The Low Incomes Tax Reform Group report on self-employment and universal credit

General Features **Personal tax**

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The LITRG have published a report summarising the main shortcomings of the current universal credit system in respect of the self-employed and suggesting positive reforms that would encourage entrepreneurial activity and relieve administrative burdens.

Universal credit is gradually replacing working tax credit and child tax credit, so advisers whose clients currently claim tax credits can expect them to be moved to universal credit over the next few years. LITRG began to raise concerns about self-employment in universal credit when the universal credit White Paper was first published and the Welfare Reform Bill began its passage through Parliament in 2011.

Although some minor changes to the rules have been made since then, many of the major concerns remain. At present, the system does not work well for self-employed claimants who have fluctuating income and/or expenses, or who have a large, one-off business expense in a particular month, nor does it give people long enough to establish and grow their business. In addition, the universal credit assessment period is one month as against one year for tax, definitions of income and profit from self-employment differ for universal credit and tax, and universal credit operates a cash basis which diverges from the cash basis option for tax.

The report recommends:

In each Jobcentre office, a small number of staff should undergo specialist self-employment training to become ‘subject experts’ with access to a central expert team who are supported by HMRC.

Self-employed claimants should see a work coach at least once every 12 months to ensure compliance with the gainful self-employment test. There should be consistency to ensure that claimants who are classed as self-employed by HMRC are also self-employed for universal credit purposes. All claimants passing the test should have the opportunity to access business support from a trained Jobcentre adviser.

The current one year start-up period should be extended to two years.

- A general anti-abuse provision should ensure people cannot manipulate their income in order to claim universal credit or more universal credit. This would apply to both employed and self-employed claimants and would remove the need for the complex surplus earnings rules that are due to come into force from April 2018.
- Self-employed claimants with fluctuating income or profits should be given an option of averaging their income over a period up to one year.
- All definitions should be fully aligned with the HMRC cash accounting rules and thought should be given to how the system can deal with those who are unable to use the HMRC cash basis for tax purposes.
- In cases where earnings are averaged, we propose that the system of reporting monthly income and expenses should be changed so that it follows the period of which earnings are averaged.

- The minimum income floor should remain from Year 3 onwards but should be calculated after deduction of pension contributions as well as tax and national insurance. This is to ensure self-employed claimants are treated as favourably as employees who make pension contributions.
- Two exceptions should be made to the minimum income floor. First, a three month grace period in each 12 month period to allow someone to deal with unexpected events or a one-off large expense without any adverse impact. Secondly, we propose a discretion for DWP staff to dis-apply the MIF in certain situations.

The report can be found on the LITRG website.