Tax-free childcare – top up help with childcare costs

Tax-free childcare is a new scheme, due to start late 2015, which will provide working parents with a government top up to funds they pay into a dedicated childcare account.

The term 'tax-free' refers to the 20 per cent of the total represented by the government top up. If a parent contributes £200, the government will contribute £50 – which is 20% of the total £250. The maximum the government will contribute is £500 per child per quarter which is £2,000 per child per year (or £4,000 for a disabled child). That means the maximum contribution on which a parent would get a government top up would be £8000 per year per child (for a child who is not disabled). Parents can put more into the accounts if they wish, to help with budgeting, but these payments will not receive any government support.

Key design features

- Tax-Free Childcare is by child not by parent or household.
- Tax Free Childcare works on a quarterly cycle with reconfirmation every three months.
- Changes of circumstances within the three months do not affect entitlement.
- Deposits to the childcare account are topped up by 20% of the gross i.e. £80 deposit topped up by £20.
- Maximum top-up of £500 per quarter*.
- Funds can accumulate in the childcare account for as long as the parent wishes for maximum flexibility.

* £1000 per quarter for disabled children

Who is eligible

To use the tax-free childcare scheme, parents must:

- Be responsible for a child under 12, or a disabled child under 17 (entitlement stops the September after the child's 11th birthday, or after the 16th birthday if the child is disabled.)
- Use a childcare provider approved by the relevant body for instance OFSTED who is signed up for tax-free childcare.
- Live in the UK , apart from temporary absences. However some people are treated as if they are not ordinarily resident here, and so can't use the scheme, for example, people subject to immigration control.[6] Members of the British armed forces who are posted overseas will be treated as living in the UK, and so could qualify for the scheme.
- Be in paid work (including their partner if they have one). This can be employed or self-employed, and they must expect to earn at least eight times the minimum hourly wage per week (currently that would be £52 a week) for the next three months.
- Their taxable income does not exceed £150,000 a year, and neither does their partner's
- They must not be receiving tax credits, Universal Credit or any publicly-funded support for childcare costs (for example, Care to Learn or a childcare grant).

Any amount of tax credits or Universal Credit prevents access to the tax-free childcare scheme. An award of tax credits or Universal Credit will be terminated if a parent applies for and is entitled to tax-free childcare. This means all tax credits and all Universal Credit will end, not only the childcare element. So where a parent's award of Universal Credit is considerable, or gives them access to other help, it may be better to claim Universal Credit. Similarly, if a parent currently receives tax credits and Housing Benefit, they may get more overall from these benefits than they would from tax-free childcare.

Requirement to be in paid work

Usually, both partners in a couple must be in paid work, but there are exceptions, when one is in paid work (of at least eight times minimum hourly wage per week), and the other is receiving:[7]

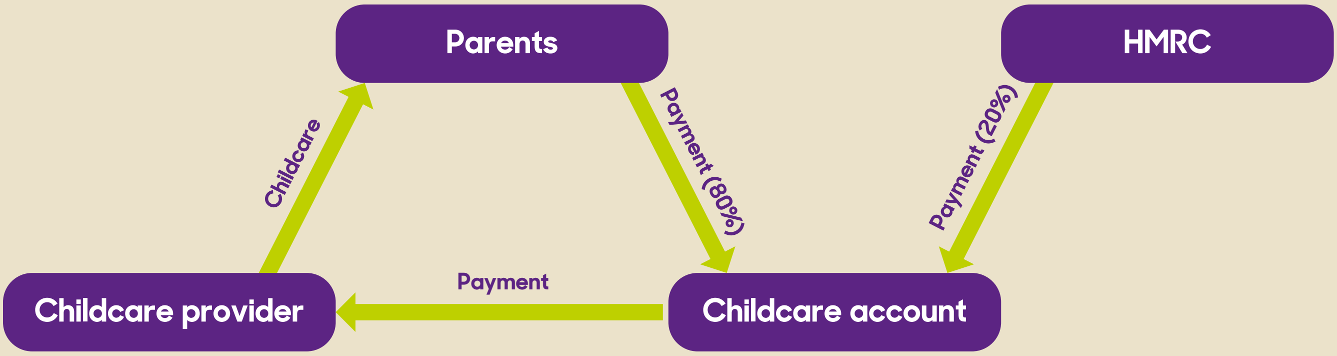
- Carer's Allowance
- Contributory Employment and Support Allowance (ESA)
- National Insurance credits for limited capability for work
- Incapacity Benefit or Severe Disablement Allowance (for most claimants, these benefits have been replaced by ESA).

Parents are also treated as being in paid work during periods when they receive sick pay, maternity pay, paternity pay, adoption pay, and during unpaid parental leave or shared parental leave.[8]

6 Reg 7 Childcare Payments (Eligibility) Regs 2015
7 Reg 13, Childcare Payments (Eligibility) Regs 2015
8 Reg 12, Childcare Payments (Eligibility) Regs 2015

Opening a tax-free childcare account

Parents will need to open a tax-free childcare account online. They will first need to obtain access to government online services. They will have to check that their childcare provider is 'signed up' to receive payments via tax-free childcare. Only one tax-free childcare account can be opened for a child, so if there is joint responsibility, parents will have to talk about who should open the account. If they can't agree, HMRC will decide.



Concerns for parents

At this stage there are many concerns amongst parents, who are confused about the new schemes and their implications. Some of these concerns are based on misconceptions about the new arrangements, whilst in other cases, they reflect real changes, which may be overcome by clearer information.

- Parents may know that Universal Credit is being introduced but may not be clear that tax credits, housing benefit and certain out-of-work means-tested benefits are being abolished.
- In-work conditionality – having to look for work even if you are in work – is a concern for some parents who depend on tax credits to boost their working income. This will be a feature of Universal Credit, but usually only up to a certain level of earnings.
- Reporting childcare costs – some parents already struggle with reporting requirements within tax credits. Universal Credit requires childcare costs to be reported when they are paid, so may in practice be easier to understand even though reporting is more frequent.
- Childcare voucher schemes provided by an employer – parents who are happy with childcare voucher schemes may be concerned that they will lose these. In fact, they will have the choice to remain in a scheme for as long as it is provided by their employer and they remain with that employer, but in that case they will not have access to tax-free childcare.
- Budgeting within Universal Credit – Universal Credit is one payment, made to one person, paid in respect of a monthly assessment period. Parents may be worried about how to budget for food, fuel, travel, rent and childcare as well as all their other expenses. New Universal Credit claimants needing money advice should be directed to local or national support. In addition alternative payment arrangements may be considered for those who are likely to struggle with monthly payments, payment to one person or being responsible for paying rent themselves.
- Online claiming – both Universal Credit and tax-free childcare will be claimed online. As with other online applications, if parents have all the information to hand when they start the process, this should not be too difficult. Applications can be saved and returned to later.

Factors which may indicate Universal Credit is a better option include:

- Families who pay rent, as Universal Credit includes a housing element. Help with a mortgage is not included in Universal Credit once there is any earned income although claimants with no housing costs may be eligible for a higher work allowance.
- Income is low and parents will struggle to contribute to the tax-free childcare account. No help is received under tax-free childcare unless a parental contribution is made. Universal Credit includes elements for the claimant and for children which may make a Universal Credit award worth more than the government top up within tax-free childcare.
- There is a non-working partner. Universal Credit includes a carer element or an element for limited capability for work which may make the Universal Credit award worth more.
- 'Passported benefits' such as help with health costs are important to the family and their Universal Credit award helps them to access this support.
- Families who currently do not work enough hours to get help with childcare via Working Tax Credit should think carefully before opening a tax-free childcare account. They may be better off with Universal Credit, although it may be some time before they have the option of transferring.

Factors which may indicate tax-free childcare is a better option include:

- Families who may be concerned by the conditionality requirements of Universal Credit (which will require some parents to look for more work although they have a job) may prefer tax-free childcare. However, conditionality under Universal Credit is tailored in the light of an individual's circumstances and to fit around employment and childcare responsibilities.
- Families who would prefer managing their childcare costs via a tax-free childcare account rather than as part of the single payment per household and wider requirements of Universal Credit.
- Parents whose Universal Credit is not much more, or less, than the government contribution they could receive within tax-free childcare. A 'better-off' calculation may be needed to assess this, bearing in mind that Universal Credit entitlement can vary from month to month if a parent's income is not static.

Interaction with existing help

The simple message for parents when discussing new ways to help with childcare costs is that they are exclusive – they cannot be combined with existing help for childcare costs. The only exception is the free childcare offer, this can be used in conjunction with other state help if a parent needs additional paid-for hours in order to work. For example:

- A parent cannot usually use tax-free childcare if they or their partner get tax credits or Universal Credit.

Where someone correctly declares they are eligible and are going to claim for tax-free childcare, any award of Universal Credit or tax credits should be terminated.[9] Generally, a declaration of eligibility for tax-free childcare means the parent agrees they won't be getting Universal Credit or tax credits during the entitlement period. It's possible to be disqualified from tax-free childcare if this rule is ignored.[10] However, many changes of circumstances would allow a parent to avoid being disqualified from tax-free childcare, for example, a change in employment, a partner or child leaving the household, or another child arriving.[11] Circumstances may mean a parent needs to claim tax credits or Universal Credit within a tax-free childcare entitlement period. Their entitlement to tax-free childcare won't end until the end of the entitlement period, so for a short time, both types of help will be available. Tax-free childcare payments received during that entitlement period won't affect the amount of Universal Credit or tax-credits.

- A parent cannot claim Universal Credit and Tax Credits. If a parent on tax credits becomes part of a household on Universal Credit, their tax credits will stop and they become part of the Universal Credit claim.
- A parent cannot use tax-free childcare if they or their partner get Universal Credit or any other form of state support with childcare.
- A parent cannot use tax-free childcare if they or their partner are in a childcare voucher scheme.

The only situation in which existing help can continue along with tax-free childcare is where an employer provides childcare onsite, such as a workplace nursery.

9 sections 30 and 31 Childcare Payments Act 2014
10 sections 32 and 33 Childcare Payments Act 2014
11 reg 18 Childcare Payments (Eligibility) Regs 2015