These notes refer to the Tax Credits Act 2002 (c.21) which received Royal Assent on 8 July 2002

TAX CREDITS ACT 2002

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 1: Tax Credits

Section 7: Income test

51. *Subsection (1)* of section 7 provides that entitlement to a tax credit is dependent on the income of the claimant or the combined income of persons making a joint claim. The starting point is that an income threshold will be determined in the matter set out in regulations. If the income of the claimant or claimants falls below the threshold, their entitlement is to the maximum rate of the tax credit appropriate to their circumstances. But if their income exceeds the threshold, all or part of that entitlement may be withdrawn (see section 13).

52. The income test introduced by this section is not to apply in the case of claimants entitled to prescribed social security benefits. Such claimants automatically receive tax credits at the maximum rate for as long as they stay on those benefits (*subsection (2)*).

53. The income to be taken into account in determining entitlement to tax credits will be income for a tax year. The basic proposition is that awards are based on the current year income. But the section allows regulations to be made to enable previous year income or an adjusted measure of current year income to be used in certain circumstances. The regulations may set monetary thresholds related to changes in income between the current and previous years. A change in income smaller than the threshold(s) prescribed in regulations would mean claimants received tax credits based on their previous year income. If income moved between one year and the next by more than the threshold(s), the amount of tax credit due would depend either on the current year income, or, if regulations so provided, on current year income adjusted by the threshold (*subsection (3)*).

54. The effect of this is to provide flexibility for entitlement to tax credits not always to be based on actual income in the current year. So it would be possible for claimants with relatively small changes in income to have awards based on their known previous year income. The regulation-making powers would also make it possible for changes in income below prescribed amounts to be ignored and for the first slice of a change in income to be left out of account in determining entitlement.

55. This section provides that, for joint claims, the income for a tax year is the aggregate income of each of the partners for that year (*subsections (4) and (5)*). Regulations may allow income to be treated as belonging, or not, to a particular tax year (*subsection (6)*). In particular, they may allow income of particular types for the last tax year but one to be treated as the previous year income of that type, instead of the actual amount for that year (*subsection (7)*).

56. Regulations may also make provision as to what is, or is not, income for the purposes of tax credits and as to the calculation of income (*subsection (8)*). A person may be

treated in certain circumstances as not having income which he does have or as having income which he does not (*subsection (9)*).

57. The section also enables the Board to make an estimate of the income of an individual claimant, or the aggregate income of joint claimants, in order to make, amend or terminate an award. Such an estimate does not change the actual entitlement of the claimant or claimants to tax credits for the year (*subsection (10)*).