EXPLANATORY MEMORANDUM TO

THE INCOME TAX (EXEMPTION OF SOCIAL SECURITY BENEFITS) REGULATIONS 2022

2022 No. 529

1. Introduction

1.1 This explanatory memorandum has been prepared by HM Revenue and Customs and is laid before the House of Commons by Command of Her Majesty.

1.2 This memorandum contains information for the Select Committee on Statutory Instruments.

2. Purpose of the instrument

2.1 The purpose of the instrument is to exempt three social security payments from income tax, with retrospective effect. This includes the Scottish Government's Adult Disability Payments (ADP), made from March 2022; the United Kingdom Government's Discretionary Fund payments, that are part of the governments package to support households with rising energy bills, from April 2022; and Household Support Fund (HSF), from October 2021.

3. Matters of special interest to Parliament

Matters of special interest to the Select Committee on Statutory Instruments

3.1 Section 13 of the Finance Act 2020 ("FA 2020") conferred on the Treasury the power to exempt social security payments from income tax with retrospective effect by making regulations. It is a negative procedure instrument. The parliamentary procedure for this instrument is contained in section 1014 of the Income Tax Act 2007, which applies to all regulation-making powers under the Income Tax Acts. The Interpretation Act 1978 defines "the Income Tax Acts" as being all enactments relating to income tax, which includes section 13 of FA 2020.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is the United Kingdom.

4.2 The territorial application of this instrument is the United Kingdom.

5. European Convention on Human Rights

5.1 The Rt Hon Lucy Frazer QC MP, the Financial Secretary to the Treasury, has made the following statement regarding Human Rights:

"In my view the provisions of the Income Tax (exemption of social security benefits) Regulations 2022 are compatible with the Convention rights."

6. Legislative Context

6.1 This instrument is being made to set out the tax treatment of three new social security payments. The instrument will provide that these payments are exempt from income tax with retrospective effect from the date of their respective introductions.

6.2 Section 13 of FA 2020 contains a regulation-making power for the Treasury, by regulations, to amend Chapter 4 or 5 of Part 10 of Income Tax (Earnings and Pensions) Act 2003 ("ITEPA 2003"), so as to provide that no liability to income tax arises on social security benefits of a description specified in the regulations (section 13(1)).

6.3 The instrument will modify Chapter 5 of Part 10 of ITEPA 2003, as if there were inserted into Part 1 of Table B in section 677, payments made under the HSF and Discretionary Fund or any scheme or grant in Scotland, Wales or Northern Ireland corresponding to the HSF or Discretionary Fund. This will have the effect of wholly exempting these social security benefits from income tax

6.4 The instrument will amend Chapter 5 of Part 10 of ITEPA 2003 by inserting ADP into Part 1 of Table B in section 677, which will have the effect of wholly exempting this social security benefit from income tax.

7. Policy background

What is being done and why?

<u>Scottish Social Security Payments</u>

7.1 Social security payments are administered by a number of different government departments and the devolved administrations (DAs) in the United Kingdom.

7.2 The tax treatment of social security payments is legislated for in income tax legislation, and the tax treatment of each new payment should be confirmed when it is introduced.

7.3 The Scottish Government's Fiscal Framework 2016 ("the Fiscal Framework") underpins the powers over tax and welfare that are devolved to Scotland through the Scotland Act 1998. The Fiscal Framework states that a new benefit introduced by the Scottish Government will not be deemed to be income for tax purposes unless it 'tops up' a taxable benefit.

7.4 The Scottish Government have introduced ADP as a new social security payment through the Social Security (Scotland) Act 2018. That Act also allows the Scottish Ministers to legislate the eligibility conditions for each social security payment.

7.5 The ADP will be replacing the DWP's Personal Independence Payments (PIP) and adult Disability Living Allowance (DLA) from 21 March 2022. Initially, the ADP will be trialled in three local authorities, with a phased rollout, extending to the whole of Scotland by August 2022.

7.6 The ADP is designed to aid working age adults with a disability in Scotland. Social Security Scotland will make decisions about the entitlement to ADP. Individuals currently in receipt of PIP and Adult DLA will be automatically transferred to ADP from Summer 2022.

7.7 The ADP should not be taxable, as a matter of principle, under the Fiscal Framework. However, it could be chargeable to income tax, as a matter of law, under the income tax annual payment rules provided for in section 683 Income Tax (Trading and Other Income) Act 2005, if certain conditions are met.

7.8 As ADP could be taxable under the annual payment rules, the Government wishes to clarify the tax treatment for both payments as exempt from income tax in order to comply with the 2016 Fiscal Framework.

Discretionary Fund (energy support package)

7.9 The UK Government introduced a package of support known as the Energy Bills Rebate to help households with rising energy bills in 2022-23. The package included a £144m Discretionary Fund for local authorities to support vulnerable people and individuals on low incomes that do not pay Council Tax, or that pay Council Tax for properties in Bands E-H. The funding was provided to county councils and unitary authorities, under section 31 of the Local Government Act 2003 ("LGA 2003").

7.10 The Devolved Administrations (DAs) received equivalent funding in April 2022.

7.11 Payments made through the Discretionary Fund are unlikely to be taxable under current income tax legislation, but the government wishes to clarify the tax treatment of the payments, so that individuals know that they do not need to report receipt of the payments to HM Revenue and Customs (HMRC).

7.12 The exemption applies equally to any schemes or grants in the DAs corresponding to the Discretionary Fund.

7.13 The question of whether or not a scheme or grant in the DAs corresponds to the Discretionary Fund can be determined by reference to various objective criteria, including firstly, that the method of administration of payments in a DA would need to be similar to a grant or scheme made to LAs under section 31 of the LGA 2003 and, secondly, that the purpose of the assistance would need to be the same as that set out in paragraph 7.9 above.

Household Support Fund

7.14 The Department for Work and Pensions introduced the HSF in October 2020 as a £500m fund delegated to Local Authorities (LAs) to support vulnerable households as the country recovers from the Covid-19 pandemic. In March 2022, the HSF was provided with an additional £500m bringing the total to £1bn. The HSF supports vulnerable households with food, clothing, energy and water costs.

7.15 The Devolved Administrations (DAs) received equivalent funding in October 2020 and March 2022.

7.16 The funding was provided to county councils and unitary authorities (including metropolitan councils and London boroughs), under section 31 of the Local Government Act 2003 ("LGA 2003"), to administer the grants and provide assistance to vulnerable families with children, pensioners and other vulnerable households.

7.17 Payments made through the HSF are unlikely to be taxable under current income tax legislation, but the government wishes to clarify the tax treatment of the payments so that individuals know that they do not need to report receipt of the payments to HM Revenue and Customs (HMRC).

7.18 The exemption applies equally to any schemes or grants in the DAs corresponding to the HSF.

7.19 The question of whether or not a scheme or grant in the DAs corresponds to the HSF can be determined by reference to various objective criteria, including: firstly, that the method of administration of payments in a DA would need to be similar to a grant or scheme made to LAs under section 31 of the LGA 2003; and, secondly, that the purpose of the assistance would need to be the same as that set out in paragraph 7.14 above.

8. European Union Withdrawal and Future Relationship

8.1 This instrument does not relate to withdrawal from the European Union.

9. Consolidation

9.1 There are no plans for consolidation. This instrument amends ITEPA. However, it would not be proportionate to carry out a consolidation exercise of that Act on the basis of the minor revisions contained in this instrument.

10. Consultation outcome

10.1 No formal consultation exercise has been held as these are minor changes which are wholly relieving to the taxpayer.

11. Guidance

11.1 HMRC will update the guidance on non-taxable social security benefits guidance in line with the changes made by the instrument. That guidance can be found at: www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim76100

12. Impact

12.1 There is no, or no significant, impact on business, charities or voluntary bodies.

12.2 There is no, or no significant, impact on the public sector.

12.3 A full Impact Assessment has not been prepared for this instrument because is contains no substantive changes to tax policy.

13. Regulating small business

13.1 The legislation does not apply to activities that are undertaken by small businesses.

14. Monitoring & review

14.1 There are no plans to monitor or review the instrument.

14.2 The instrument does not include a statutory review clause because it does not make or amend regulatory provisions that relate to business activity.

15. Contact

15.1 Francesca Din at HM Revenue and Customs Telephone: 03000 593634 or email: Francesca.Din@hmrc.gov.uk can be contacted with any queries regarding the instrument.

15.2 Jackie McGeehan, Deputy Director for Income Tax Policy, at HM Revenue and Customs can confirm that this Explanatory Memorandum meets the required standard.

15.3 The Rt Hon Lucy Frazer QC MP, Financial Secretary to the Treasury, can confirm that this Explanatory Memorandum meets the required standard