child poverty.**

**Local authorities and regions** **5.22** If child poverty is to be eradicated, it must be a priority at all levels of Government. Central Government has prioritised tackling inequalities through schools funding. Local authorities have a vital role to play by leading local action, developing joined up local strategies and delivering front-line services. Many local authorities have shown their commitment to this by putting child poverty among their top priorities, but more needs to be done. In some cases, local authority distribution of resources to their schools does not fully reflect the distribution of deprivation. The Department for Children, Schools and Families (DCSF) is working with the local authorities concerned in this spending review period to ensure low-income families and their children do not miss out.

**5.23** Local authorities have a key role to play in tackling child poverty and the Government is committed to working together with them and their partners to ensure that issues around child poverty are tackled effectively and the voices of vulnerable families are heard. **The Government will work now to identify more clearly the indicators that impact most directly on child poverty.** It will work with stakeholders to refine the set of national indicators from which local authorities can select child poverty priorities in future. **Building on the progress made to date, the consultation on child poverty legislation will include the role that local authorities have in eradicating it.**

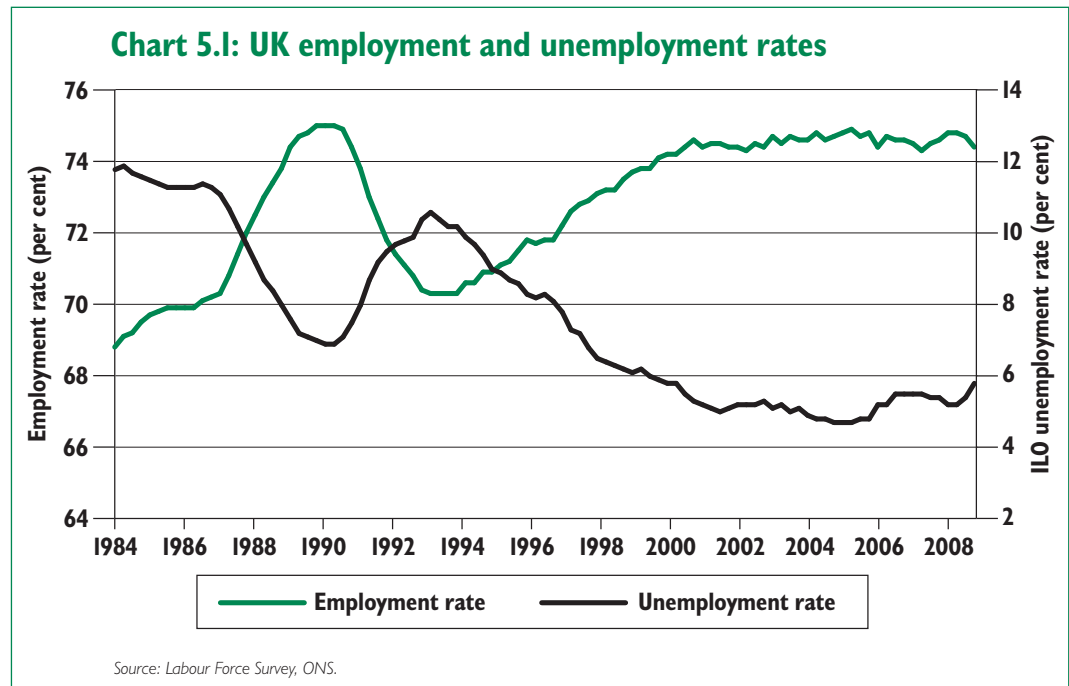
**5.24** While good progress has been made nationally, child poverty in London has fallen by less than elsewhere in the UK. In Budget 2008, the Government asked delivery agencies to collectively identify better ways of working together to tackle child poverty and increase parental employment in the capital. The Government, in conjunction with delivery partners, on 19 November published a document setting out a framework, and key principles, to improve delivery and co-ordination of services in the capital.<sup>2</sup> A wider range of organisations, including employment services, local authorities, health services, and charities have also signed the London Child Poverty Pledge and set out specific actions they will take to improve their services and employment terms.

## Labour market performance

**5.25** The Government's labour market policies are focussed on improving incentives to work and providing active help for people who need it, with a tax and benefits system that

<sup>2</sup>London's children: our future capital, <http://www.everychildmatters.gov.uk>

supports these aims. A series of welfare reforms over the past ten years have led to record increases in employment and falls in the number of people claiming unemployment benefits. It is from this historically strong labour market position that unemployment is now rising as the economy slows. The latest unemployment data, released in November 2008, shows an increase in the claimant count of 36,500 in October and a rise in International Labour Organisation (ILO) unemployment of 140,000 in the three months to September.



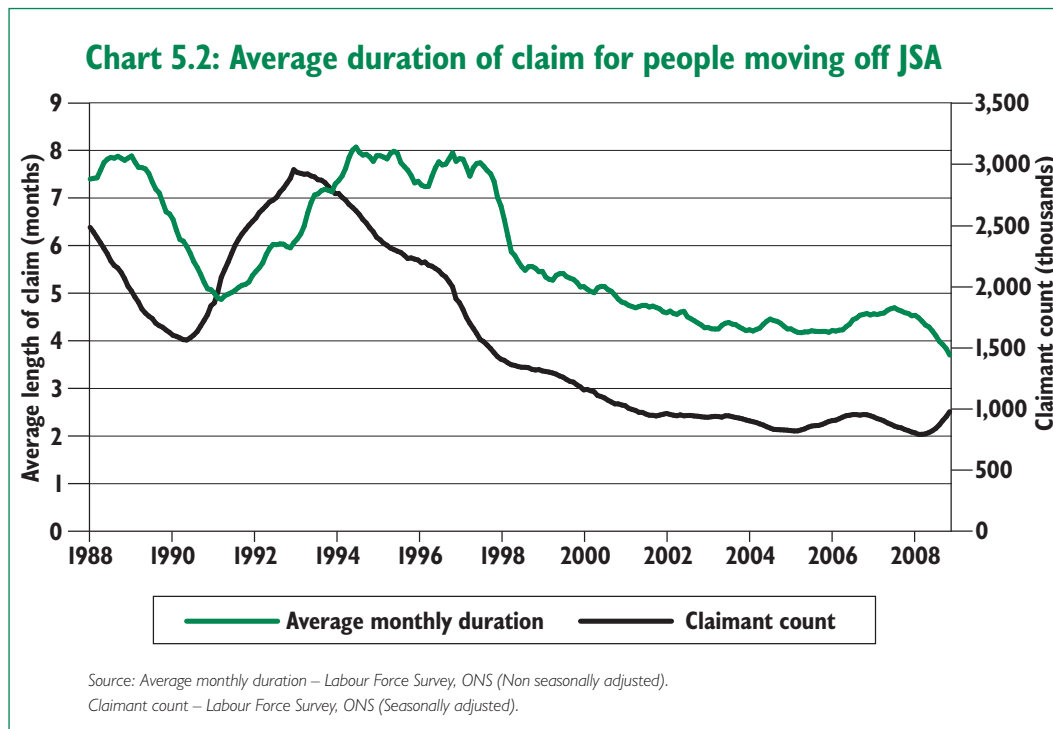
## Responding to the labour market conditions

### Jobcentre Plus support

**5.26** There are real challenges in responding to the current labour market conditions. The UK's dynamic labour market and welfare reforms of the past ten years put the country in a good position to respond to the consequences of the economy slowing. The key to meeting this challenge is to build on the strong foundations that are already in place, focusing support on the interventions that are most effective in helping people move quickly back into work.

**5.27** Reforms to Jobcentre Plus and Jobseeker's Allowance (JSA) since the late 1990s have provided a strong regime that will enable the UK to meet the challenges of rising unemployment. The JSA intervention regime has been successful in ensuring that the newly unemployed find work again, by facilitating and actively supporting swift and effective job matching. As a result, the majority of new claimants find new jobs quickly.

**5.28** With these reforms, the rise in unemployment is now starting from a much lower base than was the case in the previous recession. In addition, unlike during the last recession, off-flows from JSA remain high and there is currently still significant demand for new workers, with over half a million unfilled vacancies in the economy. In the three months to September, 1.2 million people – or four per cent of the workforce – started a new job. Furthermore, as chart 5.2 shows, the average time spent on JSA is short compared with the late 1980s and early 1990s. At 3.7 months, the average for October is broadly consistent across all regions of the UK.



**5.29** The most effective way of limiting a rise in the claimant count is to ensure that the existing regime continues to deliver a rapid return to work for the majority of new claimants. Additionally, the Government is putting in place measures to strengthen support for the newly unemployed, those faced with redundancy and the groups most at risk of being marginalised from the labour market as the economy slows.

### Partnership with employers

**5.30** Efficient matching between jobseekers and vacancies requires effective cooperation between employers, workers and the Government. Partnership working between Jobcentre Plus and employers is already taking place at the local level through the Government's highly successful Local Employment Partnerships (LEPs), in which employers commit to taking on the long-term unemployed. Businesses report that, through LEPs, they have received a much improved recruitment service from Jobcentre Plus. To date, over 70,000 people have found work through LEPs.

### National Employment Partnership

**5.31** The Government intends to significantly expand this successful approach of working with employers, and **is setting up a National Employment Partnership, including Chief Executives from across British business as well as the public sector.**

**5.32** The Prime Minister will chair the Partnership's discussions of how employers will support the Government's efforts to help the rapid re-employment of people facing redundancy. Members of the Partnership will work with the Government to agree what more employers can do to help tackle rising unemployment by helping widen and expand LEPs – such as committing to advertise vacancies through Jobcentre Plus, speeding up recruitment, and enabling greater access to work-related training. Members will work as ambassadors within their respective sectors, and with their supply chains, to engage the commitment of as many employers as possible to offer this support through LEPs.

**5.33** **To support the aims of the National Employment Partnership, this Pre-Budget Report announces a substantial expansion of Jobcentre Plus' local and regional employer engagement capacity** to enable LEPs to focus on the short-term unemployed as well as the harder to help groups.

**Box 5.2: Government support for people facing redundancy**

Many people facing redundancy find a new job even before they are actually made redundant, and most of those who do become unemployed find work again quickly. The Government offers a wide range of support to help people move straight back into work.

Jobseekers are entitled to:

- financial support, through Jobseeker's Allowance, for those who fall out of work;
- personalised jobsearch planning and job-matching, with direct access to vacancies. **The refocusing of LEPs will expand the number and range of vacancies available;** and
- access to intensive support and training for people with difficulty finding suitable work.

In addition, **the Rapid Response Service – which will now be available to small as well as large scale redundancies – offers support for those facing redundancy**, delivered in the work-place:

- help with looking for suitable jobs, including direct access to nearly 400,000 vacancies;
- help with writing a CV, and interview skills;
- a personal analysis of the additional skills or training that might be needed to find work;
- advice and support on self-employment and setting up a business; and
- training for developing the skills to change career path, where necessary. **The extension of Train to Gain will enable individuals to re-train before they are made redundant, to equip them with the skills to move swiftly into a new job.**

**Support for people facing redundancy**

**5.34** As set out in Chapter 4, the Government has already put aside additional money over the next three years to support people faced with redundancy and those looking for work. This additional funding will contribute to the further steps the Government is taking to strengthen pre-redundancy support, which includes:

- **extending Train to Gain programmes to provide training and support to individuals in pre-redundancy situations**, to help them to develop the skills needed to move seamlessly into a new job, either in their existing sector or in a new one;
- **the Government will establish Skills Hubs – networks of local partners providing job brokerage services, training and other support – in response to large-scale redundancies**. Skilled employees in sectors with long term skills shortages will be matched into new jobs to ensure their skills are not lost to the sector;
- **the Rapid Response Service is being further expanded so that support can be made available to smaller redundancies as well as larger ones;** and
- to ensure that every region is well placed to respond to redundancies, **regional Ministers will work with Regional Development Agencies to develop contingency plans to enable coordinated responses to large-scale redundancies, as soon as they are notified.**

**Additional funding for Jobcentre Plus**

**5.35** As well as strengthening partnerships and increasing support, it is critical that Jobcentre Plus is able to maintain its strong record and deliver the core JSA regime effectively for higher numbers of people. This will ensure all claimants continue to get the dedicated support they need to move rapidly back into work. **The Government is setting aside an**

additional £1.3 billion<sup>3</sup> for the Department for Work and Pensions (DWP) over the next two years to deliver effective support for the unemployed.

**Welfare Reform Green Paper** **5.36** Although the key priority in times of rising unemployment must be to prevent short-term unemployment leading to long-term detachment from the labour market, it is important to maintain support for those with greater labour market barriers to prevent them getting left further behind. The last eleven years have seen a transformation from a largely passive welfare state into an active one. The Government will continue to build on this progress, with further radical reforms to the UK welfare system to tackle long-term unemployment and economic inactivity, based on the principles of rights and responsibilities.

**5.37** The Welfare Reform Green Paper<sup>4</sup> set out a radical package of new measures, including further personalised support to help disabled people address the particular barriers to work that they face, piloting 'work for your benefit' programmes for the long-term unemployed and the payment of private and voluntary sector providers who work with long-term Incapacity Benefit claimants for a number of years from benefit savings. The Government has consulted on these proposals and will respond shortly.

## Supporting working households

**5.38** The Government recognises that working households are facing uncertainty in the current economic climate. In addition to the employment package set out in this Chapter to respond to labour market conditions, the Government will continue to take action to make work pay by improving incentives to participate and progress in the labour market. Through the Working Tax Credit (WTC) and the National Minimum Wage (NMW), the Government has boosted in-work incomes, improving work incentives and tackling poverty among working people.

**Working Tax Credit** **5.39** The WTC provides financial support to working households on low incomes. In April 2008, 1.7 million working families and 375,000 working households without children were benefiting from the support it provides. To ensure work continues to pay, **the Government will maintain the childcare element of the WTC and uprate all other elements in line with RPI.** To ensure that all people on low incomes will benefit from the uprating of WTC, **from April 2009 the disregard for tax credits in Housing Benefit will increase by RPI.**

**Take-up of Working Tax Credit** **5.40** The Government is also taking steps to ensure that childless workers claim and receive the support they are entitled to. Since last year, HMRC has been working in partnership with other organisations to promote WTC in innovative ways. They are currently reaching over 500,000 employees at 40 organisations. **In the coming year HMRC will aim to double this coverage, working with employers' Corporate Social Responsibility programmes and using the National Employment Partnership to raise employers' awareness of the WTC.** HMRC will also work alongside Jobcentre Plus, ensuring that people who find employment receive integrated advice on the support available.

**National Minimum Wage** **5.41** The NMW ensures a fair minimum rate of pay while retaining flexibility for employers. The Government, accepting the recommendations of the independent Low Pay Commission, increased the adult rate of NMW to £5.73 from 1 October 2008, the development rate for 18-21 year olds to £4.77, and the youth rate for 16-17 year olds to £3.53.

**Tackling the unemployment trap** **5.42** The unemployment trap occurs when those without work find the difference between in-work and out-of-work incomes too small to provide an incentive to enter the labour market.

<sup>3</sup>As set out in table B5, £800 million of this will be funded via the 2008 Pre-Budget Report scorecard. The remainder will be funded from DWP's stock of money not spent in earlier years.

<sup>4</sup>No one written off: reforming welfare to reward responsibility, DWP, July 2008.

Table 5.1 shows that, since the introduction of the NMW in April 1999, the Government has increased the minimum income that people can expect when moving into work which has increased the gains to work and reduced the unemployment trap.

**Table 5.1: Weekly minimum income guarantees (MIGs)**

|  | April 1999 | April 2009 | Percentage increase in real terms <sup>2</sup> |
|--|------------|------------|--|
| Family <sup>1</sup> with 1 child, full-time work | £182       | £304       | 29%  |
| Family <sup>1</sup> with 1 child, part-time work | £136       | £236       | 34%  |
| Single person, 25 or over, full-time work        | £113       | £196       | 34%  |
| Couple, no children, 25 or over, full-time work  | £117       | £231       | 52%  |
| Single disabled person in full-time work         | £139       | £244       | 35%  |
| Single disabled person in part-time work         | £109       | £176       | 24%  |

*Assumes the prevailing rate of NMW and that the family is eligible for Family Credit/Disability Working Allowance and Working Tax Credit/Child Tax Credit. Full-time work is assumed to be 35 hours. Part-time work is assumed to be 16 hours.*

<sup>1</sup> Applies to lone parent families and couples with children alike.

<sup>2</sup> RPI growth is taken from HM Treasury's economic forecasts.

**The poverty trap 5.43** The poverty trap occurs when those in work have limited incentives to move up the earnings ladder because it may leave them little better off. Marginal deduction rates (MDRs) are one measure of the extent of the poverty trap. They show how much of each additional pound of gross earnings is lost through higher taxes and withdrawn benefits or tax credits. Budget 2007 noted that there are a number of limitations to MDRs as a measure of incentives to progress. In particular, MDRs are calculated with respect to an additional pound earned whereas most evidence shows that in-work labour market transitions are much more substantial, for example, movements from part to full-time working.

**5.44** Table 5.2 shows the reduction in the number of families facing MDRs in excess of 70 per cent as compared to 1997. Increased numbers facing MDRs between 60 and 70 per cent are primarily due to the extension of financial support to a greater number of families through tax credits, including, for the first time, support for families without children. In 2009-10 there will be a smaller increase in the number of families who may face MDRs above 70 per cent. This is largely due to the introduction of a disregard for Child Benefit in Housing and Council Tax Benefits from October 2009. This contributes to a package of measures since Budget 2007 that is expected to lift around 500,000 children out of poverty. The disregard delivers an improvement in in-work incomes, and so incentivises work, for all low-income families facing withdrawal of Housing Benefits under the 2008-09 benefit system. In practice, such families will face increased MDRs over relatively short income intervals, meaning MDRs may exaggerate any changes in effective incentives to progress.

**Table 5.2: The effect of the Government's reforms on high marginal deduction rates**

| Marginal deduction rate <sup>1</sup> | Before Budget 1998 | 2009-10 system of tax and benefits |
|--------------------------------------|--------------------|------------------------------------|
| Over 100 per cent                    | 5,000              | 0                                  |
| Over 90 per cent                     | 130,000            | 60,000                             |
| Over 80 per cent                     | 300,000            | 225,000                            |
| Over 70 per cent                     | 740,000            | 305,000                            |
| Over 60 per cent                     | 760,000            | 1,960,000                          |

<sup>1</sup> Marginal deduction rates are for working heads of families in receipt of income-related benefits or tax credits where at least one person works 16 hours or more a week, and the head of the family is not receiving pensioner or disability premia.

Note: Figures are cumulative. Estimates for the 2009-10 system of taxes and benefits are calibrated to tax credits statistics for April 2008, and earlier data for Housing and Council Tax Benefits. The estimates make explicit allowance for families newly entitled to Housing and Council Tax Benefits from October 2009, but any such estimates are subject to significant uncertainties, in particular concerning likely take-up.

### Reform of Housing Benefit

**5.45** The Housing Benefit (HB) review, announced at Budget 2008, is now underway. It is focussing on ensuring work incentives are protected and that the system represents better value for money for the taxpayer. The review covers those of working age in both the private and social rented sector. The current HB rules for those in the private rented sector can result in claimants living in properties that cannot be afforded by their working peers on a low income. The review is therefore looking at ways to ensure households receiving HB are no better off than working households in the same area who are not receiving HB.

### Local housing allowance

**5.46** The Local Housing Allowance (LHA), introduced in April 2008, is a flat rate of HB based on the area in which the claimant lives and family size. The Government is concerned that the costs of the LHA are greater than had been anticipated. **From April 2009, the maximum amount of LHA that can be received will be the five bedroom rate**, and the Government will be urgently looking at the scope to constrain these costs.

## Helping homeowners and first time buyers

**5.47** The housing market has recently experienced significant challenges as a result of turbulence in the global financial markets. However, the long-term challenge remains to meet the housing needs of an ageing, growing population, while helping families and first time buyers priced out of the property market. The Government is committed to promoting the long-term stability of the housing market and meeting the long term challenge of increasing the housing supply, including through releasing more public sector land for housing, while providing support to homeowners through these difficult times.

### Support for homeowners in difficulty

**5.48** In September, as part of a £1 billion package to support homeowners, first time buyers and the house building industry, the Government announced a new suite of mortgage rescue schemes, which aim to reduce by up to 6,000 the number of repossessions of vulnerable households over the next two years. The Government also strengthened the Support for Mortgage Interest system by reducing waiting times and increasing the maximum value of eligible mortgages, which could prevent up to a further 5,000 to 10,000 repossessions. The 2008 Pre-Budget Report takes further steps to support homeowners facing difficulties.

**Box 5.3: Supporting homeowners in financial difficulty**

The Government is committed to providing additional support for those facing financial difficulties in order to help protect households against repossessions. Individuals can expect:

- the Government to provide direct support to vulnerable individuals through the recently announced mortgage rescue scheme. **This new scheme will be extended to include second charge mortgages;**
- the Government to provide direct support to some individuals through the Support for Mortgage Interest regime which has been strengthened following reforms in September;
- fair treatment by lenders, who will only move to repossession as a last resort. **The major lenders are committed not to initiate repossession proceedings within at least three months of an account going into arrears, and will work to develop creative and sustainable solutions to help borrowers stay in their homes;**
- support from mortgage lenders who will do everything possible to restructure payments, including providing payment holidays, and adjusting the terms of the mortgage – taking into account borrowers' individual circumstances; and
- access to high quality information and independent debt advice at the earliest possible opportunity. **The 2008 Pre-Budget Report announces an extension of debt advice services.**

**5.49 The Government announces the creation of a new Lending Panel.** Reporting to the Chancellor of the Exchequer and the Secretary of State for the Department for Business, Enterprise and Regulatory Reform (BERR), the Panel will monitor lending to both businesses and households. The Panel will bring together lenders (including banks, building societies and specialist lenders), trade bodies, consumer groups, and the Government, regulators and the Bank of England. On lending to small businesses, the Panel will incorporate the activities of the Small Business Finance Forum, which had its first meeting on 11 November. With respect to mortgage lending, the Panel will:

- establish a reporting framework to allow improved monitoring of the mortgage market;
- encourage the highest standards of industry best practice in supporting borrowers with mortgage repayment problems, consistent with statutory regulation; and
- promote better awareness of industry and Government initiatives to find alternatives to repossession and allow borrowers in financial difficulties to remain in their homes.

**5.50** The Government is committed to ensuring that the right framework is in place to help homeowners facing financial difficulties. In order to strengthen the framework of support for borrowers:

- as previously announced, **the Government will bring forward a consultation on extending the scope of FSA regulation to include the sale and rentback market;** and
- **the Office for Fair Trading will bring forward sector guidance early next year to help ensure that second charge lenders do everything possible to treat customers sympathetically and only repossess as a last resort.**

The Government will continue to keep the framework for consumer protections in the mortgage market under review.

**5.51** Supervisory and enforcement action to ensure lenders treat borrowers in arrears fairly remains a critical priority for the FSA. The FSA will also continue to keep its regime for borrowers, including those facing repayment problems, under review.

**5.52** On 22 October the Master of the Rolls approved a new protocol for mortgage possession cases, setting out the steps that judges will expect any lender to take before starting a claim. In October and November respectively, the Council of Mortgage Lenders and the Finance and Leasing Association published best practice guidance to ensure lenders continue to provide a fair deal for borrowers, including providing borrowers with early access to debt advice, and considering the full range of options to help borrowers stay in their homes. The aim is to ensure lenders have done everything possible to avoid repossession if a case comes to court.

**5.53** **The major mortgage lenders on the new Panel have confirmed that they will adopt the best practice of the leading lenders for the coming year and not initiate repossession action for at least three months after the owner-occupier is in arrears.** This moratorium will of course be subject to the wishes of the individual borrower, and does not apply in cases of fraud. This commitment gives both lender and borrower time to consider properly the options available and to find, where possible, a sustainable solution. The commitment will be kept under review and is intended to drive up best practice across the market.

**5.54** The Government intends to discuss urgently with the Lending Panel further actions to help ensure that those who are in work, but facing difficulties, can remain in their homes. Mortgage lenders will continue to explore with borrowers in difficulty all appropriate options to avoid repossession. The major mortgage lenders participating in the Lending Panel are committed to working individually and through the Panel to develop creative and sustainable solutions that will help borrowers stay in their homes, including giving their full support to mortgage rescue products (including shared equity).

**5.55** The Government will provide direct support to individuals through the recently announced mortgage rescue scheme, which will help up to 6,000 vulnerable borrowers facing repayment difficulties remain in their homes. **This new scheme will now be extended to include second charge mortgages, in order to help more vulnerable households.**

**5.56** The Government will also provide direct support to individuals through the Support for Mortgage Interest scheme. The Government has already announced reforms in September, which will strengthen the system of support for new claimants of working age by reducing the waiting period from 39 to 13 weeks, and raising the capital limit to £175,000. **The Government will increase eligibility for this support by raising the capital limit further to £200,000. The Government will also maintain the level of support at the current interest rate for the next six months for existing claimants so that net support to such claimants is increased.**

#### **Social rented homes**

**5.57** As well as supporting households facing difficulties meeting mortgage costs, the Government remains committed to increasing the supply of affordable and social housing. The September housing package, announced additional support to sustain delivery of social homes, bringing forward £400 million of spending to help provide up to 5,500 new social rented homes over the next 18 months. **As part of a broader fiscal stimulus package, the Government will bring forward a further £775 million of housing and regeneration investment, including £575 million to provide additional support for social rented homes, with £150 million to support delivery of new social housing, £250 million to sustain and accelerate the Decent Homes programme and £175 million on major repairs.** [0320]

#### **First time buyers**

**5.58** Since 1997 110,000 households have been helped into home ownership through shared equity and shared ownership schemes. In September the Government announced

further support for first time buyers, offering 10,000 more people the opportunity to purchase a home through a new shared equity scheme. The Government also announced a one year stamp duty holiday for all purchases of houses costing up to £175,000.

**Long term fixed-rate mortgages 5.59** At Budget 2008 HM Treasury published *Housing Finance review: analysis and key proposals* which identified a number of key challenges for the UK mortgage market. Since then, countries around the world, including the UK, have experienced instability in financial markets. Budget 2008 invited views on options to deliver more affordable long-term fixed rate mortgages. Unlike many other countries, there is very little mortgage debt in the UK with the interest rate fixed for more than a few years. Long term fixed rate mortgages can bring benefits for some borrowers by protecting them from unexpected interest rate rises. The Government recognises the merits of promoting a deeper market in longer-term fixed rate mortgages in the longer term and will continue to work with stakeholders and experts on how this may best be achieved.

**Crosby Review 5.60** In April 2008 the Chancellor invited Sir James Crosby to advise the Government on options to improve the functioning of mortgage finance markets. Sir James's interim analysis was published on 29 July, and his final recommendations are published alongside the 2008 Pre-Budget Report. The Government welcomes the publication of the report and thanks Sir James for the considerable work he has undertaken since the summer.

**5.61** The financial markets have experienced instability in recent months. In response, the Government implemented the bank recapitalisation scheme and the Credit Guarantee Scheme, as described in Chapter 3, to restore liquidity to the financial markets and increase confidence in banks with the purpose of enabling them to continue to fund the needs of businesses and customers. In devising the Credit Guarantee Scheme, which makes available to eligible financial institutions a Government guarantee to refinance maturing debt, the Government was informed by and benefited from Sir James's analysis. Box 5.4 summarises Sir James's findings and recommendations. Sir James finds that the closure of the securitisation market and the pressures on banks to deleverage could reduce severely the availability of mortgage finance in 2009 and 2010. Sir James's principal recommendation is that the Government should support the mortgage market by providing, for a temporary period, guarantees on the interest and principal of high quality mortgage-backed bonds backed by lending for new housing transactions.

**5.62** The Government shares concerns about the availability and cost of mortgage finance to homeowners in the future, and has taken steps to help banks continue to lend, including supporting the Special Liquidity Scheme, the bank recapitalisation plan and the Credit Guarantee Scheme. In the case of RBS, Lloyds and HBOS, where the Government is expected to take a significant shareholding, these banks have made commitments to the Government to support the mortgage market going forward. It is not yet clear how far the measures recently taken will mitigate the risks to the mortgage market which Sir James highlights in his report.

**5.63** To implement Sir James's recommendation, the Government would need to obtain State Aid approval from the European Commission and resolve a number of technical and practical considerations. The Government:

- supports Sir James's encouragement of new industry standards on transparency and standardisation;
- supports ongoing dialogue on the issue of the application of fair value accounting principles; and
- will now proceed to work up a detailed scheme based on Sir James's recommendations and seek State Aid approval to proceed. The Government

will take into consideration the interaction between Sir James's recommendations and the Credit Guarantee Scheme and update on its position by the Budget. It will continue to keep under review what more can be done to ensure the continued supply of secured and unsecured credit in the economy.

#### Box 5.4: Summary of Sir James Crosby's findings

Securitisation markets have been a very important source of finance for mortgage lenders. These markets involve packaging and reselling mortgage assets to investors. Well-functioning securitisation markets have helped to ensure the supply of a wide range of affordable products to individuals and have grown rapidly over the last decade. Following developments in the US sub-prime market, however, there has been a significant reappraisal and re-pricing of risk in financial markets. Securitisation markets around the world have been particularly affected and the UK has been no exception. Primary markets remain effectively closed to new issuance, and secondary markets are illiquid as evidenced by extremely high spreads. The collapse in demand for UK mortgage backed bonds reflects the disappearance of a large proportion of the previous investor base, as well as the reluctance of remaining and new investors to enter these markets. While securitisation markets are expected to recover in time, their closure has significant implications for the UK mortgage market and the macro-economy. Sir James's interim report considered a wide range of proposals made by stakeholders, including market-led initiatives to strengthen the markets over the longer term and a Government guarantee of mortgage-backed debt issued by financial institutions. His final report is published alongside the Pre-Budget Report. In summary, Sir James recommends that the Government should:

- encourage the industry, both domestically and internationally, to adopt new standards of transparency and standardisation in the mortgaged-backed securities market, to help ensure that, as the market recovers, it functions more effectively;
- encourage the International Accounting Standards Board to continue to review the application of fair value accounting to illiquid assets, without compromising the principle of transparent disclosure; and
- consider a temporary guarantee at a commercial rate, of the interest and principal on residential mortgage-backed securities or covered bonds backed by new mortgage lending.

## Helping people manage their finances

**5.64** The Government recognises that in difficult times people can require additional support in managing their finances. The Government wants to support everyone in making informed financial decisions and in accessing help if they need it.

**Debt advice 5.65** The Government is committed to ensuring that every household struggling with debts can access free impartial debt advice and get the help they need. Since April 2006, BERR's face-to-face advice project has helped over 169,000 clients with their debt problems. The Government also provides £2 million funding a year to support telephone debt advice. Building on this, the Pre-Budget Report announces:

- **an additional £5.85 million in funding between November 2008 and March 2011 to increase the provision of free telephone debt advice** which could assist 70,000 people each year with their debt problems;
- **a further £10 million in funding between November 2008 and March 2010 for Citizens Advice Bureaux** to expand local face-to-face advice capacity which could assist a further 335,000 people each year; and

- **the Government will establish an online destination on Directgov which will provide people with free and impartial sources of advice and support.** Information on financial support, along with debt advice, will be further promoted from January 2009, as part of a campaign to promote Directgov services.

**Illegal lending 5.66** Households' ability to access mainstream, unsecured credit may become more restricted in a challenging economic climate. More people may come under greater pressure to use sources of credit they cannot afford, or even turn to loan sharks. Since September 2004, the Government has committed £11 million to tackling the problem of loan sharks. BERR will continue to fund teams to tackle illegal money lending in every region in Britain until March 2011.

**Affordable credit 5.67** Since 2005 the Government has committed £80 million to increase the capacity of third sector lenders, including credit unions and community development finance institutions, to make personal loans. This has enabled over 110,000 affordable loans to be made since July 2006, providing an alternative to high cost credit and loan sharks. In December 2007 the major retail banks made a commitment to support third sector affordable credit, including actions to develop new provision in 25 high priority areas. The Government now seeks to build on this commitment from the banks and ensure that clear plans are in place in each of the high priority areas.

**Money Guidance 5.68** The Government also wants to ensure that people have the support and guidance to help them tackle financial choices. **The Government and the FSA are on track to launch the £12 million Money Guidance pathfinder in the North West and North East of England in spring 2009.** It will target those who are vulnerable to the consequences of poor financial decisions. The service will be available via the internet, phone and face-to-face and aims to reach between 500,000 and 750,000 people.

**Financial inclusion 5.69** The Government remains committed to ensuring that everyone has the opportunity to access the financial services products needed to participate fully in modern-day society and the economy. In December 2007 the Government published *Financial Inclusion: an action plan for 2008-11*, which set out how the Government will use the £130 million Financial Inclusion Fund over the current spending period.

**Saving and asset ownership 5.70** The Government recognises the importance of savings and assets in providing people with independence throughout their lives and security if things go wrong. The Government's savings strategy has focused on seeking to support savings and asset ownership for all across the lifecycle – from childhood, through working life and into retirement.

**5.71** Since 1997 the Government has improved incentives to save by introducing the Child Trust Fund (CTF) and Individual Savings Accounts (ISAs). To support people going forward, the Government now wants to do more to ensure that children are taught about the benefits of saving, to improve incentives for people on lower incomes to save and to consider whether first time buyers need additional tax-free incentives to help them to save for their first home.

**Financial education 5.72** The Government is committed to ensuring that children learn money skills in school. Financial capability and economic wellbeing is now a strand in Personal Social Health and Economic (PSHE) education for the secondary school curriculum in England. In October, the Government announced its intention to make all strands of PSHE statutory, including financial capability, and established an independent review to investigate how to achieve this. Financial education in schools is being supported by an £11.5 million personal finance education package. This will teach children how to open a bank account, understand basic financial

concepts like interest rates and learn important skills to plan for their financial future. A national Money Week will take place in schools in summer 2009.

**Child Trust Fund 5.73** The CTF, introduced in 2005, will ensure that, in future, every child has an asset at the age of 18, regardless of family background. Every child receives a Government contribution of £250 (£500 for children from lower income families) at birth and a further payment when they reach age seven. An important part of the Government's strategy for the CTF is to use it as a tool to make personal finance real and tangible for children. The first children that benefited from the CTF started school last year and teachers are already using the CTF as a way of teaching financial education in maths lessons.

**5.74** The £11.5 million package of support will be used in part to create financial materials based on the CTF, to bring finance to life in the classroom. Further Government contributions into children's CTF when they reach age seven will provide another opportunity for schools to focus on financial education. Combining financial education with the experience of having their own savings product will help children to understand the value of money, help to teach them how to interact with financial services providers, and better equip them to avoid financial problems in later life.

**Saving Gateway 5.75** Since 2001, the Government has been exploring matching – a Government contribution for each pound saved – as an incentive to save for those on lower incomes. Two pilots have taken place confirming the success of matching as a saving incentive and in promoting financial inclusion.

**5.76** Following the success of the pilots, as announced in Budget 2008, the Government is introducing the Saving Gateway nationally, with the first accounts available to savers in 2010. **The Government announces that, to provide a strong and easily understood incentive to save, it will contribute 50p for each pound saved in the scheme.** Around eight million people will have the opportunity to open an account and to earn a Government contribution of up to £300. Saving Gateway accounts will be provided by financial institutions and will be available through the Post Office. The Government also continues to work closely with a range of potential account providers on the design of the Saving Gateway and will publish a summary of responses setting out the final details of the scheme later this year.

**Individual Savings Accounts 5.77** The Government introduced ISAs in 1999 with the aim of extending the saving habit and ensuring a fairer distribution of tax relief. Over 18 million people now have an ISA. Earlier this year the Government made ISAs simpler, more flexible, and extended the ISA allowance to £7,200 of which £3,600 can be held in cash. **The Government is now extending the range of qualifying investments for ISAs to include securities issued by Multilateral Development Institutions.**

**First time buyers 5.78** Many young people already use their ISA allowance to save for a deposit for a house. Following the Government's support for first time buyers in September, the Government is now considering whether it needs to do more to help first time buyers save for their first home. **The Government welcomes views from industry and from individuals on whether creating a new tax-relieved savings scheme targeted at first time buyers would be a helpful step forward.**

**Protecting people's savings 5.79** The Government has also demonstrated its commitment to protecting people's savings by its recent actions in response to problems within the worldwide banking system. The FSA raised the limit for deposits covered by the Financial Services Compensation Scheme to £50,000, meaning 98 per cent of all savings accounts are now covered by the scheme. The Government acted swiftly to ensure that ISA savings that have been invested in Icesave retained their tax-advantaged status.

## Supporting people in later life

**5.80** The Government is committed to tackling pensioner poverty, rewarding saving, and helping people meet their income aspirations in retirement. It does this through providing incentives for people to save, and supporting all pensioners in retirement, with additional support targeted on those who need it most. The Government is also taking forward pension reforms for the long term that will help meet the challenges of an ageing population.

### Financial support for pensioners

**5.81** The Government recognises the importance of continuing to support pensioners appropriately through the global economic downturn and to providing a safety net for the very poorest. To provide additional support for the poorest pensioner households, **the standard minimum income guarantee in Pension Credit will have an above indexation increase, rising by £5.95 to £130.00 a week for single pensioners and by £9.10 to £198.45 a week for pensioner couples.**

**5.82** To support pensioners more broadly, **the level of the full State Pension will rise in line with prices by £4.55 to £95.25 a week in April 2009.** For those women whose entitlement is based on their husbands' pension, the full couples' rate increases to £152.30. In addition, in order to provide further support for pensioners during the economic downturn, **the Government announces that it will make a payment in the New Year of £60 for each pensioner, equivalent to bringing forward uprating of the basic State Pension from April to January.** Around 12.5 million pensioners will benefit. A £60 payment will also be made to 2.5 million individuals who are in receipt of certain other benefits.<sup>5</sup>

**5.83** Winter Fuel Payments of £200 for households with someone over 60, £300 if over 80, have been committed for the lifetime of this Parliament. As announced at Budget 2008, this winter, households with those aged over 60 will receive an additional £50 or £100 for those with someone aged over 80.

**5.84** The Government wants to ensure that all pensioners claim the benefits they are entitled to and are taxed fairly. In October the Government introduced a simplified claims process for eligible pensioners to claim Housing Benefit and Council Tax Benefit alongside Pension Credit. **To support those pensioners who pay income tax, the Government will raise in line with prices the age-related tax allowances in April 2009 to £9,490 for people aged 65 to 74 and to £9,640 for people aged 75 and over.** By April 2010 only 40 per cent of pensioners aged 65 or over will pay income tax.

**5.85** **The Government is launching a campaign to encourage people on low-incomes, in particular pensioners, to register to receive interest on their bank or building society accounts tax-free and to claim back any tax they have overpaid.** The campaign is aimed at around 1.5 million pensioners who could be getting more value from their savings every year by registering to receive their interest tax-free.

### Pension reforms

**5.86** The pension reforms already legislated for will provide a more simple and generous State Pension. From 2010, the number of years needed to qualify for the basic State Pension is being reduced to 30 and the contributory system is being modernised to ensure that carers have improved opportunities to build State Pension entitlements. Building on this, and as announced in October, **the Government will change the class 3 voluntary national insurance contribution rules to allow those reaching state pension age between April 2008 and April 2015 with 20 qualifying national insurance years to purchase up to six additional years from 1975-76. The package is intended to be cost neutral overall and the class 3 rate will therefore rise accordingly to £12.05 a week in April 2009.** The changes will particularly benefit women and carers, and help 110,000 people improve their state pension outcomes. Pensioners and

<sup>5</sup> Eligibility will be the same as for the annual Christmas Bonus.

those relying on savings income will not be affected by the wider changes to NICs set out earlier in the chapter, since employee NICs do not apply to those over state pension age or to income from savings or a pension.

**5.87** The reforms to private pension saving in the current Pensions Bill will mean that for the first time employers will be required to contribute to workers' pensions, providing a clear incentive to save and helping those on lower incomes to build a pension. The package of pension reforms will be supported by an information and communications strategy to ensure individuals auto-enrolled into a pension scheme will have the information they need to make informed pension choices.

**Pensions tax simplification** **5.88** The Government's simplified tax regime for pensions was introduced in April 2006, to help maintain stability and fairness and to encourage long-term pensions saving. Generous tax reliefs, estimated to be worth around £30 billion in 2007-08,<sup>6</sup> incentivise pensions saving and produce an income that lasts across retirement.

**5.89** On the introduction of the simplified pensions rules in April 2006, the Government set a lifetime allowance (LTA) to provide an overall cap on tax-relieved pension savings, set at an initial £1.5 million in 2006-07, rising to £1.8 million by 2010-11. In line with its core principles<sup>7</sup> and to ensure fairness, affordability and sustainability of tax reliefs, **the Government will maintain the LTA at £1.8 million for a further five years, up to and including 2015-16.** This only affects the largest pension pots, those above £1.8 million over this period. **The annual allowance will also be held constant at £255,000.**

**Open Market Option** **5.90** The Government continues to work with industry to ensure that savers are able to get the best annuity deal when they come to draw their retirement income. **Shortly after the Pre-Budget Report, the Government will publish an update on the review of the operation of the Open Market Option,** detailing progress against the recommendations of the review published at the 2007 Pre-Budget Report.

## A MODERN AND FAIR TAX SYSTEM

### Modernising tax administration to support taxpayers

**Review of HMRC powers, deterrents and safeguards** **5.91** The Review of HMRC's powers, deterrents and safeguards continues to take forward a programme of work that will provide greater consistency across taxes; strong safeguards for taxpayers; and a modern framework of law and practice for HMRC. This work will reduce costs for compliant businesses and individual taxpayers by supporting those who seek to comply, while preventing a minority gaining an unfair advantage through not meeting their obligations. **The Government announces that HMRC will set up a new joint forum with representatives from the private sector to oversee the implementation of the legislative outcomes of the Review. Additionally, HMRC is publishing the Review's Work Programme alongside the Pre-Budget Report.**

**5.92** This Pre-Budget Report also announces consultations on:

- **modernising and aligning penalties for late filing of tax returns and late payment of tax and harmonising and simplifying the rules for interest on tax paid late and on repayments of tax overpaid;**

<sup>6</sup>Gross tax relief is estimated at £29.3 billion in 2007-08. Income tax on pensions in payment is approximately £10.4 billion, making net tax relief £18.9 billion.

<sup>7</sup>The Government's principles for the taxation of pensions were set out in the speech by the Economic Secretary to the Treasury to the NAPF Investment Conference, Edinburgh on 15 March 2007.

- **repeal of a number of specialist compliance checking powers which will no longer be needed following Finance Act 2008 and on the application of the new compliance checking framework to other taxes administered by HMRC;** and
- **further changes to make it easier for taxpayers to pay what they owe on time and to support HMRC in effectively tackling those who pay late.**

**A Charter for HMRC** **5.93** An important complement to the Review of HMRC's powers is a clear statement of the principles governing HMRC's relationship with citizens and businesses. HMRC does not currently have a single document that clearly sets out in one place the rights and responsibilities of customers. The Government has, therefore, consulted on the scope of a Charter for HMRC. In the light of responses, published alongside the Pre-Budget Report, the Government has decided to include in next year's Finance Bill a clause giving the Charter explicit legislative authorisation. **The Government announces that it will begin a new consultation in January on the wording of the Charter, and that HMRC and DWP will work towards a joint launch for their respective charters in 2009.**

**Reducing burdens** **5.94** In support of the Government's programme of tax simplification highlighted in Chapter 4, the Government will reduce burdens on employers and the self-employed and make the administration of tax more straightforward by:

- **simplifying the collection of Class 2 NICs, initially by aligning payment dates with those for Self Assessment liabilities, to reduce the number of bills issued, and improving the information provided to contributors;** and
- **simplifying, from April 2011, the Pay As You Earn arrangements for all working students** and reducing burdens on their employers.

In addition, the Government will continue to explore with stakeholders the scope for collecting tax on benefits in kind and expenses through the payroll.

## Protecting tax revenues

**5.95** The vast majority of taxpayers seek to contribute their fair share towards funding public services. The small minority who do not put pressure on the public finances and impose costs on others, undermining fairness and economic performance.

**Tobacco and alcohol strategies** **5.96** **HMRC and the UK Borders Agency (UKBA) are publishing a joint counter tobacco smuggling strategy alongside the Pre-Budget Report.** This explains how, building on successes to date, they will work together to tackle the evolving smuggling threat. **The Government also announces that HMRC, together with the UKBA, will publish a refreshed alcohol strategy by the time of Budget 2009.** This will strengthen the current spirits fraud strategy and extend it to cover all forms of alcohol fraud ensuring that the approach to tackling alcohol fraud and smuggling keeps pace with developments in this area.

**Missing Trader Intra-Community (MTIC) fraud** **5.97** **HMRC is publishing *Measuring Indirect Tax Gaps – 2008* alongside the Pre-Budget Report.** This sets out the latest estimates of revenue losses in VAT and excise duties. Estimates of Missing Trader Intra-Community fraud included in this publication show a further reduction in fraud levels in 2007-08, demonstrating the continuing effectiveness of the Government's anti-fraud strategy. The targeted reverse charge introduced in 2007 has played a key role in driving down MTIC fraud. The Government has applied to the European Commission to renew the reverse charge derogation.

**Offshore disclosure** **5.98** The Government announces that HMRC will be giving offshore account holders a new opportunity in 2009 to disclose, of their own accord, if they have unpaid tax or duties and to settle debts. A further announcement will be made in early 2009.

**Tackling avoidance** **5.99** Avoidance schemes identified by HMRC are unfair on the majority of taxpayers who do pay their fair share. **Since Budget 2008, the Government has taken action to:**

- prevent loss of tax through the leasing of plant and machinery;
- prevent a loss of tax on the sale of a company that is an intermediate lessor of plant or machinery; and
- counter avoidance involving businesses leasing films to others under a long funding lease.

**5.100** The Government will also take action to provide certainty that authorised investment funds cannot be used by financial traders to reduce corporation tax.

**Principles-based anti-avoidance legislation** **5.101** At the 2007 Pre-Budget Report the Government announced it would consult on the possible introduction of principles-based legislation to counter avoidance in the area of financial products. Following that consultation and subsequent work with stakeholders on the proposals, **the Government is publishing a further consultation document, that includes draft legislation on disguised interest and transfers of income streams, with the intention, if appropriate, of introducing legislation in Finance Bill 2009.**

**Change of accounting practice regulations** **5.102** The Government can announce its intention to amend the **Change of Accounting Practice (COAP) Regulations dealing with the taxation of loans and derivatives.** This will prevent future double taxation or double relief under the COAP Regulations with regard to foreign exchange gains or losses on certain foreign currency denominated financial instruments. This measure will apply with effect from 1 January 2009. The Government will publish draft legislation shortly.

**Income shifting** **5.103** The Government firmly believes it is unfair to allow a minority of individuals to benefit financially from shifting part of their income to someone else who is subject to a lower rate of tax, known as income shifting. The Government has consulted on this issue but, given **the current economic challenges, the Government is deferring action and will not bring forward legislation at Finance Bill 2009.** The Government will instead keep this issue under review.

**Tax relief for travel expenses** **5.104** Following the consultation *Tax relief for travel expenses: temporary workers and overarching employment contracts*, the Government has decided to leave the current rules unchanged. However, in the light of evidence from the consultation confirming poor levels of compliance in this area HMRC will refocus its efforts to ensure that the current regime is properly applied. If compliance does not improve, the Government may return to this at a later date.

**False self-employment in construction** **5.105** The Government is concerned about false self-employment within the construction industry. This can result in an unfair commercial advantage and possible exploitation of vulnerable workers. The Government will continue to work with the construction industry and others to find a way to address this problem, taking account of challenges facing the industry and its need for a flexible labour supply.

**REITs** **5.106** **The Government will legislate in Finance Bill 2009 to restore the original objectives of the UK Real Estate Investment Trusts (UK REITs) regime** by preventing groups of companies which own property, but are not property rental companies, from being part of the UK REITs regime unless at least 75 per cent of their gross income comes from the rental of property to tenants.

- VAT anti-forestalling** **5.107** To prevent the creation of artificial arrangements to avoid the return of the VAT rate to 17.5 per cent, **anti-forestalling legislation will be presented to Parliament as part of Finance Bill 2009.**
- Disclosure regime** **5.108** The Disclosure of Tax Avoidance Schemes regime uses scheme reference numbers (SRNs) to identify users of disclosed schemes. Following discussions with business, **regulations will be introduced to simplify and improve the way users report a SRN back to HMRC.**
- 5.109** In April 2008 the Government announced that the Stamp Duty Land Tax (SDLT) disclosure regime would be extended to residential property. **Following consultation, the Government has decided that it will also introduce a means to identify SDLT scheme users.** Draft regulations to this effect will be published for consultation.

## Making a fair contribution

- Income tax and NICs rates** **5.110** For 2009-10 the basic and higher rates of income tax will remain at 20p and 40p respectively. The starting rate for savings income only will remain at 10p and its threshold will be increased by indexation. All NICs thresholds and limits will be increased in line with indexation in 2009-10, with the exception of the Upper Earnings and Profits limits which will be aligned with the higher rate threshold, the level at which higher rate tax starts to be paid. There will be no change to NICs rates for employers and employees in 2009-10, or to the profit related NICs paid by the self employed. Annex B provides further details of rates and allowances. Paragraphs 5.8, 5.9 and 5.10 set out reforms to income tax and NICs for future years.
- Alcohol duty** **5.111** **The Government will increase the overall duty on alcohol from 1 December so that the total VAT and duty remain broadly unchanged following the reduction in VAT to 15 per cent.** The increase in duty will be maintained when the VAT rate is returned to 17.5 per cent in January 2010.
- Tobacco duty** **5.112** Maintaining high levels of tax on tobacco helps to reduce overall tobacco consumption. **Tobacco duties will, therefore, be increased from 6pm on 24 November** to ensure that the overall level of taxation on tobacco remains broadly unchanged following the reduction in VAT to 15 per cent. The increase in duty will be maintained when the VAT rate is returned to 17.5 per cent in January 2010.
- National Lottery** **5.113** Following in depth analysis of the impact of switching lottery duty to a gross profits tax, **the Government announces that it will retain the stakes based system of lottery taxation** due to uncertainty over the likely impact of a change at this time.
- Tax charges on stock lending** **5.114** Current financial instability and related insolvencies could cause some companies which have entered into stock lending arrangements to face tax charges as a result of a borrower's insolvency. In response to this, and subject to appropriate safeguards, **the Government will introduce measures with effect from 1 September 2008 to limit such charges.**
- Further modernisation** **5.115** The Government also announces further measures to modernise the tax system, to support taxpayers and, where appropriate, provide clarification by:
- **extending small business rate relief** by allowing eligible small businesses in England to claim relief from business rates from the day they begin to occupy a new property with a low rateable value;
  - **modifying the tax law relating to trade debt releases** to ensure that releases between connected companies are tax-neutral for both debtor and creditor; and

- **continuing discussions with business on options for changing the corporation tax rules on the late payment of interest between connected parties** before introducing legislation in Finance Bill 2009.

**Charities 5.116** The Government is considering carefully the responses to the recent consultation on the anti-avoidance rules around substantial donors to charity, and will give its detailed response early next year. The Government continues to explore some of the more complex suggestions arising from the 2007 Gift Aid consultation.