

Opportunity and Independence for All

Proposals to Improve the Tax and Benefits System

Policy Paper 7



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Opportunity and Independence

The purpose of taxation is to raise money to create opportunity for all. The purpose of benefits is to distribute that money wisely to reduce disadvantage, and to encourage enterprise and independence.

This paper starts by setting out the prerequisites of a successful tax system:

Fairness: Tax bands, rates and reliefs should ensure that everyone contributes according to their ability to pay and that the overall burden is fairly shared. Liberal Democrats would take some low earners out of the tax net altogether, phase out those tax reliefs and allowances which give greatest benefit to high earners, and establish a more progressive series of tax bands.

Efficiency and Simplicity: Waste and bureaucracy must be reduced, to leave more resources available for investment in opportunity and quality services. Liberal Democrats would reduce bureaucracy by abolishing complex contributions records, combining employees' national insurance contributions and income tax, and simplifying employers' national insurance contributions.

Honesty: Taxpayers should be able to see for themselves how their taxes are being spent. That is why we have made a clear commitment to invest an extra penny per pound of income tax in education. We would rename as a 'pensions payment' the element of integrated income tax with which we would replace employees' NICs, and earmark this payment to pay for state pensions. A separate working group is examining other ways of increasing transparency and obtaining public consent for tax reform.

Sustainability: Taxes should discourage the things the community does not want, like pollution, and encourage the things it does want, such as more jobs. Liberal Democrats would begin a long term shift in the burden of taxation from employment to resource depletion and pollution.

The money raised by a fair, efficient, honest and sustainable tax system must be used to increase independence, enhance opportunity and promote social justice. This is our objective in overhauling the benefits system. We would give priority to the following proposals that aim to help people off benefits into independence, by enabling them to work:

- For mothers, we would retain the universal nature of Child Benefit and increase its value by up to £5 per family per week, paid for from the abolition of the Married Couple's Allowance .
- For parents, we would create a system of childcare vouchers, provided by employers to parents with children under school age. For the long term unemployed, we would expand and improve the working benefit scheme, to help them back into work and give them valuable skills training.
- For people with disabilities, we would establish a new Partial Capacity Benefit, to help those people back into work who would otherwise be unable to support themselves other than from the benefit system.

- For carers, we would transform the Invalid Care Allowance into a new Carer's Benefit, which would allow carers more scope to work without substantial loss of benefits.

We are further committed to cutting waste and bureaucracy, limiting confusion and reducing the poverty trap in ways including the replacement of Family Credit and Income Support with a single means-tested benefit called Low Income Benefit.

Recognising the limitations on resources, we would also look to improve the benefits system in other ways over time, to ensure that poverty ceases to be a barrier to the full opportunities which society has to offer. Liberal Democrats would:

- Make improvements to the scope and level of Housing Benefit, and create a parallel benefit for home owners of Mortgage Benefit, paid for by the phasing out of Mortgage Interest Tax Relief.
- Make improvements to the Social Fund, which is unjust, inconsistent and inefficient.
- Restore the right of young people between the ages of 16 and 18 to Income Support if they are not in work, education or training and not supported by their parents.

Our objective through all those proposals is simple: to establish a fair and effective system of tax and benefits, which opens up opportunities, encourages enterprise and independence, and enables all Britain's citizens to live in dignity.

(Please Note: This paper does not deal with specific tax or benefit rates. The level of taxes and benefits and the timing of changes must be determined in the light of the prevailing economic conditions.)

The Liberal Democrat Vision

1.0.1 Liberal Democrats seek to establish a fair and effective system of tax and benefits, one which opens up opportunities, encourages enterprise and independence, and enables all Britain's citizens to live in dignity. We reject the notion that the tax and benefits system should enforce a moral code concerning the conduct of private lives, but we believe that it does have a role to play in helping families stay together. Our concern is to be honest about taxation, fair in the distribution of benefits and rewarding of individual endeavour.

1.0.2 Taxation is not inherently evil. It is a means of paying for the things all Britain's citizens want: better schools, high quality health care, action to relieve poverty. The burden of paying for these things should be shared by us all, each according to our means. The important thing is to ensure that precious taxpayers' money is not wasted by inefficiency or frittered away on red tape.

To provide high quality public services costs money. Our aim is to say what Britain can afford and what Britain cannot.

1.0.3 The Conservatives used to pretend that taxes could be continuously reduced without any damage to the quality of public services. They forgot what everyone else who pays for prescription charges, season tickets or eye tests knows all too well: *there is no such thing as a free tax cut.*

1.0.4 The Conservatives' dishonesty has been exposed by their broken promises: VAT on heating bills, increased national insurance contributions and frozen personal allowances - income tax hikes by any other name - to name but a few. At the Chancellor's own admission, Conservative tax increases in the 1993 budgets

will amount to the equivalent of 7p on the basic rate of income tax over the next two years.

1.0.5 Labour has largely shaken off its tendency of promising more of everything without costing anything. Now, however, it has swung to the other extreme: too scared to say anything, or even to indicate priorities. Labour in its latest incarnation pretends that all the improvements needed for public services can be achieved without an extra penny being spent.

Our aim is to be honest about taxation and to obtain consent for it.

1.0.6 We will not make promises we know we cannot keep. That is why Liberal Democrats believe that taxation should be open and comprehensible and specific in its purpose. That is why, when we propose to increase taxes, we tell people why we are doing it.

***There is no such thing
as a free tax cut***

1.0.7 The difference between the Liberal Democrats and the two old parties is that, unlike the others, we trust voters to make fair and sensible decisions, given the right information.

Liberal Democrats believe that the tax and benefits system should facilitate independence.

1.0.8 This means:

- *Closer integration between taxation and social security to reduce poverty traps.*

- A *progressive tax system*, which rewards the work that individuals do and asks each to contribute according to ability to pay.
- A *benefits system which encourages, rather than discourages, work*, but which ensures that those who cannot work or are unable to find a job can live in dignity.

Our aim is to provide a universal ‘entry ticket’ to the rights and responsibilities of citizenship.

1.0.9 Under the Conservatives, the welfare state has been targeted for cuts and privatisation. The Conservatives have fuelled the “*I’m all right, Jack*” attitude; increasingly, it is becoming acceptable to ‘opt out’ of responsibility for the fate of one’s fellow citizens. As a result, the welfare state has fallen into disrepute. It is failing the people it is supposed to serve. If people are shut out from the rights and responsibilities of the welfare state then the country’s whole economic well-being and social fabric suffers. The young man found stealing to pay his poll tax is a paradigm of Conservative Britain.

The time has come to reinvent the Welfare State so that Britain becomes a society of opportunity.

1.0.10 The *Opportunity Society* which Liberal Democrats envisage is one in which all people - individuals, families, neighbours and communities - take responsibility for providing support, care and, most importantly, opportunities for their fellows. The *Opportunity Society* we envisage is about

enhancing independence. The *Opportunity Society* we envisage offers individuals not a hand out, but a hand up.

Creating an Opportunity Society is the key to liberating the economic potential of individuals.

That is what this paper is about.

1.1 The Scope of this Paper

1.1.1 *Opportunity and Independence for All, does not deal with specific tax or benefit rates.* The level of taxes and benefits and the timing of changes must be determined in the light of the prevailing economic conditions.

1.1.2. Instead, the paper sets out the Liberal Democrats’ priorities and the structural changes which we believe are necessary to ensure fairness, efficiency, honesty and sustainability. Additionally, the paper aims to give a clear indication of our approach to setting tax and benefits rates at elections and in our alternative budgets.

1.1.3 This paper deals only with direct taxation. Federal Green Paper 32, *Taxing Pollution, Not People* (1993), considers the possibility of raising significant new sources of revenue through indirect taxes based on anti-pollution and energy efficiency and conservation measures. Corporation tax will be considered in the future economics policy paper.

Being Fair, Honest and Efficient

2.0.1 Honesty, fairness and efficiency are our key objectives in reforming the tax system. The way in which people are currently taxed on income - through the two components of national insurance contributions (NICs) and income tax - is dishonest, unfair and inefficient.

- *It is dishonest* because, for example, it enables the Conservatives to claim that they have lowered income tax, without admitting that for some the overall tax on income has increased, as a result of the rise in the standard rate of employees' NICs from 6.5% in 1979 to 10% in 1994.
- *It is unfair* because, for example, it enables some high earners to pay taxes at lower marginal rates than those earning less. This is because NICs are only paid on income below £430 per week.
- *It is inefficient* because, for example, it requires two separate bureaucracies to administer what is essentially a single tax on income.

2.1 Simplifying Tax on Income

2.1.1 Liberal Democrats are determined to simplify taxes on income and end the injustices inherent in the current system. *We are therefore committed to abolishing national insurance contributions and creating an integrated tax on income (replacing NICs and income tax).*

2.1.2 At present, the tax contribution an individual makes in NICs determines whether they are entitled to receive certain 'contributory' benefits, most notably the state pension and Unemployment Benefit. The trouble with this contributory principle is that many of the poorest people - particularly women - are unable to make the necessary contributions. Furthermore, those who do make full contributions have no guarantee

of entitlement to particular benefits. For example, this Government is increasing NICs by 1%, but cutting entitlement to Unemployment Benefit by half. *For these reasons, in 1993, the Party voted overwhelmingly to end the contributory principle (see Federal Green Paper 31, Retirement with Dignity, 1993).*

2.1.3 The objective that lay behind the contributory principle - that people should know how their money was being spent - is, however, valuable and worth preserving. When we integrate income tax and NICs, we will include a component in place of employees' NICs, earmarked to pay for state pensions. This component would be called the *pensions payment*.

2.1.4 *The pensions payment would be a contribution by today's working population to the pensions of today's old people.* As such, it would be the first step in a series of measures to increase transparency in taxation by earmarking taxes to particular purposes (see Appendix).

2.1.5 Abolishing the contributory principle would mean all retired UK residents would receive state pensions, regardless of whether they themselves had paid the pensions payment when they were younger. The pensions payment would *not* be payable by those over sixty. With this exception, however, the tax base for the pensions payments would be the same as that for income tax, greatly reducing administrative costs. Our proposals would mean that:

- *Roughly 50,000 of the lowest paid people would stop having to pay any tax on income.* Pensions payments would start at the same income as income tax (currently £3,445), rather than the low rate for NICs (£2,964).
- *Tax would be levied according to each individual's ability to pay, by phasing out the ceiling on NICs.* It is anomalous (and certainly anti-progressive) for the marginal rate of tax to fall as earnings increase.

- *All income would be treated the same, regardless of its source.* We would make pension payments payable on all income over the starting point for income tax, while protecting those on modest incomes derived in part or in whole from capital (see 2.1.6).

2.1.6 Our proposals would produce a fairer, simpler tax system. Most people would gain from them. Any losses would be reduced by:

- Raising the starting point for higher rate tax.
- Giving a tax credit against taxes on income on the first slice of investment income.

2.1.7 Pensions payments would be payable at a rate closer to the contracted out rate for NICs (8.2%) than the full rate (10%), since employees formerly in SERPS would contribute to private pensions schemes instead. The self-employed should pay the same rates of tax on income and should be entitled to the same pension benefits.

2.2 Reducing Bureaucracy and Helping the Low Waged

2.2.1 *Liberal Democrats would simplify employers' national insurance contributions to reduce the burden of bureaucracy on businesses, help the very low waged and take account of the abolition of the contributory principle.* The way in which employers' NICs are currently structured encourages employers to keep staff on wages below the £57 threshold at which NICs become payable. Such low rates of pay are indefensible for full-time or nearly full-time workers. They are also uneconomic as most such workers would have their incomes topped up by benefits.

2.2.2 We would reform employers' NICs' to make each business' tax liability calculable as a percentage of its total wage bill, rather than on the basis of a contribution for each individual employee. This would have two advantages:

- *First*, it would remove the incentive for employers to keep employees on wages below the thresholds for paying NICs.
- *Second*, it would massively reduce the administrative burden on employers by saving them from having to make an individual calculation for each employee.

2.2.3 Over time, we would aim to shift the burden of taxation from employment to resource depletion and pollution. Extra revenue raised by an EU-wide carbon/energy tax would (after providing for any necessary compensation and grants to encourage energy efficiency) be reinjected into the economy via reductions in employers' NICs (see Sustainable Economics policy paper, 1994).

2.3 Setting Fair Tax Rates

2.3.1 *Our primary objective is to ensure that everyone contributes according to their ability to pay.* At present, the top income tax rate of 40% starts at £27,145 for single taxpayers with no other allowances. This means that some people with incomes under £30,000 are being asked to pay tax at the same marginal rate as really high earners, on salaries in excess of £100,000.

2.3.2 While all rates and bands need to be reviewed from time to time, we do not believe that those earning just over £27,000 should pay significantly more tax. We would ensure that integrated pensions payments did not lead to automatic increases in tax rates on incomes above the current NIC ceiling. To avoid this, we propose three higher rate tax bands - more than three would be over-complicated - with rather smaller steps than the present single jump from 25 to 40 per cent. The first higher rate would start at an income level significantly (not less than £5,000) above that at which the current 40% rate starts. The highest tax rate would not exceed the 60 per cent (inclusive of pensions payments) which operated during most of Mrs Thatcher's premiership, and would only be charged on incomes exceeding £100,000.

Tax: Taking Account of Special Needs

3.0.1 Income tax is not in itself enough to guarantee that everyone pays according to means. A series of nearly 200 allowances and reliefs against income tax, capital gains tax and inheritance tax have developed over the years. Some are necessary because:

- *Either*, they provide incentives to work and reduce bureaucracy by taking those on low incomes out of the tax net altogether (like personal allowances).
- *Or*, they take into account the extra financial burdens which individuals may face as a result of circumstances which are not otherwise accounted for by the benefits system (like relief for blind or partially sighted people).
- *Or*, they give encouragement to activities which are considered to be desirable (like tax relief on savings).

3.0.2 This chapter considers a number of distinct and separate allowances and tax reliefs and examines how each one accords with our aims for the tax and benefits systems set out in Chapter One.

- In those cases which accord with our aims, such as *personal allowances* and *tax relief on savings*, we propose extensions to enable more people to benefit from them.
- In those which do not, such as *Mortgage Interest Tax Relief* and *Married Couple's Allowances*, we propose their replacement with more equitable forms of financial support directed towards meeting real needs.

3.1 Taking Low Earners out of the Tax Net

3.1.1 Taxing people on very low incomes reduces the incentive to work and can force people back into dependence on benefits. Our first priority is to prevent people from being put in the ridiculous position in which they cannot afford to work. *The best way to achieve this is to take very low earners out of the tax net altogether.*

Taxing people on low incomes reduces the incentive to work. We would take very low earners out of the tax net altogether

3.1.2 This, of course, is the purpose of personal allowances. Currently, however, there are two problems with personal allowances:

- They are too small to take enough low earners out of tax.
- They save high earners more money than low earners.

We are committed to addressing this first problem by raising the level at which people begin to pay tax on income (see 2.1.5).

3.1.3 We would address this second problem by transforming personal allowances into tax credits, with the effect of making them more progressive. The current personal allowance

reduces the tax liability of basic rate taxpayers by £861 a year and the liability of higher rate taxpayers by £1,378 a year. A tax credit system gives a flat-rate credit against tax rather than an allowance against income. It therefore reduces the tax liability of higher rate and basic rate taxpayers by the same amount. *The main advantage of this is that higher rate taxpayers would gain only the same benefit from their allowance as basic rate taxpayers gain from theirs.*

3.1.4 A tax credit of £150 could also be used to replace the 20% tax band with two distinct advantages:

- Some people currently paying tax at 20% would no longer pay any tax at all, while others paying at 20% would receive a small benefit.
- The reduction in the number of bands at the lower end of the tax scale would increase simplicity.

We therefore propose to replace the 20% tax rate with an additional tax credit.

3.2 Replacing Mortgage Interest Tax Relief with Mortgage Benefit

3.2.1 Mortgage Interest Tax Relief (MITR) is unrelated to need. It puts pressure on those who would prefer to rent than to buy. It distorts the market in favour of investment in housing rather than investment in industry. It raises house prices. It is expensive. *It is neither fair nor progressive and should be gradually phased out and replaced with something fairer.*

3.2.2 Everyone agrees that MITR should be phased out - housing experts, economists and even the Government - yet, when Liberal Democrats have been honest and said so, the Conservatives have attacked us. Now they are quietly phasing it out themselves, restricting it to 20% from April 1994 and to 15% in 1995.

We would continue the process, moving towards abolition in measured steps.

3.2.3 We do not believe that it is the place of the tax or benefits systems to distinguish between tenures. *Consequently, we would extend Housing Benefit to cover mortgage interest as well as rent.* We endorse proposals by the Institute for Fiscal Studies for the introduction of a Mortgage Benefit, paid for from part of the savings on MITR (see section 4.1).

3.3 Easing the Financial Pressures on Families

3.3.1 The increase in family breakdown - often as a result of poverty - is causing widespread concern. Liberal Democrats are determined that the tax and benefits system should be used to ease the financial pressures on families, targeting support on those caring for children. *We are therefore committed to increasing Child Benefit by £5 per family per week (see 5.1.1), funded by phasing out the indiscriminate Married Couple's Allowance.*

3.3.2 Married Couple's Allowance gives beneficiaries an additional allowance of £1,720 a year of tax-free income. The allowance is unrelated to the needs of families or children. It gives the same benefit to a well-off, childless couple with a dual income as to a family with two children and one working parent. The allowance is an out-dated relic from the days when a husband was taxed on his wife's income as well as his own. It contravenes the principle that marriage should be tax-neutral and we therefore reaffirm our commitment to phase out the Married Couple's Allowance for those below pension age.

3.3.3 The Conservatives have already restricted the allowance to 20% in 1994 and 15% in 1995. We call upon the Government to come clean about its intentions, to give people the opportunity to plan for the future. Liberal Democrats urge the Government to use the money saved from phasing out Married Couple's Allowance to give real and

meaningful financial support to those caring for children.

3.4 Encouraging Saving

3.4.1 *We believe that the tax system should encourage saving, so as to maintain and improve levels of investment throughout the economy.* Reliefs given to schemes such as PEPs and TESSAs probably do little to increase net saving, however, instead merely diverting savings from less tax-effective forms of investment.

3.4.2 *We recommend the replacement of these reliefs with a tax credit (see 3.1.4) against the first slice of tax due on all investment income.* This would encourage small savers and would help to offset the effect of the pensions payment on investment income. We would retain tax relief on pension schemes.

3.5 Gifts and Inheritances: Taxing According to the Ability to Pay

3.5.1 We believe that, in general, it is right to tax transfers of wealth, although we make exceptions for ordinary gifts and transfers between spouses and to charities.

3.5.2 We would, however, reform the way in which tax on gifts and inheritance is levied, with the aim of reducing taxes on small gifts or inheritances, but ending the avoidance of inheritance tax by those who can afford to make large lifetime gifts. We would:

- *Replace the present, ineffective inheritance tax with an accessions tax, which is a tax charged not to the person who has died, but to the recipient.*
- *Tax gifts as income, if they exceed an annual exempt amount.*
- *Tax inheritances, in such a way that beneficiaries from inheritances could offset accessions tax against unused past (and possibly future) tax exemptions.*

3.5.3 We would give relief, up to an appropriate limit, from tax on inheritance of business assets, including agricultural land and shares in a family company, to prevent a forced sale of these assets. We do not propose that the relief be an absolute exemption (as at present), but a deferment of tax liabilities until the asset is sold, subject to a similar ‘rollover’ relief to that available with capital gains tax.

Benefits: Meeting Basic Needs

4.0.1 This Chapter is about reforming and updating the benefits system. And after fifteen years of mutilation by this Government, it is in desperate need of reform. Rather than being a springboard which people can use to escape to independence, the benefits system has become the trap which imprisons people in poverty and unemployment. It is:

- *Over-complex*, excluding some people from benefits which are really needed, while imprisoning others in severe poverty traps.
- *Discriminatory*, failing to address the basic needs of large sections of the population.
- *Expensive*, so that the costs of administration and policing reduce the money available for benefits themselves.

Our objective in proposing reforms to the benefits system is to make it easier to understand, easier to claim, easier to escape from, easier to administer and open to all.

4.0.2 To these ends, this chapter proposes:

- *The restoration of Income Support entitlement for those between the ages of 16 and 18, if they are not in work, education or training and not supported by their parents.*
- *The restoration of the full Income Support rate to those between the ages of 18 and 25.*
- *An additional element to top up the basic state pension, payable to those in most need. This proposal has already been endorsed by Party Conference in Federal Green Paper 31, Retirement with Dignity (1993).*
- *Improvements in the scope of Housing Benefit, to include those who buy as well as those than rent.*

- *Restoration of the death grant* (recoverable from sufficiently large estates), and the *maternity grant*, to be funded from *an improved Social Fund*.
- *Retention of current Unemployment Benefit* entitlement and opposition to the proposed Job Seekers' Benefit.
- A benefit transfer scheme to help the long term unemployed back into work.
- The creation of a comprehensive framework of *financial support for people with disabilities*.
- *A simplified Low Income Benefit to replace Family Credit and Income Support*, thus reducing confusion and the problems of poverty traps.

4.0.3 In Federal Green Paper 11, *Common Benefit* (1989), we proposed the longer term objective of creating a partial basic income or citizen's income. Section 4.6 reexamines the cases for and against such a scheme.

4.1 Improving Housing Benefit and Extending it to Home Owners in Need

4.1.1 There are enormous regional variations in housing costs: the rent on a flat in central London may well be three times as much as that for a similar flat in Manchester or Cardiff. Since housing costs take up a large proportion of the income of low income families, it is essential that these huge regional variations are reflected through the benefits system. Liberal Democrats therefore reaffirm our commitments to:

- *Retain Housing Benefit* and, subject to available resources, make the taper (the rate

- at which the benefit is withdrawn as income increases) gentler.
- *Work towards the abolition of overlapping tapers* between Housing Benefit and other means-tested benefits, which are equivalent to very high marginal rates of tax.
- *Restore entitlement to Housing Benefit* to students, including postgraduates, and 16 and 17 year olds.

4.1.2 *Liberal Democrats do not believe that government should discriminate between different forms of tenure.* Housing Benefit is only available to those who rent. Home owners get Mortgage Interest Tax Relief instead. This relief gives indiscriminate subsidies to all home owners, regardless of need, yet fails to provide meaningful support to those home owners on low or substantially reduced incomes.

4.1.3 *Liberal Democrats propose to rectify this problem by introducing a new Mortgage Benefit - a form of housing benefit for home owners.* The Mortgage Benefit would be organised on a similar basis to Housing Benefit, keeping administration costs to a minimum and enabling speedy implementation. In time, the two benefits could be merged into a single, unified system for home owners and tenants. The Mortgage Benefit would provide 100% assistance with mortgage interest (subject to a ceiling) for home-owning families on Income Support and others on similarly low incomes. Other low income home owners would also be eligible for assistance but subject to the same 65% tapers as currently apply to rent rebates under Housing Benefit.

4.1.4 The cost of such a scheme could be funded from the revenue saved by phasing out MITR. Under the new Mortgage Benefit scheme those mortgage holders in the greatest need would receive more support than they do at present from MITR.

4.2 Improving the Social Fund

4.2.1 Few aspects of the benefits system have caused as much dissatisfaction as the Social Fund, with good reason. Its failings are numerous:

- *There is no real distinction in terms of need between successful and unsuccessful applications to the Fund* (the conclusion of both the Social Security Advisory Committee and Social Policy Research Unit at York University).
- *The region in which an applicant lives is as likely to determine the outcome of a claim as the merits of the case.*
- *The grounds for the rejection of applications are often scandalous,* not least the grounds that an applicant is unlikely ever to be able to repay the loan.
- *Terms for loan repayments are too harsh* and require repayment to be made too rapidly.

Mortgage Benefit, housing benefit for home owners, ensures that help gets to the households in greatest need, whether they rent or own their home.

4.2.2 These problems are primarily caused by a lack of money. We believe that increasing the Social Fund's budget should be a high priority for any government. New funds should be used to address the problems above. Liberal Democrats would:

- *Introduce specific criteria of eligibility for special grants for particular items,* with a smaller discretionary element on top, to allow for unusual circumstances.
- *Ease the repayment terms* and make loans available to pay rent deposits.
- *Increase the contingency reserve,* so that the area in which a person lives does not

- determine whether, for example, they have a bed or a cooker.
- *Provide grants for 'major life events', such as moving house or having a child, including the restoration of the maternity grant.*

4.3 Guaranteeing Support for Unemployed People

4.3.1 The Government plans to abolish Unemployment Benefit and replace it with a Job Seeker's Benefit incorporating Income Support. Liberal Democrats reject the implication behind the name of the new benefit which is that people who are unemployed are not looking for jobs. The practical effect of replacing Unemployment Benefit with a Job Seeker's Benefit will be to reduce the period during which those in receipt of Unemployment Benefit are entitled to its higher disregards. The Conservatives claim to believe in the contributory principle, but the Job Seeker's Benefit will unilaterally alter the 'insurance' contract.

4.3.2 *We believe that Unemployment Benefit should be kept separate from Income Support, at least until such a time as the former's higher rates and disregards can be aligned with those of the latter, so that the long term unemployed are no longer penalised.*

4.3.3 If the Job Seeker's Benefit is to be introduced, its administration must seek to balance the duty of unemployed people to look for work against the duty of the state not to use starvation as an instrument of policy. Liberal Democrats would find it unacceptable, for example, for an illiterate person to be asked to produce a written record of job applications or for an asthmatic to be required to work as a painter. Those who are penalised must not be left without a safety net.

4.3.4 We would not limit the number of hours which could be spent in education, training or voluntary work whilst in receipt of Job Seeker's Benefit, so long as such activities could be terminated at reasonable notice or continued in parallel if a job opportunity arose.

4.3.5 We endorse the proposal in the forthcoming Employment Policy Paper (1994) to introduce a benefit transfer scheme to help the long term unemployed back to work. The proposal would enable someone out of work for more than six months to have their benefits transferred to an employer who recruited them, to help pay the new employee's wage for a period of up to two years. The employer would be required to provide training as well as employment.

4.4 Improving Benefits for People with Disabilities

4.4.1 *Liberal Democrats have long argued for improvements to benefits for people with disabilities. The new Incapacity Benefit is, however, a retrograde step.* If it is introduced as currently proposed, eligibility will be determined using tests which show no understanding of disability or chronic illness:

- The tests are not to be undertaken by medically-qualified staff.
- They take no account of pain caused by performing a task.
- They assess only whether an activity can be undertaken once, not repetitively as is the case in most jobs.

4.4.2 We will press for incapacity tests to be related to work that the person might have had the ability to undertake were they not incapacitated. We oppose the use of the test in cases of mental illness.

4.4.3 *In power, we would abandon the Incapacity Benefit altogether.* We would simplify benefits for people with disabilities, to take account of the severity and cost of disability, and to ensure that everyone can afford to live with dignity and, where practicable, independently.

4.4.4 We believe that there are three elements necessary to provide comprehensive financial support to people with disabilities:

- A *Disablement Costs Allowance*, to help compensate people for the costs of disability, replacing Disability Living Allowance.
- A *Disablement Pension*, to provide support for those of working age but unable to work. (It would replace Invalidity (or Incapacity) Benefit and Severe Disability Allowance.)
- A *Partial Capacity Benefit* to provide financial incentives to work for those capable of limited employment.

4.4.5 The *Disablement Costs Allowance* would be payable on the basis of severity of disability, not according to means or cause. It would help provide compensation for the actual costs of disability rather than pain caused, and would not be means tested. It would provide help, for example, with the extra costs of public transport, health and social care, dietary requirements and so on. Eligibility would be based not on an over-simplistic medical test, but on an assessment of an individual's real skills and abilities by a medical practitioner. The assessment procedure would be drawn up in consultation with groups for and of people with disabilities.

4.4.6 The *Disablement Pension* would be payable to people of working age unable to work as a result of sickness or disability. It would replace Invalidity Benefit and Severe Disablement Allowance and would be set at a level which would make it unnecessary for recipients to claim Income Support. A person would be able to claim the pension immediately, if they were likely to be incapable of work for at least 28 weeks. The pension would be taxable on the same basis as the retirement pension.

4.4.7 The *Partial Capacity Benefit* would provide support for people able to work but without sufficient earnings capacity to support themselves entirely. Its aim is to reduce the dependency of disabled people on state benefits.

4.4.8 The Party has recently reaffirmed its commitment to replacing the Invalidity Care Allowance with a more generous Carer's Benefit. This proposal is explained in detail in Policy Paper 1, *A Caring Society* (1993).

4.5 Simplifying Benefits: Low Income Benefit

4.5.1 The sheer number of different means-tested benefits can exacerbate the problems which they seek to address:

- Potential claimants can be confused and fail to claim benefits to which they are entitled.

***Our aim is to help
people escape from poverty
and back into work***

- Overlapping tapers (the rates at which benefits are withdrawn) can create severe poverty traps, as can the withdrawal of 'passported' benefits (benefits, such as free prescriptions and school meals, which are linked to being on Income Support).

Some individuals - particularly the increasing numbers of low paid and part-time workers - are excluded from benefit entitlement altogether, although they live in poverty.

4.5.2 It is our aim to ensure that everyone can afford to work and that no-one is worse off as a result of taking a job. If we are to achieve this aim then the benefits system needs to be radically reformed to make it simpler, more accessible and to reduce the poverty trap. We propose:

- *To reduce the problem of overlapping tapers*, we would combine Family Credit (the main 'in-work' benefit) with Income Support (the main 'out of work' means-tested benefit) to create a single Low Income Benefit.
- *To reduce the poverty trap created by the loss of passported benefits (such as free prescriptions and dental checks)*, we would modify the rate at which they are withdrawn as income rises.

- *To make the benefits system more accessible* (particularly to low paid and part-time workers), we would ensure that Social Security Offices opened outside normal working hours.

4.5.3 *Low Income Benefit would be tapered as Family Credit is now.* This would mean that people on Income Support would no longer lose their benefits pound for pound if they take on a part-time job. It would end the nonsense whereby if one member of a family goes on to Income Support, the household may be better off if the other spouse gives up a part-time job. A single Low Income Benefit would also end the complications of having to move from one benefit to another as eligible people move in and out of work - one of the reasons for the relatively low take-up of Family Credit.

4.5.4 We propose that Low Income Benefit be split and paid in two halves where both partners are either earners or non-earners, or paid to the non-earner, where one of the partners is earning. Claimants would be able to choose between weekly and monthly assessments of earnings.

4.6 Citizen's Income

4.6.1 *A Citizens' Income or Basic Income* is a relatively simple concept. It is based on the idea that tax credits (see section 3.1) which are unused because an individual's income is too small should be paid out in cash. For individuals on benefits, a repaid tax credit would replace an equivalent amount of benefit.

4.6.2 In *Common Benefit*, we proposed a partial basic income which was only slightly greater than the equivalent present personal tax allowance. This would not initially have helped those on present benefits very much, but the intention was to progress to a partial basic income for each adult comparable to half the current Income Support payment for couples.

4.6.3 We have never supported a full basic income, sufficient for subsistence and enabling most existing benefits to be abolished, because income tax on all other income would then have to be levied at a very high marginal rate.

Option A

4.6.4A *We reaffirm our commitment to a partial basic income system for the following reasons:*

- It would be more redistributive than the current tax system because the standard rate of income tax would be about 10 pence in the pound higher, although the majority of people would pay less than now after netting their tax credit against their income tax.
- Some income-tested benefits would have to be retained, but they could be smaller than now and less steeply tapered.
- It would be payable equally to all women and men, including those doing unpaid or intermittent work, as well as those earning full-time.

Option B

4.6.4B *We reject the option of a partial basic income system for the following reasons:*

- It would leave most people now receiving means-tested benefits still in need of them and no better off.
- The individuals who would benefit most - those with low incomes or no incomes but not receiving means-tested benefits - are not necessarily poor, because many of them live in households with good incomes.
- An increase of ten pence in the basic rate of income tax is completely unacceptable.

Looking After Children - Not Judging Parents

5.0.1 This Government has noticed that there are far more lone parents, unemployed people and recipients of Invalidation Benefit than there used to be. Its reaction has been to attack people in these categories, through rhetoric and benefits cuts, rather than to investigate the causes of the increases and seek to reduce the number who need extra assistance.

5.0.2 Liberal Democrats are not interested in identifying scapegoats. We are concerned with providing financial support where it is really needed. Our objects are twofold:

- *To alleviate poverty among families with children, through the social security system.*
- *To help parents to independence, by amending the tax and benefits system.*

These are the primary objectives of the recommendations which follow.

5.1 Retaining and Improving Child Benefit

5.1.1 *We are committed to retaining the universal nature of Child Benefit and increasing it, to compensate for the loss of the Married Couple's Allowance. The money saved by ending the Married Couple's Allowance could be used to increase Child Benefit by up to £5 per family per week (see section 3.3).*

5.1.2 Child Benefit is a universal benefit. Its universal nature guarantees it an extremely high take-up and makes it easy to administer. It is therefore particularly effective at providing financial support to those with child care responsibilities at a relatively low administrative cost. It would be impossible to meet the same

objectives so cost-effectively through a means-tested benefit. *We are therefore committed to retaining and building on Child Benefit as a universal benefit.*

5.1.3 The taxation of Child Benefit is another option. We oppose this change, however, for two main reasons:

- The sums which could thus be raised would be relatively small, would increase poverty traps and would provide a disincentive to women to go out work.
- The cost of collecting such a tax would be out of proportion to the sums collected.

5.1.4 We would retain the higher payment for the first child.

5.2 Reforming the Child Support Agency

5.2.1 The old system of child support was not a success. Maintenance awards varied enormously from case to case and whether payments were made at all depended upon the goodwill of non-custodial parents. Consequently, many single mothers were forced to live off barely adequate benefits, whilst their partners took no responsibility whatsoever for their children.

5.2.2 The aim of the Child Support Act was to tackle these problems by ensuring that:

- Non-custodial parents made a contribution to their children's well-being.
- The state took responsibility for ensuring that custodial parents got this contribution.

- The level of contributions was assessed on a consistent basis.

We continue to support these objectives.

5.2.3 In practice, however, the operation of the Act has been seriously flawed. In part, this is because it is retrospective and takes too little account of previous settlements and new family arrangements entered in good faith. The formula by which liability is calculated is too inflexible.

5.2.4 We would fundamentally reform the operation of the Act to address these faults by:

- *Amending the formula to take account of any transfer of property rights* from the non-custodial to the custodial parent in the divorce settlement, including any transfer of money from the sale of the marital home at the time of divorce.
- *Changing the Agency's operational priorities* from increasing payments from parents already paying something, to recovering maintenance from those who pay none.
- *Repealing the provision in the Act which enables a lone mother's benefit to be reduced if she refuses unreasonably to disclose the father's identity.* Instead, we would provide an incentive for disclosure by introducing a higher disregard for Income Support on money from maintenance. As a result, if the Child Support Agency recovered maintenance payments the custodial parent's total income would increase, as is already the case when that parent is not in receipt of benefit.
- *Setting up a body to review cases in which assessments cause extreme hardship.*

5.3 Improving Child Care

5.3.1 The cost of child care often traps parents, particularly women and lone parents, in their homes. It can make work financially unrewarding, so fuelling the dependency culture. Liberal Democrats believe that helping parents to meet the costs of child care is an essential ingredient in breaking the cycle of dependency. We are therefore committed to giving this a high priority, particularly for single parents.

5.3.2 The introduction in the 1994 Budget of a 'disregard' for Family Credit purposes of £28 of earnings spent on child care will help. It still falls short of the realistic costs of child care, however, and Liberal Democrats would seek to develop it further and extend it to Income Support.

5.3.3 Liberal Democrats would also give help with the child care costs of working parents not eligible for Family Credit or Income Support. *At the very least, we would extend the present tax relief on workplace nurseries to other forms of child care.* This would enable those employers that chose to, to offer their employees help with the costs of child care by any approved nursery or childminder, without the employee having to pay tax on the benefit.

5.3.4 Dependent upon resources, *Liberal Democrats would extend this concession further to allow any employee to claim tax relief - up to a set limit - on the costs of child care* by any approved nursery or childminder. The self-employed could be allowed to treat these charges as directly deductible expenses. We would use a voucher system to enable employed parents to claim tax relief. The limit on the tax relief which parents could claim would be set dependent upon available resources, with the aim of increasing it over time.

5.3.5 Liberal Democrats would encourage councils to provide or support nurseries giving free or subsidised care for children under the age of three. We remain committed to providing access to nursery education for all three and four year olds (English White Paper 4, *Excellence for All*, 1992).

Appendix: Being Honest about Taxation

Liberal Democrats believe that politicians should be honest about taxation, saying what it is for and obtaining public consent for it. Taxpayers know that if they want good public services, they have to pay for them. Increasingly, however, they are not prepared to sign a blank cheque and trust the politicians to spend money wisely.

This paper, *Opportunity and Independence for All*, does not deal with these issues.

Instead, Liberal Democrats consider them to be important enough to merit a paper of their own. *Being Honest about Taxation* is the title of the Liberal Democrats' preliminary report examining ways of increasing public confidence in how taxes are raised and spent. The final report is due early in 1995. *Being Honest About Taxation* is available from Liberal Democrat Publications, 8 Fordington Green, Dorchester, Dorset, DT1 1GB priced £1.95, plus 20% for p & p.

This Paper has been approved for debate by the Federal Conference by the Federal Policy Committee under the terms of Article 5.4 of the Federal Constitution. Within the policy-making procedure of the Liberal Democrats, the Federal Party determines the policy of the Party in those areas which might reasonably be expected to fall within the remit of federal institutions in the context of a federal United Kingdom. The Party in England, the Scottish Liberal Democrats and the Welsh Liberal Democrats determine the policy of the Party in all other areas, except that any or all of them may confer this power upon the Federal Party in any specified area or areas. If approved by Conference, this paper will form the policy of the Federal Party.

Many of the policy papers published by the Liberal Democrats imply modifications to existing government public expenditure priorities. We recognise that it may not be possible to achieve all these proposals in the lifetime of one Parliament. We intend to publish a costings programme, setting out our priorities across all policy areas, closer to the next general election.

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