

THE TAX TREATMENT OF THE FAMILY UNIT

by

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PART II

STUDIES AND CRITICISMS OF THE
UNITED KINGDOM SYSTEM

Chapter 7 : A Review of the Principle of Aggregation.

Chapter 8 : A Review of the Principle of Accountability.

Chapter 9 : A Review of the Principles Underlying
the Allowances.

Part I of this thesis discussed the principles which currently govern the taxation of the family unit in the United Kingdom and the historical development of those principles. This Part examines the occasions upon which these principles have been reviewed and criticised.

Such consideration has been directed mainly towards the three main principles which govern the taxation of husband and wife, namely, aggregation, accountability and allowances, and a chapter is, therefore, devoted to each principle. No reference is made in this Part to the capital taxes or the taxation of children : these subjects have received very little consideration or criticism, and such consideration as they have received has already been mentioned where appropriate in Chapter 4 (capital taxes) and Chapter 5 (children).

CHAPTER 7 - A Review of the Principle of Aggregation

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CHAPTER 7

A REVIEW OF THE PRINCIPLE OF AGGREGATION

Section

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This chapter discusses the occasions on which the principle of aggregation has been reviewed. The reports of the three main Reform Committees (Colwyn, Radcliffe and Meade) are, of course, of prime importance in this context, as is also the Green Paper on the taxation of husband and wife¹ published in December 1980. But other studies are also relevant and, in particular, a review of the Parliamentary consideration of the subject sheds much light on contemporary

1. Cmnd 8093.

thinking and develops the reasons which were advanced at different times both in favour of, and against, the retention of the principle of aggregation.

A chronological treatment of the subject has been adopted because it is thought that this best highlights the development of the differing views on the subject and places these within the correct historical context. A surprising feature emerges from this treatment, namely that, in the final analysis, the reasons put forward both in favour of the retention of aggregation and also in favour of its abolition are limited in number and recur with great frequency : further, some of the reasons are of considerable antiquity. The reasons on both sides will be identified as they occur so as to enable the development of each to be traced through its historical evolutions; references will also be made to proposals for the replacement of the existing system of aggregation by some alternative systems.

1. Before 1894

Although the principle of the aggregation of the incomes of husband and wife was first introduced in 1805 it took nearly a century for any fundamental reform to be proposed. This may be explained in three ways. First, income tax was, at that time, in principle a proportionate tax and not a progressive tax and thus aggregation, of itself, did not affect the amount of tax paid to any large extent. As is stated in the Radcliffe Report¹ :-

1. Paragraph 117. Royal Commission on the Taxation of Profits and Income, Second Report, 1954, Cmd 9105.

"It is worthwhile to point out that so long as income tax remained a proportional tax, as it did in substance throughout the 19th century, the principle of aggregation raised no issue of major importance".

However, it will be recalled that in both 1805 and in 1842 an exemption was given for small incomes and it would therefore seem that perhaps there should have been some objection made to the aggregation rule which could have resulted in two persons both with incomes below the exemption limit losing both exemptions on marriage. The reason why no such objection was made could be explained by the second and third reasons, namely that during the years 1816 - 1842 there was no income tax at all and when it was re-introduced in the latter year the Married Women's Property Act was still forty years away; it is therefore understandable that until the general law relating to married women's property was changed there would be no pressure for the reform of the income tax laws; finally, it is probable that in these years very few married women had earnings of their own.

The acceptance of the principle of the aggregation rule can be deduced from the fact that the Select Committee on Income and Property Tax, under the chairmanship of Mr. Joseph Hume, which was appointed in 1851 and reported in 1852, made no mention of the taxation of husband and wife. This is of particular significance as one of the witnesses, Mr. John Stuart Mill, who gave evidence to the Committee on a number of matters relating to the tax, did not mention the tax treatment of married women; as a distinguished and widely known champion of their rights it is thought that he would then have raised the question if he had thought it relevant or if there had been any widespread feeling in

support of a change.

The Married Women's Property Act was passed in 1882 and the first discussion of the aggregation rule took place twelve years later, in 1894.

2. 1894 - Disaggregation of wife's earnings

The first discussion of a proposal for disaggregation arose out of the injustice felt at the loss of the two exemptions for small incomes on marriage. When income tax was re-introduced in 1842¹ persons with incomes of less than £150 a year were exempt from tax. This was reduced to £100 in 1860.² but there was an abatement where income did not exceed £150. The figures were altered in 1872 and again in 1876³ when the £150 exemption limit was restored and an abatement given for incomes below £400. Of course, the incomes of husband and wife were aggregated for the purpose of these exemptions and abatements as for all other purposes.

Following the passage of the Married Women's Property Act 1882 the income tax provisions began to give rise to dissatisfaction and this came to a head in 1894 when the Finance Bill contained a clause designed to increase the exemption limit for small incomes to £160 with abatement for incomes under £500. In the same year estate duty was introduced and, it will be recalled, that whereas legacy and succession duties had contained some reliefs for transfers

1. Section 163 5 & 6 Vict c. 35.

2. Section 9 23&24 Vict c. 14.

3. Section 8 Customs and Inland Revenue Act 1876.

between husband and wife, estate duty when it was introduced, contained no relief at all.

(1) Amendment in Committee

The first move was made during the Committee stage of the Finance Bill¹ when Mr. Darling moved an amendment to clause 29 which imposed the charge to income tax for that year : the amendment would have resulted in complete disaggregation and read:-

"The income of any married woman shall, for the purposes of this Act, be deemed to be her own separate income and she shall be chargeable with income tax thereon as if she were actually sole and unmarried".

In moving this amendment Mr. Darling referred to the first two reasons for reform which will occur with great frequency.

<u>First Reason</u>	:	<u>The tax laws should follow the</u>
<u>for reform</u>	:	<u>property laws.</u>

In 1894 Mr. Darling was able to say that "it would astonish a good many members to know that even though the Married Women's Property Act had given a married woman the right to own her own property, no amendment had been made in the income tax laws". He went on to say:-

"The husband was assessed just as though the income of the wife was his own. If the income of the wife was taken as it ought to be, as separate from that of the husband, in many cases both would be entitled to a large abatement or be completely exempt. By uniting the incomes the married woman was deprived of the relief which was given to a single woman".

Of course, the husband would also be deprived as

1. Hansard 28th June 1894 Col 492.

well. Mr. Darling then gave details of actual cases where married couples paid more tax than two single persons and said that he did not put forward the amendment on behalf of the "idle and rich" but gave, in particular, the example of a schoolmaster and schoolmistress, both with modest incomes, who lost their reliefs on marriage.

Mr. Darling then referred to the second reason for reform.

<u>Second Reason</u>	:	<u>Reform was being demanded</u>
<u>for reform</u>	:	<u>by many people</u>

Mr. Darling said that he had received letters on this subject and a deputation had visited him to discuss the position; the amendment was one "designed to remedy a wrong that was felt to bear hardly on a large and deserving class of people".

In replying to the proposed amendment Sir William Harcourt brought forward two reasons against reform which were to be heard very frequently on future occasions.

<u>First reason</u>	:	<u>Advantages depend on</u>
<u>against reform</u>	:	<u>proportions of income in</u>
		<u>household</u>

This reason for retaining the aggregation rule has been brought forward on very many occasions but here let it be stated in Sir William Harcourt's own words:-

"Take the case of a husband and wife, each with an income of £500. Though the joint income was £1,000 a year each of them would get an abatement. Take, again, the case of a man with a little over £500 a year who had a wife with no money at all. He would get no abatement; so that the joint ménage with £1,000 a year would receive two abatements while the other establishment with half the income would get none".

The fallacy of this argument is, of course, that if two unmarried persons lived together, each with £500 a year, they would each get an abatement and, again, if one of the unmarried persons had slightly more than £500 and the other had nothing, there would be no abatement : so that the unmarried joint ménage with £1,000 a year would receive two abatements while the other establishment with half the income would get none. Unlike rates, income tax is a tax on persons, not on households, and the equity of the tax is constructed by a comparison of individuals and not of households. It is a logical fallacy to introduce the household concept only when discussing married couples and to ignore it when discussing other households; if the household argument had ever had any validity then it should have been applied to all adults sharing the same household and not just to those who were married.¹

Sir William Harcourt also referred to the second reason against reform, which is still used at the present day.

<u>Second Reason</u>	:	<u>It would cost too much</u>
<u>against reform</u>	:	

In 1894 the figure given as the 'cost' of disaggregation was "£500,000 a year and more probably £750,000 a year". The cost made it impossible to accept the amendment, said Sir William Harcourt.

It is perhaps appropriate at this stage to consider why the representatives of government have always

1. See the discussion in Chapter 1 pages 33 and 34 and ante about the relevance of the 'household' to the assessed taxes, which preceded income tax and also the 'reporting' duty of a householder in the first Income Tax Act of 1799.

considered the argument as to cost to provide an adequate answer to proposals for reform. It is not thought that such representatives were so naïve as to confuse the tax base with the tax yield : they must have known that if the tax base had been altered by disaggregation then the yield could have been maintained by an (upward) adjustment of the rates. And it is thought that that is, in fact, the true reason behind the continuing opposition to disaggregation, namely that an upward adjustment of the rates of income tax was politically unacceptable : it is always more acceptable to announce a (comparatively) low basic rate of tax knowing that the operation of the aggregation rule would disguise the fact that the effective rate for much of the population would be higher : again, politically it is always more acceptable to announce (comparatively) high exemptions and reliefs knowing that the aggregation rule would operate to reduce these substantially for most of the population. Compare these two announcements : either : the mortgage interest relief limit is to be £25,000 : or : the mortgage interest relief limit is to be £12,500 except for single persons who will get a limit of £25,000. It is clear which is most acceptable politically and it is thought that this is the (unspoken) reason why the aggregation rule has remained so long.

After pronouncing these two reasons against reform Sir William Harcourt may have thought there was little more to say, but the accuracy of the estimated cost of reform was questioned and a request made for disaggregation, at least for married couples with joint incomes

below £750 a year and the possibility of an amendment at Report stage was promised. Before the debate concluded Mr. A.J. Balfour offered for consideration the third reason for reform.

<u>Third reason</u>	:	<u>The tax laws should be con-</u>
<u>for reform</u>	:	<u>sistent between themselves</u>

Mr. Balfour said that he had watched throughout the whole debate the principles which the Government held as subsisting between the relation of man and wife -

"...and he found that the view the Government took of the matter was that when they considered it could be profitable for the Exchequer to consider a man and wife as one then they were considered as one. On the other hand when it was to the advantage of the Revenue to consider them as two distinct persons then they were considered as two...For the purpose of calculating income tax husband and wife were considered as one ...for the purpose of death duties two... could any system be more absurd, more indefensible, more unjust?"

(It will be recalled that estate duty had been introduced in 1894 containing no reliefs for transfers between spouses).¹

(2) Amendment on Report

The second move towards disaggregation was made also in 1894 during the Report stage of the Finance Bill when Mr. Darling moved an amendment² to clause 33 (the charge to income tax) which would have resulted in the complete disaggregation of joint incomes below £500. However, at the same time Sir William Harcourt moved an amendment

1. See Chapter 5 page ante.

2. Hansard 16th July 1894 col. 111.

to clause 34 (abatements and reliefs) giving a separate "small income" exemption if two conditions were satisfied: first, the joint income had to include earnings of the wife; and, secondly, the joint income had to be below £500. The new relief was, of course, given to the husband as a reduction in the tax payable by him on the joint income. The amendment, therefore, provided the first alternative to disaggregation

<u>The first alternative</u>	:	<u>Partial disaggregation</u>
<u>to disaggregation</u>	:	<u>of wives earnings only</u>

The principle of a partial disaggregation was not accepted by Mr. Darling : he did not see why the new arrangements should not also apply to a wife with investment income as she would have had an abatement if she were not married and pointed out that the amendment

"did not accept the fact that it dealt with two separate incomes of two separate persons...what they were dealing with was not joint income at all but two separate incomes, the one the income of the husband and the other the income of the wife".

However, the amendment was agreed to, although the view was expressed that it was to be regarded as a partial improvement only and that logically completely separate taxation was desirable. Thus, at the end of the year 1894 three of the reasons for reform (that the tax laws should follow the property laws, that reform was required by many people, and that the tax laws should be consistent between themselves); two of the reasons against reform (that the advantages would depend upon the proportions of income in a household and that it would

cost too much); and one alternative proposal (partial disaggregation of wife's earnings) had all been ventilated and the latter had also been implemented.

3. 1894 - 1909

Although throughout the period from 1894 - 1909 the position was not considered to be satisfactory, no comment was made on the subject of family taxation in the Report of the Departmental Committee on Income Tax, under the chairmanship of Mr. Charles T. Ritchie, published in 1905.¹ Again, the Select Committee, which reported in 1906,² made no mention of the aggregation rule which is significant in view of the fact that their report dealt with differentiation and graduation and graduation would have had an effect on the aggregated incomes of husband and wife.

(1) Questions in the House of Commons

By 1906, however, the movement in favour of some alleviation of the treatment of married couples was gathering force. On 10th December 1906³ a request was made for greater relief for married persons; on 11th April 1907⁴ a question was asked in the House of Commons about "the estimate of the cost to the Revenue of separately assessing for abatement the several incomes of man and wife" :

1. Paper 365.

2. Cd. 2575.

3. Col. 1559.

4. Cols 333 and 334.

the reply was given that "the Inland Revenue had no materials for forming such an estimate".

On 24th April 1907¹ the view was expressed that the time had come when some relief should be given to married persons who each had a small income:-

"A man and a woman with incomes of £400 a year got a rebate each of £160 when single but if these two were married their incomes were put together and they were not allowed to claim any abatement. Yet two sisters or two brothers who had similar incomes and lived together could each claim abatement".

Here, then, is the fourth reason for reform.

<u>Fourth reason</u>	:	<u>A man and a woman who are</u>
<u>for reform</u>	:	<u>married should be no worse off</u>
		<u>than two single persons. There</u>
		<u>should be "no penalty on</u>
		<u>marriage"</u> .

The extract quoted above is enlightening in two respects : it compares a married man and woman with their position before marriage and also with other unmarried persons who share households.

In reply, however, Mr. Asquith called in aid the Second Reason against reform : it costs too much; "the loss to the Exchequer would be far greater than (the mover of the amendment) had any conception of".

(2) Two new clauses moved in 1907

On 11th July 1907 a new clause was moved during the Committee stage of the Finance Bill ² in which it was proposed that the incomes of husband and wife should be

1. Col 119.

2. Col 190.

added together and divided by two for ascertaining the exemption or abatement of income tax.

"the point was that when husband and wife were living together their incomes should be taken as that of separate people and not of one person".

Here is the first mention of the second alternative to complete disaggregation.

<u>The second alternative</u>	:	<u>The division of the joint</u>
<u>to disaggregation</u>	:	<u>incomes by two : the</u>
		<u>"quotient system".</u>

Under the "quotient system" husband and wife are both treated as being in receipt of half of the joint income : this system recognises a married couple correctly as two individuals rather than one but in its operation it will always give a married couple a tax advantage over two separate individuals save in the unlikely case where two individuals have exactly similar incomes.

The reply given to this proposal by Mr. Asquith repeated the Second Reason against reform : it would cost too much. "Such a change would involve the Revenue in a loss of most enormous magnitude". The reply also introduced a new reason against reform.

<u>Third reason</u>	:	<u>Married couples are members</u>
<u>against reform</u>	:	<u>of one household and have</u>
		<u>a joint income.</u>

Let the third reason be stated in the words of Mr. Asquith:-

"The theory of the law was that where two persons became domestic partners they became members of one household and their two incomes were fused together".

The third reason against reform is, in fact, a variant of the first reason (which compared households not

individuals). As stated by Mr. Asquith, however, it is open to a number of objections. First, 'the theory of the law' is mentioned without any reference to which law : it certainly could not have been the general law of the land, because, since 1882, the principle of separate incomes had applied to husband and wife; the only law to retain the theory was income tax law and it was income tax law which it was proposed to amend : it is no answer to a proposal for an amendment of the law to reply that "the theory of the (existing) law is against the amendment". Secondly, Mr. Asquith states as a generality that "when two persons became domestic partners they became members of one household and their two incomes were fused together;" this was also true as regards unmarried persons sharing a household but their incomes were not aggregated for tax purposes. Finally, the illogicality of importing the 'household' concept into a tax which is levied on individuals is discussed on page 321 above.

The new clause was, by leave, withdrawn, but on 10th July 1907¹ during the Report stage of the Bill another new clause designed to introduce the quotient system, was again introduced. In reply, Mr. Asquith mentioned again the Second Reason against reform : it would cost too much : the loss to the Exchequer would be "very considerable indeed". He also brought forward two new reasons against reform.

<u>Fourth reason</u>	:	<u>Aggregation does not stop</u>
<u>against reform</u>	:	<u>people from marrying</u>
<u>Fifth reason</u>	:	<u>All cases of hardship are met</u>
<u>against reform</u>	:	<u>by the partial disaggregation</u>
		<u>of wives earnings.</u>

1. Col 578.

Although Mr. Asquith could correctly state that "he did not know anyone who had failed to marry because of the aggregation rule" that is really no reason for perpetuating an unjust tax. If a tax were to be levied on children it would not be a valid argument in favour of the tax to say that one did not know anyone who had failed to have children because of the tax.

The illogicality of countering an argument for complete disaggregation by a reference to provisions for partial disaggregation is self-evident. Before leaving the subject Mr. Asquith did give a specific reply to the proposal for a quotient system - he pointed out the advantages which such a system gave to married couples as against single individuals, namely

"that a husband with an income of £999 and a wife with an income of £1 would be taxed as two incomes of £500, each of which would be entitled to an abatement".

This is a valid comment to make on the quotient system. The new clause was, by leave, withdrawn.

(3) A new clause moved in 1908 - Disaggregation

The point was, however, pursued the following year. On May 25th 1908¹ Sir William Bull drew attention to the fact that two married people paid more tax than if they were not married - the Fourth Reason for reform. He asked if it was right that "the state should offer an annual premium to the man and woman who would consent to live together...without entering into the married state".

1. Cols. 838-840.

He thought not and concluded that the tax imposed "was a penalty on marriage". On July 15th 1908¹ Mr. Watt moved a new clause to the effect that "the income of husband and wife be taken to be the income of separate persons". He gave in support the First Reason for reform : that the tax laws should follow the property laws; he said that "the tendency of the law during the last thirty years had been to separate the incomes of husband and wife and the last link that remained with the past was the system of estimating the two incomes as one for the purposes of the income tax".

In reply Mr. Lloyd George referred to the Second Reason against reform (it would cost too much) and here it is interesting to note that the cost of implementation had now risen to £1,500,000. He also called in aid the Third Reason against reform (married couples are members of one household and have a joint income) : the merits of this are discussed on page 321 above.

Thus, between the years 1894 and 1909 no progress was made towards any further disaggregation but a persistent pressure for reform has been present; one further argument in favour of reform (that there should be no penalty on marriage); three further arguments against reform (that married couples are members of one household and have a joint income; that aggregation does not stop people from marrying and that all cases of hardship are met by partial disaggregation of wife's earnings); and one more alternative (the "quotient" system) have all been discussed.

1. Cols 941-942.

4. 1909 - Supertax

In 1909 two Finance Bills were passed, the first in the Spring and the second in the Autumn. In the spring budget¹ resolutions a reference was made to the fourth reason for reform : the penalty on marriage, which it was thought could lead to immorality "because a man and a woman living together both got reductions whilst if they were married no reductions were made". During the debate on the Second Reading² a reference was made to the First Reason for reform (that the tax laws should follow the property laws) and it was pointed out that since 1882 a husband had no control over his wife's income yet was still liable for tax on it. The autumn Finance Bill of 1909 was of interest in two respects : it imposed the super-tax on incomes in excess of £5,000 and so, for the first time, a return of total income from all sources was required. Secondly, it extended the legacy and succession duties to property passing between husband and wife, although admittedly at a lower rate than applied to other beneficiaries.

The new liability for supertax - the first truly graduated tax - brought to the fore once again the anomalous position of husband and wife.

On 20th September 1909, during the committee stage of the Bill, the disquiet which was felt was summarised by Mr. Walter Guinness³ as -

1. Hansard 17th May 1909 col. 99.

2. Hansard, May 1909, vol.6 col. 164.

3. Col. 94.

"If one partner has £2,000 and another £3,000 it is very hard, just because they are married, that they should pay an extra tax...surely if it is fair to lump the incomes of husband and wife together you ought to lump the incomes of brother and sister when they live together".

In replying to the amendment the Chancellor of the Exchequer brought forward again the third reason against reform (married couples are members of one household and have a joint income) and also a new reason.

<u>Sixth reason</u>	:	<u>Disaggregation would lead to</u>
<u>against reform</u>	:	<u>tax avoidance by transfers of</u>
		<u>property.</u>

Responding to this Mr. Snowden¹ referred to these two reasons for opposing the amendment:

"The first was that for the purpose of assessing for income tax the household is regarded as a unit. I do not think that that is the case at all. I have always understood that the income tax was a personal tax. It is only where husband and wife are assessed together that income tax can be regarded as a household tax. In the case of a son over 21 years of age his income is not taken as that either of the husband or the wife".

Turning then to the proposal that disaggregation would lead to tax avoidance through transfers of property Mr. Snowden pointed out that details of ownership would be in the possession of the Inland Revenue. There is, however, a more fundamental response to this reason against reform, namely that a right to enter into bona fide transfers of property, even with motives of tax avoidance, is given to every other taxpayer subject to the "settlement

1. Col 102.

provisions" referred to in Chapter 3.¹ There is prima facie no justification for withholding such a similar right from husband and wife although it is appreciated that the tax code² does nullify certain obvious forms of tax avoidance, e.g. revocable settlements and settlements on children. The types of tax avoidance which are nullified in this way must remain a matter for political decision but in reaching a conclusion on which transactions should be nullified the legislation will, no doubt, evaluate the ease with which tax can be avoided and whether such avoidance causes genuine detriment to the transferor. For example, a distinction could be drawn between the desire of a taxpayer to share his income with a stranger (which can be tax effective within certain limits) and the desire of a taxpayer to share his income with his wife, whom he has an obligation to support and from whom he could expect some benefit in return. On the other hand, income splitting between spouses is not considered reprehensible in many of the overseas countries considered in Part III and, indeed, in some of these countries income is split by statute to give maximum tax relief for spouses. Although therefore, the repeal of the aggregation rule would mean that consideration would have to be given to tax avoidance provision for spouses, the conclusion is reached in Part IV of this thesis that such provisions should not be introduced but that the capital taxes exemptions for spouses should be withdrawn so that in all respects bona fide transfers of property between spouses are taxed in exactly the same way as

1. See page 216 ante.

2. Part XVI Taxes Act.

such transfers between other persons. During Report stage of the 1909 Bill¹ a further new clause, designed to bring about complete disaggregation, was moved, referring to the fourth reason for reform (there should be no penalty on marriage).

"It is a very hard case indeed that if a man lives with a woman who happens to be his wife they should be in a worse position than if she was not his wife".

In reply Mr. Lloyd George found nothing new to say; he referred to the second reason against reform "a serious diminution of the revenue could result from the amendment"; and again referred to the third reason against reform : "married people live together and have a joint duty in regard to the expenses of the household".

The logical fallacy of the 'household' test had been exposed on so many previous occasions that Sir William Bull could not let this rather tired reference to it slip by without expostulating:-

"A brother and sister live together, and they pool their incomes, and they go to the household expenses in exactly the same way as husband and wife but their incomes are not aggregated together for income tax purposes".

The new clause was defeated by 119 votes against 46 and thus supertax was introduced with no amelioration in the aggregation rule. However, a sixth reason against reform had been brought forward - namely that disaggregation would lead to tax avoidance by transfer of property.

1. Col. 1607.

5. 1910 - 1914 : Pressure for Reform

In the years following the introduction of supertax the main difficulty which was brought to the fore concerned the husband's liability to make a return of total income, including his wife's income, when he had no means of discovering what that income was. This difficulty will be discussed more fully in Chapter 8, which deals with accountability, but here it may be noted that on those occasions when accountability was considered, aggregation was also discussed.

(1) 1912 - Income tax on married women's property

For example, in the debates in the House of Lords on the subject of Income Tax on Married Women's Property¹ Earl Russell referred to the first and fourth reasons for reform (the tax laws should follow the property laws and there should be no penalty on marriage) when he said:-

"This is really an antiquated piece of legislation, no longer appropriate to the circumstances of the case...It is unreasonable because you are putting a particular difference in taxation upon two people who live together when they happen to be husband and wife as distinct from the case when they are father and son or two brothers or two sisters in the same house".

In reply, Lord Ashby St. Ledgers said:-

"If the incomes are taken together for the purposes of abatement they should be taken together for the purposes of collection. Perhaps you may say, why not treat the husband and the wife's incomes as entirely separate? That is a suggestion that appears

1. Hansard 14th October 1912 Cols. 823-834.

to have some advantages but it would be attended with much loss to the Exchequer and on that ground alone...it is not likely to be contemplated".

Here again is the second reason against reform - it would cost too much; and the Marquess of Landsdowne pointed out that the incomes were aggregated for income tax purposes but taxed separately for the purposes of the death duties. In winding up the debate the Lord Chancellor (Lord Haldane) accepted that:-

"in the case of income tax, the law dates from a period when the position of married women was very different from what it is today...the result of that is, of course, hardship...and my Rt. Hon. Friend the Chancellor of the Exchequer...has undertaken to consider it".

(2) 1913 - The Budget Resolutions

On 7th May 1913¹ Mr. Cassell moved an amendment to the Budget Resolutions to the effect that "the separate income of a married woman should not be deemed to be the income of her husband but should be treated as her separate income". Unfortunately, but inevitably, such an amendment was ruled out of order on the Budget Resolutions but it did give Sir F. Banbury the opportunity of attacking the aggregation rule, comparing the position of a husband and wife on the one hand with that of a brother and sister and that of two unmarried people living together on the other.

1. Hansard Vol. 52 Col. 2108.

(3) 1913 - The Women's Tax Resistance League

On 10th June 1913¹ a deputation from the Women's Tax Resistance League attended on Mr. Lloyd George at the Treasury and "laid before him what they considered to be grievances in connection with the taxation of married women". The deputation discussed both aggregation and accountability. On the subject of aggregation, Miss Amy Hicks said:-

"that although for all other purposes the married woman was allowed to have a separate income, yet for the purposes of taxation her income was still considered simply as part of her husband's. That imposed an unfair tax on marriages. The income tax law ought to be brought up to date and the income of husband and wife made separate taxable units".

Replying, Mr. Lloyd George said that he admitted that the present condition of the income tax law was adapted to a condition of things which existed before the new views with regard to married women's property came into existence but there were practical difficulties in the way of any change.

"He agreed that in its present form the law rather treated married women as if they had no legal existence at all. That was a legal humiliation and they were entitled to protest against it but the difficulties were of a political character...It would involve his finding £1,500,000 of revenue elsewhere immediately. He could not find that money elsewhere without imposing it on other people and married people, like others, would have to bear their share of it".

This exchange is of interest because the Chancellor appears to acknowledge the difficulty and to give some hope

1. The Times, 11th June 1913, page 10.

for the future; here again is the second reason against reform (it costs too much); no doubt the Deputation would have agreed that the money could not be found without imposing upon other people but would have wondered why that should not be done; if married people were to bear their share, why should not those who were not married bear their share also?

(4) Question as to timing of amendment

On 4th August 1913¹ Mr. Snowden referred to the Chancellor's reply to the Deputation and asked why the matter had not been dealt with in the Revenue Bill : the Chancellor replied that he hoped "to deal with the position of married women as regards income tax in committee in the Finance Bill".

(5) 1914 - The Debate on the Budget Resolutions

During the debates on the financial statement on 4th May 1914² Mr. Cassel referred to the promise made in the previous session to alter the law "in connection with the income tax levied on the joint incomes of husband and wife"; no amendment had been proposed by the Government and Mr. Joynson-Hicks pointed out that the budget "was dealing with income tax and supertax combined of something like 2/- in the £" and thus:

"the hardship to a married couple becomes very much more intensified than it was a few years ago".

1. Hansard Vol. 56 Col. 1038.

2. Hansard Vol. 62 Col. 98.

It will be noted that these remarks were addressed at the aggregation rule and a feeling appears to have been abroad that something was about to be done. For example later in the Debate Mr. J.M. Henderson¹ said that:

"some time ago, when the married women went as a deputation to the Chancellor of the Exchequer they seemed to a large extent to prevail upon him their case being absolutely unanswerable".

But some foreboding that all might not be as it should may have visited Mr. Evelyn Cecil who, during the course of the same debate, commented on the

"perpetual hostility which the Treasury show to man and wife...they are always trying to load the dice against the man and the wife".²

Mr. Henderson put the whole of the aggregation problem in a nutshell when he said:³

"It seems to me absolutely indefensible that you should treat a man and his wife as one individual for the purposes of taxation. They are two people. Their expenses are those of two individuals and so are their responsibilities".

In reply Mr. Lloyd George brought out once again the second reason against reform (it costs too much):

"The effect would be to put up the taxes of other persons and the point is whether they can in justice demand that other people should share the burden of £1,500,000 in order to redress what they regard as an injustice".

1. Hansard, 11th May 1914 Col 816.

2. Hansard 18th May 1914 Col. 839.

3. Col. 1346.

This point was ably answered by Captain Clive a little later in the debate when he said:-

"I cannot understand how the Chancellor of the Exchequer is able to dismiss the grievance (of married people) with so little sympathy. His chief argument seems to be that although there was some justification for the grievance it would cost £1,500,000 and he asked who is to pay that. I do not know why, if the grievance is admitted, it should not be removed simply because it is the bachelors and those who are not married who would have to pay a little more".

Mr. Lloyd George may have anticipated some such reply because he also brought out once again the third reason against reform (the household reason) and said:-

"I think the question is the income available for running the household".

This must have sounded entirely unconvincing because at this stage Viscount Hemsley 'made a remark which was inaudible in the Press Gallery' - or at least the delicacy of the editor of Hansard led him to record it as such. Mr. Lloyd George then went on to promise that a clause would be moved "when the Revenue Bill got into Committee".

However, nothing emerged and on 29th June, 30th June, 1st July, and 2nd July questions were asked as to how the Chancellor of the Exchequer intended to deal with the point. On 2nd July he promised that a new clause 'would be tabled next Monday'. Mr. Hoare stated that he was very anxious that the matter should be raised

"because there is a good deal of feeling in the country about it...time after time, owing to some particular reason, we have been prevented from dealing with it".

In fact, it was not until 15th July 1914 that the new clause was introduced.

6. 1914 - Option for Separate Assessment

On 15th July 1914 the House of Commons got its first opportunity of debating the new clause containing "provisions with respect to income tax of married persons". The clause, of course, deals only with accountability and is therefore fully discussed in Chapter 8. However, comments were made later in the debate ¹ about the fact that the proposals had been brought in 'almost at the last moment' and had not been included in the Finance Bill as originally presented. Mr. Dickinson said:

"I had hoped that when we were called upon to deal with it it would not be in relation to a clause brought in at the last moment".

The fact that the clause did not deal with aggregation did not prevent Mr. Cassel from introducing that subject when he rose to speak to the House. In acknowledging that the clause might be of assistance in removing the difficulties arising out of accountability he deplored the fact that nothing had been done to effect disaggregation. He referred to the first reason for reform (the tax laws should follow the property laws) and said:-²

"The anomalous position of the law at the present moment arises from the fact that the Income Tax Act of 1842 was passed long before the Married Women's Property Act.

1. Col. 2041.

2. Col 2016.

It was passed in the time while married women were still incapable of owning property and that property was, in fact and in law, considered the property of the husband...Under our law you still treat the income of husband and wife added together, although it is the income of two persons, with the requirement of two persons, as if it were the income of one person. The result is that husband and wife are called upon to pay more income tax in proportion to their ability to bear taxation than either bachelors or spinsters or persons who live together or whose relationship is of any other description than that of husband and wife legally married".

This was, of course, a re-statement of the fourth reason for reform (there should be no penalty on marriage). This point was reinforced later when Mr. Cassel stated specifically:-

"It is impolitic and unjust to select marriage as the one relationship for special and penal taxation...as a result of this clause not a single married couple will be relieved from a single farthing of what I call the marriage tax".

Then Mr. Cassel introduced a fifth reason for reform:

<u>Fifth reason</u>	:	<u>Husband and wife were two</u>
<u>for reform</u>	:	<u>persons and should be taxed</u>
		<u>as such.</u>

"You treat husband and wife as if they were one person when for all practical purposes and requirements they are two persons. They eat twice as much - they want twice as much clothes [An Hon. Member: "Three times as much"]. They require more house accommodation and for that reason they contribute more to the local authority in the shape of rates (and indirect taxes)".

Later¹ Mr. Cassel suggested two further alternatives to disaggregation:

1. Col 2023.

<u>Third alternative</u> :	<u>Partial disaggregation of</u>
<u>to disaggregation</u> :	<u>all income up to a specified</u>
	<u>limit (£700)</u>
<u>Fourth alternative</u> :	<u>A percentage deduction from</u>
<u>to disaggregation</u>	<u>the tax payable by a married</u>
	<u>couple</u>

No doubt bearing in mind the speedy success enjoyed by Mr. Darling in 1894, when he suggested partial disaggregation as an alternative to complete disaggregation, another version was proposed : this would apply to both earned and unearned income, up to a joint limit of £700, and would no doubt have made the wife separately accountable, although that point was not elucidated. The fourth alternative, of allowing married persons "a certain percentage off the tax which otherwise they would have to pay" was suggested as having the merits of simplicity.

In replying to Mr. Cassel, Mr. Lloyd George dealt at length with the whole subject of aggregation bringing forward again the arguments which had been used on previous occasions to prevent reform. Before these are considered, however, it may be of interest to note that Mr. Lloyd George referred to the deputation which had attended on him on 10th June 1913 and described the cases which had then been mentioned to him; all these concerned accountability and in respect of them all, he said, the clause provided a remedy. Without specifically saying so, he implied that the deputation had not been concerned with aggregation. But later in the Debate¹ Lord Robert Cecil said:-

1. Col. 2045.

"I do a little regret that the Chancellor of the Exchequer should have been led... to have said that in the deputation he received no claim was made in respect of the substantial question namely that husband and wife are treated as one person for the purpose of income tax. He is entirely mistaken. That point was certainly raised. I find that Miss Amy Hicks said this:-

"You lay stress on the fact that it is the household which should be taxed and not the separate parties making up that household. I should like to know if there is any reason why a husband and wife should be singled out for taxation and why the household should not be taxed in the same way as for instance, a mother, brother and sister or father and daughter ...why is the household regarded as the unit?"

"That is the whole argument and the Chancellor of the Exchequer dealt with it afterwards and if you read the whole of his speech it is quite plain that that was by far the largest part of the matter which was brought before him on that occasion".

Turning now to the reasons against reform developed by Mr. Lloyd George the interesting fact emerges that nearly all repeat the reasons already described and, although these appeared in a different order in his speech it is proposed here to treat them in the order which has been established by reference to their first appearance in point of time. To begin, then,

<u>The first reason</u>	:	<u>Advantages depend on</u>
<u>against reform</u>	:	<u>proportions of income in</u>
		<u>household</u>

This reason was first put forward in 1894 and is mentioned on page above. Let the argument be stated again by Mr. Lloyd George:-

"Take, first, a case where there is an income of £400 all belonging to the husband - £200 earned and £200 unearned. In that case the tax paid is £10. 16s. 8d. But supposing it is a joint income of which £200 earned belongs to the husband and £200 unearned belongs to the wife. In that case, if this amendment were carried, they would pay only £3. 10s. Is that fair? Is it fair that a man whose income is his own should pay £10. 16s. 8d. while in the other case, simply because the income is divided between husband and wife, only £3.10s. should be paid as the contribution of that household to the state? Where is the justice of that?"

The justice, is of course, that income tax is a tax on individuals, not on households. Husband and wife are two individuals and should therefore be taxed separately on two incomes. If the desire was to tax households then the principle should be applied to all households and not just to husbands and wives. Further, as was pointed out later in the debate,¹ "if a husband has £600 a year it is all in his control but if he has £300 and his wife has £300 the wife could spend all her money".

<u>Second reason</u>	:	<u>It costs too much</u>
<u>against reform</u>		

In 1894 the figure for disaggregation was £500,000 a year; in June 1913 it was £1,500,000 a year; in July 1914 it was £2M a year "without making any allowance for the kind of arrangement that would undoubtedly spring up" and with that "the deficiency would mount up by millions".

<u>Third reason</u>	:	<u>Married couples are members</u>
<u>against reform</u>	:	<u>of one household and have</u>
		<u>one income.</u>

1. Col. 2043.

Perhaps because the 'household' argument is by now beginning to look a little thin, it is for the purposes of this debate somewhat rephrased as:-

"The essential principle of marriage is identity of interest - you cannot have it both ways - that goes to the very root idea of the marriage law".

This statement is difficult to place within the context of English law : there has never been any system of community of property in England, and the property of the spouses was completely separate at law since the Married Women's Property Act: finally the so-called "identity of interest" was then mainly ignored for death duties, thus enabling the Inland Revenue, but not the married couple, to 'have it both ways'. Later in the debate¹ Lord Robert Cecil provided a very complete answer to the 'household' argument when he said, in referring to the theory that income tax depends on the ability to pay:-

"Of course, in that sense, that is true of every tax but the theory of the income tax is a much simpler matter. It is a tax upon the income of the individuals who make up the population...There is no trace of any other form of taxation in the whole of the income tax and it is perfectly plain that that is so because, in fact, households are not taxed. The incomes of households are not taxed in any other case whatever...Each individual is taxed".

Later he says:-

"I know of my own knowledge several households where unmarried sisters, who have been left tolerably well off, have lived together for the purpose of joining their incomes and living more comfortably, treating their joint incomes as one for the purposes of the household...In none of those cases are the individuals taxed on their household income".

1. Col. 2046.

And later Mr. Pretzman put it this way:-¹

"We do not tax households, we tax individuals. If our taxation were based on a tax on households the argument would have very great force but we do nothing of the kind...we should have to remodel our entire law if we were going to start on a basis of taxing households instead of taxing individuals".

<u>Fourth reason</u>	:	<u>Aggregation does not stop</u>
<u>against reform</u>	:	<u>people from marrying</u>

Again Mr. Lloyd George brings forward the argument that aggregation does not stop people from marrying. He was supported later in the debate by Mr. Rees Smith² when, in speaking of the fact that he knew of no single case where a couple were deterred from marrying because of tax, made the astonishing statement:-

"If such a case had occurred I should say that the Chancellor of the Exchequer had acted like a wise father in forbidding the marriage because neither of them are likely to bring happiness to the other or to anyone else".

<u>Fifth reason</u>	:	<u>All cases of hardship are</u>
<u>against reform</u>	:	<u>dealt with by partial dis-</u>
		<u>aggregation of wife's earnings</u>

Strangely, this reason against reform was not brought up in the debate.

<u>Sixth reason</u>	:	<u>Disaggregation would lead to</u>
<u>against reform</u>	:	<u>tax avoidance by transfers</u>
		<u>of property.</u>

This argument had first been used in 1909 and was re-stated as:

1. Col 2137.

2. Col. 2056.

"Husband and wife would undoubtedly make arrangements to reduce their taxation... stocks, shares and other property would be put in the name of the wife, or the husband as the case might be, in order to save income tax".

The examples which followed assumed that such transfers would only be of investments, thus favouring the family with a large unearned income at the expense of a family whose resources lay in one income which was all earned. This, however, ignores the fact that transfers of income, earned or unearned, under the covenant procedure were then available to other taxpayers and the abolition of the aggregation rule would have made the same procedure available to husband and wife; so the argument that families with unearned incomes would benefit at the expense of those with earned incomes appears misconceived. The fact that transfers of property, even for tax avoidance, are permitted to other taxpayers and should be permitted for married persons is developed on page above but was also referred to later in this debate by Mr. Pollock¹ when he referred to the provisions of the death duties "which would prevent the wholesale alteration in the tenure of property" and again by Mr. Reif Jones who said²

"The idea of collusive arrangements is very much exaggerated. They are rather difficult to carry out. I do not see amongst my acquaintance any marvellous generosity of character in husbands handing over half of their incomes to their wives to do what they like with. These arrangements involve a complete giving up of the control of the money".

1. Col. 3037.

2. Col. 2140.

<u>Seventh reason</u>	:	<u>Husband and wife get advantages</u>
<u>against reform</u>	:	<u>with death duties</u>

This is the first appearance of the seventh reason against reform and it was in fact brought forward to reply to the fourth reason for reform - that there should be no penalty on marriage. Mr. Lloyd George thought that the aggregation rule did not work unfairly for married persons

"because this was a case where the death duties come to the rescue".

He pointed out that brothers and sisters cohabiting together would pay death duties as if they were strangers. Now it will be recalled that before 1909 legacy and succession duties were not imposed on transfers between husband and wife but in that year Mr. Lloyd George had actually imposed such duties on property left between husband and wife, albeit at a lower rate than if they were strangers,¹ and although in 1909 a limited exemption had been introduced into estate duty law it only applied on the death of the surviving spouse and therefore benefited only the ultimate beneficiary. Further, the death duty saving, such as it was, only benefited those spouses with capital, whereas the aggregation rule penalised those spouses who both had incomes; it was likely that those who benefited were not the same as those who were penalised. Thus the reason given was not quite as valid as might be thought and the same could be said for the next new reason against reform which was then introduced.

1. See Chapter 5 page 287 ante.

<u>Eighth reason</u>	:	<u>It would not be used</u>
<u>against reform</u>	:	<u>in practice</u>

"I believe that even if the grievance were attempted to be redressed the vast majority of people would not claim this special treatment so complete is the identity of interest among married people".

This is, in fact, a reason for reform, as if it were correct then nothing would be lost by introducing the amendment. Thus, all the reasons against reform, with the exception of a reference to partial disaggregation, were re-stated. Two alternatives to disaggregation were also mentioned; a very brief reference was made to the second alternative, i.e. the 'quotient' system by Mr. Rawlinson, and Mr. Lloyd George discussed the fourth alternative (a percentage deduction from tax payable by a married couple) and this appeared to find some favour. However, no amelioration of the position was made; the Chancellor thought that he might prefer to give some relief through the child allowances and said that the point would be referred to "the Committee to enquire into the question" : it is thought that this is a reference to the Colwyn Commission which reported in 1920 and which did ultimately recommend alterations in the wife allowance: this will be discussed further in Chapter 9.

As the draft clause introduced into the 1914 Finance Bill dealt only with accountability the position with regard to aggregation remained unchanged. The debates, had, however, seen a re-statement of the arguments for and against reform and a discussion of some of the alternatives to aggregation. One new argument in favour (that husband and wife should be treated as two persons) had been

mentioned, and also two new arguments against reform (that husband and wife enjoyed advantages with death duties and that the reform would not be used in practice). Also two new alternatives to disaggregation were mentioned, namely, the partial disaggregation of all income below a specified limit and a percentage deduction from the tax paid by a married couple.

During the year following 1914 the debate on aggregation lay somewhat dormant, the emphasis being placed now on the allowances which are considered in Chapter 9. The next occasion for a review of the principles was occasioned by the Report of the Colwyn Commission in 1920.

7. 1920 - The Colwyn Report

The Report of the Royal Commission on the Income Tax in 1920, (the Colwyn Report)¹ deals with the tax treatment of the family unit in eight pages (54-62) and 45 paragraphs (238-283). On the subject of aggregation three paragraphs (263-265) are devoted to a discussion of the quotient system (the second alternative to aggregation already mentioned) and thirteen paragraphs (248-261) to an examination of the existing aggregation rule. A brief reference will therefore be made to the discussion of the 'quotient' system before the consideration of the aggregation rule is reviewed.

1. Cmd 615.

(1) The quotient system

The Colwyn Report examines the quotient system only in its "extreme form" which

"involves the aggregation of the incomes of the members of a household or family and the division of the aggregate amount by the number of the individuals maintained out of the income".

The proposal is discussed only in its application to a family with children and not to husband and wife alone; the proposal for a family quotient system did not find favour with the Commission and here it may be appropriate to regret that the Commission did not devote a little time to examining the proposal as an alternative to the aggregation rule within the context of the taxation of husband and wife only.

(2) The aggregation rule

It is clear that prior to the Colwyn Report the subject of aggregation had received a great deal of public attention:-

"The correct method of assessing married persons has received a great deal of public attention both before and since the appointment of this Commission. The matter has been freely ventilated in the Press and has been raised on several occasions in the House of Commons. In the course of our enquiry a considerable volume of evidence on the subject has been presented to us and we have examined witnesses from representative women's societies: we have also received a large number of letters in connection with this part of our investigation".

This would support the second reason for reform - that a change was demanded by many people. The Report refers to the option for separate assessment introduced in

1914 and records that many witnesses were unaware of the option "which had rarely been taken advantage of". It was acknowledged that this option did not affect the aggregation of the joint incomes and it was disaggregation, the assessing of husband and wife as "separate taxable units" which was urged by many witnesses. Reference was made to the fourth reason for reform, stated by these witnesses that there should be no penalty on marriage, and also to a variant of the first reason, namely:-

<u>Sixth reason</u>	:	<u>The principle of absolute</u>
<u>for reform</u>	:	<u>equality gives the right</u>
		<u>to separate taxation</u>

The reason is stated more fully in paragraph 251 of the Report:-

"By those who take this view it is claimed that the right to a completely separate assessment is an essential part of separate citizenship and that the principle of absolute equality in regard to civil obligations should override any principle of taxation".

Having thus referred briefly to three out of the six reasons for reform so far identified the Report proceeds to deal in detail with the reasons against reform. many of the points are now very familiar and indeed the wording used in one or two places almost exactly echoes the wording used on previous occasions. Although the reasons advanced in the Report appear in a different order they will be considered here in the order which has now been established by reference to the date of their introduction

<u>First reason</u>	:	<u>Advantages depend on</u>
<u>against reform</u>	:	<u>proportions of income in</u>
	:	<u>household.</u> ¹

The Commission is very impressed at the anomalies which would result

"if different sums of income tax were levied on two married couples enjoying equal incomes merely because in one case the income belonged wholly to one spouse and in the other to both".

No reference is made to the similar anomalies faced by unmarried households; the Commission thinks that, as regards married persons only, an amendment which would result in such anomalies would be both inequitable and ridiculous. Figures are quoted which compare a household where a husband earns £1,000 a year and his wife nothing (tax of £187. 10s. 0d) with a household where the husband earns £500 and the wife £500 (tax of £120. 0s. 0d). The Commission fail to point out that the same position would apply to a comparison of, say, a household where an earning son supported a widowed mother on the one hand and another household of two sisters with similar incomes on the other.

<u>Second reason</u>	:	<u>It would cost too much</u>
<u>against reform</u>	:	

In 1894 the cost of reform would have been £500,000 a year, in June 1913 it would have been £1,500,000 a year; in July 1914 the figure was £2M a year and in 1920 it had risen to £20M "increasing possibly to £45M in consequence of avoidance of tax by transfer of income from the husband to the wife"²

1. Colwyn Report - paragraphs 252 - 253.

2. Colwyn Report - paragraph 255.

<u>Third reason</u>	:	<u>Married couples are members</u>
<u>against reform</u>	:	<u>of one household and have</u>
		<u>a joint income</u>

The Colwyn Commission refers to the third reason against reform in these words:-

"We must regard the social conditions of the country in which the taxation is imposed. The great majority of married persons live together and use their several incomes for common purposes".¹

The Commission repeatedly emphasise this principle by reference to "the law of taxable capacity" and "the ability to pay". So -

"The incomes are aggregated because the law of taxable capacity is the supreme law in matters of taxation and taxable capacity is in fact found to depend upon the amount of the income that accrues to the married pair".²

and

"The outstanding principle of ability to pay which we recognise as governing all questions of taxation".³

Again, no reference is made to the "ability to pay" of households shared by unmarried persons. It is thought that the severe inadequacies of the third reason against reform are fully dealt with earlier in this Chapter, but two short references are particularly appropriate here. In 1914 Mr. Cassel had said:⁴

"Under our law you still treat the income of husband and wife added together as if it were the income of one person. The result is that husband and wife are called

1. Colwyn Report, paragraph 258.

2. Paragraph 259.

3. Paragraph 258.

4. Page 342 above.

on to pay more income tax in proportion to their ability to bear taxation than either bachelors or spinsters or persons who live together or whose relationship is of any other description than that of husband and wife legally married".

And again, in 1914, Lord Robert Cecil referred to the theory that income tax depended on the ability to pay but pointed out that income tax was a tax on individuals, not on households, because households were not taxed in any case other than husband and wife.¹

<u>Fourth reason</u>	:	<u>Aggregation does not</u>
<u>against reform</u>	:	<u>stop people from marrying</u>

The Colwyn Commission² had an answer for those who said that aggregation did stop people from marrying. It said:-

"If the allegation is correct that joint assessment is conducive of immorality (an allegation unproved in the course of our enquiry and characterised by one of the women witnesses as being neither reasonable nor probable) the logical, even if not the practicable, remedy is to render liable to joint assessment the income of two unmarried persons living together".

The further logic would be to jointly tax any unmarried persons, whether two or more, sharing the same household : this was clearly further than the Colwyn Commission wished to go and they agreed that even their suggestion was 'impracticable'.

<u>Fifth reason</u>	:	<u>All cases of hardship are</u>
<u>against reform</u>	:	<u>met by partial disaggregation</u>
		<u>of wife's earnings</u>

1. See page 344 above.

2. Paragraph 254.

As in 1914 this reason against reform is not brought forward on this occasion : this seems to indicate that it was widely considered to provide no answer to the difficulties and, in any event, the Report later recommended the abolition of the provision.²

<u>Sixth reason</u>	:	<u>Disaggregation would lead to</u>
<u>against reform</u>	:	<u>avoidance by transfers of</u>
		<u>property</u>

The Commission refers¹ to the cost of reform and the additional loss which would arise from transfers of income between spouses. The continuation of the rule which deprives married persons from exercising rights available to all who are unmarried is justified in this way:

"To shift a burden from the shoulders of persons whose joint income is such that their ability to pay permits of its being equitably borne by them and to place that sort of burden, by means of an increased rate, upon the shoulders of other taxpayers would be, in our opinion, entirely contrary to all principles of equitable assessment".

The equity in a system which prevents a husband with £1,000 a year from sharing it with his wife, while permitting the man next door, with £10,000 a year to share it with his mother, or common law wife, is sometimes hard to discern.

<u>Seventh reason</u>	:	<u>Husband and wife get</u>
<u>against reform</u>	:	<u>advantages with death duties</u>

The Colwyn Commission point out³ that "the joint dependency is recognised, to the benefit of the wife, for other purposes of taxation, e.g. legacy and succession

-
1. Paragraph 233.
 2. Paragraph 255.
 3. Paragraph 258.

duties payable by a widow are less than those payable by a person unrelated to the deceased". To the extent that some benefit was available, this is a valid comment, but it is thought that, on balance over the whole field of taxation, the aggregation rule in itself brought more disadvantages than advantages to married persons.

<u>Eighth reason</u>	:	<u>A change would not be</u>
<u>against reform</u>	:	<u>used in practice</u>

Again, this reason is not mentioned by the Colwyn Commission, rather wisely it is felt. The Commission did, however, introduce a new reason against reform - the ninth.

<u>Ninth reason</u>	:	<u>Disaggregation would result in</u>
<u>against reform</u>	:	<u>the abolition of the marriage allowance</u>

"It seems to us that it would be quite illogical, under the same system of taxation, to make an allowance which recognises the joint responsibilities of husband and wife and at the same time to grant relief to each of the partners to the union as though they were complete strangers. If separate assessment were granted the marriage allowance should logically be abolished and the result would be a shifting of burdens from rich to poor because in the vast majority of cases the wife has either no separate income at all or a separate income less than the amount of the present marriage allowance and far less than the allowance we suggest should be made".¹

Now this reason against reform is defective in two respects. First, the abolition of aggregation would not 'logically' lead to the abolition of the marriage allowance. The two matters are entirely distinct : each has a separate history and separate statutory provisions : aggregation existed for nearly a century and a quarter without the marriage allowance and the marriage allowance could exist

1. Paragraph 257.

independently without aggregation : other personal allowances, e.g. child allowances and housekeepers allowances were given to taxpayers who supported others out of their income without any concomitant requirement of aggregation. Child allowance has, of course, now been abolished¹ but other minor personal allowances still exist on this basis. It is in fact a major defect of the Green Paper on the Taxation of Husband and Wife² that it fails adequately to distinguish between the effects of the abolition of the aggregation (and accountability) rules and the completely separate considerations which apply to the marriage allowance. The subject of the allowances is considered more fully in Chapter 9, but here it may be recorded that any difficulties as to the future of the allowance are not relevant to a consideration of the aggregation rule; this is shown by a consideration of the systems adopted in Canada and Australia, dealt with in Part III.

The second defect in the ninth reason against reform is that it ignores the fact that with the abolition of aggregation transfers of income would be available to all husbands and wives, whether the income were earned or unearned; each wife would have her own (full) personal allowance to use in respect of such transferred income: there would be no shifting of burdens from rich to poor - the poor would benefit the most from the arrangement.³

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1. Other than the child allowance for unmarried persons in section 14 Taxes Act.
 2. Cmnd 8093.
 3. The concept of transferred income is discussed in Chapter 16 post; it is, however, not put forward as the ideal practical solution to the provision for a nil or low income spouse - a claim for a transferred allowance is preferred.

Finally, the Colwyn Commission led into the tenth reason against reform:

<u>Tenth reason</u>	:	<u>The obligations of marriage</u>
<u>against reform</u>	:	<u>recognised by the wife</u>
		<u>allowance</u>

"There are two methods of recognising, by diminished taxation the obligations of marriage. One is to make an allowance... The other method is by a complete severance in the treatment of husband and wife for income tax purposes...The first method, seeing that it affects every married couple is far more likely than the second to encourage marriage".

The distinctions between the aggregation rule and the allowances are discussed above : the two provisions are completely distinct and the marriage allowance could continue after disaggregation although the consequent entitlement of the wife to her own full single personal allowance would diminish its importance substantially. Following the publication of the Colwyn Report no amendment in the aggregation rule was made, although alterations in the allowances were introduced and these are discussed in Chapter 9.

The Report is of great interest in this respect; it referred briefly to two of the reasons for reform (that it was demanded by many people and that the aggregation rule was a penalty on marriage) and introduced one new reason, namely, that the principle of equality gives the right to separate taxation. But in enumerating the reasons against reform all the old arguments are used : it is true that two new reasons are introduced but both these concern the allowances which had only been first given in 1918 and could not therefore have been considered on a previous occasion.

8. 1954 - The Radcliffe Report

The Radcliffe Report dealt rather more fully than had the Colwyn Report with the subject of family taxation : aggregation, however, is considered quite briefly in nine paragraphs (113-121). As did the Colwyn Report, it considers some alternatives to aggregation before considering the rule itself.

(1) Alternatives to aggregation

Three alternatives are discussed : one is the second of the alternatives already mentioned (the quotient system) and two new alternatives are introduced, namely separate taxation with a wife allowance and separate taxation with the right to opt for a quotient system. A short reference will be made to each.

<u>Second alternative</u>	:	<u>The quotient system</u>
<u>to aggregation</u>	:	

The Colwyn Commission considered the quotient system only in its application to a family with children; the Radcliffe Commission also considered its application to husband and wife. The quotient system, as applied in France, was summarised as:-

"The incomes of husband and wife are aggregated...the aggregate income is then divided... and tax is charged separately on each part...Thus in effect a married couple pays twice the tax paid by a single person with half their joint income...If this system were to be adopted its immediate effect would be a marked improvement in the relative position of most married couples...in the upper income ranges". 2

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1. The Report of the Royal Commission on the Taxation of Profits and Income, Cmd 9105.
 2. Paragraph 114.

The adoption of the quotient system is not recommended:-

"Adoption would mean a shift in the distribution of the tax burden from married persons to single ones to an extent that seems to us excessive".¹

This is a valid comment : the quotient system not only neutralises the effect of aggregation but gives a positive tax advantage to married persons over single persons unless both husband and wife enjoy nearly identical incomes. One disadvantage of the quotient system, however, lies in the fact that a joint account of income is essential - there is no possibility of separate accounting.

<u>Fifth alternative</u>	:	<u>Separate taxation with</u>
<u>to aggregation</u>	:	<u>wife allowance</u>

The Report points out that in Canada and Australia the incomes of husband and wife are separately taxed but that:

"if...a wife...has no income or only a small one the husband receives a special personal allowance varying with the amount of the wife's means".

Unfortunately, apart from mentioning this alternative, the Report contains no further comment on it; at least it is not specifically rejected as are the other two alternatives which are discussed.

<u>Sixth alternative</u>	:	<u>Separate taxation with option</u>
<u>to aggregation</u>	:	<u>to choose quotient system</u>

In the United States, says the Report:-

"assessment of husband and wife is made separately but they have the right to choose aggregation (under the quotient system) in which event the tax charged is twice the tax on half the joint income".²

1. Paragraph 121.
2. Paragraph 115.

The Report does not recommend the adoption of this system; in addition to the shift in the burden of taxation which results from the quotient system, and which is mentioned above, the following reason is given:-

"The U.S. system is based on an equation between the combined incomes of husband and wife and the separate income of two individuals which does not strike us as sufficiently convincing".¹

This is a valid comment on the quotient system generally; the advantage of the U.S.A. system over the French system is that the former gives an initial right to separate accounting but with the option to choose the money advantages of the quotient system if the spouses are willing to forego the right to separate accounting : with the French system a joint account is compulsory.

(2) The aggregation rule

Having referred to the alternatives to aggregation discussed in the Report a reference can now be made to the discussion of the aggregation rule itself : and here it is disappointing to note that no new reasons are mentioned either for or against reform : the old ground is re-trodden once more with some of the illustrations brought up to date. Here the reasons are considered in the order previously adopted in this Chapter, beginning with the three reasons for reform which are briefly mentioned.

<u>First reason</u>	:	<u>The tax laws should follow</u>
<u>for reform</u>	:	<u>the property laws</u>

1. Paragraph 121.

The Report stated:-

"It is true that aggregation has been a feature of the tax since it was first imposed in the year 1799:¹ and that a married woman's legal control of her property was restricted then and thereafter in a way that it is not now...It does not follow that aggregation has ever had any real connection with her 'servile' status in relation to her property...It is more likely that aggregation was introduced (because) it afforded a convenient means of collecting the tax, more especially as the husband was a necessary party to any suit against his wife at common law...In fact the historical argument seems to us neither a good argument for retaining the rule, nor a good argument for abolishing the rule if it is a good one".

Now the statement that the aggregation rule was introduced purely as a means for collecting the tax must be misconceived, as husband's accountability was introduced six years before aggregation; further, for other persons under a disability in 1799, e.g. children and "lunatics" arrangements were made for the tax to be collected from other persons, usually trustees, without any necessity for aggregation : finally, where the wife had separate trustees the tax could have been collected from them without any intervention by the husband. Although the historical argument may not be a good argument for abolishing the rule "if it is a good one" the historical argument does show the complete change in the underlying principles upon which the rule was constructed and the burden of proof that the "rule is a good one" must therefore change so that those who argue for retention

1. It will be recalled from Chapter 1, page 40, that aggregation was not in fact introduced until 1805.

of the rule have to make out a positive case in support.
The view is taken that this has not been done.

<u>Second reason</u>	:	<u>Reform was demanded by</u>
<u>for reform</u>	:	<u>many people</u>

The Report says that the Commission

"received such a volume of representations from different quarters to the effect that aggregation of incomes of husband and wife ought to be abolished and the income¹ of each assessed as that of an individual"

that they found it necessary to express an opinion on the rule. This confirms the view that the rule was of concern to many people and reflects a similar statement made by the Colwyn Commission (page above).

<u>Fourth reason</u>	:	<u>There should be no penalty</u>
<u>for reform</u>	:	<u>on marriage</u>

"It was said to us that aggregation is socially undesirable since it tends to discourage marriage and to induce a man and woman with separate incomes to live together without becoming husband and wife.. We can give very little weight to this argument...It is not true as a general statement that aggregation operates as a tax on marriage. It is only true of a man and woman both of whom have incomes and then only if certain ranges of income are exceeded".

The Report then points out that, as a result of the system of allowances, a two-earner married couple could, in 1955, be paying less tax than two single persons. This is a valid comment but it ignores the fact that the system of allowances is completely distinct from the system of aggregation. The disadvantages of aggregation have always been most acutely felt in cases where both

1. Paragraph 116.

husband and wife had incomes and where certain ranges of income were exceeded but there are other disadvantages also which could apply in any income range : these arise out of the inability of a wife to enjoy a separate personal allowance against her own investment income however small; the inability of a husband to transfer income or assets to his wife or vice versa; and the restriction of some quite substantial reliefs and exemptions (e.g. mortgage interest relief and the capital gains tax relief) so that husband and wife have only one set between them and not two. The fact that aggregation is not a tax on all marriages is not an answer to the fact that it is a tax on some.

The reasons against reform which are contained in the Report have all been heard before.

<u>First reason</u>	:	<u>Advantages depend on pro-</u>
<u>against reform</u>	:	<u>portions of income in</u>
		<u>household</u>

Here is this reason in the words of the Radcliffe Commission:-

"Such a method of taxation (i.e. disaggregation) would mean that one married couple bore a greater or less burden of tax than another according to what must surely be an irrelevant distinction for this purpose, namely the proportion in which the combined income was divided between the partners, for under a system of graduation if each of two married couples has the same combined income but one owns its combined income in proportions more nearly equal than the other, that one would be the likely to pay the less tax".¹

The logical fallacy of comparing the joint income of married couples in a tax system which only taxes individuals and not households has been fully discussed above.

1. Paragraph 119.

Second reason : It costs too much
against reform :

In 1894 the cost of reform had been £500,000; in 1913 £1,500,000; in 1914 £2M; in 1920 £20M and in 1955 £143M, assuming that all married couples would equalise their incomes, and

"even if transfers of holdings are not contemplated there would necessarily be a big loss of tax in abolishing aggregation".

The true reason behind the argument of cost is discussed above and the problem is becoming more difficult to solve with the passage of time.

Third reason : Married couples are members
against reform : of one household and have a
joint income

This is the way the Radcliffe Commission put it:-

"It does appear to us that marriage creates a social unit which is not truly analogous with other associations involving some measure of joint living expenses and that to tax the incomes of two married people living together as if each income were equivalent to the income of a single individual would give a less satisfactory distribution than that which results from the present rule".

The reasons for the "less satisfactory distribution" are given as the first, second and sixth reasons against reform; namely, that the advantages would depend upon the proportions of income in the household, that it would cost too much, and that disaggregation would lead to avoidance through transfers of property; these are considered in the appropriate order but here it may be noted that no attempt is made to define the way in which, for income tax purposes, the social unit of marriage in fact

differs from other associations involving joint living expenses. Further, the surprising statement that any new rule would treat the incomes of two married people living together "as if each income were equivalent to the income of a single individual" ignores the fact that each income is the income of a single individual.

<u>Fourth reason</u>	:	<u>Aggregation does not stop</u>
<u>against reform</u>	:	<u>people from marrying</u>

The Commission say:

"We are sceptical of the suggestion that men and women are in fact dissuaded from marriage by any such nice calculation of the financial odds. In the nature of things it is impossible to establish or reject it by any concrete evidence...the present treatment of the income of married couples for the purposes of tax is not more likely to lead people away from marriage than to tempt them into it".

This is fair comment : but it does not remove the injustice which results from retaining the rule.

<u>Fifth reason</u>	:	<u>All cases of hardship are</u>
<u>against reform</u>	:	<u>met by the partial dis-</u>
		<u>aggregation of wife's earnings</u>

It will be recalled that the partial disaggregation of wife's earnings, which had been introduced in 1894, had been abolished in 1920 after the Report of the Colwyn Commission. This reason against reform was not therefore relevant in 1954 and was not mentioned in the Radcliffe Report.

<u>Sixth reason</u>	:	<u>Disaggregation could lead to</u>
<u>against reform</u>	:	<u>tax avoidance by transfers of</u>
		<u>property</u>

The Commission say that if the aggregation rule were to be abolished:

"there would be a natural tendency for husbands to try to arrange to transfer so much of their incomes to their wives as would produce an equal division".

They go on to say that no doubt legislation could be introduced to counteract this but:

"it would mean an arbitrary insistence on maintaining the existing position as between different married couples at the date of the new system and would thus confer a permanent but unreasonable advantage on those whose combined incomes at that date happened to be more or less equally divided".

The ability of any non-married taxpayer to transfer income and assets quite freely is discussed above : such transfers must be bona fide, though, and the genuine relinquishing of control over the assets or income would be a disincentive to wholesale transfers especially in cases of some marital disharmony. In addition, the capital taxes on such transfers would have to be taken into account.¹

<u>Seventh reason</u>	:	<u>The husband and wife have</u>
<u>against reform</u>	:	<u>advantages with death duties</u>

By 1955 legacy and succession duties, which had given some advantages to transfers between husband and wife had been abolished and the limited advantage given by estate duty was of benefit to the remainderman only after a limited interest to the surviving spouse. Rather wisely, the Commission did not mention this reason against reform. However, in 1982 there is no doubt that husband and wife do have advantages with capital transfer tax and also some advantages with capital gains tax although here

1. See further discussion in Chapter 16 post page 627.

account must also be taken of the disadvantages : all these are fully discussed in Chapter 5 above.

<u>Eighth reason</u>	:	<u>It would not be used in</u>
<u>against reform</u>	:	<u>practice</u>

Wisely, it is thought, the Radcliffe Commission made no mention of this reason against reform, originally suggested by Mr. Lloyd George in 1914 and sensibly forgotten about ever since .

<u>Ninth reason</u>	:	<u>It would lead to the abolition</u>
<u>against reform</u>	:	<u>of the marriage allowance</u>

<u>Tenth reason</u>	:	<u>The obligations of marriage</u>
<u>against reform</u>	:	<u>are recognised by the wife</u>
		<u>allowance</u>

The Radcliffe Commission consider these two reasons together as follows:-

"An income on which two people have to live as married persons has not the same taxable capacity as the income of a single individual. But in our view the right way to allow for the difference is to make an appropriate allowance for the fact of marriage in the assessment of the unit... given aggregation the marriage allowance is due whatever the size of the wife's income".

If the Radcliffe Commission had accepted the logical corollary of their first sentence, namely that two incomes on which two people have to live as married persons have the same taxable capacity as the income of two single individuals, they would not have confused disaggregation with the question of allowances. But the inability of the Commission to see married people as two individuals seriously affected the quality of the recommendation they made which was:

"that taxation of the combined incomes of husband and wife is to be preferred to their separate taxation as separate units because the aggregate income provides a unit of taxation that is fairer to those concerned".

Whether this means fairer to married people or to unmarried people is not stated : the system is not fair because it does not provide equity as between individuals : a married woman generally pays more tax than a single woman and a married man pays less tax than a single man. The present system of allowances has created distortions but, leaving allowances aside, aggregation can only bring disadvantages to married couples as compared with single tax payers.

9. 1969 - A New Clause

During the 1960's pressure for some reform of the tax system as it affected married women began to mount : as a result of the 1944 Education Act the 1950's had seen the entry of more young women into higher education and then into the professions : more women were earning high incomes and more women wished to continue with their professions after marriage. In 1968 Mr. Heath set up a Committee of the Conservative Party (the Cripps Committee) and as a result proposals were put forward for discussion; a study group of the Labour Party was also set up to examine the subject. Both subsequently recommended separate taxation for married women. At about the same time the Women's Taxation Action Group, an offshoot of the Women's Interprofessional Working Party, also issued

a report calling for separate taxation.

On 6th January 1969 The Times published a letter from Dr. Hilary Summerskill about the tax burden on professional women. She said:

"Two people each earning £5,000 a year pay a total of £3,031 in tax if they are single but £4,062 if married".

She said that the country was being deprived of the talents of many professional women, especially doctors and scientists, and recommended that husbands and wives should be capable of being separately assessed for tax purposes.¹ Published correspondence followed, some in support, some not, and on January 17th The Times published an article showing that the additional tax paid by a married couple with joint earnings of £20,000 was £4,000. A couple with four children and joint earnings of £9,500 would be £841.13s. 6d. better off after a divorce.

Other newspapers took up the theme. The Guardian on 25th March 1969 said:

"Society has changed but the law and administration have not kept pace".

On the same day the Financial Times said that any revenue estimate of the cost of a change

"must take account of the fact that many women might then find it worth their while to work and be taxed who now find their husband's rate of surtax too formidable a deterrent";

and on 28th March the New Statesman said:

"The system actively discourages many trained doctors and teachers from practising their professions".

1. The Times 6th January 1969 p. 19a.

On 17th April 1969, during the debate on the Budget Resolutions Mr. Patrick Jenkin deplored the lack of any amending provision and promised to bring the subject forward in Committee : he said that

"The Treasury have long had a hostility to married women".

Later in the same debate Mr. Houghton said:-

"It is time...that we relieved women of some of the humiliations and injustices of the taxation system".

The new clause was introduced as promised by Mr. Patrick Jenkin in Standing Committee on 26th June and briefly debated. The clause was designed to disaggregate the earnings of a married woman, entitling her to get her own allowances and reliefs against her own income, but on the basis that the existing levels of married man's allowance and wife's earnings allowance should remain.

In introducing the clause Mr. Jenkin referred to the first, second and fourth reasons for reform.

<u>First reason</u>	:	<u>The tax laws should follow</u>
<u>for reform</u>	:	<u>the property laws</u>

"The Victorian attitudes to married women which are enshrined in our tax legislation ...stem from an age when a married woman was regarded as subsidiary and inferior to her husband and indeed in some ways little better than a mere chattel".

"The fossils of the ancient common law view of women lie deeply embedded in our tax laws many of them unchanged for over a century".

"All this stems from the basic concept that a married woman has no separate fiscal existence".

And later in the same debate Mr. Macleod said:

"I regard the taxation of married women in this country as barbaric in comparison with the way in which many other countries treat the same problem".

<u>Second reason</u>	:	<u>Reform was demanded by</u>
<u>for reform</u>	:	<u>many people</u>

Mr. Jenkin referred to "the growing resentment about this tax treatment of married women", and later:-

"The women's organisations of all sorts have been pressing for relief along these lines for many years".

Sir Henry D'Avigdor Goldsmid referred to the Press Campaign which has been mentioned, and later Mr. Macleod referred to the people who had been writing to him "to express very deep resentment" at the state of the law.

<u>Fourth reason</u>	:	<u>There should be no penalty</u>
<u>for reform</u>	:	<u>on marriage</u>

In 1969 Mr. Jenkin could state that the tax laws were preventing at least one couple from marrying but the main thrust of the 1969 debate was that the tax laws were a disincentive to married women who wished to work - this was a new penalty on marriage

"The new clause, by disaggregating the earned income of married women...would give great encouragement...to those many women who would work were the tax penalty not so high".

Mr. Jenkin made it clear that the limitation in the clause to disaggregation of wives earnings was only a first step on the way to complete disaggregation, the clause was to be a "modest start".

In replying to the address on the new clause Mr.

Diamond, to his eternal credit, brought out only one of the previously stated reasons against reform - the second - and put forward no less than five new reasons; they were not very good reasons but at least they were new.

Second reason : It would cost too much
against reform :

The previous costs given for complete disaggregation had been:

1894	500,000
1913	1,500,000
1914	2,000,000
1920	20,000,000
1955	143,000,000

The cost of disaggregation of wife's earnings only in 1969 was to be £9M and Mr. Diamond said:

"I could not possibly suggest to the Committee that if we were going to reduce the tax yield by £9M the first to benefit would be those bearing heavy rates of tax because of their high joint incomes".

This ignores two points : it was not necessary to reduce the yield as the rates could have been adjusted; and the change need not necessarily have benefited persons with high incomes - the compensating taxes to maintain the yield could have been levied at the higher rates.

These were the new reasons against reform introduced in 1969:-

Eleventh reason : At lower income levels a
against reform : married couple are better
off than two single persons

This is true but it results in the distortions arising from the anomalous provisions regarding allowances and is no answer to a proposal for disaggregation. In any

event, the clause proposed would have retained the existing allowances.

<u>Twelfth reason</u>	:	<u>Husband and wife both earning</u>
<u>against reform</u>	:	<u>pay less tax than if all</u>
		<u>income earned by husband</u>

This is an extraordinary statement. What it means is that two people pay less tax than one person with an income equal to their joint income. As this is an essential result of any progressive tax system it is not thought that the point takes the discussion any further.

<u>Thirteenth reason</u>	:	<u>Married women work for satis-</u>
<u>against reform</u>	:	<u>faction and not for money</u>

Mr. Diamond said:

"The satisfaction felt by a married woman in resuming her professional work is to my mind far more important than the remuneration involved. We all have massive experience of this sort of thing - that they enjoy their work and are not concerned with the level of taxation that is brought to bear".

Why married women should feel more satisfaction in their work than single or widowed women, or any men, is hard to see. Replying, Mr. Macleod said:

"I do not meet these saints as regularly as the Chief Secretary. The people who write to me express very deep resentment at the state of the taxation law".

<u>Fourteenth reason</u>	:	<u>The Royal Commission did not</u>
<u>against reform</u>	:	<u>favour disaggregation</u>

Said Mr. Diamond:

"The principle is one...which was examined by the Royal Commission...who found nothing to object to in the idea of aggregating husband's and wives income".

Comments on the views of the Royal Commission (in the Radcliffe Report) are set out above.

Fifteenth reason : The present rule only adversely
against reform : affects a few higher rate tax-
payers

Mr. Diamond put this reason this way:-

"This is broadly a surtax problem...the difficulty arises at an area not below £5,085 a year"

In replying to this Mr. Macleod said:

"The fact that comparatively few people are involved is never acceptable to me as an argument for perpetuating an injustice if an injustice exists".

He concluded with a commitment that as soon as his party had an opportunity of doing so, they would greatly improve the position : the new clause was lost. Perhaps this is not surprising when it is borne in mind that the Government of the day had, only the previous year, introduced the aggregation of the investment income of minor children.

10. 1971 - Disaggregation of Wife's Earnings

When the Conservative Party formed the next Government they fulfilled their promise and clause 15 of the Finance Bill in 1971 introduced provisions for an option for disaggregation of wife's earnings. The principle was similar to that introduced in 1894 and abandoned in 1920 but there were many differences in detail. Among the points of similarity were that in both cases the disaggregation only extended to a wife's earnings and not her investment income, and for the purpose of the rule in each case the wife's earnings were treated as one income and the rest of the couple's total income (husband's earnings

and investment income of both spouses) formed another income. The differences were more numerous : in 1894 there was a maximum limit on the joint income (£500) above which the rule could not apply : no such limit was imposed in 1971. Again in 1894 the husband, on behalf of both husband and wife, had to make the claim for relief and the relief was given against his total liability : in 1971, the option had to be exercised by both husband and wife as, on exercise, the husband lost the (higher) married man's allowance and the wife was given the relief against her earnings. The 1894 option was only of benefit to low-income couples : the 1971 option was only beneficial to wives who either had high earnings themselves or whose husbands had a high income. In neither case did an option alter the principle of husband's accountability.

The Reports of the two Royal Commissions (Colwyn and Radcliffe) and the Parliamentary Debates previously referred to exhaustively considered all the reasons against reform so it is refreshing to note in the debates on clause 15 a re-statement of the existing six reasons for reform and the propounding of two new reasons.

<u>First reason</u>	:	<u>The tax laws should follow</u>
<u>for reform</u>	:	<u>the property laws</u>

This reason could not have been better stated than it was by Mr. David Marquand who, on other grounds, opposed the clause; he said:

"...it is monstrous in the present day and age that Victorian conceptions of the status of married women should still be enshrined in the taxation system".

Second reason : Reform was demanded by
for reform : many people

The Solicitor-General, Sir Geoffrey Howe said:-

"The truth is that the change in question has been recognised as both necessary and fair...by all the women's organisations over a number of years...it has been supported by the Women's Taxation Action Group, The Interprofessional Working Party, the Association of Headmistresses, the British Dental Association, the Medical Women's Federation and other bodies".

Third reason : The tax laws should be con-
for reform : sistent between themselves

As was pointed out by Mr. Derek Coombes:-

"On death capital is treated as if it were separately owned. Surely that is totally contradictory when income from capital is treated and taxed jointly in life".

Such comments must, of course, now be read subject to the capital transfer tax provisions, introduced in 1975, which do provide for exemption on transfers between husband and wife.

Fourth reason : There should be no penalty
for reform : on marriage

The obvious reason for the introduction of the clause, namely to reduce the penalty on marriage, is mentioned by the Solicitor-General:-

"The object of the clause is to remove the inequity of the harsh effect of aggregation on the minority who pay more tax because they are married - in effect to remove the tax on morality".

The disparity between married and unmarried couples is also mentioned by Mr. Hamling:-

"It is becoming increasingly common for couples not to marry but simply to live together in which case...they make tax returns as single people - Increasingly as the custom grows of couples living together but not marrying there will be an increase in anomalies in this regard".

Finally, the disincentive effects on working wives of the tax laws generally were widely discussed : the other "penalty on marriage" was the lack of any adequate financial reward for work, after the high rates of tax had been paid.

<u>Fifth reason</u>	:	<u>Husband and wife should be</u>
<u>for reform</u>	:	<u>taxed as two persons</u>

Mr. Marquand accepts the argument:-

"that married women ought, on principle, to be treated as separate individuals for tax purposes because it is inherently discriminatory to treat them as though their incomes belonged to their husbands".

and later Sir Brandon Rhys Williams said:-

"The income of every man woman and child should be taxed at the same rate. It is objectionable to treat a married woman as an adjunct. She should be treated as a person in her own right".

<u>Sixth reason</u>	:	<u>The principle of equality</u>
<u>for reform</u>	:	<u>gives the right to separate</u>
		<u>taxation</u>

Mr. Hamling, although opposing the clause, agreed:-

"I accept the argument for separate taxation of incomes of husband and wife on the ground of sexual equality".

and later:

"I submit that if we are to proceed along the road of sex equality then all her income should be regarded as hers and...no income of hers ought to be aggregated with that of her husband".

The two new reasons for reform were:

<u>Seventh reason</u>	:	<u>Disaggregation should also</u>
<u>for reform</u>	:	<u>apply to investment income</u>

It was widely agreed that the provisions of the clause were only a "modest start". Mr. Derek Coombes said:-

"The clause should apply to all income and not just to earnings".

Mr. Bruce-Gardyne did not like the

"distinction between so-called earned and so-called investment income".

The Solicitor-General refers to the 'Treasury argument' that to include investment income in the clause "would allow manipulation between two investment incomes" but prefers his own argument for confining the clause to earned income namely that

"If one begins recasting the whole tax system upon the theoretical basis of equality of the sexes one embarks upon an exceedingly complex task",

and that equity in the way proposed in the new clause "seems to be enough to be going on with".

<u>Eighth reason</u>	:	<u>An injustice which only</u>
<u>for reform</u>	:	<u>affects a minority is still</u>
		<u>an injustice</u>

In support of the clause the Solicitor-General said:-

"Of course if one is removing an inequity from a minority it is by definition a minority but that does not destroy the strength of the case for removing the inequity".

Objections were made to the clause on the erroneous

ground that it conferred some benefit on those with large incomes which was not available to those on small incomes; this, of course, was not the case. The clause gave no right to separate accounting at all and at lower income levels a married couple benefited from the combination of the (higher) married man's allowance and the wife's earnings allowance; these were both lost when the option under the clause was exercised and replaced by two single personal allowances.

A considerable amount of discussion also took place about the timing of the notice required under the clause but ultimately the clause was accepted and still represents the only alternative to aggregation : its defects have been mentioned above but here it may be recalled that among these are:-

- (1) the option must be exercised by both husband and wife : a wife alone has no entitlement to disaggregation under the clause;
- (2) the option does not extend to a wife's investment income;
- (3) the option does not involve separate accounting although this could be achieved by an option for separate assessment, the complexities of which, however, are daunting;
- (4) the advantages of the option depend on a number of ever-changing factors, e.g. size of incomes of both spouses, the amount of personal allowances and the level of higher rate tax bands: spouses have to be constantly vigilant in

exercising the option if it is advantageous and withdrawing it if it is not; and

- (5) the clause did not provide any solution to the other disadvantages of aggregation i.e. no transfers of income between spouses and no entitlement to a second set of reliefs.

11. 1975 - The Institute for Fiscal Studies

In 1975 Mr. Graeme Macdonald gave a lecture to members of the Institute for Fiscal Studies on "Taxation and the Family Unit". Mr. Macdonald later became a member of the Meade Committee and some important ideas which were subsequently developed in the Report of that Committee first appeared in the 1975 lecture.

The author accepts that "horizontal equity" means "that people with the same taxable capacity are taxed in the same way" but does not quite extend this correctly to married persons. So he asks the question:

"Does a married couple, each spouse earning £2,500 have a taxable capacity equal to a single person with an income of £5,000 or one equal to half a single person with a £5,000 income?"

The answer is, of course, neither; in this case the married couple have a taxable capacity equal to two single persons each with an income of £2,500. Again, another question is asked:-

"Does an income of £10,000 for a married unit really represent twice the £5,000 income of a single unit or is it equivalent to only half of the £10,000 of another single unit. The individual basis avoids such questions..."

It does implicitly deny, however, the argument that two can live more cheaply than one : that an income of £10,000 to a married unit is worth more than the sum of two £5,000 incomes each accruing to an individual unit".

This passage is full of difficulties : for example, what does the phrase "two can live more cheaply than one" really mean? An income of £10,000 to a married unit is not worth more than the sum of two £5,000 incomes each accruing to an individual unit. To the limited extent that a shared household can reduce expenses, then an income of £10,000 to persons sharing might be more than two £5,000 incomes to persons living separately, but this is not what is actually said.

The author concludes that an individual basis cannot produce equity and brings out the first reason against reform, i.e. that advantages depend upon the proportions of income in the household.

"The individual basis could easily prove to be inequitable : depending on the rate schedule a couple relying on one income of £5,000 might find themselves more heavily taxed than one with two incomes of £2,500 each".

The author agrees that aggregation can prove inequitable between married couples and other individuals living together but concludes that this is not a significant problem as "income levels of individual units are so significantly lower than those of married units that even if incomes of single individuals were aggregated there would not be many in the higher tax ranges". Now this appears to ignore the fact that married units comprise two persons and single units only one.

The author then points out that if an individual basis of taxation were adopted there would be an incentive to equalise investment income by transfers of property and recommends

"that to avoid encouraging such transfers of property purely for tax reasons it would seem preferable under the individual basis to legislate formally for what would otherwise be possible informally by attributing half of aggregate income to each spouse".

The author concludes that he regards the application of the individual basis to married units as inequitable but does favour the adoption of a quotient system (mentioning a ratio of 1:1.4); however this is not meant to apply to investment income; finally, the author clearly regards the present disaggregation of wife's earnings as "excessively lenient".

12. 1978 - The Meade Report

After the Report of the Radcliffe Commission in 1954 no large scale review of income taxation was made until the publication of the Meade Report¹ in 1978. Again, family taxation was only one of the many topics covered in the Report and the recommendations made have to be read in the light of the underlying proposal in the Report that the basis of taxation should be altered away from incomes and on to expenditure. The interesting proposals for an expenditure based tax will, however, not be considered here

1. The Structure and Reform of Direct Taxation - Report of a Committee chaired by Professor J.E. Meade.

as they are not relevant to a review of the existing system.

As might be expected from such a distinguished committee the treatment of "The Tax Unit" in Chapter 13 of the Report is thorough and constructive. One need not agree with all the conclusions but one must be impressed by the detailed analysis of the principle of aggregation and by the number of useful alternatives proposed.

The Report deals with three main questions : first the eight criteria which, it is considered, should form the basis of the tax treatment of married couples; next the reasons for rejecting the adoption of an individual basis of assessment (i.e. complete disaggregation); and finally the description of a number of possible alternatives to complete disaggregation. Each will be considered separately.

(1) The eight criteria

The Report lists eight criteria to be adopted when determining the basis of assessment for married couples and concludes that, as a number of these conflict, the solution must be a matter of compromise. The statement of these criteria in itself assists in understanding the nature of the conflict : it becomes obvious that some are relevant to a tax system constructed by reference to individuals and some are relevant to a tax system constructed by reference to "families" or to "persons living together". Now the tax system in the United Kingdom is constructed by reference to individuals only and the importation of concepts relevant to a "family" based system or a "household" system must give rise to conflicts

and illogicalities. It would be perfectly possible to construct a tax system based on families or households, as defined, but it would not be possible, for example, to have a family based tax which imported households or vice versa. The solution to the problem of the conflict in the eight criteria is not to compromise but to choose one basis of taxation and apply it consistently throughout. The difficulties in the present system arise from the fact that the concept of 'a married couple' has been imported into a tax on individuals.

Bearing this in mind, the eight criteria can be logically re-organised as follows:-

- (a) Criteria affecting all tax structures. These criteria are mainly of an administrative nature and would be relevant in any tax structure. They are:-

8. The arrangements involved should be reasonably simple for the taxpayer to understand and for the tax authorities to administer.

This criterion would favour an individual basis but if a family basis or household basis were logically and consistently adopted both could in theory comply with this criterion; for example, rates are assessed consistently on a 'household' basis and are reasonably simple to administer. However, rates are a proportional tax whereas income tax is a progressive tax and it is thought that, as presently structured, income tax could not be imposed either on a full

family basis (i.e. not just husband and wife) or on a household basis. The complications which were experienced in 1969-72 in attempting to aggregate an infant child's investment income on divorce illustrate the problems of interpretation and definition which could arise.

7. The choice of tax unit should not be excessively costly in loss of tax revenue.

Actually, no choice of tax unit would result in a "loss of tax revenue"; any base can yield any amount of tax if the rates are correctly structured.

- (b) Criteria relevant to an individual based structure.

These criteria would be satisfied only by the adoption of an individual - based structure:-

1. The decision to marry or not to marry should not be affected by tax considerations. Not only would this criterion exclude the present United Kingdom system of aggregation but it would also exclude the 'quotient' system which gives a positive advantage to marriage.
3. The incentive for a member of the family to earn should not be blunted by tax considerations which depend on the economic position of other members of the family.

This points to complete independence of allowances and to complete disaggregation at least as regards earnings.

(c) Criteria relevant to a "family-based" tax.

2. Families with the same joint resources should be taxed equally.
4. Economic and financial arrangements within the family (e.g. as regards the ownership of property) should not be dominated by sophisticated tax considerations.
5. The tax system should be fair between families which rely upon earnings and families which enjoy investment income.

The difficulty of these criteria is that 'family' is not defined; it could be meant to refer either to husband and wife, or it could also include children, either minor only or adults as well, or it could include other 'families' e.g. a man and woman living together. If a tax system were constructed so that all citizens belonged to a "family" by reference to which they were taxed then these criteria would be relevant : the great difficulty would be in defining a "family" for this purpose. But in a tax system which is structured on individuals it is illogical to single out one type of family (i.e. husband and wife) for special tax treatment and ignore all the other types of family which exist.

(d) Criteria relevant to "household" based tax.

6. Two persons living together and sharing household expenditures can live more cheaply and therefore have a greater taxable capacity than

two single persons living separately.

"Two persons living together" are not restricted to husband and wife and the same principle would surely apply to three, four or more persons living together. However, the great difficulty in imposing a 'household' tax would be the problem of aggregation; rates is a household tax but it is at a flat rate; a proportional tax could never be imposed on a 'household' basis and that is why it is unjust to impose it on husband and wife who represent only one of the many types of household.

The conclusion therefore is that it is not possible to have equity between families in a system structured by reference to individuals and it is not possible to have equity between individuals in a system which is structured by reference to families : a choice must be made and consistently applied : the injustice of the United Kingdom system arises from the fact that the system is based on individuals with an artificial deeming of two individuals (husband and wife) as one for the purpose of the tax. Those who support a 'family' tax or a 'household' tax should be prepared to carry their proposals to their logical conclusion and not restrict them to husbands and wives only.

(2) The rejection of an individual basis of assessment.

Although the Meade Report clearly holds the view 'that there should be no penalty on marriage' it does not recommend the adoption either of the 'quotient' system

or of the individual basis of assessment; either of these would neutralise a penalty on marriage and no other system does so. The 'quotient' system is mentioned below : in rejecting the individual basis the Report brings out a number of the familiar 'reasons against reform'.

<u>First reason</u>	:	<u>Advantages depend upon</u>
<u>against reform</u>	:	<u>proportions of income in</u>
		<u>household</u>

"The adoption of an individual basis would mean that the tax burden for two families with the same total income would not be the same if the income were concentrated in the hands of one partner in the one family but divided between the two partners in the other".

This reason against reform was first mentioned in 1894 and is commented on above. It ignores the fact that if an individual basis were adopted spouses could choose to equalise their incomes. If this reason had any validity the solution would be to adopt the 'quotient' system, under which all households are deemed to hold income in the same proportions i.e. equally.

<u>Second reason</u>	:	<u>It would cost too much</u>
<u>against reform</u>	:	

"Another possible disadvantage of this arrangement (i.e. the individual basis) is that it could easily lead to a substantial loss of tax revenue".

Here the Report confuses the tax base with the tax yield and this has been fully commented on above.

<u>Third reason</u>	:	<u>Married couples are members</u>
<u>against reform</u>	:	<u>of one household and have</u>
		<u>a joint income</u>

"Two persons living together and sharing household expenditure can live more cheaply and therefore have a greater taxable capacity than two single persons living separately".

Any saving from joint housekeeping comes not by being married but by setting up a joint household : in any event the major expenses of life are not substantially saved by joint housekeeping : the individuals do not eat less, or wear less clothes; although they may live in the same house they will certainly require more house accommodation than one single person. Minor savings may be made, as the couple may, for example, share furniture, motor cars, etc., but most married persons would agree that in practice joint housekeeping leads to an expansion of consumption rather than a reduction.

<u>Fifth reason</u>	:	<u>All cases of hardship are met</u>
<u>against reform</u>	:	<u>by (partial) disaggregation</u>
		<u>of wife's earnings</u>

The Meade Committee accept that husband and wife should be assessed separately on their earned income:-

"We all agree that it is desirable to have a tax treatment for married couples, which allows separate assessment of the earned incomes of the two partners".

The Committee do not, however, agree with disaggregation of investment income, mainly because its continuing aggregation is a feature of the expenditure tax proposed elsewhere in the Report.

<u>Sixth reason</u>	:	<u>Disaggregation would lead to</u>
<u>against reform</u>	:	<u>tax avoidance by transfers</u>
		<u>of property</u>

The Report points out that:-

"it would always be possible for a couple who owned property to seek to equalise their taxable incomes by a suitable transfer of the ownership of income-yielding property from one partner to the other...some would regard it as a positive virtue of a tax arrangement that it would encourage a more equal division of income between married partners ...But to treat the individual as the tax unit...would lead to property arrangements between spouses planned in such a way as to avoid taxation".

The fact that such property transfers are available to non-married persons is mentioned above, and also mentioned is the deterrent effect of loss of control over the income or assets transferred. Further, this argument proceeds on the basis that all investments are owned by one spouse, the husband :the situation where investments are owned equally by the spouses, the wife's investments possibly purchased from savings from earnings, is ignored and the injustice suffered in this case gets no comment.

<u>Seventh reason</u>	:	<u>Husband and wife get advantages</u>
<u>against reform</u>	:	<u>with death duties</u>

This reason against reform was again relevant in 1978 as capital transfer tax, introduced in 1975, did give spouses valuable exemptions and further, capital gains tax, introduced in 1965, gave exemption for transfers between husband and wife, the value of which, however, was reduced by the aggregation rule which gave only one set of exemptions and reliefs to a married couple. The Meade Report stressed that if an individual basis of assessment was adopted, then "a further set of tax considerations" would need to be considered in connection with transfers of property to equalise incomes : this is a valid comment.

<u>Ninth reason</u>	:	<u>It would lead to the abolition</u>
<u>against reform</u>	:	<u>of the marriage allowance</u>

The Report indicates that if the individual basis were adopted "there would be nothing corresponding to the allowance for dependent wives". This is, however, not an automatic result of disaggregation as the allowances are imposed separately and could be constructed so as to retain an allowance for a dependent wife with disaggregation. In any event, with an individual basis, a wife would be able to use her own full personal allowance against her own investment income or against income transferred to her by her husband.

<u>Eleventh reason</u>	:	<u>At lower income levels a</u>
<u>against reform</u>	:	<u>married couple are better</u>
		<u>off than if they were</u>
		<u>single</u>

The Report does not in fact use this effect as a reason against moving to an individual basis - it recommends that the anomaly be removed in any event:-

"We all agree that the present arrangement by which, when both husband and wife are earning, the couple can enjoy both the married man's allowance and a single person's allowance against the wife's earnings is unsatisfactory and that when a personal allowance is claimed against the wife's earnings the husband should enjoy only a single person's allowance".

The Report does not mention the other reasons against reform previously proposed (that aggregation does not stop people from marrying (fourth); that a change would not be used in practice (eighth); that the obligations of marriage are recognised by the wife allowance (tenth); that husband and wife both earning pay less tax than if

income earned wholly by the husband (twelfth); that married women do not work for money (thirteenth); that the Royal Commission are against it (fourteenth); or that the present rule only adversely affects surtax payers (fifteenth).

Having rejected the individual basis the Report examines some alternatives to the present system - these include a reference to the second alternative already mentioned (the quotient system) and four new alternatives.

(3) Alternatives to the present system

The Report considers and rejects the second alternative to aggregation.

<u>Second alternative</u>	:	<u>The division of the joint</u>
<u>to aggregation</u>	:	<u>incomes by two- the</u>
		<u>"quotient" system</u>

The Report calls this the "unrestricted quotient system" and considers that it is open to three serious objections. First, "it gives to every married couple, whether working or not, the equivalent of two personal allowances". Now why a personal allowance for each person, whether working or not, should be available to every single taxpayer except to a woman who is married is hard to discern. Secondly, says the Report, the quotient system "makes no allowance at all for the fact that by sharing household expenses a married couple can probably live more cheaply than can two single adults". Now a married couple sharing a house and two single adults sharing a house have exactly similar expenditures : on the other hand two single adults sharing a house might be able to live more cheaply

than two single adults living separately but, as mentioned above, it is just as likely that the facilities required by the joint household will expand leading to additional expenditure. Finally the quotient system is rejected because it will provide a disincentive for a wife to work as if her personal allowance is already covered by the split income of her husband she will be taxed on the whole of her earnings. This is a valid point but actually applies to every individual after the personal allowance is absorbed and the fact that after that level any individual is taxed on the whole of his earnings does not operate as a disincentive in practice. Three of the four new alternatives proposed in the Meade Report all proceeded on the basis of a disaggregation of wife's earnings but with different treatments for the couple's investment income.

<u>Seventh alternative</u>	:	<u>Separate taxation of earnings</u>
<u>to reform</u>		<u>and all investment income</u>
		<u>added to highest earnings</u>

"In order to rid the tax system of its present sex discrimination it might be ruled that the couple's investment income should be aggregated and added not to the husband's earnings but rather to the higher of the two sets of earnings".

This is called "a radical modification of the present system".¹

The Meade Committee acknowledges the two disadvantages of this system, namely the disincentive effect of a high rate of tax on the highest earner and also the

1. This is the system adopted in Sweden - See Chapter 13 page 577 post.

'serious tax on marriage' which would result. Actually, both of these disadvantages exist under the present system where the highest earner is usually the husband : at least the present system could possibly produce a benefit for a wife with very high earnings and very high investment income with a husband with very low earnings and investment income : by disaggregating her earnings only, she could possibly reduce the rates on her investment income which is deemed to belong to the husband; the seventh alternative proposed by the Meade Committee would remove this unlikely, but possible, advantage.

<u>Eighth alternative</u>	:	<u>Separate taxation for earnings</u>
<u>to reform</u>	:	<u>and quotient system for</u>
		<u>investment income</u>

This is called "partial income splitting".

"With this system each partner in a marriage would be taxed...on his or her earnings plus one half of their joint investment income against which each partner could set a single personal allowance...Equalisation of investment income for tax purposes would be brought about automatically without the need for any equalisation of the income-yielding property".

The disadvantages of this system are the same as those applicable to the full quotient system - namely that it gives a positive advantage to married persons : the disadvantage is that it retains the need for joint accounting. In addition this system would give advantages to married couples with investment income owned by one partner (split between two) as against those where all income is earned by one partner (no split).

<u>Ninth alternative</u>	:	<u>A married couple progressive</u>
<u>to reform</u>	:	<u>scale of one and a half times</u>

This is called "the restricted quotient system" and would operate as follows:

"The earnings and the investment income of the partners in a marriage would be aggregated...the married couple would unconditionally enjoy only one single person allowance with an additional single person allowance that could be set only against the second set of earnings if both partners were earning. After deduction of these personal allowances the combined income of a married couple would be subject to tax on a married couple progressive scale the brackets in this scale being, say, one and a half times as broad as those applying to a single person".¹

This is a variant of the fourth alternative to reform, first proposed in 1914, namely that there should be a percentage deduction from the tax payable by a married couple. The Meade Report discusses the advantages and disadvantages of this alternative as compared with the eighth alternative (partial income splitting) and also draws attention to its serious disadvantage - namely that it renders the fact of marriage as a determinant of tax liabilities - at lower income levels marriage will increase liability (if one partner had investment income but no earned income where the personal allowance would be lost on marriage); with unequal high incomes marriage could reduce liability.

<u>Tenth alternative</u>	:	<u>Separate taxation for earnings</u>
<u>to reform</u>	:	<u>but investment income aggregated and taxed on a one and a half times scale</u>

1. This is similar to the system adopted in the U.S.A. See Chapter 14 post.

This is a variant of the eighth alternative (partial income splitting) and the ninth (the restricted quotient) and is called the partial quotient system. This would permit:-

"separate assessment for earned incomes
but joint assessment with a quotient of, .
say, 1.5 for investment income"¹

Again, this alternative would avoid many of the disadvantages arising out of the eighth and ninth alternatives but, as proposed, it would be extremely complicated to administer.

(4) Conclusions

The Meade Report concludes:-

"If investment income is aggregated on marriage...there are bound to be certain tax implications from a decision of two individuals to be married".

However, within the context of the Meade Report the aggregation of investment income on marriage was an essential feature of the expenditure tax and it remains open to question whether the Committee could not have recommended disaggregation of investment income if this Report had only reviewed the existing system : the Committee concluded that none of the alternatives they proposed was perfect.

13. The Equal Opportunities Commission's Campaign for Reform

Between 1977 and 1979 the Equal Opportunities

1. This is similar to the system adopted in Norway.
See Chapter 13 page 573 post.

Commission conducted a campaign for reform : the main areas of concern which were highlighted in that campaign concerned the principle of accountability and are fully discussed in Chapter 8. Here, however, it may be convenient to note the discussion of two matters concerning aggregation : neither of these were mentioned in the 1977 consultative document¹ but both were raised in the analysis of the response to the consultative document.² The first is the aggregation of investment income and the second is the subject of the tax unit.

(1) Aggregation of investment income

"The present treatment of the investment income of married couples and the desire to change this...was a major concern in the comments received...this complaint - the high level of taxation resulting from aggregation of investment income - was frequent..."²

Although the Commission appreciates the difficulties of disaggregating investment income, i.e. income splitting by transfers of property, it suggests that the capital taxes could be modified in this area in order to maintain the tax yield.

(2) The tax unit

"The fundamental question posed by the Commission's consultative document was that of the basic tax unit : should this be the family or the individual? The view that this unit should be the individual was almost unanimous. This is the only aspect of the response received which shows a consistency throughout all the comments made".

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1. Income Tax and Sex Discrimination: Equal Opportunities Commission.
 2. With all my worldly goods I thee endow...except my tax allowances.

A number of alternatives to aggregation are discussed and reference is made to the quotient systems adopted in the United States, France and Germany; these are more fully discussed in Part III.

During 1980 the campaign was further stimulated by two Articles published in the British Tax Review which concluded that an individual basis of taxation should be introduced.¹

14. 1980 - The Green Paper

As has been said above, the Green Paper² does not distinguish in terms between aggregation, accountability and allowances. Each of these can be considered separately : this Chapter is concerned only with the aggregation rule and here it may be useful to summarise the effects of the rule as it exists today.

(1) The effects of the present rule

First, then, the wife's income is deemed to belong to the husband : only one set of rate bands, including investment income threshold, is available for the joint income; and, generally, only one set of reliefs (mortgage interest, capital gains tax exemptions etc), are available for the married couple.

There is only one exception to the aggregation rule - and that is the option introduced in 1971 for

1. N.A. Barr: The Taxation of Married Women's Income. B.T.R. 1980.

2. Taxation of Husband and Wife Cmnd 8053.

disaggregation of wife's earnings. The net effect, therefore, of the present aggregation rule, is that the wife's investment income is added to her husband's total income for tax purposes and there is no entitlement to a second set of reliefs. Further, although like all other taxpayers, spouses may transfer assets or income between themselves, unlike other taxpayers, the aggregation rule nullifies any tax saving effect of such transfers.

The Green Paper acknowledges

"the criterion that where husbands and wives both have investment income the tax bill can be higher than if they were two single people with the same total investment income split between them. This criticism is more frequently heard now that there are some 2½ million wives with income-producing assets".

It also recognises that the abolition of the aggregation rule would render inter-spouse transfers tax effective and

"measures would be needed to prevent avoidance through schemes for transferring income between spouses".¹

There is, however, no recognition of the effect of aggregation on the other reliefs although paragraph 86 recognises that disaggregation would result in separate thresholds for the investment income surcharge.

(2) The reasons for reform

The Green Paper sets out the reasons both for and against reform and proposes some alternatives to complete disaggregation. These will now be considered in the

1. Paragraph 87.

order previously adopted in this Chapter.

<u>First reason</u>	:	<u>The tax laws should follow</u>
<u>for reform</u>	:	<u>the property laws</u>

The Chancellor of the Exchequer states in the Foreword:-

"It is not surprising that there has been growing criticism of a tax code which proceeds on the basis (originally enacted in 1806)¹ that "a woman's income chargeable to tax shall...be deemed for income tax purposes to be his income and not to be her income".

And later² -

"A good deal of the recent criticism of the present system...has been directed initially at the aggregation rule...under which a wife's income is deemed to be her husband's for tax purposes".

Surprisingly, however, the Green Paper makes no mention of the changes in the property laws made since these provisions were enacted : the impression is gained that the desire for change is of recent origin and arises out of modern notions of tax equality and the recent incidence of working wives. So -

"There has been a growing dissatisfaction with the present system, particularly over the last few years".³

and -

"Within the last 50 years society has changed dramatically and it is these changes which underlie much of the present criticism of the taxation of married couples...Much the most important social development has been the changing role of a married woman within the family. At the time the income tax system took shape the vast majority of women gave up work on marriage to spend the rest of their lives looking after their home and family. This is not true today".

1. Actually, this should be 1805. See Chapter 1 page 40 ante.

2. Paragraph 6.

3. Paragraph 2.

4. Paragraph 27.

From the historical outline earlier in this Chapter it will be seen that the aggregation rule had been strongly criticised since 1894 and it was not criticised so much for social reasons as for legal reasons - namely that it ignored the property amendments of 1882. However, in the light of the Green Paper perhaps the first reason for reform could be stated as : the tax laws should follow the property laws and respond to social changes.

<u>Second reason</u>	:	<u>Reform was demanded by</u>
<u>for reform</u>	:	<u>many people</u>

In the Foreword the Chancellor of the Exchequer acknowledges

"Many people feel that we should break away from present arrangements".

and later -

"Many would not accept the (present arrangement) as the foundation upon which the tax laws should be built".¹

<u>Third reason</u>	:	<u>The tax laws should be</u>
<u>for reform</u>	:	<u>consistent between them-</u>
		<u>selves</u>

In 1980 the application of the capital taxes to husband and wife had reached the confusion outlined in Chapter 5. The point is dealt with fully in paragraph 88 of the Green Paper where the changes to the capital taxes which would be required on the introduction of independent taxation are discussed; while noting in passing that the separate capital gains tax reliefs are not mentioned, one can agree with the conclusion that many more transactions would become subject to capital taxes but the fact is that

1. Paragraph 2.

an overall saving of tax is likely to be seen by those with higher incomes and modest capital at the expense of those with more modest incomes but with substantial capital.

<u>Fourth reason</u>	:	<u>There should be no tax</u>
<u>for reform</u>	:	<u>penalty on marriage</u>

The Green Paper accepts¹

"that for investment income (the present system) is arguably unfair : the tax bill on the combined incomes may be greater if the couple are married than if they are two single people...Critics could fairly point out that, in this admittedly limited area, there is a fiscal disincentive to marriage".

No mention is made of the other "fiscal disincentives" i.e. the halving of reliefs available to two single persons and the restriction on tax effective inter-spouse transfers.

<u>Fifth reason for</u>	:	<u>Husband and wife are two</u>
<u>reform</u>	:	<u>persons and should be</u>
		<u>taxed as such</u>

Nowhere in the Green Paper is it acknowledged that husband and wife are two separate individuals : throughout, the discussion takes place on the basis that the mere fact of marriage alters the status of the individuals concerned : no attempt is made to justify this : it is accepted as a fact.

<u>Sixth reason</u>	:	<u>The principle of equality</u>
<u>for reform</u>	:	<u>gives the right to separate</u>
		<u>taxation</u>

1. Paragraph 4(b).

The Green Paper does not recognise that the principle of equality gives the right to separate taxation; there is much discussion of the various alternatives to aggregation, and of the difficulties of introducing any reform, but no acknowledgement of any "rights".

<u>Seventh reason</u>	:	<u>Disaggregation should be</u>
<u>for reform</u>	:	<u>complete and should not be</u>
		<u>restricted to earnings</u>

The Green Paper recognises the criticisms of the aggregation of investment income -

"that the system is unfair because it is not neutral as between the married couple and two single people living together..."¹

but concludes that individual taxation would require "measures to prevent avoidance through schemes for transferring incomes between spouses", and re-consideration of the capital taxes exemptions; no reason is given as to why avoidance measures would be necessary, nor is any justification attempted as to why some measures should apply to inter-spouse transfers only and not to transfers between two single people living together.

<u>Eighth reason</u>	:	<u>An injustice to a minority</u>
<u>for reform</u>	:	<u>is still an injustice</u>

The Green Paper recognises that the criticism of aggregation of investment income

"is more frequently heard now that there are some 2½ million wives with income-producing assets".²

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1. Paragraphs 86-88.
 2. Paragraph 38.

(3) The reasons against reform

The Green Paper, being a discussion document, also discusses many of the reasons against reform.

<u>First reason</u>	:	<u>Advantages depend on pro-</u>
<u>against reform</u>	:	<u>portions of income in</u>
		<u>household</u>

The Green Paper recognises the impossibility of importing the concept of a family tax into a system structured around individuals. So -

"No system can satisfy all criteria; for example it is inevitably difficult to reconcile sex equality with those definitions of fairness which favour families rather than individuals"₁

But later, confusion is introduced by using the "family" as the comparative base -

"Mandatory independent taxation would mean a substantial shift in the relative tax bills paid by different types of family".₂

and -

"Whether allowances were fully or partially transferable there would be an effect on the relative incidence of taxation among different types of families".

As in the Meade Report, "family" in this context is not defined but probably means "husband and wife"; no attempt is made to discuss the underlying question as to why "husband and wife" units should have any special treatment in a tax system which is structured on individuals and ignores all other household units.

<u>Second reason</u>	:	<u>It would cost too much</u>
<u>against reform</u>	:	

1. Paragraph 8.

2. Paragraph 40.

The Green Paper does not distinguish the 'cost' of disaggregation from the 'cost' of revising the personal allowance but does¹ indicate two types of cost which require consideration. The first is the cost to the Exchequer of financing the changes:

"The more substantial the change the greater the cost of ensuring that those who are made worse off in relative terms are protected, wholly or in part, from an increase in their tax bills".

This does recognise the difference between altering the tax base and the tax yield but it is not clear why "those who are worse off should be protected" when no such protection is offered when tax bills are increased in any other way. The second type of cost is -

"the administrative cost, which includes the number of additional civil servants needed to operate a change in the system...the more far reaching the change the greater the number of extra civil servants likely to be needed".

Again, no distinction is drawn between the administrative cost of disaggregation as such and the administrative cost of re-structuring the allowances on the lines discussed in the Green Paper. As far as disaggregation only is concerned much administrative cost would be saved by the abolition of the wife's earnings election and by the treatment of all women as individuals throughout their life, with no necessity for a change of treatment on marriage or divorce, thus eliminating the need for costly liaison between the tax offices of husband and wife during marriage.

1. Paragraph 9.

<u>Third reason</u>	:	<u>Married couples are members</u>
<u>against reform</u>	:	<u>of one household and have a</u>
		<u>joint income</u>

The Green Paper accepts that joint taxation is possibly not appropriate where husband and wife each have an income -

"In most cases, where husband and wife each have an income, the best answer probably lies in some form of separate taxation".¹

but returns to the "household" concept when discussing the allowances.²

"The married man's allowance is essentially an allowance for two people but it has always been less than twice the single allowance since the expenses of two married people sharing the same household are considered less than those of two single persons maintaining separate households".

No mention is made of two single persons sharing one household or two married people maintaining two separate households. No mention is made of the fourth to eighth reasons against reform but the ninth reason is mentioned as follows:-

<u>Ninth reason</u>	:	<u>It would logically lead to</u>
<u>against reform</u>	:	<u>the abolition of the marriage</u>
		<u>allowance</u>

"... a mandatory system of independent taxation would mean the abolition of the marriage allowance and of the aggregation rule so that all married women would become taxpayers in their own right, with their own personal allowance and rate bands".

Chapter 6 of the Green Paper discusses the effects of a system of mandatory independent taxation. Of its 23 paragraphs (67-89), 19 discuss the personal allowance,

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1. Foreword.
 2. Paragraph 13.

3 the effect of disaggregation on investment income and one the 'other effects' of independent taxation which concern privacy of accounts and the allocation of reliefs. There is no acknowledgement that aggregation could be achieved without any statutory alteration in the personal allowances and that the effects of disaggregation would include a doubling of certain reliefs and exemptions. The tenth reason against reform is not mentioned.

<u>Eleventh reason</u>	:	<u>At lower levels a married</u>
<u>against reform</u>	:	<u>couple are better off than</u>
		<u>if they were single</u>

"Mandatory independent taxation would mean a substantial shift in the relative tax bills paid by different types of family. In particular couples where both spouses are earning would, in relative terms, be worse off than at present".¹

This argument, of course, applies only to a change in the allowances and not to disaggregation as such but in any event the present advantage to two earner couples cannot be justified especially as the same system penalises the one-earner couple.

(4) The alternatives to disaggregation

The Green Paper discusses two types of alternatives to disaggregation : first a new tax unit (Chapter 5) and secondly some developments of the present system Chapter 4).

(a) The quotient system. In discussing a new tax unit reference is made to the second alternative system already mentioned.

1. Paragraph 40.

Second alternative : The quotient system
to reform :

The Green Paper distinguishes the quotient system as applied to husband wife and children, as it applies in France, with the system as applied to husband and wife only, as applied in West Germany, and, to a limited extent in the U.S.A.¹ However, the basic disadvantages of "considerable shifts in the tax burden of different family groups" and the necessity for joint accounting are given as reasons why "it seems unlikely that...a family tax system...would be generally acceptable in the U.K. today".

(b) Some developments of the present system. In discussing possible developments of the present system, the Green Paper mentions four new alternatives to disaggregation.

Eleventh alternative : Joint taxation
to disaggregation :

"Several variants would be possible but essentially this would involve substituting for the present aggregation rule a rule under which the income of husband and wife would be jointly returnable by them, and jointly assessable on them, and there would be a joint responsibility for payment of the tax".²

Now this arrangement would have no effect at all on the aggregation rule, which determines the amount of income on which tax is paid and the amount of reliefs available : it is in fact only a change in the accountability rule and has the grave disadvantage of placing a joint liability for her husband's income tax on the non-earning wife.

1. The quotient system also applies in Luxembourg and Ireland - see Part III.

2. Paragraph 45.

Twelfth alternative : Re-wording the aggregation
to disaggregation : rule

"The aggregation rule could be re-worded not to provide for joint taxation but simply to treat the income of husband and wife as if it were one income, the tax remaining assessable etc. on the husband with the existing exceptions of separate assessment and wife's earnings election..."

Such a re-wording is not considered to be an alternative to the aggregation rule : it is purely cosmetic in effect and would have no effect on the quantum of tax payable, or indeed on the accountability principle.

Thirteenth alternative : Option for individual
to disaggregation taxation

"This would mean extending the existing wife's earnings election to investment income".¹

Although at first sight, this appears to offer a genuine possibility of disaggregation, there are a number of unsatisfactory features. First, it is not proposed that the option would be accompanied by separate accounting automatically although -

"it would seem sensible to allow a husband and wife to make separate returns if they wished".

Next, this alternative is proposed as an option and before the option is exercised

"husband and wife would have to tell each other sufficient about their incomes to establish that it would be beneficial to take up the option".

Again, it appears that this would be an election requiring the consent of both spouses, as it would result

1. Paragraph 46.

in the loss of the married man's allowance; thus there would be no automatic entitlement to the option. Further, there is no indication that the exercise of the option would entitle each spouse to a full set of reliefs and the impression is gained that these would have to be shared in some way; and finally it is proposed that the option would make it -

"necessary to give consideration to the prevention of artificial methods of reducing the tax bill by transferring income between husband and wife or vice versa. It would certainly be necessary to nullify for tax purposes inter-spouse payments under covenants".

Thus the option for individual taxation falls very far short of treating married persons in the same way as other individuals.

<u>Fourteenth alternative</u>	:	<u>Option for equal split</u>
<u>to disaggregation</u>	:	<u>of allowances and rate</u>
		<u>bands</u>

The thirteenth alternative (the option for individual taxation) would not be beneficial if the loss of the married allowance was greater than the benefit of a full personal allowance against the wife's investment income and a separate set of rate bands : the fourteenth alternative therefore proposes a variant of separate assessment where the allowances and rate bands are split equally between husband and wife, and not in proportion to income as under the present procedure. The advantages would be greater privacy and more simplicity : the disadvantages would be that the principle of aggregation would continue : only one set of reliefs and allowances would remain available and the anomaly of the married man's allowance would be retained.

(5) Conclusion

The Green Paper accepts that mandatory independent taxation "would totally end the problem of discrimination between husband and wife" but in its treatment of an individual basis it confuses aggregation, accountability and allowances. The criticism to be made of all the alternatives to disaggregation posed in the Green Paper is that they all retain the concept of the "married couple," and the married man's allowance, with a complicated system of elections : even with the most favourable alternative, the option for independent taxation, neither spouse individually has the right to exercise the option and it is not clear whether, on exercising the option, each spouse will become entitled to a full set of reliefs, although it is made clear that inter-spouse transfers will be restricted.

(6) The response to the Green Paper

The Green Paper attracted submissions from over forty organisations and several hundred individuals¹ who "almost unanimously" declared themselves in favour of a change to a system of mandatory independent taxation.

15. Conclusions

Although the aggregation rule was modified in 1971, on the introduction of the wife's earnings election, it otherwise remains today as it was first enacted in 1805;

1. The Taxation of Husband and Wife : A view of the debate in the Green Paper. John Kay and Catherine Sandler June 1982.

there can be no disaggregation of spouses' investment income and, for the purposes of reliefs, two married persons are treated as one individual. The principle has been under attack since 1894 since which date eight major arguments have been proposed for reform of the rule and fifteen reasons have been given for its retention; no less than fourteen alternatives have been proposed. However, all pressure for reform has come from Opposition Members of Parliament, the taxpaying public and learned commentators, and most of the justification of the present system has been made by the three main Commissions (Colwyn, Radcliffe and Meade) and supported by the Government in power; however the impression is gained that the better view now supports a move towards mandatory independent taxation, i.e. the complete abolition of the aggregation rule.

CHAPTER 8 - A REVIEW OF THE PRINCIPLE OF ACCOUNTABILITY

Section 1. Introduction.

Section 2. 1894 - Limited Disaggregation of Wife's Earnings.

Section 3. 1909 - The Introduction of Supertax.

Section 4. 1911 - Inland Revenue's Power to Charge Wife.

Section 5. 1912 - The Case of Mr. Wilks.

Section 6. 1914 - The Option for Separate Assessment.

Section 7. 1920 - The Colwyn Report.

Section 8. 1955 - The Radcliffe Reports.

Section 9. 1956-78 - The Tax Reform Papers.

Section 10. 1977-79 - The Equal Opportunities Commission's
Campaign for Reform.

- (1) 1977 - Publication of consultation document.
- (2) 1978 - The Press campaign.
- (3) 1978 - Statutory and administrative changes.
- (4) 1979 - A response to the consultation document.
- (5) 1979 - Further administrative changes.
- (6) 1979 - A review of the altered position.

Section 11. 1980 - The Green Paper.

- (1) Joint taxation.
- (2) Rewording the aggregation rule.
- (3) Option for individual taxation.
- (4) Option for independent taxation with equal split.
- (5) Mandatory independent taxation.

Section 12. Summary.

CHAPTER 8

A REVIEW OF THE PRINCIPLE OF ACCOUNTABILITY

Section

1. Introduction.
2. 1894 - Limited Disaggregation of Wife's Earnings.
3. 1909 - Introduction of Supertax.
4. 1911 - Inland Revenue's Power to Charge Wife.
5. 1912 - The Case of Mr. Wilks.
6. 1914 - The Option for Separate Assessment.
7. 1920 - The Colwyn Report.
8. 1954 - The Radcliffe Reports.
9. 1956-78 - The Tax Reform Papers.
10. 1977-79 - The Campaign for Reform.
11. 1980 - The Green Paper.
12. Summary.

1. Introduction

Although the principle of husband's accountability is even older than the principle of aggregation, it is not always appreciated that the two concepts are distinct and have an existence independent of each other : their history and development differ widely. Aggregation could exist without accountability and in fact does so in those cases where an election for separate assessment under section 38 Taxes Act 1970 is in force; and accountability could exist without aggregation, and does to the limited extent permitted by law where an election for separate taxation of

wife's earnings under section 23 Finance Act 1971 is in force.

The principle of accountability has a number of different facets each of which has given rise to discussion at different times followed by some modification. However, in its basic form as originally enacted in 1799 and re-enacted in 1842 the principle involved the following:-

- (1) Making the return. The husband was responsible for making a return of the wife's income; this gave rise to difficulties after the passing of the Married Women's Property Act 1882 as, after that date, a husband might not know what his wife's income was and had no means of finding out where the wife refused to tell him, the wife being then under no legal obligation to inform her husband of her income.
- (2) Privacy. The wife was not able to preserve any privacy as regards her income, as, in practice, she had to disclose this to her husband to enable him to complete the return, whereas the husband was under no corresponding obligation to disclose his income to his wife.
- (3) Paying the tax - the husband's responsibility.
 - (a) The husband was liable to pay the tax on his wife's income even though she was under no obligation to assist him with such payment and might be in receipt of a larger income than his.
 - (b) The husband was liable to have distraint levied on his goods for his wife's unpaid tax but no

distrainment on the wife's goods was possible as she was under no legal obligation to pay the tax.

(c) The husband was liable for imprisonment for non-payment of his wife's tax.

- (4) Repayments. All repayments due in respect of a wife's income were sent to her husband.
- (5) Correspondence. All correspondence as regards the wife's income tax was sent to the husband.
- (6) Claiming the allowances. Only the husband could claim any reduced rate relief for his wife and later, when personal allowances were introduced, all had to be claimed by the husband, including the wife's earned income allowance. The same principle applied to other reliefs (e.g. mortgage interest relief and life assurance relief) due in respect of payments by the wife and all expenses incurred by her in connection with her trade or employment. The wife had no means of insisting that such claims be made.
- (7) Benefiting from the allowances. The husband had first call on the allowances, except for the wife's earned income allowance which was available only against the wife's earned income. The husband was, and is, entitled to the relief in respect of any mortgage interest paid by his wife (even if the house is solely owned by her) and where the joint income was liable to higher rate tax the husband had the benefit of the whole of the lower bands.

Since 1914 it has been possible for the spouses to overcome these difficulties by opting for separate assessment

under what is now section 38 Taxes Act 1970, but that procedure has a number of disadvantages more fully described in Chapter 2. These include (1) the need for an election - the provisions are not automatic; (2) the election cannot be retrospective; (3) the calculations required are extremely complicated; (4) neither spouse individually can check that the calculations are correct; (5) complete privacy cannot be preserved as it is always possible to guess at the other spouse's income and reliefs; (6) the apportionment of reliefs under the statutory rules may not produce an equitable result in practice and (7) the option is not widely published and spouses may well be ignorant of its availability.

In addition to the provisions of section 38, there are also provisions which enable the Inland Revenue to ignore the principle of husband's accountability when it suits them to do so : these are referred to in Chapter 2 above and are now found in section 40 Taxes Act 1970.

Finally, there are a number of administrative departures from the principle of accountability which have not been mentioned previously but to which reference will be made in this Chapter.

Once again, a historical treatment has been adopted as it is thought that this is the only way in which the enactment or adoption of the various provisions can be adequately explained, and, as with the aggregation rule, the first voices dissenting from the principle are heard in 1894.

2. 1894 - Limited Disaggregation of Wife's Earnings.

It will be recalled¹ that the first debates after the enactment of the Married Women's Property Act 1882, on the subject of the tax treatment of husband and wife, took place in 1894. During those debates attention was focused mainly on the injustices of the aggregation rule but attention was also drawn to the anomalies resulting from the continued retention of the principle of accountability when the basis upon which it had been enacted no longer existed. So -

"It would astonish a good many members to know that...the assessment was on the husband notwithstanding that the wife had power to dispose of her own income as she thought proper".²

and -

"Women now had powers concerning their property which were undreamed of when the Act of 1842 was passed...it was perfectly sensible to impose the tax on the husband in those days as he had the spending of the wife's money; but the Married Women's Property Act had altered that".³

Although the Finance Act 1894 introduced a limited disaggregation for wife's earnings by permitting an additional 'low income exemption' in certain circumstances, such exemption was given to the husband as a relief against the total joint income and no alteration in the principle of accountability was then made. It may be interesting at this stage to consider why the principle of accountability

1. See Chapter 7.

2. Mr. Darling. Hansard 28th June 1894 col. 492.

3. Mr. Darling. Hansard 28th June 1894 col. 493.

did not give rise to more concern in view of the fact that the husband's liabilities were retained after the control of his wife's property had passed from him; and it is thought that the answer lies in the fact that at that time almost all tax was suffered by deduction at source and very little by direct assessment; even the 'small income exemption' had to be applied for and was given by way of repayment. When tax is levied on a proportional basis, deduction at source can be almost universal and no additional assessments need be required. Accordingly, although the theory of husband's accountability remained, in practice very few husbands would have received tax bills in respect of their wives' income - the wife would suffer the tax by deduction at source.

3. 1909 - The Introduction of Supertax

In 1909, however, supertax was imposed and the machinery for collecting the tax relied upon a return of total income from each taxpayer followed by direct assessment by the Inland Revenue : under such a system it became clear that husbands would first need to find out what their wives' incomes amounted to and, secondly, could actually receive tax bills in respect of their wives' income. This virtual increase in the husband's liability gave rise to considerable disquiet. So -

"I do not look on this as a question of the rights of women. It is really a question of the rights of man. The husband does not receive his wife's income yet he may be called upon to pay supertax in respect of it.

He may never touch that income and yet he is to pay the tax upon it? He may be unable to recover a farthing from his wife...surely it would be far better to make the incomes separate for all purposes?"₁

and -

"You may get cases where possibly a man's whole income will be absorbed in paying the supertax on his wife's income".₂

During the same debate it was pointed out that although a husband was obliged to make a return of the total income of himself and his wife he had no way of insisting that the wife tell him of her income and there was, of course, no comparable obligation on the husband to tell the wife of his income.

No amendment was made during the debates on the Finance Act 1909 to deal with these problems and subsequent events proved that real practical difficulties did result. At first, the Inland Revenue 'turned a blind eye' when problems occurred, hoping no doubt that the deficiencies of the system would not become widely known and exploited; so, in November 1910, Mr. Walter Guinness was able to refer to the fact that it was known that if a husband told the Inland Revenue that his wife would not tell him what her income was, no action to recover the tax was taken:-

"There was one case in the daily Press where a husband was called upon to make a return of his wife's profits in her business. He refused saying that he had no means of ascertaining his wife's income and the wife refused to send in a return on the ground that the law did not treat the income as hers

1. Mr. Cave Hansard 20th September 1909 Col.95.

2. Mr. Walter Guinness. Hansard 20th September 1909 Col.95.

and I understand that the Inland Revenue have dropped the case. It is most unfair that money should be extorted from the ignorant while those who have a special knowledge of the law are able to escape and are not proceeded against by the Inland Revenue".¹

And later Mr. Stuart Wortley expressed the view that it was wrong to have a principle and to pursue it against people of small means and fail to pursue people "who may be able to fight".

One of those who was able to fight and was not pursued was the eminent author Mr. George Bernard Shaw who, in 1910, wrote to the Inland Revenue in the following terms:-

"I have absolutely no means of ascertaining my wife's income except by asking her for the information. Her property is a separate property. She keeps a separate banking account at a separate bank. Her solicitor is not my solicitor. I can make a guess at her means from her style of living exactly as the Surveyor of Income Tax does when he makes a shot at an assessment in the absence of exact information : but beyond that I have no more knowledge of her income than I have of yours. I have therefore asked her to give me a statement. She refuses on principle. As far as I know I have no legal means of compelling her to make any such disclosure and if I had it does not follow that I am bound to incur law costs to obtain information which is required not by myself but by the State. Clearly however it is within the power of the Commissioners to compel my wife to make a full disclosure of her income for the purpose of taxation; but equally clearly they must not communicate that disclosure to me or to any other person. It seems to me that under these circumstances that all I can do for you is to tell you who my wife is and leave it to you to ascertain her income and make me pay the tax on it. Even this you cannot do without a violation of secrecy as it will be possible for me by a simple calculation to ascertain my wife's income from your demand".

1. Mr. Walter Guinness. Hansard 23rd November 1920. Col.330.

In fact, Mr. Shaw was wrong in thinking that it was "within the power of the Commissioners to compel my wife to make a full disclosure of her income for tax purposes". The Commissioners had no such power. In the event, the Inland Revenue did accept separate returns from Mr. & Mrs. Shaw and assessed Mr. Shaw for any tax underpaid".¹

The main difficulties encountered at this time therefore involved the first and third facets of accountability referred to above, namely, making the return and paying the tax. But difficulties were also arising from the fourth facet, i.e. repayments : on 6th July 1910 Mr. Bottomley asked the Secretary to the Treasury whether he was aware:-

"that where a married woman claimed or obtained a rebate or return of income tax the authorities insisted on making out the order for repayment in the name of the husband".

The Financial Secretary replied that he was aware of the practice:

"A married woman living with her husband is not entitled to prefer a separate claim for repayment on her own behalf. The claim must be made by the husband and consequently the repayment is made to him".

The procedure for repayments caused no problems for the Inland Revenue but the publicity given to their failure to pursue claims against husbands must have caused some embarrassment as steps were hastily taken to provide a remedy : their practice of taking no action in difficult

1. See Sunday Times, May 7th 1978 page 43.

cases was mentioned in the House of Commons on 23rd November 1910 and a clause designed to overcome these difficulties was included in the Revenue Bill which was introduced in March 1911.

4. 1911 - Inland Revenue's Power to Charge Wife

Clause 10 of the Revenue Bill 1911 provided for the "assessment and recovery of part of supertax from the wife in certain cases". If the Special Commissioners considered that a husband's return of total income for the purposes of supertax was unsatisfactory as regards his wife's income they could ask a wife to make such a return "as if she were not married"; a proportion of the supertax due was then to be assessed and recovered from the wife and not the husband; the provisions were backdated to the date of the introduction of supertax (6th April 1909) and were enacted without debate as section 11 Revenue Act 1911. This section was the forerunner of the somewhat differing provisions which are now found in section 40 Taxes Act 1970.

Here, then, is another example of the Inland Revenue's ignoring the aggregation and accountability principles when it suits them to do so : as soon as it can be shown that these principles could possibly be disadvantageous to the Inland Revenue in practice, steps are taken to remedy the matter at the earliest opportunity; such speed can be compared with the tardiness of any improvement which might benefit husband and wife. Again, when the Inland Revenue introduce a new provision for their own protection this rarely has the result of making the

situation any better for the married couple and frequently makes it worse. For example, section 11 Revenue Act 1911, while imposing an additional obligation on a wife did not give the wife the right to make a separate return - the operation of the section was left to the discretion of the Special Commissioners; and even where the section was applied the husband's obligations did not altogether cease.

During 1911 further questions were asked about the right of married women to receive their own repayments. Mr. Weir¹ asked why a married woman had to get her rebate through her husband and was referred to section 42 Income Tax Act 1842; and later² Mr. Weir asked specifically if a married woman could be enabled to recover her own rebate without relying on her husband and Mr. Lloyd George answered in the negative. The matter was pursued in 1912 when Mr. Walter Guinness³ referred to the fact that rebates for married women were sent to their husbands and asked the Chancellor of the Exchequer if he would consider an amendment to the law to enable married women to recover on their own behalf. Mr. Lloyd George replied that:

"Such an amendment...would involve very considerable changes and adjustments in the income tax law and I cannot at present undertake to propose it".

In reply Mr. Walter Guinness referred to the fact that -

"many letters had been received from married women to the effect that they can only get their income tax back by forging their husband's signatures and opening their letters as otherwise the husband will keep the money".

1. Hansard 1911 Vol. 23, Col. 782.

2. Hansard 1911 Vol. 23, Col. 1948.

3. Hansard 1912 Vol. 43, Col. 840.

The Chancellor of the Exchequer did not consider that this merited any reply.

It is possible that no amendment would have been introduced to assist married women to obtain their own repayments if it had not been for what came to be known as "the case of Mr. Wilks".

5. 1912. The Case of Mr. Wilks

Although the Inland Revenue had taken power in section 11 Revenue Act 1911 to obtain direct from a wife details as to her income for supertax purposes, and had also taken power to assess and recover from a wife a proportion of such supertax, no comparable amendment had been made to the income tax provisions and this was at the root of what became known as "the case of Mr. Wilks". Let the facts of the case be narrated by Earl Russell:-¹

"Mr. Wilks is a schoolmaster in which capacity he earns a comparatively humble income. His wife, Elizabeth Wilks, practises as a doctor in which capacity she earns an income...considerably superior to his. The exact amount I do not know because Mr. Wilks was unable to inform me any more than he was unable to inform the Commissioners of Inland Revenue. He has no means of ascertaining the amount of his wife's income but it is admitted to be considerably larger than his own...Dr. Elizabeth Wilks was asked for payment of her income tax ...and she refused to pay...Naturally the Inland Revenue were not going to be done out of their taxes...they therefore adopted the ordinary methods and finally the method of distraint. The distraint was made upon the separate goods of Dr. Elizabeth Wilks.

"Mrs. Wilks then decided to assert the rights which it appeared to her the Income Tax Acts gave her. She pointed out that under those

1. Hansard H.L. 14 October 1912 Col.823.

Acts she was not liable either to make a return or to pay the taxes; that under those Acts the income of a married woman living with her husband was deemed to be his income and that therefore the obligation was on Mr. Wilks to make the return and, when the assessment had been made, to pay the taxes. The Treasury accepted that view and applied to Mr. Mark Wilks for the return. Mr. Wilks replied that he was not in a position to make a return of his wife's income because she had no idea how much it was and she did not choose to tell him. That is a position which, under the Married Women's Property Act, she is perfectly justified in taking up. Her husband has no concern with her income and can receive no information about it except by her courtesy. He has no more right to demand any particulars of her income, or to handle her income, than I have to handle the income of any of your Lordships. Mr. Wilks therefore informed the Treasury that he could not make the return".

The Treasury then made an estimated assessment on Mr. Wilks and refused him the reduced rate to which he was clearly entitled on his own income; subsequently they took proceedings against him for the sum of £33.12.10d.

"Mr. Wilks replied that he did not receive his wife's income; that he had not got it to pay with; that his own income - £150 a year - was barely sufficient for his maintenance, and that it was impossible for him to raise such a sum of money".

After lengthy correspondence -

"a writ was issued and Mr. Wilks was taken up and lodged in Brixton Goal".

He sent a petition for his release to the Chancellor of the Exchequer and to the Inland Revenue but they replied -

"Your attitude has throughout been one of refusal to recognise the liability which the law clearly imposes on you".

No move to release Mr. Wilks was made until the day before Parliament reassembled when -

"without having made any arrangement to pay the money or any proposal for the liquidation of the debt due to the Crown, and most decidedly without his having paid for it, he was released from Brixton Prison".

Two years later the release was described in the following way:¹

"They let Mr. Wilks out of prison the day before the House reassembled because they could not face the criticism to which they would be subjected in this House".

Such criticism was, nevertheless, fully voiced in a debate on a resolution moved in the House of Lords on the 14th October 1912, which resolution said:-

"That in the opinion of this House the present state of the law which renders a man liable to indefinite terms of imprisonment for matters over which he is by statute deprived of any control is undesirable and should be amended".

In support of his resolution Earl Russell said:-

"The law is an absurd law; it is contrary to the Married Women's Property Act and should therefore at the earliest possible date be amended. I in no way challenge the legality of what has been done but I do challenge its natural justice and its common sense...The provision is such that in the case of a man totally impecunious married to a wife with a considerable separate income it would be absolutely in the wife's power to have him detained in prison whenever she chose not to make a return and not to pay her income tax. We are told sometimes that legislation is unduly favourable to men but this particular legislation might hit us very hardly if our wives were inclined to take advantage of it...when a wife's income was in effect her husband's income, when he had control of it and was able to use it, it was extremely reasonable to require him to make a return of it and to let the obligation for any taxes imposed upon it fall upon him. But the whole circumstances

1. 15th May 1914, Col. 1332.

have been altered by the passing of the Married Women's Property Act and the provision is no longer justifiable".

Lord Ashby St. Ledgers, replying for the Government, sought to justify the arrest of Mr. Wilks because his non-payment -

"was not a normal case exemplifying the hardship of the present system. This is something in the nature of a political demonstration".

This was a reference to the fact that Dr. Elizabeth Wilks was a suffragette and believed in the principle of "no taxation without representation". Later, Dr. Elizabeth Wilks

"stated, very fairly, that since she incurred the penalty by refusing to pay, she expected to pay the penalty";

she felt it a grievance that her husband had to pay the penalty instead.¹

Whether Lord Ashby St. Ledgers was convinced by this argument is difficult to say but he did admit that -

"there is a certain substratum of hardship in the fact that a husband should be imprisoned for failure to pay the income tax on his wife's income...It is true that the Treasury regulations on this subject were framed many years before the Married Women's Property Act of 1882 and therefore there is a certain anachronism in maintaining the present Treasury regulations. In view of that Act...I am very glad that my Rt. Hon. Friend, the Chancellor of the Exchequer has promised to take the matter into consideration".

And the Lord Chancellor had this to say:

1. Hansard 15th July 1914, Col. 2020.

"Today we treat the income of a married woman as nearly as possible as though it were the income of an unmarried person and yet the machinery for enforcing the income tax laws remains in a large measure what it was half a century ago. The result of that is, of course, hardship. I entirely agree that the case of Mr. Wilks is one where there is an anomalous state of the law which cannot be defended and my Rt. Hon. Friend the Chancellor of the Exchequer has undertaken to consider it".

This promise had been given by Mr. Lloyd George on 9th October 1912¹ and, in reliance on it, Earl Russell withdrew his motion. The promise was not, however, immediately implemented and on 11th June 1913 the deputation from the Women's Tax Resistance League attended upon Mr. Lloyd George "to lay before him what they considered to be grievances in connection with the taxation of married women". The deputation was described in Chapter 7 but here it may be noted that Dr. Elizabeth Wilks was a member of that deputation and pointed out that her husband had been sent to prison for refusing to pay her tax and she expected that she should pay such penalty. In replying to the submissions made on behalf of the deputation Mr. Lloyd George said:-

"Her husband was liable for the tax and they (i.e. the Inland Revenue) could not distrain on the wife's goods although the distraint was in respect of her income tax. That was an injustice to the Revenue which he wanted to put right".

Now this is a somewhat illogical statement : if the Inland Revenue wished to retain husband's accountability they should have accepted that that meant that distraint could only be on the husband's goods : if they wanted to

1. Hansard Vol. 42, Col. 340.

distrain on the wife's goods then the wife should be made accountable for her own tax. Be that as it may, the combination of the hardship to husbands mentioned by the Lord Chancellor, and the injustice to the Revenue mentioned by the Chancellor of the Exchequer, pointed irresistibly the direction of some reform : but this would be difficult to achieve without conferring some benefit on married women. Mr. Lloyd George and the Treasury thought the problem over long and hard and the results were comprised in the new clause introduced on 15th July 1914.

6. 1914. The Option for Separate Assessment

The new clause was not introduced without many prior reminders and enquiries : in Chapter 7 details are given of the number of occasions in 1914 when enquiries were made in the House of Commons as to the time when the Chancellor of the Exchequer intended to introduce the amendments which he had promised. The clause, as ultimately introduced on 15th July 1914, comprised many of the provisions now found in section 38 Taxes Act 1970; these are fully described in Chapter 2 and the basic features included the fact that the provisions only applied after the exercise of an option and that the 'separate assessment' under the clause only applied to the 'assessment charging and recovery' of the tax; the total incomes were still to be aggregated for the purposes of the exemptions and the supertax.

Mr. Cassel summarised the deficiencies which the clause was designed to cure:-

"I do not think that the income tax law has ever been brought into conformity with these changes in the law relating to the powers of married women in connection with the ownership of property ...The wife is treated as a mere nonentity by the law as far as income tax is concerned. It is true that she pays but for the purpose of assessment, collection and fixing the amount of the abatement or exemption or the rate of tax it is treated as if the wife did not exist and it was all the husband's property notwithstanding the fact that it is not the case under the Married Women's Property Act.

"That system is unjust to the husband and to the wife. It is unjust to the husband because the husband can be actually put in prison because his wife does not disclose to him what her income is. He is supposed to return her income but has no power of compelling her to tell him what it is and he is bound to pay the tax upon her income but has no right of recovering the amount of the tax from her...

"It is also unjust to the wife because although she may be earning an income in a business or profession she is given no opportunity whatever in the making of the return. The return is made through the husband and she has no voice in the matter at all. And so far as claims to exemptions or abatement are concerned she cannot do it herself but it is left to the husband to claim it or not as he pleases and if he does claim it she has no right of recovering from him the amount which he recovered by way of abatement or exemption".

It was accepted that, if an option under the clause were exercised, these difficulties would disappear but the clause had a number of deficiencies which were mentioned in the debate.

First, the administrative complexities of the clause, which even today act as a deterrent to its utilisation, were noted with regret -

"Every possible obstacle has been placed in the way of their getting the benefit... (there are) extraordinary difficulties in administration in making apportionments between husband and wife. It also involves

the result that you must in every case where this clause applies tell the wife what the husband's income is and tell the husband what the wife's income is".

Comments were made on the difficulties of complying with the time limits for the notice but these were based upon a misunderstanding.

Next, objection was taken to the fact that, were an option under the clause was in force, the right to a limited disaggregation of wife's earnings, introduced by the Finance Act 1894, was withdrawn.

"Husband and wife have to purchase their exemption from humiliation at the expense of having to incur higher taxation".

This provision was amended on Report stage when an amendment was agreed to allow the relief under Finance Act 1894 even if an election under the clause was in force.

Finally, the clause as introduced gave the Inland Revenue unusually severe powers of distraint against both spouses, and these were not limited to cases where an option under the clause was in force.

"The clause for the first time gives the right to distraint on the wife's goods for the tax for which the husband is liable and vice versa to distraint on the husband's goods in respect of the tax for which the wife is liable".

And -

"The clause greatly increases the power to distraint on the goods of the husband or wife in respect of the tax due from the other person. That certainly seems to be a very strange way of remedying the injustice which resulted in Mr. Wilks being sent to prison".

The clause was the subject of considerable discussion and, as enacted, the clause provided that where an election

under the section was in force, and the wife did not pay her tax, the Revenue could distrain on her goods and on her husband's goods, but not vice versa. Although these provisions would have assisted the Inland Revenue in the Wilks case, if Mr. or Mrs. Wilks had claimed separate assessment under the clause (as distraint could have been originally levied against the goods of Mrs. Wilks) it would not have assisted Mr. Wilks if his wife had no goods upon which distraint could be levied; even in the emasculated form in which the clause was enacted, therefore, the Inland Revenue retained powers of restraint in the case of husband and wife which were superior to those enjoyed in respect of two single individuals.

Finally, the clause repealed the provisions of section 11 Revenue Act 1911, which it will be recalled gave the Inland Revenue power to seek a return from a wife for supertax purposes if they were not satisfied with the husband's return. The historical reasons for the introduction of separate assessment are enlightening : the provisions are sometimes referred to as indicating a willingness to give married women the same accounting rights as single women, overlooking the fact that they were only introduced to avoid hardship to husbands and give greater rights to the Inland Revenue; the completely unnecessary inclusion of the withdrawal of limited disaggregation if an option were exercised is an indication of the 'Treasury hostility to married women' which has been mentioned previously.

A further interesting facet of the reasons leading up to the enactment of these provisions is the fact that once the tax laws and the property laws diverge anomalies

and injustices are bound to result; provisions which are perfectly acceptable under one property régime can become quite unworkable under another.

7. 1920 - The Colwyn Report.

There is no doubt, however, that in theory the option for separate assessment should have solved the problems arising from the principle of husband's accountability, although it was not a perfect solution. One of its deficiencies was, and still is, the administrative complications resulting from an exercise of the option and the impression is sometimes gained that the provisions were enacted in order to provide an answer to criticism but in the hope that they would not be widely adopted in practice. So, in referring to the option for separate assessment the Colwyn Commission, reporting only six years after its introduction, said:-

"It does not appear to be very widely known. Indeed some of the witnesses seem to have been unaware of the existence of any such provision. The option is rarely taken advantage of".¹

No further discussion of the principle of accountability takes place in the report, which does however include three suggestions with regard to "minor details".²

The first such suggestion is that "the Revenue should have power of assessment apportionment and recovery

1. Colwyn Report : paragraph 250.

2. Colwyn Report : paragraph 262.

of the tax against the spouses in respect of their separate incomes where necessary to the collection of the tax". It will be recalled that a similar power had been given under section 11 Revenue Act 1911 for the wife to be assessed and charged with her own supertax : this power had been repealed in 1914 but clearly the Inland Revenue had regrets: of course, if an option for separate assessment were in force recovery could be from both husband and wife but if the spouses refused to exercise the option, the Inland Revenue could only recover from the husband : if all the couples' assets were in the name of the wife, this right of recovery could prove illusory. The right to recover from the wife, therefore, was re-enacted following the Colwyn Report and now appears in section 40 Taxes Act. Again, the existence of this provision points to illogicality of thought in the mind of the Treasury : at the same time as they were persuading the House of Commons and the Colwyn Commission that "the income of husband and wife is a joint one" and that therefore aggregation should be retained, they were also arguing that the incomes were separate where it suited the Revenue for the purposes of recovery.

The other two "minor" suggestions made by the Colwyn Commission on the subject of accountability concerned the timing of notices requiring separate assessment and the apportionment of unearned income when an option was in force. Both suggestions were subsequently enacted.

Of course the attention of the Commission would have been drawn to these three "minor details" by the

Inland Revenue; it is difficult not to compare the unqualified support given to these suggestions with the consideration given in the Report to the aggregation rule : there all the previous Treasury arguments are used to support the status quo and in spite of considerable pressure from the taxpaying public, the Treasury view triumphs in the end.

8. 1955 - The Radcliffe Reports

The Radcliffe Commission gave a certain amount of attention to the principle of aggregation but very little indeed to the principle of husband's accountability. However, in the third and final Report the Commission recommended that a wife should be required to sign her husband's tax return "for the purpose of verifying those statements in it that relate to her income". The following extract¹ from the Report explains the thinking behind the recommendation:-

"It is one of the necessities of the present system that a husband is required to make and sign a return of the income of himself and his wife : but he has no means of knowing precisely what his wife's income is and no return or verification of her husband's income is required of her. Yet if she is a woman of any independent income she will have her separate bank account. If she has a business or employment of her own her husband has no certain check on what her income is. We make no assumption either way how far this system has led to evasion. But we think that it is, in any view, unfair to the husband since it exposes him to the making of incorrect statements without any real power of safeguarding himself : and the defect is easily curable. For there is no difficulty in requiring that the wife should put her signature to her

1. Paragraph 1060; Final Report, June 1955 Cmd 9474.

husband's return for the purpose of verifying those statements in it that relate to her income, whether assigning a figure to it or declaring that she has none...We do not recommend that the husband himself should be exempt from responsibility for that part of the return that relates to the wife's income merely that he should have the security of her signature and joint liability. If he wants to go further he must apply for separate assessment."

Now this recommendation was never implemented and the reason may be the unpopularity of the proposal : if a wife were obliged to sign the tax return she would, for the first time, be given a right to have details of the husband's income. Although such a right was no doubt given in fact to many wives by their husbands, there is always a substantial number of husbands who keep their incomes a secret from their wives; a survey conducted by the Evening Standard in March 1982 indicated that this was the practice with one-fifth of married couples surveyed. And it is interesting to note that even where an option for separate assessment is in force, a wife does not have details of her husband's income.

9. 1956-78. The Tax Reform Papers

None of the tax reform papers published in the decade commencing with 1970¹ were concerned with the principle of accountability; insofar as they affected the income tax treatment of husband and wife they were concerned only with aggregation (Chapter 7) and allowances (Chapter 9). Perhaps this is not surprising in view of the

1. Inheritance Tax (Cmnd 4930 - March 1972); Tax Credit System (Cmnd 5116 - October 1972); Wealth Tax (August 1974) and Report of a Select Committee on Wealth Tax (November 1975).

subject matter of these papers but more surprising is the fact that neither Macdonald¹ nor Meade² make any reference to the principle. However the extent of the dissatisfaction felt by taxpayers with the principle of accountability was highlighted by the campaign for reform which was initiated in December 1977 by the publication of a consultation document by the Equal Opportunities Commission.

10. 1977-1979 - The Equal Opportunities Commission's Campaign for Reform

- (1) 1977 - Publication of consultation document by EOC.
- (2) 1978 - The Press Campaign.
- (3) 1978 - Statutory and administrative changes.
- (4) 1979 - A response to the consultation document.
- (5) 1979 - Further administrative changes.
- (6) 1979 - A review of the altered position.

(1) 1977 - Publication of the consultation document by EOC.

The Equal Opportunities Commission was established by the Sex Discrimination Act 1975; now that Act only applied to discrimination in certain specified areas and section 51 specifically provided that the non-discrimination provisions in the statute did not apply to existing legislation. It was clear, therefore, that tax legislation was outside the scope of the Commission's jurisdiction. However, the Commission clearly received a large number of complaints about the discriminatory nature of the income

1. "Taxation and the Family Unit" Graeme MacDonald. The Institute for Fiscal Studies 1975.

2. The Structure and Reform of Direct Taxation, op.cit.

tax system. The Commissioners therefore corresponded with the Treasury, pointing out areas for reform and a delegation of Commissioners met the Chancellor of the Exchequer in May 1977. In December the same year the Commission published a consultative document entitled "Income Tax and Sex Discrimination". Now it is a most interesting feature of that document that it was clearly published in response to a number of complaints from taxpayers all of which concerned accountability and none of which concerned aggregation. So:-

"Women form the large group of persons who have written to complain about the humiliation involved in the assumption, at all stages of their dealing with the Inland Revenue, that the joint income is the property of the husband...men have also written to complain of the burden of having to take responsibility for their wife's financial affairs, and to complain of the unfairness involved, for example, in situations where the wife has a larger (unearned) income than the husband's earned income".¹

And again:-

"The most important source of complaints about sex discrimination is the provision that, for tax purposes, a married woman's income belongs to her husband. He is assessed for income tax on the joint income (which, technically, belongs only to him); he is responsible for making the declaration of income to the Inland Revenue; he is legally responsible for paying any tax due; and he will usually receive any tax rebate owing".²

The complaints received are more fully analysed in Chapter 4 where the following six sources of dissatisfaction are identified:-

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1. Page 5.
 2. Page 10.

(1) Correspondence

"Perhaps the most common complaint made by married women about their tax position concerns the Inland Revenue's practice of conducting correspondence with the husband only...It may be suggested that such complaints are trivial. But what many married women object to is the assumption that they do not exist as far as the Inland Revenue is concerned".

The Commission suggests that this complaint could be cured by providing a joint responsibility to provide information with correspondence being addressed to husband and wife jointly.

(2) Privacy

"Because the husband is responsible for completing the tax declaration, the wife is asked to give her husband details of her income. But the reverse does not apply if there is no legal obligation on the husband to tell his wife what his income is and many wives do not in fact know how much their husbands receive".

The Commission point out that separate assessment does not completely solve the problem as "it is still possible to calculate, from the division of the allowances between the partners, how much income the other receives".

(3) Claiming and allocating the allowances

"The married man's allowance and the wife's earned income allowance are both claimed by the man".

Although the benefit of the wife's earned income allowance will be given against her earnings it has to be claimed by the husband, as must any other allowance or expense to which the wife is entitled. The consultation document also discussed an administrative practice whereby,

if either husband or wife is assessed to tax at the higher rates, the husband is given first claim on the lower rates, the wife's income bearing the higher rate tax. This was known as the "excess basic rate adjustment" and was described as follows:-

"If the couple's joint taxable income is high enough for tax to be paid at higher rates on part of it (without being sufficiently high to make a wife's earned income election worth while) the husband has first claim on the lower rate of tax. In other words his taxable income (up to £6,000) will be taxed at 34%; a proportion of his wife's earnings will be taxed at a higher rate".

Now this administrative practice had no basis in law and was most inequitable in practice : in most cases husbands have higher incomes than wives and there must have been many cases where the small (possibly part-time) earnings of a wife were depleted by the deduction of higher rate tax due on her husband's high earnings. However, the practice received no publicity and as no doubt many of the adjustments were made through the PAYE codings of married women, without explanation, the ground for complaint was not widely known.

(4) Mortgage interest relief

"Since the man, for tax purposes, owned the couple's income, this also means that he owns the couple's tax allowance - including relief given on the interest paid on a mortgage. This applies where the house is in a man's name; where it is in joint names, and even where it is owned by the woman alone. The relief on the mortgage interest payments will only be set against the woman's income when the husband gives his written consent".

(5) Tax rebates

"Many of the complaints received by the Commission arise from the fact that the

husband often receives a rebate payable on the wife's income. Where the couple are jointly taxed, the husband receives any tax rebate due on "his" income - even where the income is in fact earned by the wife - unless the income is being taxed through the PAYE system when the rebate will normally be paid through an adjustment in coding".

(6) Responsibility for payment

"Where the couple are jointly taxed, the husband is legally responsible for the tax on their joint incomes. Nevertheless, the Inland Revenue may claim the tax from the woman...in a situation where the woman is the richer partner and is not providing her husband with sufficient funds to pay the Inland Revenue".

Now, as has been noted earlier in this Chapter, all the above complaints, with the exception of lack of privacy, could be solved very easily under the existing law - namely by the wife's exercising the option for separate assessment, and, even as far as privacy is concerned, the exercise of such option would go a long way towards solving many of the problems outlined. Why, then, is this option not more widely used? The answer may be in two directions. First, in

"The Inland Revenue's reluctance to advertise certain benefits which might be advantageous to many women (such as separate assessment)",

and also the fact that if separate assessment were more widely advertised:-

"This would create many problems: the system is complicated and expensive to administer: there would possibly be delays in finalising tax bills at the end of each year".

Now, apart from putting forward the suggestion that a system of joint responsibility for income tax would solve the problem of correspondence (although it would,

incidentally, destroy all privacy for husband and wife) the Commission make no recommendations for solving the dissatisfaction shown with the principle of accountability : they do discuss a number of options for change but these are almost solely concerned with the system of allowances discussed in Chapter 9. No concrete suggestions for reform were made and it is problematical if any would have resulted had it not been for the Press Campaign which followed the publication of the consultation document.

(2) 1978 - The Press Campaign

The consultation document received a considerable amount of press publicity and during 1978 the impetus for change accelerated. On March 5th the Sunday Times reported the launch of a "Why be a wife" campaign.¹ This was concerned with both the social security and tax disadvantages of married women and as far as income tax was concerned the disabilities complained of all related to the principle of accountability i.e. the husband's responsibility for completing the tax declaration of the wife's income, the necessity for the wife to give details of her income to her husband and the fact that the reverse did not apply - there was no legal obligation on the husband to tell his wife what his income was.

On March 25th Woman's Own Magazine launched a campaign urging reform "so that women are treated as individuals in their own right". A coupon was included and 6,500 replies were received. Of the additional comments

1. See also The Times March 8th Column 4F.

received the vast majority concerned accountability, specifically, correspondence, repayments, privacy, claiming of allowances, and mortgage interest.¹

On 16th April the Sunday Times launched its own campaign. This did not mention the subject of aggregation but referred to the complaints about correspondence relating to a married woman's tax affairs being conducted with her husband, the rebates being paid to the husband, and the husband's responsibility for tax on his wife's income. Again, a coupon was included for return; 5,000 replies were received within a week and by May 7th 310,000 signatures had been received. On June 11th the Sunday Times reported that Mr. Joel Barnett, the Chief Secretary to the Treasury, had said that the Government would "look at the problems surrounding the completion of the tax forms and the payment of rebates" and there was also a promise to look at the subject of aggregation in the longer term.

(3) 1978 - Statutory and administrative changes

Having once again been subjected to pressure for change the Treasury responded in its usual way - by making a few peripheral changes leaving the main source of complaint untouched.¹ No reference is made to the advantages of an option for separate assessment but a Press Release was issued on 29th June 1978 indicating that legislation could be brought forward at the Report Stage of the Finance Bill dealing with entitlement to repayments and certain minor allowances; three changes in practice were also

1. See Appendix B Table 5 "With all my worldly goods I thee endow". Equal Opportunities Commission February 1979.

announced. First, the Inland Revenue would, in future, reply to a letter written by a married woman (but would not initiate correspondence with her); secondly, the wording on some of the forms would be changed; and finally two new leaflets would be issued about the tax treatment of married couples and the option for separate assessment "to ensure that those who wish to opt for separate assessment are aware of the relevant provisions".

The new clause dealing with repayments was introduced on 11th July 1978.¹ Previously, a wife had received a repayment in respect of tax overpaid in that year but the clause extended this right to repayments due in respect of overpayments in a previous year. Further, repayments due when the wife was the only earner, and therefore where all the allowances were claimed against her income, were to be paid to the wife (instead of to the husband as previously). However, the new clause did not apply where either husband or wife was assessed under schedule D, or where the wife had investment income, or where the joint income was liable to tax at the higher rates.

In introducing the clause the Chief Secretary to the Treasury (Mr. Joel Barnett) said:

"This clause extends the rights of married women to receive their own repayments of pay as you earn tax by statutory right. The new clause will give this statutory right to about 6 million earning wives at present within the PAYE system. Frankly, it is incredible that this has not been done before".²

1. Cols. 1256-1288.

2. Col. 1260.

And -

"I believe that this new clause does put right a very serious wrong that many married women have suffered. They have waited far too long to have it remedied. I look forward to being able to do much more in the years ahead..."₁

In reply, Sir Geoffrey Howe drew attention to the fact that the clause was

"a less than adequate response to the growing chorus of complaints about the way in which the present income tax system operated as between the sexes."₂

He pointed out that the clause did not apply where the joint income was taxed at the higher rates or where the wife was assessed otherwise than under schedule E. Further, the other grounds for complaint remained; underpayments of tax were still the husband's responsibility; the wife still had to disclose her income to her husband who was alone responsible for declaring it to the Inland Revenue; the wife had no privacy as far as her savings were concerned; she still could not get relief for mortgage interest paid by her without her husband's consent; and the Inland Revenue had not undertaken to initiate correspondence with her about her income tax affairs - only to reply to her if she wrote to them. However, with all its deficiencies the new clause was clearly a step in the right direction and was subsequently enacted as section 22 Finance Act 1978.

(4) 1979 - A response to the consultation document

Perhaps the Inland Revenue and the Treasury thought

1. Col. 1264.

2. Col. 1265.

that these statutory and administrative changes would bring the campaign for reform to an end and in one respect they were right because the Press Campaign died down. But in February 1979 the Equal Opportunities Commission returned to the attack and published the response it had received to the 1977 consultation document under the title: "With all my worldly goods I thee endow ...except my tax allowances". The response analysed the replies received to the consultative document and it is interesting to note that whereas the consultative document itself had concentrated on the principle of accountability many of the replies complained of the aggregation rule. The response noted the changes which had been introduced in 1978 and summarised the deficiencies which remained which had been outlined by Sir Geoffrey Howe during the debates in 1978. The "major areas for consideration" outlined in the response, however, concerned aggregation - (investment income and the tax unit) and allowances; no specific recommendation is made to solve the remaining injustices of the principle of accountability but the document clearly points towards the need for an individual basis of assessment which would also bring with it the advantages of completely separate accounting.

(5) 1979 - Further administrative changes

It will be recalled that a major inequity of the principle of accountability, namely, the "excess basic rate adjustment"¹ had been described in the 1977

1. Described on page 444 above.

consultation document; this discrimination was altered by a change in administrative practice announced in December 1979.¹ and the change was described by the Chancellor of the Exchequer as follows:-

"The tax tables give each employee the benefit of the full band of income chargeable at the basic rate. Married couples, like other taxpayers, are entitled to only one basic rate band, unless a wife's earnings election has been made. Consequently a reduction has to be made in the PAYE code number where husband and wife are both employed and their joint earnings are sufficient to attract liability to higher rate tax. This is to ensure that the right amount of tax is deducted during the year. This reduction, known as the excessive basic rate adjustment, has normally been made in the wife's coding. In future it will be made in the husband's coding unless the wife's earnings are expected to be greater than her husband's or the couple notify the tax office that they would prefer the reduction to be made in the wife's coding".

The same Press Release announced a change in practice regarding correspondence:-

"Hitherto [the Inland Revenue] have written only in response to letters from married women. Henceforth tax offices will normally write direct to a married woman about her own tax affairs whether or not she has first written to the Revenue".

(6) 1979 - A review of the altered position

As no changes in the principle of accountability have taken place since 1979 it might be helpful to compare the position then reached with that described in the Introduction to this Chapter under the same seven headings, namely:-

1. Inland Revenue Press Release 4th December 1979.

- (1) Making the return. The option for separate assessment introduced in 1914 permitted a husband to disclaim responsibility for making a return of his wife's income and a wife to make her own return. Legislation enacted first in 1911 and again in 1950 gave the Inland Revenue an additional right to require a return from a wife where no option was in force.
- (2) Privacy. A husband has complete privacy under the present system, a wife has none. A system of joint responsibility would remove the husband's privacy without benefiting the wife. The option for separate assessment gives a wife some privacy but this is not complete; as both spouses can guess each other's income and allowances the husband has less privacy than before.
- (3) The husband's responsibility for paying the tax. An option for separate assessment will enable a husband to disclaim responsibility for his wife's tax and will create a new responsibility for the wife. By virtue of legislation enacted in 1950 the Inland Revenue can, in any event, make a wife responsible for her own tax.
- (4) Repayments. An option for separate assessment will enable a wife to receive her own repayments. Otherwise section 22 Finance Act 1978 provides that she will receive them only if she is taxed under schedule E and only if the joint income is not liable to higher rate tax.

- (5) Correspondence. In 1978 the Inland Revenue decided to reply to married women and in 1979 said they would initiate correspondence with her.
- (6) Claiming the allowances. Only an option for separate assessment will enable a married woman to claim her own allowances, expenses and reliefs.
- (7) Allocation of allowances. Since 1979 the 'excess basic rate adjustment' is made against the husband's income rather than the wife's and certain minor allowances may be claimed against her income. But only an option for separate assessment will give her any entitlement to other allowances, including mortgage interest relief paid by her. Even the option may not allocate the allowances on an 'individual' basis as the system (explained in Chapter 2) operates by reference to a proportion of income rather than entitlement.

This, then, is the present position against which the proposals in the Green Paper fall to be considered.

11. 1980 - The Green Paper

The Green Paper recognises that privacy is a factor for judging any system for taxing married couples but despite the considerable evidence of a demand for more privacy contained in the documents issued by the Equal Opportunities Commission, the Green Paper does not find the factor conclusive. So :-

"Wives should be able to keep particulars of their income and their tax affairs confidential from their husbands (and husbands from their wives). Some would attach more importance to this than others as a necessary feature of a system; and there are those who would argue that it would be more desirable to have a system of joint taxation under which there is no privacy between husband and wife but both are jointly responsible for declaring the combined incomes and paying the total tax".¹

Nevertheless, the criticisms of the principle of accountability are mentioned as giving rise to discrimination within the family;²

"A number of people feel particularly strongly about the issue of the married woman's privacy. Because a husband is liable for tax on his wife's investment income it follows that he must get to know about any savings or investments she has. Criticism of our tax system as discriminating unfairly between husband and wife does not come exclusively from women : some even object to having to go through the process of obtaining details of their wife's income, dealing with all correspondence relating to it, and being liable for any tax due on it".

On the other hand, the solution to these difficulties, which lies in independent taxation, is said to have³

"obligations as well as rights; every man and woman, married as well as single, would be responsible for filling in his or her own tax return, dealing direct with tax authorities and paying his or her own tax bill".

In fact, the only persons affected by the change would be married women as all these obligations fall on other taxpayers in any event.

1. Paragraph 7.

2. Paragraph 32.

3. Paragraph 40.

The Green Paper puts forward a number of suggestions for reform, each of which would have a different effect on accountability and a reference is now made to each.

(1) Joint taxation (paragraph 43).

"This would involve substituting for the present aggregation rule a rule under which the income of husband and wife would be jointly returnable by them and jointly assessable on them and there would be a joint responsibility for payment of the tax".

This system would have two major disadvantages; the husband would lose his present right to privacy and a wife, who may have little or no income, would become liable for her husband's income tax.

(2) Rewording the aggregation rule (paragraph 44).

"The aggregation rule could be re-worded simply to treat the income of husband and wife as if it were one income, the tax remaining assessable etc. on the husband".

This alteration has cosmetic significance only - although the wife's income will no longer be specifically stated to be deemed her husband's income, it will remain so in fact. The change would remove none of the disadvantages of accountability.

(3) Option for individual taxation (paragraph 46).

"The extension of the wife's earnings election to investment income would remove the discrimination against married couples with investment income...a wife would get a single person's allowance against her investment income...(but) the husband would lose (the married man's allowance).

Although this option would give complete privacy once exercised, it has two major disadvantages. First, it

will not always be beneficial and spouses therefore will require details of each other's income in order to decide whether it should be exercised; and secondly, it is proposed that the election should have to be made jointly (paragraph 53). So, although the election could give some degree of independent accounting, it has to be exercised and does nothing to help those couples who do not exercise it either because it is not beneficial to do so or otherwise.

(4) Option for independent taxation with equal split
(paragraph 51).

"It would be relatively simple to alter the rules for separate assessment in such a way that, for cases where it would not be beneficial for the couple to choose to be taxed as two single individuals (i.e. under Option (3) above) they could nevertheless opt for separate responsibility with an equal split of the available allowances and rate bands".

The existing disadvantages of the options for separate assessment are recognised - the allocation of allowances is not always fair; the arrangements are complex and infrequently used; and the calculations mean that privacy is not preserved. The "equal split" would solve these problems to some extent -

"in many cases the privacy would be complete; even where it was not only the spouse with the higher income could calculate the amount (although not the source) of the other spouse's income".

However, the exercise of the option could affect the allocation of the allowances between the couple and does not preserve complete privacy.

(5) Mandatory independent taxation (paragraph 73).

"A mandatory system of independent taxation would mean...that all married women would become taxpayers in their own right... They would complete their own tax returns, conduct their own dealings with tax offices, and be ultimately responsible for paying any tax due on their own incomes".

This would clearly answer all the criticisms of the principle of accountability but almost immediately a new complication is introduced - the transferable allowance. This will be discussed in Chapter 9 but here it may be noted that a system of transferable allowances could re-introduce the difficulties of husband's accountability.

12. Summary

The option for separate assessment introduced in 1914 goes some way to reducing the disadvantages flowing from the principle of accountability; but it is complex to administer; it is not a complete answer to the problems as the allocation of allowances and the question of privacy are not considered to be satisfactory; and it is not widely known.

The alterations since that date have benefited both the Inland Revenue and the taxpayer but there are still considerable areas of dissatisfaction. None of the proposals in the Green Paper provides a complete answer, either, except for that of mandatory independent taxation but even there problems could arise if a system of transferable allowances was adopted.

The whole subject of the allowances for husband and wife is now considered in Chapter 9.

CHAPTER 9 - A REVIEW OF THE PRINCIPLES UNDERLYING THE
ALLOWANCES

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CHAPTER 9

A REVIEW OF THE PRINCIPLES UNDERLYING THE ALLOWANCES

Section

1. Introductory.
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5. 1954 - The Radcliffe Report.
6. 1971 - Separate Taxation of Wife's Earnings.
7. 1972.- Proposals for a Tax Credit System.
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9. 1977-79 - The Campaign for Reform.
10. 1980 - The Green Paper.
11. Conclusions.

1. Introductory

Part II of this thesis reviews the studies and criticisms of the present rules concerning the tax treatment of the family unit. The three main principles of aggregation, accountability and the allowances are considered separately as each is independent of the other and each has a separate historical development. This Chapter considers the principles underlying the allowances and these, in particular, repay close scrutiny as without an understanding of their historical development the present arrangements would be

difficult to comprehend. From the first, the allowances given to married couples have created anomalies and it is thought that it is the existence of these anomalies which are now one of the largest obstacles in the way of reform.

2. 1918 - Introduction of a Wife Allowance

It will be recalled that a child allowance had been introduced at an extremely early date in the history of income tax although it was in abeyance for a number of years. Although there was no system of personal allowances as such there was always an exemption limit below which no tax was charged; this limit applied to each individual and for these purposes, as for all others, husband and wife together constituted one individual. However, provisions were enacted in 1894 giving a husband whose wife had earnings an additional exemption where the joint income did not exceed £500.

It is doubtful whether these arrangements would have been altered had it not been for the lengthy debate during the passing of the Finance Bill in 1914 when the Chancellor of the Exchequer (Mr. Lloyd George) had replied to the mounting criticism of the aggregation rule by indicating that he saw the solution to the problems of aggregation in a review of the system of personal allowances.

Such was the background to the proposal made in the Budget statement on 22nd April 1918 that the Government intended for the first time to introduce an allowance for a wife. Mr. Bonar Law's words are most enlightening:-

"I propose to make the children allowance apply to a wife also, and so far, much to my surprise, I have had no representations from any women's suffrage societies suggesting the impropriety of proceeding on that basis. I also propose to extend a similar allowance to real dependants who are incapacitated".¹

Thus, were wives placed on the same basis as children and other incapacitated dependants. It is clear that this relief was seen in the nature of a housekeeper relief for a married man and the question was immediately raised as to why a widower or unmarried man should not have a housekeeper, too. So, Mr. Thomas:-²

"I am delighted to know that the Chancellor of the Exchequer proposes to make some allowance in regard to wives...that is a very necessary and wise provision but I would like to ask whether that includes provision in respect of a housekeeper? Otherwise you are going to have this anomaly, that a man is to have an allowance in respect of his wife but if he is left a widower he is to be placed at a great disadvantage. He will have to employ and pay a housekeeper and experience shows the difficulty and expense of that".

So the same allowance was also given to a widower who had a female relative to look after his child. When the wife allowance was introduced, by section 27 Finance Act 1918, it was the same amount as the child allowance i.e. £25. (The single person's exemption limit was then £130). This figure was doubled to £50 by section 27 Finance Act 1919 which extended the relief to any widower with a housekeeper, whether he had a child or not. Section 21 of the same Act gave the same relief of £50 to an unmarried individual who maintained a female relative to look after

1. Hansard, 22nd April 1918 col. 708.

2. Hansard, 22nd April 1918 col. 729.

his young sister or brother. The relief to the widower was not conditional upon his maintaining the housekeeper at his own expense (i.e. the housekeeper could have an income of her own) but the relief to the unmarried person was only available where the housekeeper had no other income.

Now the minor personal allowances (including the housekeeper allowance) are outside the scope of this thesis but are mentioned here in order to illustrate the context in which the first wife allowance was introduced. The wife allowance had originally been suggested as an alternative to disaggregation but when it was introduced it was given to the husband and was seen as an extension of the child allowance. Further, the extension of the same allowance to "housekeepers" imported two further anomalies into the system : first, the incomes of husband and wife remained aggregated but a widower could get an allowance for a housekeeper who could have a separate (disaggregated) income, although it is appreciated that in most cases the widower would in fact be paying the housekeeper in which case there would not really be two separate incomes. Secondly, the allowance was given only to men - husbands and widowers; there was no equivalent allowance for widows.

The wife allowance (and the housekeeper allowance) were available only to taxpayers whose income did not exceed a specified limit which was £800 in 1919. Here was the cause of yet another anomaly - a wife who earned her own income, and thereby increased her husband's deemed income could, in that way, deprive him of the additional exemption limit under Finance Act 1894 and also of the wife allowance under Finance Act 1918.

Finally, it will be noted that where a husband was entitled to the additional exemption for wife's earnings his new entitlement to the wife allowance resulted in the total allowances available to a married couple being in excess of the total allowances available to two single persons. The root of this anomaly is that the earnings exemption, being only available against a wife's earnings, is of no assistance to a couple where the wife has no earnings, even if she has investment income. Although the assistance given by means of the wife allowance does assist where a wife has no earnings, or has investment income, it was given in addition to, and not in substitution for, the earnings exemption limit. Accordingly, where a wife did have earnings, both the earnings exemption and the wife allowance were available, thus giving a two-earner couple an advantage over two single individuals, whereas a one-earner couple was at a disadvantage as against two single individuals.

3. The Colwyn Report 1920

The Colwyn Report¹ laid the basis for the present system of personal allowances and its recommendations, therefore, repay scrutiny. Before the Commission was appointed the allowances were:-

- (1) an exemption limit of £130 available to all single taxpayers and to all married men;

1. Cmd 615.

- (2) an additional exemption limit of £130 available to married men whose wives had earnings, where the joint income did not exceed £500, and
- (3) a wife allowance of £50 available to married men whose income did not exceed £800.

The Colwyn Report recommended the abolition of all these arrangements and the introduction instead of a new "personal allowance" of which the amount for a married man would be higher than that for a single person, and also of an additional exemption limit for a married man whose wife had earnings. Now it is possible that if the Colwyn Commission had not been influenced by the history of the previous exemptions and allowances they might have concluded that husband and wife should be entitled to a personal allowance each, the wife's to be available against her earnings if she had any failing which it should be available against the rest of the joint income. And, in fact, this is almost what resulted because when the recommendations of the Commission were enacted in section 18 Finance Act 1920 a single person was given an allowance of £135 and a married man an allowance of £225 plus £45 if his wife had earnings : the total available to a married man (£270) was exactly twice that available to a single person but only if his wife had earnings. The previous advantage given to some married men was thus withdrawn.¹

However, this summary anticipates the discussion in the Report which can be considered under the following heads:-

1. See page 463 above.

- (1) the basis of the personal allowance generally.
- (2) the basis of the higher married man's personal allowance and
- (3) the basis of the additional allowance for wife's earnings.

(1) The basis of the personal allowance generally.

The personal allowance was to succeed the previous exemption limit but it was clear that that limit had not been fixed by reference to any identifiable criteria. Clearly the philosophical justification of such a limit was to remove very low incomes from the tax net altogether and to allow all taxpayers a measure of tax-free income, but the amount had not been arrived at with any approach at precision. There were "different ideas in the minds of witnesses as to when real taxable capacity begins". The Commission proposed three possible tests for taxable capacity, namely after provision of:-¹

- "(a) an actual minimum income, i.e. an income sufficient for bare subsistence or
- (b) an income not merely sufficient for bare subsistence but large enough to equip and sustain a healthy and efficient citizen or
- (c) an income sufficient not only for a healthy existence but for the provision of conventional comforts and luxuries usually enjoyed by what are commonly called the "working classes"."

The Commission were clearly of the view that all of these suggestions were too generous, so:-

"The truth is that the exemption limit has never in this country been based on a figure consciously related to any kind of minimum of subsistence..."²

1. Paragraph 242.
2. Paragraph 244.

Clearly the limit was, and is, fixed with some regard to the required yield of taxation but the link with taxable capacity is acknowledged:-

"While the limits we have suggested have not been arrived at merely as representing the minimum of subsistence for the persons to be maintained out of the income we recognise that in some measure the cost of living has a practical connection with the possible taxable capacity".¹

The amount of personal allowance recommended for a single person was £135, an increase of £5 on the existing exemption limit, and this amount was enacted in section 18 Finance Act 1920.

(2) The basis of the higher married man's personal allowance

The absolute amount of the personal allowances is not relevant to this thesis but the relative amount of the married man's allowance to the single person's allowance is. The higher married man's allowance was meant to replace the wife allowance introduced in 1918. At the date of the appointment of the Commission a married man whose wife had no earnings enjoyed an exemption limit of £130 and a wife allowance of £50. The Colwyn Commission thought that this was insufficient :

"the relation that now exists between the exemption limit for the bachelor and the effective exemption limit for a married couple is not consonant with justice".²

and recommended that the married man's allowance should be

1. Paragraph 247.

2. Paragraph 275.

£225 (compared with a single person's allowance of £135). However, this recommendation was conditional upon there being no change in the basis of assessment. So:-

"it would be illogical to allow both a separate assessment of husband and wife and also a wife allowance".

This must be right, as separate assessment would automatically have given a wife an allowance of her own.

In fixing the figures of the allowances, and the ratio of the married man's allowance to the single person's allowance the Commission said

"In recommending these figures we have had regard to the ability to pay..."

It will be recalled that when the subject of aggregation was under consideration the principles of "taxable capacity" and "ability to pay" were used to support the retention of the treatment of the incomes of husband and wife as one person : in the context of the allowances, however, a non-earning wife is treated as an additional $\frac{2}{3}$ of a person.

The amended allowances recommended by the Colwyn Commission were incorporated in legislation and the proportions remain very similar today: the ratio of the single person's allowance to the married man's allowance was then 1:1.6 and it is now 1:1.56.

(2) The basis of the additional allowance for wife's earnings

The increase in the amount of the wife allowance would have exaggerated the advantages of a husband with a

working wife¹ if no adjustment had been made to the allowance for a wife's earnings. Since 1894 a husband had been entitled to a full additional abatement of £130 for his wife's earnings if the joint income did not exceed £500. This was withdrawn and replaced by an additional allowance equal to nine-tenths of a wife's earned income with a maximum of £45 and the proposal was enacted in section 18(2) Finance Act 1920. No reason was given by the Commission as to why such a drastic reduction was made in the relief for wife's earnings : a reference was made to the 1894 provisions and to the fact that:-

"The limit of £500 has been represented to us as too low in present conditions. We agree with this point of view..."²

However, instead of raising the limit the Commission immediately recommends that it be discontinued and replaced by the wife's earnings allowance mentioned above. None of the allowances recommended by the Commission was restricted by reference to the amount of the husband's income, although of course, the wife's earnings allowance was restricted by reference to the wife's earnings.

It has been noted that when the recommendations of the Colwyn Commission had been enacted a married man with a working wife received the equivalent of two single person's allowances : but the amount available in respect of wife's earnings was only £45 which compared unfavourably with the £135 available to single women. This inequity was the subject of discussion in a White Paper published in 1942 on "The Taxation of Weekly Wage Earners".

1. See page 463 above.

2. Paragraph 261.

4. 1942 - Increase of Wife's Earned Income Allowance

In 1942 the allowance for wife's earnings remained at the maximum of £45 fixed in 1920 but the other personal allowances had been reduced to £80 (single) and £140 (married). The inequity of the allowances made to a married woman and to a single woman were discussed in the White Paper on "the Taxation of Weekly Wage Earners" ¹ published in April 1942.

"Linked up with the general question of the deduction of tax from wages is the special problem of the taxation of married women in employment. There is a good deal of misunderstanding on this subject...It has, for instance, been repeatedly alleged that a single woman in industrial employment is in a more favourable position than a married woman but this is only true where the earnings are large. Where a married woman is in employment an additional personal allowance of 9/10ths of her wages, subject to a maximum of £45 is given. This £45, added to the married allowance of £140 gives a total personal allowance of £185 for the husband and wife together which is more than twice the single allowance of £80 given to a single person".²

This extract shows the confusion between the allowances given to each single person against all income, and the allowances given to a husband for his wife, part being available for all income and part available only against earnings. In attempting to preserve equity as between married men and single persons, the equity between working married women and working single women had been overlooked. The remedy proposed was to raise the allowance

1. Cmnd 6348.

2. Paragraph 43.

for wife's earnings to the level of a single person's allowance (then £80) leaving the married man with the full higher allowance. So, once again, the allowances given to a two-earner couple were greater than those given to two single persons. A clause to give effect to the recommendation was included in the 1942 Finance Bill (clause 22) and in commenting on its provisions Sir John Mellor said:-

"The clause has not touched the root of the problem. The real trouble lies with the joint assessment of husband and wife. The clause has merely added another patch, although in itself a good patch, to an existing patchwork system of allowances".¹
And:-

"The fact is that a couple gain financially by being married only if the woman has a modest earned income and no unearned income. Otherwise they lose. Is this fair or desirable...I submit that until the whole system of allowances and the incidence of taxation upon married persons are changed so that there is separate assessment of husband and wife, the allowances being recast, we shall not get a satisfactory position".²

The provisions were enacted as section 23 Finance Act 1942 and thus was the principle established, which remains today, that the allowance for a wife's earnings should be the same as the single person's allowance.

The reason for equating the wife's earned income allowance is sometimes said to be to provide an incentive for a married woman to work and at other times it is said to be a recognition of the additional expenses thrown upon a household with a working wife. These arguments will be

1. Hansard 13th May 1942 col. 1792.

2. Col. 1793.

considered later in this Chapter.

But from the Report mentioned above it is clear that the real reason was to meet the justifiable complaint that where two women worked side by side at the same employment for the same remuneration a single woman only paid income tax on earnings in excess of £80 whereas a married woman paid tax on earnings in excess of £45; it is no answer to a married woman in this situation to state that her husband has an additional allowance resulting from marriage.

5. 1954 - The Radcliffe Report

The Radcliffe Report gave detailed consideration to the subject of the personal allowances and recommended some rather complex adjustments which were not subsequently incorporated in legislation. However, the Report does merit a brief reference as it contains comments on the historical basis of the allowances and also on the philosophy underlying the allowances generally. As with the Colwyn Report a reference will be made first to the basis of the personal allowances, then to the married man's allowance and finally to the allowance for wife's earnings.

(1) The basis of the personal allowances generally

The Report appreciates the impossibility of finding any absolute answers to the question of the amount of the personal allowances:-

"We were forced to the conclusion...that we should be wasting our time if we tried to find agreement among ourselves as to ...the precise figures that ought to be allotted to the various personal allowances, both absolutely and in relation to one another. These things must remain a matter of individual judgment".¹

The basis of the allowances appear to rest on capacity to pay. So:-

"The personal allowances carry this conception of varying capacities to pay into another field and recognise that, if equal relative sacrifice is what it is sought to achieve, the same tax bill may represent very different sacrifices for two persons with equal incomes according to differences in their respective personal situations. A man with £800 a year and a wife and two children to support out of it is less able to bear a given amount of taxation than a single man with the same amount of income".²

The Commission concludes that the existing system of lump sum allowances "does not produce a very satisfactory distribution between taxpayers in the middle and upper levels of income"³ because the allowance "becomes proportionately smaller as the income increases".⁴

A radical change proposed by the Commission was the introduction of an exemption limit which would replace the earned income relief but would be in addition to the personal allowances : the Commission thought that the function of the personal allowance was primarily to ensure

"progressiveness in the effective rates of taxation as well as a method of differentiating between people with the same income but different family circumstances".⁵

1. Paragraph 109.

2. Paragraph 151.

3. Paragraph 155.

4. Paragraph 156.

5. Paragraph 160.

whereas a minimum exemption limit had a completely different function, namely "to prevent the tax impinging upon what is required for subsistence". One reason why the personal allowances could not be used as a minimum exemption limit was, that if they were set at the appropriate subsistence figure, the cost would be too high. Ultimately the Report recommended a rather complicated system of graduated minimum relief.

(2) The married man's allowances

Following its conclusion that the lump sum allowances were disproportionately disadvantageous to those with higher incomes the Commission recommended a proportional allowance for married men of :

"10 per cent of income up to £1,000 and £100 plus 6 per cent for the excess over £1,000 with a minimum of £90 and a maximum of £160".¹

This recommendation was made within the context of existing allowances of £120 for a single person and £210 for a married man. In addition, the Report recommended a higher starting point for surtax liability for a taxpayer with a wife and children.

(3) The wife's earning allowance

By the date of the Report the special treatment for wife's earnings amounted to the equivalent of an additional single person's allowance (£120). The Report traces the special treatment of wife's earnings but only

1. Paragraph 180.

as far back as 1920; it is not clear whether the Commission were aware of the earlier history or the reasons why the Colwyn Commission recommended the change which was enacted in section 18(2) Finance Act 1920, because the Report states that those provisions

"were intended as a recognition of the fact that the taxable capacity of the married couple where the wife is earning is generally speaking less than the taxable capacity of a couple where the wife has no employment; for the mere circumstance of her employment tends to throw upon the household some expenses that would otherwise have been avoided".

Now it is extremely difficult to see how the taxable capacity of a household with two members who are both earning, so that the ratio of incomes to persons is 1:1 is less than the taxable capacity of a household with two members of which only one is earning, so that the ratio of incomes to persons is 1:2. It is appreciated that the "circumstances of employment" do involve "expenses which would otherwise have been avoided" e.g. travel, meals, etc. but this is the same for any person, husband, wife or otherwise and is meant to be accounted for in the special treatment afforded to earned income. This artificial justification of the anomalies of the personal allowances given to married couples, by reference to some untenable notion of "decreased taxable capacity" is not borne out by an examination of the historical genesis of the provisions.

The Report also refers to two more probable reasons for the relief namely:

"a desire to offer to the married woman an inducement to undertake or to retain employment and by the great administrative advantage, for the purposes of PAYE, of

equating the quantum of her reliefs with those of an independent single person".

After considering the arguments for modifying or ending the relief the Report concludes:-

"We have come to the conclusion that we ought not to recommend the abandonment of the present system...in our opinion there is a valid difference between the taxable capacity of a married couple where the wife is at work and the married couple where the wife is at home...the special treatment of wives' earnings is...a device for securing a measure of distinction between two different kinds of taxable unit".

However, the Report concludes that the existing distinction was excessive:-

"The married couple of two earners is... treated more favourably than two single persons...the most natural course would be to withhold the net marriage allowance of the husband...progressively in proportion to the size of the wife's tax free earnings. But enquiry satisfied us that any such scheme...is ruled out owing to its administrative complications. The alternative method is to reduce the existing relief on the wife's earnings...by lowering the amount of her special personal allowance..."

Later¹ such a reduction is recommended combined with the recommendation that the proposed new "minimum relief" proposed for all taxpayers should also be available to a wife for use against her separate earnings.

These recommendations were not, of course, implemented.

(6) 1971 - Separate taxation of wife's earnings

It will be recalled that one result of an exercise of the option for separate taxation of wife's earnings,

1. Paragraph 65.

introduced by section 23 Finance Act 1971, was the loss of the additional married man's allowance; the married couple obtained two single personal allowances instead. In the subsequent discussion in this Chapter, therefore, references to the advantages enjoyed by a two-earner couple refer only to couples where this election has not been exercised.

(7) 1972 - Proposals for a tax credit system

The main proposals in the Green Paper on the tax-credit system,¹ published in October 1972, have not been implemented but a brief reference to these may be helpful as the subject of the allowances available to a married couple are considered and discussed; also, it is possible that the proposals may be implemented at a later date.

The publication of the Green Paper could have presented an ideal opportunity for re-casting the system of allowances available to a married couple, with a view to removing the anomalies which had crept into the system : unfortunately once again the Report preferred to retain the status quo and the opportunity for some radical re-thinking was lost.

"The tax credit system is a reform which embodies the socially valuable device of paying tax credits to the extent that they are not used up against the tax due, positively as benefit".

In this way the Foreword to the Green Paper summarises the basis of the proposals; "tax credits" were to take the place of the main personal allowances;² when

1. Cmnd 5116.

2. Paragraph 9.

paying wages the employer would always deduct tax at the standard rate and then add back the credit to which the individual was entitled; if credit exceeded tax the difference would be paid out to the taxpayer each week - there was to be no carry forward of unused credits.

As far as they affect married couples the proposals can be considered from the same three directions as previously, namely, the basis of the single person's tax credit, the basis of the married man's tax credit and the proposals for treatment of wife's earnings.

(1) The single person's tax credit

In 1972 the single personal allowance was £460¹ and the standard rate of tax was 38.75 per cent.² If the single person's credit was to replace exactly the corresponding income tax allowance it would have had to be set at £3.43 a week; the Green Paper however proposed a limit of £4 per week so as to "improve the position of people of limited means" and to reduce "the dependence of pensioners on supplementary benefit".

(2) The married man's tax credit

In 1972 the married man's personal allowance was £600. Now this was low in proportion to the single person's allowance (£460); it will be recalled that the Colwyn Commission had recommended a differential of 1:1.6 but this represented a differential of only 1:1.3. If a married man's credit was to replace exactly his corresponding income

1. Finance Act 1972, section 65.

2. Finance Act 1972, section 62.

tax allowance it would have had to be set at £4.46 a week, but the Green Paper proposed a limit of £6 which was clearly an improvement, not only on the existing amount but also on the existing differential (from 1:1.3 to 1:1.5) although the differential was not raised quite as high as had been recommended by the Colwyn Commission (1:1.6). At one stage it looked as if the Report would take the opportunity of re-thinking the basis of the married man's allowance. So

"It can be argued that two people should not be treated differently for tax purposes because they are married...In the context of a tax credit system this argument would point to fixing the married credit at twice the single credit. It would follow from this that the wife's earned income relief would disappear".¹

The Report concludes that this would not be desirable for three reasons; first, the married couple where the wife is at home would show a large relative gain; secondly, the withdrawal of the wife's earned income relief would be a disincentive to married women to seek work; and finally, the withdrawal of the wife's earned income relief would not recognise the decreased taxable capacity, of two-earner couples.

It may be useful at this stage to analyse these three stated reasons for not giving a wife a full personal allowance.

(a) Relative gain for wife at home. It is agreed that the doubling of the single person's tax credit (or tax allowance) for a married couple would give a large relative gain for the wife at home but, as is stated in the Green Paper:-

1. Paragraph 77.

"Married couples when the wife is unable to work because of young children... tend to be less affluent than married couples both of whom are able to work".¹

The same would, of course, apply to a married couple without children if the wife was unable to work because of ill-health, say, or because caring for a disabled relative.

(b) Disincentive for married women to seek work. The Green Paper anticipates that the double tax credit would always be given to the husband and that a working wife would receive no credit at all : such an arrangement would be a disincentive to married women to seek work. But it would be fairer to give a tax credit each to both husband and wife so that if a wife had earnings she could utilise her own tax credit and if she had no earnings it would be utilised by her husband. There would then be no disincentive to the acceptance of employment by a wife; although the husband would then lose his use of her credit, her income would strengthen the family's finances.

(c) Recognition of extra expenses of wife working. The Green Paper says that the withdrawal of the wife's earned income relief would not recognise that:-

"where both husband and wife work additional expense is often incurred e.g. on domestic duties otherwise undertaken by the wife and it is fair to regard their taxable capacity as less than that of a couple with the same total income which is earned entirely by the husband".

It has been noted above² that the argument of the decreased taxable capacity of a two-earner couple is not considered to be well founded : in particular the

1. Paragraph 81.

2. Page 474.

reference here to the fact that the taxable capacity of a two-earner couple is less than that of a couple with the same total income which is earned entirely by the husband fails to consider the taxable capacity of a two-earner couple with twice the total income of a couple where all the income is earned by the husband. However, these three arguments were used in the Green Paper to maintain the "less than twice" rule for the personal allowances of a married couple with a non-earning wife.

(3) Wife's earnings allowance

The Green Paper recommended the retention of the wife's earnings allowance, not as a tax credit, but anomalously, as a continuing tax allowance, "in order to recognise the two arguments of incentives and additional expenses". The allowance in 1972 would have been worth £3.43 a week which was less than the proposed single person's credit of £4.

Thus was the opportunity for rationalising the allowances lost but the Report is of interest as it does consider the possibility of a married couple being entitled to twice the credits of a single person, even though the suggestion is not adopted.

8. 1975 and 1978 - MacDonald and Meade

The future of the personal allowances under an individual basis of taxation was discussed by Mr. Graeme MacDonald at the lecture given to the Institute for Fiscal

Studies on 10th December 1975.¹ Mr. MacDonald's lecture is of interest as he subsequently became a member of the Meade Committee and no doubt contributed to the recommendations in that Committee's Report.

MacDonald viewed the additional allowance given to a married man as "representing in some degree the loss in discretionary income occasioned by the need to support two individuals". He agreed that under an individual basis of taxation the married man's allowance would be abolished but appears to assume that this would be replaced by one single person's allowance only with the retention of the wife's earnings allowance if the wife has earnings. This raises the question of how relief is to be given where a spouse cares for children and the conclusion is reached that, because of the difficulty of defining deserving cases, the married allowance would have to be retained but only where the wife has no earnings; it is "over generous" to give the married allowance in addition to the wife's earnings allowance.

Now these conclusions fail to appreciate that, on an individual basis, a wife would be entitled to a single person's allowance in her own right, to set against earned or unearned income or income transferred to her by her husband;² but by the time the Meade Committee³ had reported these possibilities had been appreciated and discussed.

The only point upon which the Meade Committee

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1. Taxation and the Family Unit - Institute for Fiscal Studies.
 2. For a discussion of transferred income see page 614 post.
 3. The Structure and Reform of Direct Taxation 1978.

made a firm recommendation was that of the abolition of the married man's allowance where the wife has earnings:-

"The fact that with this system the great majority of married couples in which both partners are working enjoy a married allowance plus a single personal allowance is open to a number of objections. It means that by marriage two wage earners can reduce their total tax liability... It is also costly in revenue".

The Committee concludes that:-

"We all agree that the present arrangement by which, when both husband and wife are earning, the couple can enjoy both the married man's allowance and a single person's allowance against the wife's earnings is unsatisfactory and that where a personal allowance is claimed against the wife's earnings the husband should enjoy only a single person's allowance".

The Report then discusses no less than seven different proposals for reform, all based on the disappearance of the married man's allowance.

The first modification proposed is simply to remove the married man's allowance where the wife has earnings. The second (radical) modification proposes the removal of the married man's allowance in all cases, whether the wife has earnings or not, coupled with a new "home responsibility payment" where a spouse stays at home to care for children or dependants. But immediately this raises the problem of older spouses who have cared for children for a number of years but not returned to work; here again is the difficulty of defining deserving cases raised by MacDonald¹ and the conclusion is reached that "some form of married allowance" would have to be retained, possibly depending on age and/or past home responsibilities.

1. See page 481 above.

Meade justifies the retention of the wife's earnings allowance by reference to the "additional expenses" argument originally mentioned in the Radcliffe Report,¹ and again in the Green Paper on the Tax Credit System;² Meade says:-

"Thus, between two families with the same total of earned income the family in which the income was due to the earnings of both partners would be more leniently treated than the family in which the same total income was earned by only one of the partners. But this might be regarded as a suitable recognition of the fact that there could be more expenses...in the case of the former family".

The Report fails, however, to appreciate that the retention of a wife's earnings allowance, coupled with the abolition of the married man's allowance, would also result in more lenient treatment being given to a two earner family with twice the income of a one-earner family.

The third proposal for reform suggested by the Meade Committee is the adoption of an individual basis; here the proposal is that each spouse would have a single personal allowance and a spouse at home caring for children would have a "home responsibility payment"; the problem of the no-income spouse who has completed the years of child care is raised but not answered. Although, in theory, under an individual basis each spouse should have a personal allowance to set against all income, earned, unearned or transferred,³ Meade thinks this is too generous; although

1. See page 474 above.

2. See page 479 above.

3. For a discussion of transferred income see page 614 post.

the concept is acceptable in the context of earned income -

"in the case of investment income it may seem anomalous that the tax burden of a family which does in fact share the use of the joint income should depend upon the accident of the division of its ownership within the family".

It is also pointed out that -

"if the individual basis were adopted for the tax unit the transfer of unearned income from the partner with income to the partner without income would, up to the limit of a second full personal allowance, attract complete relief from tax".

In order to counteract this, the suggestion is made that all personal allowances should be available only against earned income, or at least for taxpayers under 45. But this solution would affect all taxpayers and would deprive married women from using their personal allowances against their own investment income; if transfers of income are to be discouraged, a better method would be to enact specific anti-avoidance provisions.

The fourth proposal (partial income splitting) would involve the application of the individual basis to earned income but that -

"the joint investment income of a married couple should, for tax purposes, be treated as if it accrued in equal halves to each partner".

However, it is clear that such an arrangement would immediately benefit a non-income wife who would then be able to utilise her single personal allowance against her half of accrued investment income, so once again the suggestion is made that personal allowances for all persons

be available only against earned income, at least for taxpayers under 45 years of age.

The fifth system proposed (the unrestricted quotient system) would divide all the joint income, earned and unearned, between the spouses.

"with this system...one half of the total joint income (whether earned income or investment income) of the two partners is allotted to each partner who enjoys a single person's tax allowance and is subject to a single person's progressive tax schedule".

However, this system is said to have "very serious objections". It gives to every married couple two personal allowances - this is very expensive in revenue and

"it makes no allowance at all for the fact that by sharing household expenses a married couple can probably live more cheaply than two single adults".

The fact is, of course, that a married couple sharing household expenses cannot live more cheaply than two single adults sharing household expenses and, further, that two single adults sharing household expenses can live more cheaply than a married couple living in separate households. This logical fallacy has been discussed more fully in Chapter 7.¹ A more persuasive objection to complete income splitting is that it can blunt the incentives for a married woman to seek work:-

"If a man is earning more than enough to account for two personal tax allowances the splitting of his earnings between himself and his wife will exhaust the wife's personal allowance so that, if she goes out to work, she will be taxed on the whole of her earnings".

1. See page 321 ante.

This disincentive effect is discussed at page above - there is no disincentive for a married woman in such a case as she gets a full personal allowance but the husband does lose his additional allowance; on the other hand the wife's income then strengthens the family's finances.

The sixth proposal (the restrictive quotient system) suggests the aggregation of all the joint income against which only one single personal allowance is given with another allowance only against the wife's earnings : the remainder of the income is taxed on a progressive scale one and a half times as broad as that for a single person : although such a proposal would alleviate the disadvantages of aggregation for high income couples, it would still not produce equity for moderate income couples where the wife has her own investment income.

The final proposal (a partial quotient system) is to permit separate assessment for earnings but joint assessment with a quotient of 1.5 for investment income.

Apart, therefore, from recommending the removal of the married man's allowance where a wife has earnings the Meade Report reaches no conclusion as to the correct way of allocating allowances for a non-earning wife. However, underlying all of the alternatives proposed is the view that a full personal allowance for a non-earning wife would be "open to serious objections".

The Report appears to favour the replacement of the married man's allowance with a "home responsibility payment" but recognises the difficulty of defining the

circumstances in which this should be paid and concludes that some married relief should be retained. The Report is also clear that a wife should not be permitted to use a full single person's allowance against her unearned income and, to avoid this, goes as far as to suggest that all personal allowances should be available only against earned income, at least for taxpayers under 45 years of age.

9. 1977-79. The Campaign for Reform

It has been mentioned in Chapter 8 that, although the consultative document published by the Equal Opportunities Commission¹ mentioned a number of complaints which had been received, most concerned the principle of accountability. One complaint did concern allowances and that referred to the fact that it was in practice very difficult to persuade the tax office to give a wife the full benefit of allowances due -

"where the woman is employed and the man is not".

In this case

"the woman can set against her income not only the wife's earned income allowance but also the married man's allowance"

but "it is not always easy to ensure that the wife receives the full benefit of the husband's tax allowances".

Although, therefore, the subject of allowances had given rise to little complaint, the consultative document acknowledged that these would have to be considered

1. Income Tax and Sex Discrimination - December 1977.

if each spouse was to be treated as an individual. The document does not specifically recommend the abolition of the aggregation and accountability rules but this can be implied in some of the options for change discussed.

Before looking at the options proposed it is interesting to note that the simplest solution of all is not mentioned. It is not appreciated that if the aggregation rule were abolished every wife would become automatically entitled to a single person's allowance in her own right to use against any income earned, unearned or transferred.¹ The only reason why this cannot be done at the moment is that under the provisions of section 8 Taxes Act 1970 the personal allowances are only given to a "claimant" and because of section 37 a married woman cannot be a "claimant", unless she exercises the option for separate assessment under section 38 in which case the allowances are allocated as mentioned in that section. If section 37 were repealed all married women would become "claimants" in their own right; nil or low income claimants (most usually students or old persons) can utilise their personal allowances against transferred¹ income and this procedure would automatically become available to married women also.

The consultative document proceeds on the basis that the higher married man's allowance would be abolished and discusses three ways (the options for change) in which the resulting revenue yield would be distributed, namely, the individual basis, the quotient basis, and the cash payments basis.

1. The concept of transferred income is considered more fully in Part IV. See page 614 post.

(1) The individual basis

This first option anticipates that husband and wife would each have a single personal allowance for use against either earned or unearned income. But the withdrawal of the married man's allowance would mean that the majority of married couples (i.e. two-earner couples) would pay more tax. This saving could be utilised in one of three ways. First, by raising the single person's allowance; the disadvantage of this proposal is that it would benefit two-earner couples (especially high earner couples who would no longer lose allowances by opting for separate taxation of wife's earnings) and give no assistance for a wife at home. So the second suggestion would be to introduce a new tax allowance for a spouse with home responsibilities. But again the definition of "home responsibilities" creates the difficulties previously outlined by MacDonald and Meade¹ so the suggestion is made that this allowance might also be available to spouses over a certain age. But this second alternative would be of no assistance to a two-earner couple with dependant children so the third suggestion proposes a new additional allowance for two-earner couples with children in addition to their two single personal allowances.

These three alternatives to the individual basis illustrate the complexities which arise when a personal allowance is given not for being a person but for performing "home responsibilities"; immediately the phrase itself is difficult to define but then it becomes necessary

1. See page 483 above.

also to consider a two-earner couple with "home responsibilities".

The inapplicability of the requirement of "home responsibilities" is illustrated by the dilemma of the treatment of a wife with unearned income : if such a wife is permitted to use her single person's allowance against her unearned income without any home responsibilities then she is given an unfair advantage over a wife with no unearned income; on the other hand if she is not permitted to use her own allowance against her own unearned income if she has no home responsibilities she is immediately placed at a disadvantage compared with all other taxpayers who are not married women. The importation of a requirement of "home responsibilities" as a condition for a personal allowance for married women only, and not for any other taxpayer, is bound to produce inequitable results.

(2) The quotient basis

The second option proposed in the consultative document adopts the quotient basis for the personal allowances this gives each spouse a personal allowance to offset against either his own or his spouse's income. Although this solution solves the problem of the nil-income wife it does so at the expense of a system of joint accounting. However the proposal has much in common with the suggestions which will be considered in Part IV of this thesis. 1

1. See page 585 post.

(3) The cash payment basis

The advantages of the individual basis and the quotient basis can only be enjoyed when the spouses have sufficient income to support the allowances given : the third option therefore proposes that the revenue saved from the abolition of the married man's allowance should be paid in the form of a cash payment either as an increase in child benefit or as a home responsibility payment. But -

"The disadvantages of a cash payment to the partner at home is that, in most cases, it reduces a married man's take-home pay and transfers money to the wife...The political repercussions of having married men pay more tax, at a time when Government was trying to hold down wages, led to the modification in 1976 of the child benefit scheme".

So an alternative suggestion, which would minimise these political repercussions, is to:-

"combine a tax allowance to a married person who is the sole breadwinner with a cash payment...(thus) some of the cash made available by withdrawing the married man's allowance could go towards the poorest families who would benefit from a cash payment but not a tax allowance".

The response received to the consultative document¹ appears to indicate that of 78 persons and organisations expressing an opinion on the three options, 35 preferred the individual basis, 20 the quotient basis and 23 the cash payment basis.² On the other hand the document itself states that "there was a narrow majority in favour of cash benefits" although "this was an issue on which opinion was deeply divided" and "the evidence...is not conclusive and

1. "With all my worldly goods..."

2. Table 3 Appendix A.

this area...will require much detailed investigation".

The advantages of cash benefits were seen as the improved status of a person caring for dependants, the benefit to families without taxable income, and the fact that the benefit was enjoyed by the spouse with home responsibilities (whereas the benefit of a tax allowance is of course enjoyed by the spouse with the income).

Although there was no clear cut preference, therefore, for any of the options proposed, on one point a decisive view was expressed:-

"The response indicated very decisively that there was little or no support for retaining the married man's allowance on the present basis".

The method of dealing with the allowances under a reformed system was next discussed in the Green Paper on the Taxation of Husband and Wife.¹

10. 1980 - The Green Paper

Before looking at methods for the reform of the present system the Green Paper helpfully summarised the basis of the existing allowances. On the subject of the basis of the personal allowances generally it said that:-

"Their purpose is to recognise that, because of varying circumstances and family responsibilities, people whose incomes are the same may not be equally able to pay tax on them. They are not intended to reflect actual expenditure, as that can vary widely between households of the same size, but serve to graduate the personal tax burden broadly according to family circumstances".²

1. Cmnd 8053.

2. Paragraph 13.

The basis of the married man's allowance is discussed and it is appreciated that this raises the question as to whether the present differential of between 50 and 60 per cent is about right.¹ This is justified, however, on the grounds that although:-

"the married man's allowance is essentially an allowance for two people...it has always been less than twice the single allowance, since the expenses of two married people sharing one household are considered less than those of two single people sharing the same household".²

Now the logical fallacy of the 'household' test has been discussed in Chapter 7,³ but in any event this has never been used to explain the basis of the married man's allowance. Initially the allowance was introduced to equate a wife with a child and was later increased following the Colwyn Report with "regard to the ability to pay".

The Green Paper gives details of the gaps between the single and married allowances over the years since their introduction : the gap has ranged from 1:1.3 to 1:1.8 but recently stabilised at about 1:1.6. The Report recognises however that

"in recent years there have been suggestions that the married allowance for one-earner couples should be increased to the equivalent of the allowances given to two single persons".⁴

But the grounds for this proposal are not the recognition of a married woman as a person but the encouragement of a mother to stay at home with her children and that then raises

1. Paragraph 4a.

2. Paragraph 14.

3. See page 321 ante.

4. Paragraph 36.

the question of what treatment is appropriate for women without children who do not work. So -

"The obvious answer to those who want more encouragement for family life in its traditional form would be to award the equivalent of two single allowances to all one-earner couples. But this would be objectionable to those who maintain that only families where the non-working wife has specific home responsibilities should qualify for additional tax relief".¹

The basis of the wife's earnings allowance is discussed in this way:-²

"During the last war it was increased to the same level as the single allowance specifically to encourage married women to remain in employment in the public interest. It has remained at that level ever since partly because it has not been felt appropriate to remove the incentive for married women to work, and partly because it is administratively convenient for the wife's earned income allowance to be the same amount".

The main criticism of the wife's earned income allowance is noted to be:-

"As long ago as 1954 the Royal Commission on the Taxation of Profits and Income concluded that the present arrangements were over-generous to two-earner couples because they gave them greater relief than two single earners. Their proposed solution was to restrict the wife's earned income allowance but it is now commonly argued that it is the continued entitlement of the husband to a full married man's allowance, while his wife is enjoying the equivalent of a full single allowance, which creates the imbalance between two-earner couples and others."

The Green Paper discusses the future of the personal allowances for married couples and these can be

-
1. Paragraph 39.
 2. Paragraph 15.

considered within the context of its five different proposals for reform mentioned in Chapters 7 and 8.¹ The first two suggestions for reform (joint taxation and a rewording of the aggregation rule) make no mention of the future of the allowances. The third proposal is that of an option for independent taxation as an alternative to the existing system; if such an option were exercised a wife would obtain her own single person's allowance for use against her earned or unearned income and the husband would lose the married man's allowance; the disadvantages of this system are that it requires the exercise of an option by both spouses and whereas a wife with unearned income would gain from its exercise her husband would lose and may not therefore be inclined to join in the election; further, such an option is of no assistance at all to low or nil income wives. The fourth proposal (for independent taxation with equal split of allowances) is similar to the present option for separate assessment but with all the allowances split equally and not in proportion to income. Again, this is put forward as an option, albeit exerciseable by either spouse, as it would not assist all taxpayers : in particular it would not assist a nil - or low-earning wife to obtain a personal allowance of her own; although it would give her a proportion of her husband's married man's allowance this would be of no value if she had insufficient income against which it could be set; and even where she did have sufficient income her husband might not be pleased to lose a part of his personal allowance in this way.

1. See pages 411 and 415 ante.

The fifth proposal for reform in the Green Paper is for mandatory independent taxation. Here:-

"Proponents of a system of independent taxation must face the question of providing for the case where one spouse has little or no income so that he or she cannot use, or fully use, the single allowance".

The solution proposed in the Green Paper is not to give a supported spouse an allowance in her own right to use against income transferred to her but to provide a machinery for the supported spouse to transfer her or his allowance to her husband or wife. This is another way of proposing the extension of the concept of the existing married man's allowance in those cases where the wife or husband has little or no income, as is clear from the reasoning underlying the proposal, namely:-

"There is clearly a strong case for such a provision (i.e. an allowance higher than the single allowance) on grounds of equity. In the present system the married allowance recognises the special legal and moral obligations on a husband to support his wife. In recent years the tendency has been for these obligations to become reciprocal. All this suggests that with the abolition of the married allowance, some allowance in excess of the single allowance is needed in recognition of the support the one spouse gives to the other out of his or her own income...In so far as the need to support the dependant spouse reduces taxable capacity, then tax relief should be increased to take account of it".

Although the Green Paper appears to accept the principle of a married couple's entitlement to two single allowances this could only be achieved if the allowance of the supported spouse was fully transferable. A fully transferable allowance would, of course, bring advantages

to the husband of a wife at home as instead of the present married man's allowance of 1.6 of a single allowance he would receive two single allowances but the Green Paper appears to think that this would then operate as a disincentive to wives to enter paid employment. The disincentive argument is discussed at page 479 above - such a system is no disincentive to wives who lose nothing by taking up employment although their husbands do. A stronger objection to a fully transferable allowance is the fact that it means that privacy cannot be maintained as the transferee spouse requires details of the transferor spouse's income and the present objections of wives to disclosing small amounts of income on savings to husbands will not be met.¹

To meet these difficulties a partially transferable allowance is suggested; although no fixed limit is suggested for the part of the supported spouse's allowance which can be transferred, it is thought that such a limit could be flexible and varied

"according to the view taken of the reduction in taxable capacity arising from the need to support two married persons on one income".

The arguments in favour of a partially transferable allowance are that it would reduce the disincentive to married women to work² and would mean less invasion of privacy so that a married woman with a small unearned income would not be required to declare this to her husband if it fell within the non-transferable part of her allowance. The

1. See Chapter 8 above.

2. The 'disincentive' argument is discussed at page 479 above.

Green Paper discusses the question previously raised by MacDonald, Meade, and the Tax Credit Green Paper, namely as to whether the transferable allowance (either full or partial) should be conditional on the transferring spouse carrying out "home responsibilities" :-

"It could be argued that the circumstances where one partner has no family responsibilities but does not work should not be reflected in the tax bill of the partner with the income and that there should be no allowance unless the non-working spouse had specific home responsibilities".¹

But once again there are problems of definition and -

"one would be likely to find that on the merits few cases would fall into the restricted (i.e. no home responsibilities) category".

So the conclusion is reached that

"On fiscal grounds, the case for an unrestricted allowance is strong. Likewise administrative considerations would point this way since restrictions would inevitably introduce complexity. And, if on the merits the majority of supported spouses would fall outside the restriction it seems doubtful whether, even on social grounds, there is a good case for it".

Finally, the Green Paper discusses the alternative of a cash payment to a supported spouse, to take the place of the tax allowance to the supporting spouse; this proposal was originally raised in the Meade Report² and developed as Option 3 in the Consultative Document issued by the

1. Paragraph 76.

2. See page 483 above.

Equal Opportunities Commission in December 1977.¹ The two advantages mentioned in the latter document are repeated in the Green Paper, namely that the money goes directly to the person undertaking the home responsibilities and such benefits are available to families below the level of the tax threshold. But once again the political difficulties mentioned by the Equal Opportunities Commission are noted namely that:-

"with the abolition of the married allowance married men might be even more inclined to regard themselves as "losers".¹

The Green Paper concludes that the arguments against cash payments are "very weighty" :-

"and it follows from this that, if the married man's tax allowance is to be abolished, there is a very strong case for replacing it with a transferable tax allowance along the lines examined ...above".

11. Conclusions

A review of the allowances available to a married couple shows that they consist of a patchwork of anomalies resulting from the continuation of the historical fiction that a married woman is not a person in her own right. The first anomaly (that of the additional exemption for wife's earnings enacted in 1894) had its roots in the injustice caused by the aggregation rule but its limitation to the case where the wife had earnings created an imbalance between those cases where a wife had no earnings or had

1. See page 491 above. Paragraph 84.

investment income. This was corrected by the "wife allowance" in 1918 which was again introduced to remedy the injustice of the aggregation rule but which immediately created the anomaly that some two-earner couples had better tax treatment than two single persons. This imbalance was corrected by the Colwyn Commission which restored the total allowances available to a married couple to the equivalent of two single allowances but, by restricting the amount available against a wife's earnings, immediately created another imbalance namely between the earnings of a married woman on the one hand and the earnings of a single woman on the other. This was corrected in 1942 when all women who had earnings were treated in the same way but as no adjustment was made to the married man's allowance the old anomaly of the better treatment of two-earner married couple was revived. (Throughout this time, it will be borne in mind, that all the allowances, including those for wives' earnings, were given to the husband).

Although both Colwyn and Radcliffe saw the source of the anomalous treatment of married couples' allowances as the special allowance for wives' earnings recent opinion sees it in the retention of the married man's allowance and there appears to be some support for its abolition accompanied by a number of proposals for a new treatment for a nil- or low-earning wife : these fall into three broad categories, namely an additional allowance for the supporting spouse, or a cash payment to the supported spouse, or some system of sharing allowances between the spouses. However, it does not appear to be generally appreciated that

if the aggregation rule were to be abolished each married woman would become a taxpayer in her own right and so entitled to use her personal allowance against transferred income.¹

The history of the allowances points to the inevitable conclusion that it is not possible to preserve equity between couples and equity between individuals unless each spouse is treated as an individual taxpayer in all respects but here it may be noted that this would necessarily involve the abolition of the married man's allowance and there appears to be considerable "political difficulties" involved in such a step as, in 1982-83, such a reform would mean that a married man paying tax at the standard rate would have his take home pay reduced by £5.07 per week. And it is thought that it is this simple fact which is now delaying the complete reform of the taxation of husband and wife.

1. See further discussion in Chapter 16 page 614 post.

PART III - INTERNATIONAL COMPARISONS

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Chapter 11 - The Common Law Jurisdictions

Chapter 12 - The Civil Law Jurisdictions

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PART III - INTERNATIONAL COMPARISONS

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CHAPTER 10

A COMPARISON OF MATRIMONIAL PROPERTY LAWS

Part III of this thesis examines the way in which the family is taxed in a number of overseas jurisdictions. There are at least two¹ most helpful modern studies which contain a factual analysis of the tax treatment of the family unit in specified foreign countries but these studies are of the contemporary position only and they do not shed any light on the reasons why different countries have established different systems for dealing with the same social phenomena.

It is true that the actual tax paid by a family unit will not depend solely on the system under which it is assessed but will depend upon a combination of rates allowances and credits : in other words the mere presence or absence of an aggregation rule is not conclusive in

1. See "The treatment of family units in OECD member countries under tax and transfer systems" OECD Paris 1977 and Background Paper 4 to the Green Paper on Taxation of Husband and Wife - International Comparisons 1981.

determining whether a particular system is or is not advantageous to the family as the negative effects of aggregation can be neutralised by favourable rate schedules (the quotient system) or by favourable allowances or credits. However, the objective of this thesis is to determine a method of taxing the family unit in the United Kingdom and it is thought that this must commence by ascertaining the correct structure of the tax before imposing on that structure a system of rates and allowances; accordingly, this examination of the tax systems in overseas jurisdictions will concentrate on the structure of the tax although a reference will be made in each case to the method of dealing with the allowances.

It is hoped that the preceding Chapters of this thesis have demonstrated that the tax treatment of the family unit in the United Kingdom is closely bound up with the development of the law concerning the proprietary rights and the contractual capacity of married women and that many of the unsatisfactory aspects of the present tax laws arise from the fact that they have failed to keep pace with developments in property law and in the law of contractual capacity. This consideration of the tax treatment of the family unit in foreign jurisdictions will, therefore, be undertaken against a background of the development of the laws of property and contractual capacity as they affect married women.

Before undertaking these comparisons, however, it may be helpful to summarise very briefly the ancient legal sources which have led to the development of these systems as they exist today. Unfortunately, this must be a very

abbreviated summary of a fascinating area of law as -

"A first glance at the province of law which English lawyers know as that of Husband and Wife...will, if we do not confine our view within the limits of our own system, amaze and bewilder us".¹

and -

"The status of the married woman is one of the most difficult of all the problems of private law and to it legal systems have given, and still give, the most diverse answers...It is obvious that the answer will be coloured by prevailing views as to the constitution of the family ...It is not surprising that to a problem so delicate, so many sided, and complicated by so many varying ideas, new and old, as to the nature of the family and the conception of marriage, there should have been many different answers".²

From these "many different answers" three major strands have predominated; first, the supremacy of the husband; second a system of joint, or community, property; and finally the individual system. As Maine has said, the history of developing societies shows a move from status to contract³ and this is illustrated by the treatment of married women where the more primitive systems of supremacy of husband and community of property have given way to the treatment of a woman as an individual. A similar development took place in Roman law.

Originally, in Roman law⁴ marriage was a patriarchal system and a wife stood in manu mariti when

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1. Pollock and Maitland : A History of English Law : 2nd Edition 1898 Vol.II p. 399.
 2. W.S. Holdsworth : A History of English Law : Vol.II p. 387.
 3. Sir Henry Maine; Ancient Law.
 4. Schulz: Principles of Roman Law.

"she was incapable of having any property of her own; all property which she possessed during marriage, and that which she acquired later, was automatically acquired by her husband".

However, in the second century BC leading Roman society refused to conclude marriages with manu and

"the humanistic aim of putting husband and wife on a par was radically carried through. Wife and husband alike remained the owners of their respective property... in short, it is the system of separation of goods, which is, since 1882, the English system".¹

The Roman lawyers at no time adopted a system of community of property -

"The keen individualism of the Roman lawyers had no sympathy with matrimonial community of any kind".

The development of Roman Law from a patriarchal to an individual system has been assessed in this way:-

"The classical law of marriage is an imposing, perhaps the most imposing achievement of the Roman legal genius. For the first time in the history of civilisation there appeared a purely humanistic law of marriage, ... as being ...of two equal partners".¹

Unfortunately, Roman Law was abandoned in Western Europe in the Middle Ages and it took the law of England nearly two millennia to arrive at the same stage of development; the fact that such development has not yet been finally completed is the reason for this thesis.

However, if we return to the Middle Ages -

1. Schulz; Classical Roman Law.

"we see a perplexed variety of customs (concerning husband and wife) for which it is very difficult to account...For the most part we shall be able to trace them back to ancient Germanic usages since the Roman Law of husband and wife has kept itself aloof and refused to mix with alien customs. However, the number of schemes of marital property law seems almost infinite..."¹

From this "infinite number" two schemes soon dominate. In the Middle Ages -

"the idea of a community of goods between husband and wife springs up in many parts of Europe from Ireland to Portugal"

but -

"our own law at an early time took a decisive step - it rejected the idea of community".

Two reasons are given for this preference by the English legal system of the doctrine of the supremacy of the husband. First, about the year 1200 all jurisdiction over movables passed to the church and

"the canonists' conception of marriage as a sacrament...makes the husband and wife one flesh and gives the husband dominion over the wife".

Secondly, the system of community of goods was a custom of the lower orders and the merchants; in France this custom spread upwards to the nobility but in England the reverse occurred; in England -

"The common law made the law of the nobles the law of all : community was the law of merchants not nobles. This lived on in some borough customs which treated the woman who carried on a trade apart from her husband as, in some aspects, independent but otherwise the system of community is abandoned".²

1. Pollock and Maitland.

2. Holdsworth.

So, taking a broad view of the systems in Western Europe two main régimes dominate namely régimes which recognise a system of community of ownership between husband and wife and those which do not. It will not come as a surprise to find that the income tax treatment of husband and wife also differs in a similar way.

Chapter 11 will consider developments in some common law jurisdictions where there is no community of property and Chapter 12 will consider developments in the civil law jurisdictions where community of property still exists.

CHAPTER 11 - THE COMMON LAW JURISDICTIONS

Section 1. Introductory.

Section 2. Australia.

- (1) Constitutional development
- (2) Matrimonial property
- (3) 1901 Constitution
- (4) 1915 Income Tax Act
- (5) Tax avoidance
- (6) Capital taxes
- (7) Children

Section 3. New Zealand.

- (1) Constitutional development
- (2) Matrimonial property
- (3) The first Income Tax Act - 1891
- (4) Tax avoidance
- (5) Capital taxes
- (6) Children

Section 4. Canada.

- (1) Constitutional development
- (2) Matrimonial property
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- (1) Constitutional development
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Section 6. Conclusions

CHAPTER 11

THE COMMON LAW JURISDICTIONS

Section

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1. Introductory

A study of the common law jurisdictions is most illuminating : each imported English common law but each has developed along a separate path to the state where each now treats husband and wife as separate individuals for income tax purposes. The position at common law in 1765 can be summarised in the words of Blackstone¹ :-

"By marriage the husband and wife are one person in law. That is, the very being or legal existence of the woman is suspended during marriage or at least is incorporated or consolidated into that of the husband, under whose wing, protection or cover she performs everything, and is therefore called in our law - french a feme-covert...and her condition during her marriage is called her coverture. Upon this principle of union of person in husband and wife depend almost all the legal rights duties and disabilities that either of them acquire by the marriage".

1. Commentaries on the Laws of England 1765. William Blackstone, Book 1, page 430.

Among these disabilities are the fact that all the wife's personal property vests absolutely in the husband on marriage and in real estate he gains title to the rents and profits during coverture. Also -

"During the marriage the husband is, in effect, liable to the whole extent of his property for debts incurred...by his wife ...(and)...During the marriage the wife cannot contract on her own behalf".¹

This, then, is the basis of the law exported to Australia, Canada, New Zealand and the Republic of Ireland. It is most interesting to see how each country developed it in a different way.

2. Australia

- (1) Constitutional development
- (2) Matrimonial property
- (3) 1901 Constitution
- (4) 1915 Income Tax Act
- (5) Tax avoidance
- (6) Capital Taxes
- (7) Children

(1) Constitutional development

The first Australian state to be settled was New South Wales in 1788,² the others being settled later.

Although it was generally assumed that the law of England applied, this was specifically enacted in 1828 in this way³:-

"All laws in force within the realm of England on July 25th 1828 should be applied in the administration of justice in the courts of New South Wales and Van Diemen's land respectively".

1. Pollock & Maitland p. 405.

2. The British Commonwealth : General Editor G.W. Paton.

3. 9 Geo 4 C. 83 section 24. Statutes at Large, Volume 68, page 569.

Each state was, however, an independent sovereignty subject only to the overriding powers of the Imperial Parliament and to the doctrine that there was no power to pass laws which were repugnant to the laws of England. The fact that there are six independent states makes it difficult to generalise about Australian law : in spite of a desire that the statute law of each state should be as uniform with that of England as local policy allows, there has been little deliberate attempt to keep statutes uniform as between different states and even in following English law there is sometimes a considerable time lag.

(2) Matrimonial property

These discrepancies are very well illustrated by the law of real property and, in particular, by the Married Womens' Property legislation; there is no federal Australian real property law - each of the six states has passed its own legislation. Nevertheless, starting from the same basis of English common law, each state has passed similar legislation to the English statutes and it is not therefore surprising that there are many similarities. So, following the English Married Womens' Property Act of 1882 the states enacted similar legislation in: 1890 (Queensland), 1892 (Western Australia), 1884 (Tasmania), 1893 (New South Wales), and (1898) Southern Australia. The lack of complete uniformity is however illustrated by the fact that the restraint on anticipation, which was abolished in England in 1949, is still in force in New South Wales.

(3) 1901 Constitution

The Commonwealth of Australia was established in 1901 by the Commonwealth of Australia Constitutions Act and by that time, of course, the principle of separate property was well established in all the states. In the Commonwealth Act the legislative powers of the Commonwealth were specifically enumerated, the remainder being left with the individual states. So whereas real property law was left to the individual states, section 81(2) of the Constitution Act gave the Commonwealth power to make laws with respect to taxation¹ and, as a practical matter, the Commonwealth has acquired exclusive powers to impose income taxes and duties of customs and excise leaving other taxes (stamp duties, death duties, gift taxes) to be levied by the individual states.

(4) 1915 - Income Tax Act

Although income tax had been levied by the states some years previously the first Commonwealth Income Tax Act was passed in 1915 and from the very beginning husband and wife have been treated as two completely independent persons for income tax purposes with the result that they are separately assessed to tax on their respective incomes. This principle was reviewed as recently as 1975 by the Taxation Review Committee (The Asprey Committee) in its Report published on 31st February 1975 page 134 as follows:-

1. Australian Federal Constitutional Law : Howard :
2nd Edition.

"The adoption of a compulsory family unit basis must be rejected on grounds of general social principle. The right to be taxed as an individual has always been accorded in Australia".

As far as the allowances are concerned there are no personal allowances as such but a rebate is available to any person who contributes towards the maintenance of a spouse, daughter, housekeeper, or parent.¹

(5) Tax avoidance

It may be thought that, with a system of completely separate taxation, some tax avoidance provisions would have been introduced in order to prevent income-splitting. Although, as we shall see, quite detailed rules have been enacted about children's income and tax avoidance, there are no general tax avoidance prohibitions concerning transfers between husband and wife. In general, alienation of income is permitted under rules corresponding to the covenant provisions familiar in the United Kingdom.

The Australian tax legislation does contain a rather wide tax avoidance section² which reads:-

"Every contract, agreement, or arrangement entered into, orally or in writing, ... shall so far as it has or purports to have the purpose or effect of, in any way directly or indirectly

- (a) altering the incidence of any income tax.
- (b) relieving any person from liability to pay any income tax or make any return.
- (c) defeating, evading or avoiding any duty or liability imposed on any person by this Act or

1. Australian Income Tax Guide 1981. E.F. Mannix & J.E. Mannix.

2. Section 260 Uniform Income Tax Assessment Act 1936.

(d) preventing the operation of this Act
in any respect

be absolutely void".

At first sight it might appear that such wide provisions would nullify any property or income transfers between spouses designed to effect income-splitting for tax saving and, although a number of cases¹ have reinforced the application of the Section in a wide variety of cases, nevertheless in one case the taxpayer was successful in challenging the application of the Section and that case concerned transfers to a spouse and child.

In DFLT v. Purcell² the taxpayer owned certain grazing property and declared himself a trustee of it for himself, his wife and his daughter, reserving to himself wide and unusual powers of management control and investment. He was assessed to income tax on all the income but objected on the ground that the income was received by him as trustee for himself, his wife and his daughter in equal shares. The court held that the appellant had intended that his wife and daughter should become the beneficial owners of two-thirds of the property and although in forming this intention, he was influenced to some extent by a desire to lessen the burden of taxation the predecessor of section 260 was inapplicable. The court said:-

"It would be unreasonable to construe the section so as to include a genuine gift which had the incidental effect of diminishing the donor's assets and income... If a person actually disposed of income-producing property to another so as to

1. See Manual of The Law of Income Tax in Australia :
Ryan p. 261.

2. (1921) 29 CLR 464.

reduce the burden of taxation the Act contemplates that the new owner should pay the tax".

(6) Capital taxes

It has been noted that whereas under statute the Commonwealth has exclusive power to impose duties of customs and excise and, as a practical matter, the Commonwealth has acquired exclusive power to impose income tax, the individual states have retained the power to impose other taxes, including stamp duties, and death, estate and gift duties.¹ There is also Commonwealth estate duty enacted in the Estate Duty Assessment Act 1914-1967. The only provisions which specifically affect spouses are those found in section 18A which gives a number of statutory exemptions : estates left to a widow, children or grandchildren are exempt up to 20,000 dollars but the exemption reduces for higher estates and is nil at 100,000 dollars; estates left to other persons are exempt up to 10,000 dollars.

There is also a gift duty levied under the Gift Duty Assessment Act 1941-67. Again, there are very few special provisions for spouses but section 14 gives exemption for premiums within a stated limit on a policy for the benefit of a wife and children and also reasonable gifts for the maintenance, education or apprenticeship of any person.

(7) Children

Both the property laws and the tax laws

1. Australian Federal Constitutional Law: Howard: 2nd Ed.

concerning children are in an advanced state in Australia. The general rule is that an infant may hold a proprietary interest of any kind but may disclaim it during infancy or within a reasonable time of coming of age; any contract is therefore voidable.¹ However, statutory rules in all states have provided machinery whereby an interest in land held by an infant may be transferred without the threat of later disclaimer by the infant. For example, section 22 of the Minors (Property and Contracts) Act 1970 of New South Wales provides that if a minor makes a disposition of property pursuant to a contractual duty binding on him the disposition will itself be presumptively binding.²

This acknowledgement of a child as a separate person continues into the tax field. There are no tax allowances (rebates) for dependant children, although there are cash benefits. However, a unique feature of the Australian system is the discriminatory tax treatment of children's income.³ This was introduced in 1979 by the Income Tax Law Amendment Act (Act No. 19) of 1980; the effect is to tax the income of children at a rate higher than that of adults. The reason for the introduction of this legislation is said to be:-

"Tax rate progressivity had led to the creation of many devices and plans for making income in high-income families taxable to family members other than the head of the family - income-splitting".

Accordingly, although the adult rate of tax provides

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1. David C. Jackson : Principle of Property Law p.211.
 2. The law of minors in relation to contracts and property. David J. Harland.
 3. Taxation of Children's Income in Australia : Bernard Marks.

for a nil rate band (4041 dollars), a band taxed at the rate of 32 per cent (up to 17,239 dollars), a further band taxed at 46 per cent (up to 34,479), and the remainder taxed at 60 per cent, unmarried children below the age of 18 pay 46 per cent on income in the band 1040-34,479 and 60 per cent thereafter. Income from employment and income of married infants is excluded.

This represents a novel way of counteracting tax avoidance: rather than providing that transfers shall be deemed to be ineffective, which is the United Kingdom approach, the transfer itself is recognised but a heavier rate of tax is levied; on the other hand the Australian system cannot be selective - all the income of a child, transferred or not, is taxed at the higher rate.

However, where infants are entitled to Trust income, the position is somewhat different : usually the Trust is not assessed to tax, but the beneficiary entitled is; if there is no beneficiary the Trust estate is liable at the rate of 60 per cent.

3. New Zealand

- (1) Constitutional development
- (2) Matrimonial property
- (3) First Income Tax Act
- (4) Tax avoidance
- (5) Capital taxes
- (6) Children

(1) Constitutional development

In 1769 Captain Cook took possession of New Zealand in the name of George III; although New South Wales subsequently tried to annex the territory, British

sovereignty was declared in 1840.¹ The Imperial statute was enacted in 1852² to "grant a Representative Constitution to the Colony of New Zealand". When British Sovereignty was claimed New Zealand became subject to the laws of England but in 1858 the New Zealand Parliament removed any doubts by providing, in the English Laws Act, "that the laws of England, so far as they were applicable to the circumstances of the Colony should be deemed to have been in force in the Colony since January 14th 1840".

(2) Matrimonial property

As New Zealand therefore absorbed the common law of England, the property law of New Zealand is based on, and is in the main the same as, English law. However,

"although New Zealand was well to the fore-front in the movement to give women enhanced political and social status, being the second country in the world to grant them the franchise, the legislature of the country displayed no similar initiative in removing the many disabilities which married women suffered at common law, but merely contented itself with adopting the various measures of law reform which have from time to time been instituted in England on this subject".

So the legislation which was passed in 1882 in England was enacted in 1884 in New Zealand and the English 1935 legislation was enacted in New Zealand in 1936.

(3) The First Income Tax Act 1891

Although an ad valorem property tax was introduced in 1879, this was abolished by the Land and Income Assessment Act of 1891 which substituted a land tax and a progressive income tax. The statutory provisions

1. The British Commonwealth: The development of its laws and constitutions. 4. New Zealand. J.L. Robson. 2nd Ed.

2. 15 and 16 Vict. c 72.

are now found in the consolidated Income Tax Act of 1976. Husband and wife have always been treated as separate individuals for income tax purposes. The New Zealand tax system used to allow each taxpayer a personal rebate but this was abolished on 1st April 1979. (The rebate is a deduction from the actual tax assessed and can be distinguished from an allowance which is a deduction from assessable income). However, a dependent spouse rebate has been retained and, in practice (although not in law) this is allowed for a de facto spouse.¹ The rebate is a maximum of 156 dollars reduced by 20 cents for each dollar by which the spouse's income exceeds 520 dollars; thus where the spouse's income exceeds 1,300 dollars there is no rebate available.² This arrangement is a variant of the partially transferable allowance proposed by the Green Paper.

(4) Tax avoidance

Section 99 Income Tax Act 1976 is a very wide tax avoidance section on lines very similar to the Australian section 206 but among transfers not intended to be caught by the section are those where the purpose is a genuine transfer and not merely tax avoidance. The ambit of the section has given rise to much comment in the legal journals³ but the better view appears to be that the section does not avoid normal transfers between spouses; the

1. Sections 51 and 52 Income Tax Act 1956.

2. New Zealand Income Tax Law and Practice : Simcock & Rooke, Vol. 1 Para. 26.020.

3. Article by Wilfrid J. Sim Q.C. N.Z. Law Journal 1967 p. 396 entitled "Land and Income Tax Act 1954 - Family and Commercial Arrangements".

following dicta from the Australian case of DFLT v. Purcell¹ are also applied to section 99 -

"Its office is to avoid contracts etc. which place the incidence of tax or the burden of tax upon some person or body other than the person or body contemplated in the Act. If a person actually disposed of income-producing property to another, so as to reduce the burden of taxation, the Act contemplates that the new owner should pay the tax. The incidence of the tax and the burden of the tax fall precisely as the Act intends, namely upon the new owner".

So any transfers of assets between spouses, and any alienation of the right to receive income, do not appear to be ineffective for income-splitting purposes, so long as they are bona fide genuine transfers.

New Zealand law does contain a special provision in section 106(1)(d) which prohibits the deduction of any expenditure represented by payments of any kind by one spouse to another unless the Commissioners are satisfied that the payment is bona fide or for services rendered (not being domestic services).²

(5) Capital taxes

An estate duty and a gift duty were both introduced in New Zealand in 1909, in the Death Duties Act 1909.³ The provisions were similar to the United Kingdom legislation, giving originally a surviving spouse relief up to 60,000 dollars. However, the Estate and Gift Duties Amendment Act 1979 withdrew the relief available in

1. See page 515 above.

2. Simcock & Rooke, Vol. 2, para. 40-560.

3. Richardson & Congreve 5th Edition.

respect of succession by a spouse for deaths after 21st April 1979. This was explained by the fact that, with the lifting of the general minimum level for payment of estate duty, there was no longer any need for a specific surviving spouse relief. However, there are special reliefs available for a "Joint Family Home".¹ For these provisions to apply a house must be registered as a "Joint Family Home" by both husband and wife : irrespective of the proportions of contribution, each is deemed to have an equal beneficial interest. When the first spouse dies, his share passes to the survivor free of estate and gift duty.

The settlement of a joint family home is not a gift for the purposes of the gift tax : in addition there are exemptions from the gift tax for small gifts and gifts for the maintenance and education of a family.

(6) Children

Although the personal rebate was abolished in 1979² three rebates concerning children were retained. First, a child taxpayer rebate of 78 dollars is available for a child below 15 who has a small income of either earned or unearned income (section 50A); next, a young family rebate of 468 dollars is available where the claimant has a child under 5 and where the claimant's income is less than 13,700 dollars; there is a sliding scale which reduces the rebate where the claimant has income in excess of this figure so that no rebate is available where his income

1. See Joint Family Homes Act 1964 as amended.

2. See page 520 above.

exceeds 17,600 dollars. Only one rebate is available for each family, irrespective of the number of children, but a sole parent may be a claimant. Finally, there is a low income family rebate of 468 dollars, where a claimant has a child of any age so long as the claimant's income does not exceed 13,700 dollars; again, only one such rebate can be claimed for each family.

There used to be an infant child relief for estate duty purposes which exempted transfers of up to 1,000 dollars but this was withdrawn in 1979 : the duty excludes all small gifts and also gifts made for the maintenance and education of the family.

4. Canada

- (1) Constitutional development
- (2) Matrimonial property
- (3) First Income Tax Act
- (4) Tax avoidance
- (5) Capital taxes
- (6) Children

(1) Constitutional development

Just as it is not possible to consider an 'Australian' law without reference to the separate states, so no consideration of Canadian law can ignore the fact that Canada is also a confederation of Provinces and in Canada particular regard must be paid to the special position of the province of Quebec; the other provinces inherited a common law jurisprudence whereas Quebec inherited a jurisprudence derived from the civil code. The close proximity of the province of Quebec in Canadian jurisprudence makes Canada a most interesting study for

the purposes of this thesis as the interaction of the two legal systems has had interesting repercussions on the discussion surrounding the tax treatment of the family unit.

As far as real property is concerned, it is perhaps surprising that the law in Quebec and that in the common law provinces developed separately but it appears to be accepted that:-

"there has been very little mutual interaction or interchange over the years, in spite of the obvious opportunities for cross-fertilization between the Quebec civil law and the jurisprudence of the common law provinces".¹

Prior to the Canadian Constitution Act of 1982 the Canadian constitution was a statute of the United Kingdom Parliament, namely the British North America Act 1867. The common law of the English speaking provinces was, in its historical roots, "received" English common law brought over (according to the conventional legal fiction) to North America by the first English settlers to the extent that its substantive provisions were applicable to conditions in the new colonies.²

(2) Matrimonial property

Although, therefore, the English speaking provinces of Canada adopted the English common law of husband and wife, they also subsequently adopted some of the statutory amendments to the law of real property made by

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1. Canadian Jurisprudence : The civil law and common law in Canada : edited by Edward McWhinney.
 2. Per Griffiths, C.J. in R.V. Kidman (1915) 20 CLR 432, 435.

the English Parliament. Such adoption has, however, not been comprehensive and, for example, the 1925 property legislation has not yet been enacted in Canada. However, statute has modernised the rights of married women and generally speaking the capacity of a married woman to acquire, hold and dispose of land has, by statute, been equated to that of a feme sole.¹ On the other hand the influence of the civil code can perhaps explain the enactment in the common law provinces of special "homestead" provisions which are unknown in English common law. Although there are different rules in force in the different provinces the basic principle is that neither spouse can dispose of the "homestead" without the other's consent and such a disposition without consent gives rise to a remedy in damages.

In Quebec the law of property follows the French code of 'community property'; all property owned before marriage by either spouse is the separate property of that spouse and property acquired after marriage by gift or inheritance is separate property. All other property is owned jointly by the spouses who must both consent to any transfer. On divorce, each spouse is entitled to his separate property but the community property is divided equally. The husband is designated the "manager of the community" for administrative purposes.

In a recent comprehensive survey of the law of real property in New Brunswick the authors of the Report²

1. Law of Vendor and Purchaser : Di Castri. Second Edition. And see section 233 Married Women's Property Act RSBC 1960 and section 262 RSO 1970.

2. By Alan M. Sinclair and Douglas C. Rouse Q.C.

compared the régime of separate property inherited from English common law and statute with the community property régime applied in the province of Quebec; the problems of community property (identifying the assets, disputes between spouses, rights of creditors etc), were fully discussed but the authors concluded that:-

"the adoption of community of property, in the context of a jurisdiction that has always had a separation of property, would be a radical alteration of existing customs, practices and traditions involving the necessity of new complex rules being learned and employed in daily affairs, not only by married couples but also by those dealing with them".

(3) The income tax régime

Before confederation in 1867 80 per cent of revenues arose from customs and excise. The first personal income tax was imposed in British Columbia in 1876 and the first federal income tax was imposed in 1917; the provinces have now abandoned the rights to levy income and inheritance taxes to the federation.¹

In Canadian Federal Income Tax the individual has always been the taxpaying unit but whereas this causes no difficulty under an English system of separate property difficulties can arise when the principle is applied to a community property system. The question as to whether married persons domiciled in Quebec, who had not excluded the provisions of the civil code governing community property, could split their matrimonial income for income

1. Tax rental agreements 1941-62. See also Constitutional Law of Canada : Hogg.

tax purposes¹ was considered in the case of Sura². On appeal the court held that, for income tax purposes, the property was to be treated as that of the husband.

It may have been difficulties such as these which led a Royal Commission on Taxation in 1966 to suggest that a more appropriate base for taxation might be the family. The main argument in favour of such a change was that "an individual's well-being is more closely indicated by the income of the family to which he belongs than by his own income. Family income is in some sense "shared" among individuals of a family and is partly used for expenditures which are jointly consumed by all members, e.g. housing, furniture, auto etc. The latter is sometimes referred to as "the economies of living together".³ The Royal Commission suggested that the treatment of single individual versus family should accord with the following principles of equity -

- Two persons earning a given amount of income should pay less total tax if living singly than if living as a family;
- The tax paid by two persons living together should be independent of the proportion in which the income is earned by the two (or more).
- An individual earning a given income should pay more tax than a family of two or more members earning the same income.

These concepts will by now be familiar to the readers of this thesis and they are fully discussed in

1. As is done in France - See Chapter 11.

2. 62 DTL 1005 [1962] CTC 1.

3. Canadian Tax Policy : Robin W. Broadway and Harry M. Kitchener.

Chapter 7. The Royal Commission concluded that the family should be adopted as the taxpaying unit with a separate rate schedule from individuals: this would mean the introduction of a type of the quotient system familiar in civil code countries.¹ Perhaps it is not surprising that the recommendation met with considerable controversy and disfavour.

Difficulties of defining the family unit, the dissolving of family units and the "incentive to live common law" in order to avoid high marginal tax rates were only a few of the criticisms levied against this proposal. The recommendation has, so far, not been enacted and the difficulty of finding a tax unit which will reconcile both the common law and civil law concepts of ownership in marriage can be summarised in these words:-

"The essential choice of a taxpaying unit involves more than pure economical analysis; it is entwined in the socio-economic objectives of any society".

Personal allowances have been part of the Canadian income tax structure since its inception in 1917 : for very many years the married allowance was exactly double the single allowance but since 1972 it has been slightly less than double. The married allowance is only given to a husband whose wife's income does not exceed the amount of the single personal allowance. This is, in effect, the system of the fully transferable allowance discussed in the Green Paper. In Canada, if a husband wishes to claim his wife's unused allowance the spouses file a joint return.

1. See Chapter 11. See also "The Individual and Tax Reform in Canada": Gordon Bale. 1971 Canadian Bar Review p.24.

(4) Tax avoidance

The Canadian income tax legislation contains general anti-avoidance provisions of wide application and there are special rules (the attribution rules) dealing with tax avoidance by transfers between spouses. The latter rules were enacted in order to prevent tax minimisation through the device of income-splitting arrangements and this is achieved by attributing income to persons who do not in fact receive it.¹ Section 74 of the Income Tax Act, originally enacted in 1917 at the commencement of income tax, provides that the income of any property transferred by a spouse to a spouse, and any income earned from any property substituted therefor, is the income of the transferring spouse for so long as the marriage continues. There are, however, a number of transactions not covered by these rules; for example, a "transfer" includes a sale for value but not a loan.² Again, income derived from investments purchased on joint credit is not within section 74. Finally, since 1971, the attribution rules include in the income of the transferring spouse any capital gain or loss arising on the transfer.³

(5) Capital taxes

There are three capital taxes in Canada - a gifts tax, a capital gains tax and an estates tax. The gifts tax is part of the income tax code and was introduced in 1968;⁴

1. Canadian Income Tax Revised - Butterworths.

2. McLaughlin v. MMR 1952 Ex CR 225.

3. See also: Income Splitting: The Labyrinth of Attribution: Robert L. Katz CA : Arthur Andersen & Co Vancouver: British Columbia Tax Conference 1980.

4. An Act to amend the Income Tax Act and the Estate Act, SC.1967-69 c 33 section 1.

transfers of property between spouses are tax free. Similarly, section 7 of the Estate Tax Act 1958 (as amended in 1968) allows for a complete deduction for property passing to a spouse. This treatment of husband and wife as an economic partnership followed closely on the Report of the Royal Commission in 1966 which, it will be recalled, recommended the treatment of the family as the tax unit. That recommendation was not, however, implemented so far as income tax was concerned, nor was it implemented for capital gains tax purposes. Capital gains tax was introduced on 6th January 1972 after the publication of the White Paper¹ containing the Government's proposals on the Report of the Royal Commission : the White Paper rejected the adoption of the married couple as the tax unit and so the capital gains tax provisions treat the spouses as separate individuals.

"The basic scheme for the taxation of capital gains and losses is that one half of any capital gain or loss is included in, or deducted from, the income base. In this sense there is no separate capital gains tax; rather the capital gains provisions have the effect of broadening or contracting a taxpayer's income base, which then bears tax at the normal income tax rates".²

There are also provisions to prevent a taxpayer from splitting his income by transferring property to another person who subsequently receives a capital gain on the transferred property; the rules require the transferor and not the transferee to include in his income the net taxable capital gain or allowable capital loss on the

1. Proposals for Tax Reform : (Ottawa. Queen's Printer 1969).

2. Butterworths Vol. 217 1.1.

transferred property. The exact application of the attribution rules depends on the relationship between the transferor and the transferee, but complete attribution takes place on transfers between spouses.

(6) Children

Children are taxed as individuals with "attribution" rules similar to those of spouses for income tax, but not capital gains tax, purposes. A child allowance is given to a parent; the allowance is increased for a child over 16 in full-time education but, whatever the age of the child, the allowance is reduced if the child has income.

The Royal Commission recommended that children should be included in the tax unit and their income aggregated with their parents but there is little likelihood of this being accepted.¹

5. The Republic of Ireland

- (1) Constitutional development
- (2) Matrimonial property
- (3) Income tax
- (4) Tax avoidance
- (5) Capital taxes
- (6) Children

(1) Constitutional development

It has been noted that the English common law was exported to Australia, New Zealand and Canada in the first half of the nineteenth century and also that each colony subsequently enacted provisions similar to those in the Married Women's Property Act 1882; as these colonies did not import the system of United Kingdom taxation, the

1. See Gordon Bale above.

treatment of married women as separate persons at law was well established before income tax was introduced; it therefore was natural that husband and wife would also be treated as separate persons for income tax purposes.

The constitutional development of the Republic of Ireland did not follow the same pattern. Eire achieved independence in 1922 and its constitution was enacted in the Irish Free State Constitution Act of that year; the constitution has been subsequently amended but the principle of a written constitution has remained.

(2) Matrimonial property

Irish land law is a mixture of English common law, English statute law, Irish statute law and Irish common law;¹ the English 1925 legislation has not yet been enacted in Ireland but there is some Married Women's Property legislation which follows closely on the English model.

(3) Income tax

In 1922 the Republic of Ireland adopted the United Kingdom tax laws (with a few modifications) up to and including the Finance Act 1922, so the two tax codes are basically similar but with discrepancies arising from subsequent Finance Acts. In 1967 income tax was consolidated in The Income Tax Act 1967 of which sections 192-198 contain the "Special Provisions as to Married Persons" which are substantially the same as those contained in sections 37-42 Taxes Act 1970, with some modifications. Because of the

1. J.C. Wylie : Land Law in Ireland.

secession in 1922, the Republic's provisions contained an option for separate assessment as introduced in the United Kingdom in 1914, but not the option for separate taxation of wife's earnings, introduced in the United Kingdom in 1971 and never adopted in Ireland. Now it has been mentioned above that, unlike the United Kingdom, the Republic of Ireland has a written constitution which contains the following provisions:-¹

Article 40.1. All citizens shall, as human persons, be held equal before the law.

Article 41.1.1. The state recognises the family as the natural primary and fundamental unit group of society and as a moral institution possessing inalienable and imprescriptible rights, antecedent and superior to all positive law.

Article 41.1.2. The state therefore guarantees to protect the family in its constitution and authority as the necessary basis of social order and as indispensable to the welfare of the nation and the state.

Article 41.3.1. The state pledges itself to guard with special care the institution of marriage in which the family is founded and to protect it against attack.

In 1978, a taxpayer, Mr. Murphy, brought an action against the Attorney-General of Ireland alleging that the system of taxation of married couples, as it related both to the personal allowances and aggregation, was in breach of the constitution.¹ At that time the allowances available to a married couple were less than those available to two single persons, with the addition of a small allowance for a working wife of slightly more than one quarter of the

1. Constitution of Ireland, Government Publications, Dublin.

single allowance; full aggregation applied both to earned and unearned income. The High Court gave judgment in favour of the taxpayer on 12th October 1979 and the Supreme Court dismissed the State's appeal against the judgment on 25th January 1980 holding that, while the provisions of the Income Tax Act 1967 on tax free allowances were not a discriminatory attack on the family as "there is a difference of social function between a husband and wife living together to which the legislature was entitled to have regard", the provision whereby the wife's income was assessed as part of the husband's income (thus tending to push their joint income into higher tax bands) was not defensible on any such ground and was a discriminatory attack on the married state and thus on the family, in violation of Article 41 as well as Article 40.1. In the Index¹ of decisions the point is made that when incomes are aggregated under a graduated system the tax burden is less on unmarried couples living together and this did not accord with the constitutional pledge by the state to "guard the institution of marriage with special care".

While the Murphy case was before the High Court the opportunity was taken to raise the married allowance to twice that of a single person (for 1978-79), but following the decision of the Supreme Court in January 1980 the legislation was radically amended.² Married couples now have three choices. First, if no election is made,

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1. The decision has not yet been reported but it is noted in the 1979 Index to Supreme Court and High Court written judgments compiled by the Law Reporting Council of Ireland.
 2. Income Tax : McAteer & Reddin : The Institute of Taxation in Ireland 1981 Chapter 16.

spouses will be treated as if they were not married. But both spouses can elect to be jointly assessed : in this case the husband is assessed on the combined income of himself and his wife but can claim double allowances, double interest relief and gets double the bands of tax available to a single person. This is, in effect, the quotient system which is, as has been seen, always favourable to a married couple as far as the quantum of tax paid is concerned. It has, however, one major drawback, namely, the necessity of joint accounting or husband's accountability. Because a mandatory quotient system would, therefore, breach the provisions of the Irish constitution the application of the second choice is governed in a pleasing Irish way : although statute provides for it only to come into force on the exercise of an election by both spouses, nevertheless spouses are deemed to have elected unless they serve a notice to the contrary. Because it may be thought that the second alternative may not be always acceptable because of the retention of the principle of husband's accountability, the third option is for "joint assessment with separate assessment"; under this system the quantum of tax payable is determined as under the "quotient" system mentioned above but assessments and returns are dealt with by each spouse separately; the personal allowances are divided equally between the spouses and other allowances and reliefs are generally granted to the spouse who bears the cost.

(4) Tax avoidance

Under a system of aggregation, such as was in operation in Ireland prior to 1980, no tax avoidance provisions

are necessary as income-splitting cannot, by definition, take place. Further, under the quotient system, which is now available to all married couples, income splitting is in fact made statutory. There are, therefore, no tax avoidance rules affecting married couples in Ireland.

(5) Capital taxes¹

A wealth tax and a capital gains tax were introduced in 1975 and a capital acquisitions tax in 1976; however, wealth tax was suspended from 5th April 1978 onwards, but its principles remain of interest. For wealth tax purposes, therefore, the taxable wealth of a husband included that of his wife and of minor children in his custody.² Although the tax was a proportional tax (1 per cent) and thus did not penalise aggregation, there were a number of exemptions, in particular the first slice of taxable wealth was exempt; for a single person this was £70,000, for a widow or widower £90,000 and for a married couple £100,000; there was an additional exemption of £2,500 for each minor child who had aggregable wealth. The capital gains tax³ provisions have many similarities to those in the United Kingdom : it is a proportional tax so aggregation as such does not entail a penalty, but a wife's gains are assessed on the husband unless either spouse elects for separate assessment. However, following the Murphy decision⁴ the law was amended to provide that the gains of a

1. Tolley's Taxation in the Republic of Ireland.

2. Section 4 Wealth Tax Act 1975.

3. Capital Gains Tax Act 1975.

4. See above page

married woman are to be calculated as if she were a single person; previously the married couple obtained only one £500 allowance, available to all other individuals; now they each obtain a full £500 allowance and, in addition, the unused portion of one spouse's allowance may be used by the other spouse. Disposals between spouses are on a no gain no loss basis and losses of one spouse may be set against gains of the other unless either spouse elects otherwise.

However it still appears to be the case that a married couple can have only one principal private residence exemption and if more than one residence is involved the election as to which is to attract the relief must be made by both spouses. The Capital Acquisitions Tax Act 1976 introduced both a gift tax and an inheritance tax; the person chiefly accountable is the recipient of the gift or inheritance; the gift tax is imposed on lifetime transfers at 75 per cent of the rate of the inheritance tax : the rate of the inheritance tax is determined by the relationship between the disponor and the donee/successor; there are four rate schedules and spouses and children enjoy the most favourable of these : cumulative transfers of up to £150,000 are completely exempt and there is a maximum rate of 55 per cent for cumulative transfers in excess of £400,000.

(6) Children

Section 141 Income Tax Act 1967 provides for a child allowance of £195 for each child reduced by the amount

by which the child's income exceeds £80. (Cash benefits are payable in addition). There is no aggregation of children's income with that of parents for income tax purposes (as was the case, temporarily, with wealth tax) but there are two specific anti-avoidance provisions affecting children. First, although in general transfers of income under the covenant procedure are recognised in very much the same way as in the United Kingdom, in general a covenant in favour of a minor child (under 21) is ineffective for tax purposes. In 1979 a restriction was placed on the amount a person could covenant to his child over 21 and this is now limited to 5 per cent of the covenantor's total income.¹ Secondly, settlements are also ineffective as a means of splitting income with a minor child; sections 443 to 448 Income Tax Act 1967 are very similar to the corresponding United Kingdom settlement provisions with similar exemptions for trusts where income is accumulated for the benefit of a minor child.

As far as capital gains tax is concerned, there are no special provisions for children, but children are in the most favoured rate schedule for the purposes of the capital acquisitions tax.

6. Conclusions

All the four common law systems analysed have a system of individual taxation for husband and wife. Australia, New Zealand and Canada introduced income tax after the passage

1. Section 33 Finance Act 1979.

of their Married Women's Property Acts and they were not, therefore, hampered by a previous history of aggregation. The Republic of Ireland, on the other hand, imported the complete United Kingdom tax system when it attained independence in 1922 and this persisted until 1980 when it was declared repugnant to the constitution.

The treatment of the spouse allowance differs from state to state; Australia and New Zealand do not have personal allowances as such but both give a rebate for a spouse who supports another spouse; in New Zealand the rebate reduces where the dependent spouse's income exceeds 520 dollars. Canada gives personal allowances and gives an additional allowance to a supporting spouse when the supported spouse's income is less than the personal allowance; the spouse allowance is slightly less than a full personal allowance, and must be claimed by both spouses filing a joint return. In Ireland each spouse gets a full allowance and where one spouse has little or no income the allowance can be used by the other spouse if both spouses opt for joint assessment.

Attitudes to tax avoidance appear to depend on the treatment of the capital taxes. Australia, New Zealand and Ireland make no restrictions on income splitting but in each country spouses get little more exemption from the capital taxes than other individuals; however, Australia does give an exemption from estate duty for small estates left to spouses; New Zealand exempts the passing of a share in a 'Joint Family Home' and Ireland gives a spouse and children a favourable rate schedule for capital acquisitions tax purposes. Canada, on the other hand, has enacted detailed

attribution rules to prevent income splitting but accompanies this by favourable treatment for capital taxes purposes; thus there is no gift tax or estate duty on transfers between spouses and the spouses have separate exemptions for capital gains tax purposes.

In no country is the income of a child aggregated with that of its parents, although Australia taxes the income of a child at a higher rate than that of an adult. Australia gives no child allowance but does give a cash benefit; New Zealand gives rebates for low income families with children; and Canada and Ireland give a child allowance which is reduced if the child has income; finally, Ireland has enacted anti-avoidance legislation to prevent income-splitting with children by nullifying the tax effectiveness of covenants and settlements.

CHAPTER 12 - THE CIVIL LAW COUNTRIES

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CHAPTER 12

THE CIVIL LAW COUNTRIES

Section

1. Introductory.
2. France.
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5. Italy.
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1. Introductory

The common law originally provided that on marriage the personality of a married woman merged with that of her husband; when income tax was introduced in the United Kingdom, in 1799, an aggregation rule was therefore adopted and it has not yet been completely revoked, even one hundred years after the passing of the Married Women's Property Act in 1882. However, the introduction of income tax in Australia, Canada and New Zealand occurred after the amendment of the property legislation with the result that the assessment of married couples on an individual basis accords with the property laws in these countries.

In the civil law countries, however, a completely different development has taken place; in general these

legal systems have recognised a community of property for married persons and the income tax laws have responded to this concept by imposing a system of joint taxation. However, the systems of joint taxation in the civil law countries differ fundamentally from the United Kingdom system; the latter treats husband and wife as one person, with some exceptions; the former usually treat them as two, except that there is usually a responsibility on the husband, or a joint responsibility to pay the tax. The married couple are not, however, treated as two separate people : they are usually given double the allowances and are sometimes given double the reduced rates available to one single person which can result in positive advantages, particularly where one spouse has a nil or low income. Accordingly, the Table on page 5 of the fourth Background Paper to the Green Paper on Taxation of Husband and Wife¹ could be misleading; although it indicates that the unit of assessment for France and Belgium is the family, and for the United Kingdom, Germany and Luxembourg it is the husband and wife, no indication is given that it is only in the United Kingdom and, to a lesser extent in Belgium, that aggregation still applies and that in the other countries mentioned the favourable quotient system ensures that married couples have positive tax advantages.

There is one common feature which is found in all the civil law countries and that is the system of matrimonial community property. The community has been

1. International Comparisons of Taxation of Husband and Wife : Note by Inland Revenue and Department of Health and Social Security : January 1981.

defined as a

"fund, allocated to the couple, but under the husband's control during the marriage and destined to be shared out afterwards between the spouses..."¹

The system of community had much in common with the system of matrimonial property in the United Kingdom before 1882 as it combined the concept of the supremacy of the husband and the incapacity of the married woman but its major distinguishing feature is that it gives a married woman a legal right to share in all the property acquired by both spouses during the marriage.

Because of the similarity of this system with the pre-1882 English system it is not surprising that all civil code countries adopted the principle of aggregation and husband's accountability for income tax, but each country differs from the other in the way in which it gives allowances for marriage.

The first four countries considered in this Chapter all adopt the favourable quotient system or have now moved to a system of individual taxation : the last two countries mentioned have retained aggregation for investment income.

2. France

- (1) Constitution
- (2) Real property - husband and wife
- (3) Income tax
- (4) Tax avoidance
- (5) Capital taxes
- (6) Children

(1) Constitution

The constitutions of the civil law countries

1. Comparative law of matrimonial property : Kiralfy p.7.

differ fundamentally from those of the common law countries.

"Anglo-American common law is essentially the body of legal techniques, concepts and procedures established by the English in areas of conquest or settlement in which the language, rules and methods of the King's courts, are an essential component...The civil law system is characterised by the Roman "idiom of thought" elaborated from Justinian texts by scholarly commentators and expressed in national codifications".¹

The "national codification" in France was enacted on 21st March 1804 but before turning to consider the provisions of the code which concern the property rights of husband and wife it may be of interest to summarise briefly the development of this branch of the law prior to codification. France was part of the Roman Empire until 476 AD during which time Roman law applied to the Gallic-Romans and local customary law applied to the indigenous inhabitants.² It will be recalled that in the first centuries of the Empire at Rome women had gained their independence and legal capacity;³ however, local customary law had always retained the principle that, on marriage, the husband became responsible for the administration of the wife's property and the wife lost her legal personality. In the South of France Roman law was adopted generally⁴ and married women preserved a measure of legal capacity;

"In the North, however, in continuation of Frankish and other Teutonic traditions, various forms of community property had come to prevail under practically all of

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1. Civil law and the Anglo-American Lawyer. Henry P de Vries
 2. Droit Francais : Rene David : Tome I page I. Translated. ..
 3. Droit Civil : Précis Dalloz : Translated.
 4. The Code Napoléon : Schwarz.

which the husband was to be the sole manager, not only of the community fund but also of the separate assets of the wife, and the wife's capacity to transact legal business was to all practical effects extinguished".

When the Code was introduced in 1804 it dealt with those branches of the law which were already "written law" promulgated as legislation before the Revolution. The most famous of these Codes, the Code Civile, contains provisions from the Digest of Justinian reworked over the years; in contracts and torts no innovations were made; however¹ in the case of matrimonial property a choice had to be made between Roman law and the customary law of community and it was the Northern system of community of movables and acquisitions that was established by the Code Civile as the common law of France. It has always been possible for husband and wife to contract out of the statutory system, but only by means of an ante-nuptial contract.

(2) Matrimonial property

There were two sections in the 1804 code which affected husband and wife : the first commenced with Article 213 which regulated the relationship of the spouses, providing that "the husband must protect the wife and the wife must obey the husband". Another section dealt with the matrimonial régime; so Article 1388 provided that the husband's position as head of the family was not susceptible of alteration by contract and by Article 1124 married women

1. Civil Law and the Anglo-American Lawyer : Henry P. de Vries.

infants, and persons of unsound mind were expressly declared to be incapable of making contracts. Although the system of the Code reflected the social facts of 1804

"it could not be continued unchanged into the twentieth century when women had come to new positions of personal independence".

Since 1804, therefore, a number of significant developments have taken place; in 1907 a woman exercising a separate profession was given power to dispose of her own salary; in 1923 the old community rules were replaced by a system of joint ownership of assets acquired during the marriage; further amendments were made in 1938, 1942, 1965, 1970 and 1975. The present Code therefore represents a considerable departure from that enacted in 1804; Articles 212-226, which regulate the rights and duties of the spouses, now provide for equal responsibilities and joint entitlement and Articles 1400 onwards provide that, if not excluded by a marriage contract, the spouses hold their property under the community system. The system, however, only applies to acquisitions during marriage and not to assets owned at the time of the marriage; further assets acquired during the marriage by gift or inheritance are also excluded.¹ There are many detailed rules regulating what is, and what is not, community property and Article 1421 provides that the husband administers the community property alone but there are detailed rules requiring the consent of the wife to a number of transactions.

Although the system of community property has

1. Article 1405.

always been capable of being excluded by ante-nuptial contract it is understood that most French people regard the community system as being appropriate for married couples and that where an ante-nuptial settlement excludes the statutory system it does so in order to impose another system of community.

(3) Income tax

Income tax law was codified in 1941 by the Code Général des Impôts (CGI) which is the major source of income tax law. Article 6.1 provides that family income is to be taxed to the head of the household; this is compulsory, even if the spouses are married under a separate property régime. The incomes of the spouses are aggregated but are then split into two parts for the purpose of assessing the amount of tax payable; the tax attributable to a single part is multiplied by two to give the total amount payable. This statutory income-splitting does not depend on whether each spouse actually has any income:

"the system is based on the assumption that the increased financial burden arising from the addition of a member to the family unit reduces the standard of living of the unit ...the family quotient system seems to take into account not only the amount of the taxpayer's income but also the number of persons who must live on that income".

It has been noted above that the quotient system is always beneficial to a married couple and is particularly beneficial where there is a nil or low earning spouse. However, these advantages are purchased at the price of the requirement of husband's (or at least joint) accountability; although such a requirement has caused difficulty in the

United Kingdom,¹ where separation of property is the general law, it is less likely to cause difficulty in France where Article 1421 of the Code Civile provides that the husband is responsible for the administration of the community property of the spouses.

No personal allowances are given in France - the quotient system adequately recognises the taxpayer's marital status and family responsibilities.

(4) Tax avoidance

A quotient system of taxation automatically makes available all the possible benefits which can flow from income splitting and tax avoidance provisions are therefore unnecessary.

(5) Capital taxes

There are two main capital taxes in France - a successions tax on transfers on death and a gift tax on gratuitous inter vivos transfers.² These taxes are levied on the amount received by each beneficiary; a major tax reform in 1959 resulted in a significant reduction of the tax on transfers to spouses and children. Such recipients now receive a substantial tax-free exemption followed by progressive rates from 5 per cent to 20 per cent depending on the size of the legacy³ whereas other recipients bear a proportional rate of tax varying from 35 per cent to 60 per cent depending on the degree of their relationship

1. See Chapter 8.

2. See World Tax Series - Harvard Law School.

3. Art. 777 CGI.

with the deceased/donor. The gift tax is calculated in the same way as the successions tax with cumulation of prior gifts from the same donor to the same donee. The favourable treatment of transfers to spouses and to children was enacted in order to favour the transmission of family assets and to encourage savings.

(6) Children

France is one of the two countries analysed which includes children in the 'quotient' arrangement. If no election for a separate assessment of the child's income is made, it is aggregated with that of the head of the household and the child counts as one additional half-part for the application of the quotient. So, in the typical case of a married couple with two dependent children the family income is aggregated and then divided by three and the tax attributable to a one-third part is then multiplied by three to give the total amount payable. This is a most advantageous system where a child has a nil or low income, but although the quotient procedure is compulsory for spouses it is possible to elect for a separate assessment of a child's income.

3. Luxembourg.

- (1) Constitution
- (2) Matrimonial property
- (3) Income tax
- (4) Tax avoidance
- (5) Capital taxes
- (6) Children

(1) Constitution

The state of Luxembourg has existed, as an

autonomous and separate state, since the Treaty of London of 19th April 1839; previously there had been connections with both the Netherlands and with Belgium.¹ The first constitution was enacted in 1831 and there have been many subsequent revisions and amendments. The 1971 constitution² provides that all citizens are equal before the law (Article 11(2)) and that the state guarantees the natural rights of the human person and the family, (Article 11(3)).

(2) Matrimonial property

The state of Luxembourg adopted a Civil Code on the lines very similar to the Code Napoléon adopted in France in 1804. As did the French Code, the Luxembourg Code regulated the rights and responsibilities of the spouses and the laws concerning matrimonial property, but whereas in France various revisions and amendments took place over the years to reflect the changes in social attitudes to married women, such changes were not followed in Luxembourg -

"so that the Grand Duchy was one of the last countries in Europe to have one half of its adult population with legal capacity and one half without it".³

However, when change did take place, it all took place at once. Major modifications were made to the Code in 1972 and 1974 : the spouses may now make whatever arrangements they please to govern the ownership of the

1. L'état Luxembourgeois, Pierre Majereuse.

2. Extrait de Annuaire Officiel d'Administration et de Legislation 1971 : Ministere D'Etat : Service Central de Legislation.

3. The Reform of Family Law in Europe : Chloros.

matrimonial property (Article 1387) but, in default of agreement, a system of community applies (Article 1400). The community fund is limited to property acquired after the marriage and the Luxembourg Code is now one step ahead of the French Code as it has abolished the supremacy of the husband as the sole administrator of the community.

(3) Income tax and allowances

The incomes of married persons are added together for assessment purposes¹ but tax is charged at twice the amount payable on the basic scale on one half of the taxable income. In other words, a full income-splitting (quotient system) applies. No separate allowances are given to individuals and no doubt the view is taken that the quotient system adequately allows for the additional financial responsibility of marriage.

(4) Tax avoidance

As has been noted above, a statutory quotient system provides all possible benefits to be derived from income splitting and no special tax avoidance provisions are required.

(5) Capital taxes

There is a capital tax in Luxembourg which is charged at the rate of $\frac{1}{2}$ per cent each year on taxable capital. There is a personal allowance for an individual of 100,000 francs with an additional 100,000 for a wife

1. Income tax outside the United Kingdom. The Board of Inland Revenue.

and a further 100,000 for each dependent child. Again, such an arrangement can never disadvantage a family unit but could bring great advantages (where some member, or members, has little or no taxable capital his allowance can be used by other members).

There is also a real property tax which is levied on the capital value of all real property; personal reliefs here are, of course, not appropriate.

(6) Children

As with France, the income of minor children is aggregated with that of the parent, with the exception of wages from employment. Also as in France, a family quotient system is adopted for each child but in Luxembourg it is much more generous. The principle is, that if aggregate taxable income does not exceed 505,200 francs (about £7,000 p.a.) and there are up to three dependent children the aggregate income is divided into parts, the tax due on one part is multiplied by the number of parts to give the tax liability. The number of parts into which the income is divided is 2.6 for one dependent child, 3.4 for two and 4.6 for three. Where income exceeds 505,200, or there are more than three dependent children there are credits against tax of varying amounts so that, for example where a taxpayer has income not exceeding 1,092,000 francs (about £15,000) and six children, the child allowance deducted from tax is 50,661.60 (£100) plus 6 per cent of taxable income.

(7) Conclusion

Luxembourg has a matrimonial property régime very similar to that of France and the tax system, too, has very many similarities. In default of any agreement to the contrary, matrimonial property is held in community and for tax purposes, the highly beneficial full family quotient system applies.

4. West Germany

- (1) Constitution
- (2) Matrimonial property
- (3) Income tax
- (4) Tax avoidance
- (5) Capital taxes
- (6) Children

(1) Constitution¹

The present constitutional law of the Federal Republic is contained in the Grundgesetz (Basic Law) of 1949, Article 6(1) of which grants to the marriage and the family the special protection of the constitution. This is a rule of constitutional law and represents a binding line of guidance for the interpretation of all legal provisions relating to marriage and the family. As we shall see, the present income tax provisions in Germany, which are favourable both to the family and to married women, are very similar to those in the other country which has a constitution which protects the family, namely, Ireland, although the historical development in these two countries differs widely.

1. Manual of German Law : E.J. Cohn 2nd Edition Volume 1.

Ancient Germanic law was a customary law but one of the major influences on its development was the reception of Roman law; by the end of the fifteenth century, Roman law, modified in some respects by canon law, had to a large extent, superseded customary Germanic law. However, Roman law was never revived in Germany in its entirety; in the law of domestic relations canon law naturally conquered a good deal of ground and in this area native Germanic institutions were never completely ousted. These remnants of germanic law were strong enough to secure a strong influence on the codification movement of the nineteenth century.

The German Civil Code (Bürgerliches Gesetzbuch (BCB)) was promulgated in 1896 and entered into force on 1st January 1900; the Code was strongly influenced by the twin legal traditions of the Roman and Germanic laws; it was largely undertaken as a means of clarification:-

"It was prepared in the nineteenth century by a distinguished and conservative group of lawyers and administrators who could, by no stretch of imagination, be described as radical reformers. The economic and political outlook reflected in the Code is often described as being that of an enlightened patriarchal owner of private property. The dominant position of the father and the husband in family life was reflected in the provisions...on the management of the household and the bringing up of the children".¹

(2) Matrimonial property

Since the BGB was promulgated in 1900 a number of amendments have been enacted and those with the strongest

1. The German Civil Code : E.S. Forrester.

impact have completely changed the rules governing the relationship between husband and wife. Formerly, the husband had power to make almost all the decisions but since 1957 the emphasis has been on joint administration; under the old Code the statutory matrimonial property régime permitted the husband, within certain limits, to administer freely the bulk of his wife's property, and he was entitled to the income from it to compensate him for the obligation to maintain his wife; since the Equality Act of 1957 the statutory régime is a "community of surplus".¹ This does not mean that the spouses own their property jointly; it means that on the termination of the marriage the "surplus" is equally divided. As there is thus now no actual community of property the law provides safeguards to ensure that the spouses cannot be defrauded of their rights - each spouse has a statutory right to demand information from the other and may petition for an immediate adjustment in certain cases; household goods cannot be transferred without the consent of both spouses.

It has always been possible to exclude the statutory régime by contract but it must now be replaced either by a régime of separation of goods or of community property; it is understood that in practice a régime of separation of goods is not infrequently chosen although it has no advantages for a wife with nil or low incomes; a community property régime is chosen rarely.

(3) Income tax

The German tax legislation is contained in a large

1. Code 1363.

number of individual statutes dealing with separate taxes, for example, income tax, corporation tax, turnover tax, etc. Income tax is contained in the Revenue Code (Reichsabgabeordnung) of 1919.¹ Husband and wife are normally assessed jointly on a quotient basis, when the amount of tax applicable to one-half of the combined taxable income of the spouses is computed and multiplied by two.² This very favourable form of statutory income splitting is available even if only one spouse has income. Where a joint assessment is made the tax returns must be signed by both spouses.

If, however, the spouses so elect, husband and wife can be assessed as separate individuals; the election need be made by one spouse only.

In all cases, the personal allowances available to a married couple are twice those available to a single person.

(4) Tax avoidance

As has been mentioned above³ statutory income splitting does not require any special tax avoidance provisions. In 1962 the Federal Constitutional Court⁴ declared any limitations on the recognition of bona fide employment contracts between married individuals, because of the fact of marriage, to be unconstitutional and void. Such employments are therefore recognised for tax purposes

1. Cohn p. 27.

2. World Tax Series - Germany - Income Tax.

3. Page 549.

4. B St B 1 1962 1 p. 506.

if the arrangements are clearly agreed and the spouse has the same conditions and remuneration as an unconnected employee.

(5) Capital taxes

The main capital taxes in Germany are an Inheritance/Gift Tax, a net worth tax and a real property transfer tax. The inheritance/gift tax was originally imposed by the Inheritance Tax Law of 1925, revised in 1959; like the French succession tax it is imposed on the recipient and the rate varies according to the relationship between donor and donee; rates for transfers between spouses and children vary from 2 per cent to 15 per cent and for transfers between unrelated persons the rates vary from 14 per cent to 60 per cent. In addition, spouses enjoy an exemption for the first DM 250,000 received and a complete exemption for any "asset surplus" received under the statutory provisions regulating matrimonial property.

The net worth tax is a tax of 0.5 per cent on total property, excluding certain assets; this tax has elements of a wealth tax on the one hand and a tax on investments on the other. Each taxpayer has a tax-free exempt band of 20,000 DM; an additional 20,000 DM is available for a wife and each child. Married couples and children are always assessed jointly.

The real property transfer tax, which probably equates most closely to the United Kingdom stamp duty, is at the rate of 3 per cent; spouses enjoy complete exemption for transfers into and out of the community property régime.

(6) Children

Germany used to provide for aggregation of a child's income with that of its parents but by a decision in 1964¹ the Federal Constitutional Court declared the provision void for unconstitutionality - the provision was repugnant to Articles 3 and 6 of the constitution.

A child tax allowance is not available to a parent but a cash benefit is.

5. Italy

- (1) Constitution
- (2) Matrimonial property
- (3) Income tax and allowances
- (4) Tax avoidance
- (5) Capital taxes
- (6) Children

(1) Constitution

"Italy has had two civil codes in its brief history as a unified modern nation. The first, adopted in 1805, closely imitated the famous French Code Napoléon. The second was enacted by Royal Decree No. 262 of October 16th 1942".²

(2) Matrimonial property

In spite of its completely different constitutional development, the law of matrimonial property, and of the application of the income tax laws to married couples, in Italy shows a marked similarity to the principles which applied in the United Kingdom. The basic matrimonial property régime in Italy was derived from Roman law and centred round the

1. B St B 1 1964 1 p. 488.

2. The Italian Civil Code : Mario Beltramo and others.

dowry; the theory was that the wife's property was used to support the domestic needs of the household whereas the husband's property was utilised for the family's business and commercial interests. The wife's property was transferred to the husband as dowry and was administered by him; a married woman had no legal capacity. The situation was one of separation of goods and recalls the system which obtained in England before 1882. After the Restoration of 1815 the codes of the various Italian states introduced a system of community property but this concept was abandoned by the authors of the 1865 Code on the grounds that such a system "did not correspond to the established customs of the country".¹ This was therefore one of the very few occasions where the Italian Code differed from the Code Napoléon; in other respects similar provisions were enacted; a wife was subordinate to her husband who was the head of the family and the wife had no legal capacity without the authorisation of the husband. The Italian system of separation of goods was thus retained.

The first reform was enacted on the 7th July 1919 (Law No. 1176) when a married woman was given the right to dispose of her own property and legal capacity. From 1925 to 1941 there was a movement towards reform to improve the position of married women and a proposal was made once again that the system of community property should be introduced on the basis that this corresponded to the needs of the lower classes where couples entered the married state with

1. Kiralfy : Comparative Law of Matrimonial Property.

very few assets indeed but where after a lifetime of work a husband could have accumulated some modest savings from which it would be unjust to exclude the wife. However, when the Code of 1942 was introduced, it contained no such reform; spouses could choose a dowry system or a community system but in the absence of agreement to the contrary a system of separation of goods applied. Article 144 of the 1942 Code also reaffirmed the supremacy of the husband and the subordinate position of the wife.

In 1948 a new constitution was enacted in Italy which affirmed the equality of the spouses; there was thus a disparity between the provisions of the Code and the provisions of the constitution but it was not until 19th May 1975 that a new régime was introduced enacting the principle of equality of the spouses in all respects and introducing a system of community of property in the absence of agreement to the contrary.

Now whereas the tendency for the other civil code countries has been to move away from a system of community property towards a system of separation of goods or of "community of surplus", Italy has moved in the opposite direction but both moves have had the same underlying motivation, i.e. to improve the rights of married women. The "classic" French system of community property was disadvantageous to a wife as it vested all the powers of administration of her property, and her legal capacity, in her husband but it did have one very positive advantage - a wife acquired a legal entitlement to a share in the community property, most usually that acquired during marriage, and could take steps to prevent its alienation; recent

developments have removed the wife's legal incapacity but retained her right to share in wealth accumulated by her husband during the marriage. In Italy, the previous system of separation of goods, coupled with the complete incapacity of the married woman, was doubly disadvantageous, and was reminiscent of the English system before 1882. Legal incapacity was removed in Italy in 1919, and the introduction of a community property system in 1975 enacts in statutory form in Italy the rights of a wife to share in the wealth accumulated during the marriage which have been recognised in the United Kingdom to a lesser extent but not yet fully recognised by statute.¹

(3) Income tax

Prior to 1974 "the most criticised part of Italian tax law" was:-

"the cumulation of income of husband and wife in particular the fact that any earned income of the wife is added to her husband's income for income tax purposes".²

1975 saw the enactment of the principle of equality in the property context and relief was also introduced in 1975 for separate taxation of the incomes of each member of the family if the combined family income did not exceed 5M lire (later increased to 7M lire); in 1976 separate assessment of both earned and unearned income, without limit, was introduced.

There are "allowances" (credits against tax) for

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1. See however the provisions of the Matrimonial Homes Act 1957 and the Inheritance (Family Provision) Acts and recent divorce cases concerning spouses rights.
 2. European Taxation : Volume 15 : 1975 page 283.

each taxpayer of 36,000 lire with an additional "wife allowance" of 72,000 lire if the wife's income does not exceed 960,000 lire.

(4) Children

Prior to 1974 the income of a child was assessed with its parents, but now it is assessed separately; there are child allowances (credits against tax) of 24,000 lire for each child.

6. Belgium

- (1) Constitution
- (2) Matrimonial property
- (3) Income tax
- (4) Tax avoidance
- (5) Capital taxes
- (6) Children

(1) Constitution¹

The Belgian Constitution was promulgated on 7th February 1831 and has since been revised on three occasions - in 1893, 1921 and 1972. Article 6(2) provides that all Belgians are equal before the law.²

The civil law of Belgium is based on the French Civil Code of 1804³ and it will be recalled that in its original form that Code was characterised by the authority of the husband and the incapacity of the married woman; the principle of incapacity did not disappear in Belgium until 1932.

1. The Political, Economic and Social structures of Belgium : Robert Senelle.

2. Le Troisieme Revision de la Constitution. Wigny. 1972.

3. Kiralfy : Comparative Law of Matrimonial Property.

(2) Matrimonial property

The 1932 Code incorporated the principle of the marriage contract : the spouses were free to adopt any matrimonial property system but if no option was adopted the code imposed a system of community of movables and acquests under which the husband had power to manage and use the common property at his discretion.

In 1948 a Special Commission was appointed to examine the provisions of the Civil Code concerning the rights and duties of the spouses and the provisions relating to systems of matrimonial property. The Report was not submitted until 1956 and was incorporated in legislation in 1958; the authority of the husband was then abolished together with the legal incapacity of the married woman but no amendment was made to the matrimonial property system. The husband remains solely responsible for the administration of the community property; and the income of a married woman's separate property belongs to the community with the result that she can only alienate the reversion and not the entitlement to the income. However, despite the lack of any positive reform there is considerable agreement that the present position is unsatisfactory and there has been much discussion as to the direction which change should take. There appears to be substantial agreement that the parties should be able to regulate their own matrimonial property arrangements but the difficulty has been in identifying which system should apply by law in the absence of agreement to the contrary. No less than five separate proposals have been discussed and a common feature of all five is an element of joint ownership by the spouses.

At present, therefore, Article 1387 of the Belgian Civil Code provides that the parties may regulate their matrimonial property by means of marriage contract but Article 1390 provides that they must be specific in their choice of system : they can choose either a community system or a dowry system and in the absence of express stipulation the community régime applies.

(3) Income tax

In view of the fact that the Belgian law of matrimonial property is less highly developed than the laws of France, Luxembourg and Germany, it is interesting to note that Belgium does not operate a "quotient" system of family taxation but instead operates a complicated system of partial disaggregation and allowances which is somewhat reminiscent of the United Kingdom system. There is a limited right of separate taxation for two-earner couples where the combined earnings do not exceed 600,000 B.Fr. (about £8,200); but the deduction of 10,000 B.Fr. available to each individual taxpayer is apportioned between husband and wife.

Where there is only one earner in a family whose earnings do not exceed 600,000 B.Frs. a reduction of 20 per cent of earnings is allowed. Where the family's earnings exceed 600,000 B.Frs. the tax due may not exceed that of a "small earning" family mentioned above plus 35 per cent of the excess; as the marginal rate for individual taxpayers is 60 per cent this represents a saving.

Where husband and wife are jointly assessed they also receive a credit against tax of 4,618 B.Frs. and the

earned income of the wife is reduced by 56,000 B.Frs. The total allowances available to a married couple thus exceeds the total available to two single individuals.

(4) Tax avoidance

No tax avoidance provisions are necessary with an aggregation system.

(5) Capital taxes

As a rule capital gains are included in earned income to which the above rules apply; there are also a number of local taxes.

(6) Children

A child's income is aggregated with that of its parents if the parents have the legal enjoyment of the income, but credits against tax are granted for each child of 5 per cent + 500 B.Frs. for one child, 15 per cent + 1250 B.Frs. for two children and 25 per cent and 2,250 B.Frs. for three children.

7. The Netherlands

- (1) Constitution
- (2) Matrimonial property
- (3) Income tax
- (4) Tax avoidance
- (5) Capital taxes
- (6) Children

(1) Constitution

Around the beginning of the Christian era the Netherlands formed part of the Roman Empire and was then

inhabited by Germanic tribes. As in other European countries, Roman power was broken in the fifth century; small feudal states came into being but were ultimately united under Charles V, Emperor of Germany and King of Spain. However, during the eighty years war the northern provinces seceded and pledged mutual allegiance in the Union of Utrecht (1579). From 1810-13 the country was annexed to the French Empire but in 1815 a new constitution was drafted and William I reigned over the Netherlands and Belgium until 1930 when the Belgians seceded. A further constitution was enacted in 1848.

During the days of Roman rule the law which applied in the Netherlands was Germanic law; it was "tribal law, popular law, custom". But from the fifteenth century the influence of Roman law gradually increased. The French codification was imposed on the Netherlands in 1810/11 and remained in force until 1838 in which year national codes were promulgated; only a few differences were created between French and Dutch law, mainly in the area of private law.

(2) Matrimonial property

Under the 1838 code the husband was the head of the family and administered the property of the wife, if the couple were married under the community régime. The wife had no legal capacity. By an Act of 14th June 1956 the spouses were declared equal and the wife was given full legal capacity. A new Family Law came into force on 1st January 1970 regulating matrimonial property and the husband's responsibility for administering the community property ceased.

Spouses are still married in community of goods if they have not made any arrangements to the contrary before the wedding; the complete community covers all the present and future property of both spouses (and also all their debts) unless a donor decides that a particular gift should not form part of the community. Before the contractual incapacity of the married woman was abolished in 1956 the community was administered solely by the husband but now each spouse administers his/her own goods subject to the rights of the community. When the marriage ends the communal property is divided into two and shared.

The system of community property can be varied by marriage settlement but 93 per cent of Dutchmen do not make a marriage settlement : of the remainder 73 per cent choose to totally exclude the community system and 10 per cent choose "community of benefit and income".

(3) Income tax

As noted above the matrimonial property régime in the Netherlands was amended in 1970 and on November 7th 1972 the Netherlands overhauled its personal income tax law : the new income tax régime came into force on 1st January 1973. Now a married woman pays her own taxes on earnings independently of her husband but the rates of tax on unearned income are still calculated by aggregating the the private wealth of both spouses.

For the purposes of the allowances, taxpayers are divided into four groups and the allowances for 1981 were:-

Group 1	Married women	2,278
Group 2	Single persons under 35	6,599
Group 3	Single persons over 35	8,871
Group 4	Married men	11,371

It will be seen that this system is very similar to that in the United Kingdom; there is a right to disaggregate earnings only and, as far as allowances are concerned, a married man is entitled to an allowance which is about $1\frac{3}{4}$ times that of a single person, with an additional allowance being available against a wife's earnings bringing the total allowances available to a married couple slightly in excess of those available to two (young) single persons.

(4) Tax avoidance

It has been stated that the reason for the retention of the aggregation of investment income was to counteract tax avoidance.

(5) Children

There are no tax allowances for dependent children but child benefits are payable

8. Conclusion

The six civil code countries examined in this Chapter show a completely different approach both to the law of matrimonial property and to income tax law from the commonwealth countries described in Chapter 11. Each country

promulgated a civil code in the nineteenth century which regulated the rights and duties of spouses and the ownership of matrimonial property and each country has made a number of amendments to those provisions, in four cases within the last ten years. Each country now operates a system of community property for spouses, although this has not always been the case in Italy. The extent of the community property differs from country to country but basically it gives each spouse a right to a one-half share in the goods acquired during the marriage. In four cases, as a result of recent amendment, the community is administered jointly by the spouses, in the other two cases (France and Belgium) the community is administered solely by the husband. In all countries except France there is a written constitution guaranteeing equality of all persons before the law. For income tax purposes, two countries (France and Luxembourg) adopt statutory income splitting by the operation of the very favourable quotient system; the same system also applies in Germany but, in addition, the spouses each have the right to elect for individual taxation and individual taxation applies mandatorily in Italy. Belgium adopts a system of its own.

Disaggregation applies only to low-earning two-income families but where aggregation is retained the allowances available to spouses are more than twice those available to two single persons; in other words favourable treatment is available for a nil or low income spouse but the disadvantages of aggregation still apply to high income couples, once the benefit of the favourable allowances has been offset. The Netherlands system is very similar to

that of the United Kingdom although there is separate accountability. As far as children are concerned, both France and Luxembourg operate the very favourable quotient system; aggregation of a child's income with that of its parents used to operate in Germany but was declared unconstitutional in 1964; it still operates in Belgium but there it is accompanied by child allowances : child allowances are also available in Italy but there is no aggregation. There are no child allowances in the Netherlands, but there are child benefits.

CHAPTER 13 - THE SCANDINAVIAN JURISDICTIONS

Section 1. Introductory.

Section 2. Norway.

- (1) Matrimonial property
- (2) Income tax
- (3) Children

Section 3. Denmark.

- (1) Matrimonial property
- (2) Income tax
- (3) Children

Section 4. Sweden.

- (1) Matrimonial property
- (2) Income tax
- (3) Children

Section 5. Conclusions.

CHAPTER 13

SCANDINAVIAN JURISDICTIONS

Section

1. Introductory.
2. Norway.
3. Denmark.
4. Sweden.
5. Conclusions.

1. Introductory

So far in this Part the tax treatment of the family unit has been examined in ten countries; in five, individual taxation is the rule (Australia, New Zealand, Canada, Ireland and Italy); in three, the favourable quotient system operates (France, Luxembourg, Germany). The remaining two countries (Belgium and the Netherlands) operate a system which has features in common with the present system in the United Kingdom but Belgium compensates for some of the disadvantages of aggregation by giving a married couple favourable allowances.

The picture presented would, it is thought, give an unbalanced view of overseas jurisdictions if no reference were made to the Scandinavian countries, particularly Norway, Denmark and Sweden. These three countries have all promulgated laws regulating matrimonial property rights under a régime of "community of surplus"; predictably

they all operate an aggregation system for income tax purposes but each has now reached the stage of disaggregating a wife's earnings (but not her investment income). To this extent these countries reflect the present system in the United Kingdom but the identification is not complete as in each country some compensatory factor is present; in Norway spouses get more than double allowances and better rate bands than single persons, and in Sweden and Denmark spouses get double allowances with the right for one spouse to utilise the unused portion of the other spouse's allowance (similar to the system of "transferable allowances" proposed in the Green Paper).

In Denmark and Sweden there is separate accounting but joint liability applies in Norway unless an option for separate assessment is made : no country operates a system of husband's accountability.

2. Norway

- (1) Matrimonial Property
- (2) Income tax
- (3) Children

(1) Matrimonial property

In the Scandinavian countries the property relations of spouses have, since the Middle Ages, been regulated according to variations of the community of property systems. In the 1920's the Scandinavian marital property law was changed by new uniform legislation; in Sweden this was the Marriage Code of 1920; in Denmark the Act of the Legal Effects of Marriage in 1925 and in Norway the Act on the Property Relations between spouses of 1927. Prior to the

1920's the community of property system had provided for the community to be administered by the husband but after the reforms the community became a "community of surplus" administered equally by the spouses and divided equally between them on the termination of the marriage.¹ The law, in fact, recognises various matrimonial systems but the system of "community of surplus" operates automatically without the need for any positive act by the spouses.²

(2) Income tax

A husband is normally taxable on his own income together with that of his wife, but where both spouses are in receipt of earned income then either spouse may claim that the one with the smaller income be separately assessed in respect of such income. Although, therefore, aggregation of investment income applies, there are two favourable compensatory factors for married persons; first a married couple obtains twice the personal allowances available to two single persons with the addition of a further smaller deduction from the earned income of the taxpayer's wife; and secondly the rate bands applicable to spouses are approximately $1\frac{1}{2}$ times those applicable to single persons at the lower ranges.³

In addition to the right to disaggregate the lower earned income there is also an option for separate

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1. Scandinavian Studies in Law 1963 Vol.7. Allocation of Taxable Income and net wealth between spouses. Anti Suviranta, p. 153.
 2. Danish and Norwegian Law: A General Survey, edited by the Danish Committee on Comparative Law; p. 55.
 3. Income taxes outside the United Kingdom. And see also The Taxation Act of 18th August 1911, Chapter II, Norwegian Laws etc. Selected for the Foreign Service, p. 567.

assessment without alteration of total liability, similar to that available in the United Kingdom.

(3) Children

Where a child allowance is claimed, children are assessed with parents; income from earnings is, however, always assessed separately. Where the child is in receipt of income from assets transferred by a parent, the income is assessed on the parent.

3. Denmark

- (1) Matrimonial property
- (2) Income tax
- (3) Children

(1) Matrimonial property

The matrimonial property régime in Denmark is regulated by Act No. 56 of March 18th 1925; in the absence of contrary agreement a system of community property applies which gives each spouse a right to a one-half share in the community property at the end of the marriage.

(2) Income tax

Married persons are normally taxable on their aggregate income with the exception of a wife's income from an independent activity. Each individual is entitled to a basic deduction from tax (in 1981 16,000 kroner); a married man, however, receives twice this (32,000 kroner) if his wife has no separately assessed earned income. Where the wife does have separately assessed earned income, the unutilised portion of the deductions due to one spouse may

be set off in charging the income of the other.

(3) Children

Children are separately assessed on their whole income except where such income is derived from gifts from their parents; there are no tax allowances for dependent children but there are cash benefits.

4. Sweden

- (1) Matrimonial property
- (2) Income tax
- (3) Children

(1) Matrimonial property

Sweden's Code of Laws, originally enacted in 1734, was revised substantially in the early years of this century and is still undergoing revision.¹

"The 1920 reform meant that the prerogatives of the husband as head of the family and sole administrator of the community of marital property were done away with and both spouses were put on an equal footing as regards assets and liabilities".

The Marriage Code of 1920 retained community of marital property to the extent of arranging for an equalisation of assets on the termination of the marriage.

"The matrimonial property - or to be more precise the net assets of each spouse - is pooled and divided into two parts. This system is often referred to as a "deferred" community system. The spouse holding the larger balance has to transfer half of the difference to the other spouse".

As in Norway and Denmark the legal régime of marital

1. An Introduction to Swedish Law : Sig. Stromholm. Vol.1.

property may be modified by marriage contract.

(2) Income tax

Each spouse is taxed individually on his or her earned income; however, for unearned income, separate accounting is retained but, in order to determine the rates, the joint investment income is aggregated with the earnings of the higher earner, after each spouse has enjoyed a slice of investment income taxed individually. Each individual receives an allowance of 6,000 kroner but if one spouse has an income (earned or unearned) which is less than that amount, then the allowance as such cannot be transferred but a corresponding credit against tax is given to the other spouse. In addition, one spouse is also usually entitled to any deductions to which the other spouse was entitled but unable to claim because of insufficient income.

Prior to 1971 the tax treatment of married couples in Sweden was very similar to that in the United Kingdom but the system was criticised

"on the ground that for tax, as well as for other purposes, the law should give equal treatment to every individual, married or unmarried, male or female. Taxation, it was argued, should not depend on sex or marital status".¹

In 1965 the Government appointed an expert committee to consider how joint taxation could be replaced with individual taxation; after the committee's report, reforms were introduced in 1970 to reflect the new policy of individual taxation.

1. The Tax System in Sweden, by Martin Norr and others.

"But the full change from joint to individual taxation could not readily be made at one time...Joint taxation therefore continues as to the unearned incomes of husbands and wives...The aim however is gradually to remove the remaining elements of joint taxation to make the system as nearly individual as possible".

It is interesting to note that in order to effect the 1971 reform income tax rates were reduced for lower and middle bracket taxpayers and increased for upper bracket taxpayers; the loss in revenue was made up by an increase in the rate of VAT from 10 per cent to 15 per cent and an increase in the upper rates of the net wealth tax and the succession and gift taxes.

(3) Children

For income tax purposes a child's income, whether earned or earned, is not aggregated with the income of his parents: if the child's income exceeds his personal allowance a separate return must be filed by his parent or guardian on his behalf.

5. Conclusions

The development of matrimonial property in the three Scandinavian countries mentioned has followed a uniform course, as has also the development of the income tax system as it affects married persons. Although all three countries still retain aggregation of investment income, no country has a system of husband's accountability and all three operate a system of allowances that is more

advantageous to the one-earner couple than the system in the United Kingdom.

CHAPTER 14

THE UNITED STATES OF AMERICA

Section

1. Matrimonial Property.
2. Income Tax.

1. Matrimonial Property

It is not possible within the scope of this thesis to examine each foreign jurisdiction and attention has therefore been focused on countries falling within three main categories of jurisdiction i.e. common law, civil law and Scandinavian law. However, it is thought that a short note of the position in the United States would not be without interest. The United States combines elements of both the common law and civil law jurisdictions; in the States of Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas and the State of Washington the community property system applies whereas in the other states the common law system of separate property prevails : statutes similar to the Married Women's Property Act have been enacted which give a wife almost unlimited control over her real and personal property.¹ However, even in those states which have inherited the principles of the common law, special provisions apply to prevent the sale or mortgage of the "homestead" without the concurrence of

1. American Law of Real Property. Little Brown & Co.
Vol.1. See also Powell on Real Property Vol. 1. p.117.

both husband and wife.

The property laws of each state, therefore, reflect the historical provenance of the legal systems to which they owe their origin: the states which have adopted a community of property system were originally governed by French or Spanish laws; the states which have adopted a common law system were originally governed by English law. Income tax is, however, a federal tax and it is interesting to note that the rules adopted to govern the taxation of husband and wife owe much to both systems.

(2) Income tax

The basic principle is individual taxation but married couples may opt to be taxed under a "quotient" system; in this case a joint return is filed and statutory income splitting is applied; however, unlike the other jurisdictions which operate a quotient system (Ireland, France, Luxembourg and West Germany) the rate bands applicable to a married couple are not double those of a single person although they are greater; there is a personal exemption for each tax payer which can be claimed for a spouse also; and there is a minimum exemption limit of 2,300 dollars for individual tax payers, 3,400 dollars for married couples filing jointly and 1,700 dollars for married couples filing separately.

CHAPTER 15

INTERNATIONAL COMPARISONS - CONCLUSIONS

The international comparisons reviewed in this Part of this thesis show that each country differs from each other country in at least one respect but that there are a number of similarities between countries in the same type of jurisdiction : the common law countries favour individual taxation and the civil code and Scandinavian countries favour joint taxation but in the latter case a number of countries operate the favourable quotient system or at least favourable rate schedules.

If the three principles of aggregation, accountability and allowances are analysed it will be noted that no other country is quite like the United Kingdom. Even where aggregation is retained only two countries operate a system of husband's accountability (France and Belgium); the other countries are able to operate a partial aggregation rule with either joint or separate accountability; and as far as allowances are concerned, most countries give all spouses (even one-income couples) two allowances, the only exception to this rule being the Netherlands.

It is thought that these international comparisons are of interest for four main reasons; first they illustrate the fact that there is no one system which is 'ideal' in all respects - each system has adapted to the circumstances in the country in which it operates; secondly, they illustrate the fact that a number of concepts which have been rejected in the studies and criticisms of the

United Kingdom system, for example, disaggregation, or the introduction of the quotient system, or the system of transferable allowances, can and do work perfectly well in other jurisdictions; thirdly, they illustrate a common theme of development and change over the years; and finally they illustrate the fact that the tax laws bear a close relation to the property laws in each country and that developments in matrimonial property law frequently lead to developments in income tax law.

In considering, therefore, a system of taxation of husband and wife for operation in the United Kingdom the conclusion would appear to be that it is to the common law jurisdictions that one must look for guidance rather than to the civil law or Scandinavian jurisdictions and, as has been noted, all the common law jurisdictions now operate a system of individual taxation.

PART IV - CONCLUSIONS AND RECOMMENDATIONS

CHAPTER 16 - THE DIRECTION OF REFORM

Section 1. Introductory.

Section 2. The Future of the Aggregation Rule.

- (1) Introductory
- (2) The retention of the rule
- (3) Alternatives to the rule
- (4) Abolition of the rule - individual taxation
- (5) The termination of marriage
- (6) Overseas jurisdictions
- (7) Conclusions

Section 3. The Future of the Accountability Rule.

- (1) The present system
- (2) Joint liability
- (3) Individual liability
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- (1) The position on abolition of aggregation
- (2) The position under individual taxation
- (3) The married woman's right to a full personal allowance
- (4) The nil or low income spouse
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- (6) Overseas comparisons
- (7) Support for dependants
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- (11) The cash benefit alternative
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Section 5. Tax Avoidance.

- (1) Prohibitions on covenanting income
- (2) Transfers of income-producing assets
- (3) Overseas comparisons
- (4) The principle of individual taxation
- (5) Position on termination of marriage
- (6) Conclusion

Section 6 - The Capital Taxes.

- (1) Capital gains tax
- (2) Capital transfer tax
- (3) Conclusion

Section 7. Children.

- (1) Introductory
- (2) Aggregation
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- (4) Tax avoidance
- (5) Conclusions

PART IV

CONCLUSIONS AND RECOMMENDATIONS

Chapter 16 - The Direction of Reform.

Chapter 17 - Conclusions.

CHAPTER 16

THE DIRECTION OF REFORM

Section

1. Introductory
2. The Future of the Aggregation Rule
3. The Future of Husband's Accountability
4. The Future of the Allowances
5. Tax Avoidance
6. The Capital Taxes
7. Children

1. Introductory

The objective of this thesis is to determine a method for taxation of the family unit, bearing in mind changing economic and social conditions. So far, this thesis has summarised the existing position in the United Kingdom; has traced the historical development of the underlying principles; has compared the tax treatment of the family during marriage with the tax treatment after

the termination of marriage; has analysed the studies and criticisms of the present system; and has examined the way in which the family is taxed in a number of overseas countries. This Part will consider the reforms which would be required to bring the tax treatment of the family unit into line with current conditions.

It is considered that the future of the income tax rules as they affect husband and wife must consider separately the three principles of aggregation, accountability and the allowances; a deficiency of some previous studies¹ has been a failure adequately to differentiate between these three principles which, although interdependent, are separate concepts. The subject of tax avoidance is frequently raised when the future of the taxation of husband and wife is discussed and this will therefore be examined in conjunction with the future of the capital taxes. Finally, the position of children will be considered.

2. The Future of the Aggregation Rule

- (1) Introductory
- (2) The retention of the rule
- (3) Alternatives to the rule
- (4) Abolition of the rule - individual taxation
- (5) The termination of marriage
- (6) Overseas jurisdictions

(1) Introductory

Although section 37 Taxes Act 1970 provides for a complete aggregation of the incomes of husband and wife, the principle was widely breached by the enactment of section 23 Finance Act 1971 which provided for an election

1. cf. The Meade Report; The Green Paper; Macdonald (IFS).

for the separate taxation of wife's earnings. However, the aggregation rule still retains three major compulsory applications, namely : the aggregation of the investment incomes of husband and wife; the restriction of the reliefs (e.g. mortgage interest relief) available to a married couple so that the two persons only receive one set of reliefs; and the rendering ineffective of inter-spouse transfers of income or assets for tax purposes. The future of the aggregation rule could lie in one of three directions : either in its retention; or in its replacement by an alternative system; or in its complete abolition when husband and wife would automatically become taxable as two single individuals. Each of these three possibilities will now be considered in turn; a reference will then be made to the position on the termination of marriage and finally the situation in some overseas countries will be compared.

(2) The retention of the aggregation rule

Fifteen reasons have been advanced over the years since the introduction of the aggregation rule to support its continued existence. Before reaching any conclusion as to whether the rule should or should not be retained each of these reasons will be referred to briefly.¹

R1.² Aggregation neutralises proportions of income in household. First mentioned in 1894, this reason for retaining the aggregation rule has received support from

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1. The reasons are more fully developed in Chapter 7.
 2. The reasons for retention are preceded by the letter 'R' to distinguish them from the alternatives to aggregation (A) and the fundamental reasons for the repeal of Section 37(F).

distinguished quarters, including the Colwyn Commission, the Radcliffe Commission and the Meade Committee; it does, however, ignore the fact that income tax is a tax on individuals, not on households, and that it is fallacious to introduce the "household" as a comparative base when discussing married couples and not when discussing other households. The argument has lost much force since the general acceptance of the disaggregation of wives earnings, especially by the Meade Committee; it is now generally accepted that a two-earner couple will, and should, pay less tax than a one-earner couple with the same total income and if the principle is acceptable for earnings it should be equally acceptable for investment income.

R2. Reform of the rule would cost too much. First used in 1894, this reason for retaining the aggregation rule has been used on nine occasions since. The cost of the change in 1894 was £500,000 but in 1955 it had risen to £143M. However, this latter figure could also have included the 'cost' of replacing the married man's allowance with two single persons allowances and the cost of disaggregation alone is not given. The current cost of disaggregation will depend on the number of wives whose investment income will be taxed at a lower rate and the number of wives who would take advantage of an additional set of reliefs or of transfers of income or assets from their husbands.¹

In considering the 'cost' of any change two points are of importance : first, the tax base should not be

1. See "Investment Income of Husbands and Wives". Background Paper 3 for the Green Paper on Taxation of Husband and Wife: Note by the Inland Revenue.

confused with the tax yield : if the base is changed (e.g. by disaggregation) then the yield can remain the same if the rates are subsequently adjusted, although this can have political repercussions; secondly, it is necessary to distinguish the cost to the Exchequer resulting from any change from the administrative costs which flow from the change. As far as disaggregation is concerned it is thought that the administrative costs of a change would be slight, as one result of the abolition of the rule will be to eliminate the need to liaise between the tax offices of husband and wife; a further result would be the abolition of the options for separate assessment and separate taxation and also substantial reductions in the administrative complications which arise on marriage or the termination of marriage.

R3. Married couples are members of one household and have a joint income. This reason against the reform of the aggregation rule was first put forward in 1907 and has been repeated on a number of occasions since; the irrelevance of the "joint household" concept is considered at R1 above; as far as the concept of "joint income" is concerned it is not correct to say that husband and wife have a joint income in the United Kingdom, unlike the continental countries.¹ There is no law of community property in this country; since 1882 a system of separate property has been established and it is the fact that the property system differs from the tax system that has given rise to the accounting difficulties mentioned in Chapter 8.

1. See Chapter 12.

R4. Aggregation does not stop people from marrying. Although this argument against reform was put forward with conviction in 1907, and again as recently as 1955, it has not been mentioned since; in the debates on the new clause in 1969 Mr. Jenkin stated that the tax laws were preventing at least one couple from getting married and an Article in the Times on Saturday 11th July 1982¹ described the views of a couple with two children who decided not to get married because of the adverse tax laws.

R5. All cases of hardship are met by partial disaggregation of wives earnings. This reason against the total abolition of the aggregation rule is somewhat more subtle as it is true to a limited extent. However, the tax system operates on a principle of horizontal equity and not on a "hardship" factor for other taxpayers and it is irrelevant to introduce such a factor for married women only. If the "hardship" factor were extended to other taxpayers it could be used to justify the confiscation of incomes in excess of a minimum subsistence level. Finally, it could be regarded as a "hardship" for a married woman to be taxed at her husband's higher tax rate on a small amount of, say, building society interest earned from savings made from her own earnings.²

R6. Disaggregation would lead to tax avoidance through transfers of property. First mentioned in 1909 and repeated by Colwyn, Radcliffe and Meade, this argument against reform

1. By Lorna Bourke.

2. See Background Paper 3 which indicates that most investment income consists of building Society interest or interest not taxed before receipt (including National Savings Bank interest); page 13, paragraph VII.

is repeated in the Green Paper. It does, however, overlook a number of points. First, disaggregation would result in a number of changes which are unrelated to inter-spouse transfers (e.g. doubling of reliefs and separate taxation of wives investment income derived from earnings) and it appears unjust to deny these reforms merely because tax avoidance by income splitting might take place. In any event, although it is assumed that income splitting is undesirable, this has not been justified : non-married persons can make tax effective property and income transfers so long as they are bona fide but the loss of control is a genuine deterrent to abuse and the yield from the capital taxes on such transfers goes some way towards compensating for loss of income tax.¹ Even if the conclusion were to be reached that inter-spouse transfers should be controlled this could be effected by the enactment of "settlement" provisions similar to those at present in force and which apply to transfers for the benefit of minor children and this could then be accompanied by the abolition of the aggregation rule.

R7. Husband and wife get advantages with death duties.

Mentioned in Colwyn, Radcliffe and Meade, this statement is more true today than it was when it was first mentioned (1914). However, the present capital transfer tax exemption, although generous, is not considered to be an adequate recompense for the refusal to disaggregate incomes : aggregation penalises couples with two incomes

1. See further Part 5 of this Chapter - tax avoidance
Page 624.

whereas the capital transfer tax exemptions only assist couples where one spouse wishes to make large transfers of capital to the other; the two categories of couple are not identical. To the extent that there is any validity in this point the solution is to disaggregate incomes and then adjust the capital taxes.¹

R8. Disaggregation would not be used in practice. Put forward as a reason against reform in 1914, this argument has, understandably, not been used since. The responses to the 1980 Green Paper have been overwhelmingly in favour of a change to individual taxation.

R9. Disaggregation would result in the abolition of the married man's allowance. The married man's allowance was first introduced in 1920 and this reason against reform has been mentioned by the four main studies published since that date (Colwyn, Radcliffe, Meade and the Green Paper). However, it shows a deep confusion between the two distinct principles of aggregation and the allowances. It would be perfectly possible to effect disaggregation by the repeal of sections 37-42 Taxes Act without any amendment at all to the allowances which are governed by section 10 Taxes Act. Although it is most likely that the allowances would receive attention at the same time, and that the married man's allowance would in fact be abolished, it could be replaced by an even more advantageous system.²

R10. The obligations of marriage are recognised by the married man's allowance. This reason against reform also

1. See further Part 6 of this Chapter - The capital taxes - Page 627.

2. See further Part 4 of this Chapter - the future of the allowances.

confuses the principles of disaggregation and the allowances : the married man's allowance is in fact not adequate to recognise the obligations of marriage within the system of the allowances¹ and, further, the system of aggregation cannot be justified merely by saying that the system of allowances is satisfactory as the two concepts are distinct.

R11. At lower income levels a married couple are better off than two single persons. This reason against reform has only been available since 1942 when the wife's earnings allowance was increased to that of a single person with no corresponding reduction in the married man's allowance. The argument is mainly concerned with the allowances, and not with aggregation, although perhaps it is true to say that some low income couples are better off than two single persons but this can only occur when the wife has little investment income but also has earnings, and where the wife has no wish to avail herself of a second set of reliefs.

R12. Husband and wife both earning pay less tax than if all income earned by husband. In a progressive tax system this statement is true for all taxpayers so that where an income of any size is enjoyed by one person he will pay more tax than would be paid if the same income were enjoyed by two or more persons. This statement cannot, therefore, be used to support the aggregation rule.

R13. Married women work for satisfaction and not for money. Originally put forward in 1969 to explain why a proposal for disaggregation of wives earnings was not then supported, this reason has wisely not been mentioned since; it does,

1. See further Part 4 of this Chapter - The future of the allowances.

however, illustrate the lengths to which Government Ministers will sometimes go in attempting to defend the status quo.

R14. The Royal Commission did not favour disaggregation.

The views of the Royal Commission (in the Radcliffe Report) are fully discussed in Chapter 7;¹ although the Commission did not favour disaggregation it has been noted above² that the inability of the Commission to see married couples as two persons rather than one seriously affected the quality of their recommendation.

R15. The present rule only adversely affects a few higher-rate taxpayers. This reason against reform is not in fact correct; the aggregation rule does not only affect a few higher-rate taxpayers. It affects any married woman with investment income of any amount whose husband either pays higher rate tax or where the couple have joint investment income in excess of the threshold so that the additional rate applies. About 2½M wives receive investment income³ either jointly with their husbands or separately, and of total investment income, 32 per cent is received by wives.⁴ Although the figures make it clear that most investment income is well within the threshold, so that the additional rate is not often relevant, it is likely that many wives with investment income will be married to husbands who are taxed at the higher rate on their earnings.⁵ The rule

1. Page 361.

2. Page 370.

3. Background Paper 3 page 5.

4. Background Paper 3 page 12 (iii).

5. Although there are no statistics to support this.

therefore adversely affects women who are married to higher rate taxpayers, even though their own investment income is small; it also adversely affects all couples where advantage could be taken of a second set of reliefs.

Even if the aggregation rule did only adversely affect a few higher rate taxpayers, that is no reason why it should not be reformed: an injustice to one category of taxpayers is still an injustice which should be remedied : this need.. not result in any additional burden on standard rate taxpayers as it should be possible to adjust the higher rates of tax and bands so as to ensure that the burdens are shared equally between all categories of higher rate taxpayers.

Conclusion

From the above it will be concluded that the retention of the aggregation rule cannot be defended and, as it perpetuates an injustice against married persons, it should be repealed. The question then arises as to whether it should be replaced by one of the alternatives to aggregation or merely abolished leaving a system of individual taxation. Both possibilities will now be reviewed.

(3) Alternatives to the aggregation rule

During the years since the aggregation rule was introduced no less than fourteen alternatives have been proposed and each will now be examined.

Al. Partial disaggregation of wife's earnings only. Originally introduced in 1894, abolished in 1920 and re-introduced in 1971 the partial disaggregation of wife's earnings is still the only possible alternative to the aggregation rule but it

is not an adequate alternative to complete disaggregation; apart from the fact that the areas of aggregation which remain create injustice and a tax on marriage, the procedural aspects of the option can cause difficulties; because the exercise of the election results in the loss of the married man's allowance, both spouses have to consent to its exercise and there is thus no entitlement for a married woman to have her earnings separately taxed : if her husband refuses to join in the election her earnings are taxed at his highest rate. Although it is possible for separate taxation to operate with separate accounting, this requires the additional exercise of the option for separate assessment with all the resulting complexities.

A2. The quotient system. Originally proposed in 1907 and discussed by Colwyn, Radcliffe and Meade, and again considered in the Green Paper, the quotient system is a genuine alternative to disaggregation; under this system the incomes of husband and wife are added together and then halved and the allowances and rate bands are applied separately to each half. This system is most advantageous for a married couple and would give married persons advantages as compared with single taxpayers, especially where one spouse has a nil or low income. It is tempting to put forward the quotient system as the ideal way in which to tax married persons but it is thought that on the whole the system should not be recommended for adoption in the United Kingdom for the following reasons:-

- (1) The quotient system is adopted in a number of

continental countries¹ where the system of matrimonial property is that of the "community" where the spouses have a joint interest in assets acquired during the marriage; as the quotient system has to operate through joint accounting, with either husband's or joint liability, it is particularly appropriate to community property systems. However, in the United Kingdom a system of separation of goods has existed since 1882 : the difficulties which have arisen from the mismatch of the property laws and the accountability rules are fully discussed in Chapter 8 and it is thought that a quotient system would give rise to similar difficulties in the United Kingdom. Husband's accountability is not likely to be acceptable and joint liability would remove the privacy at present enjoyed by married men while at the same time placing a liability for her husband's income tax on a wife with nil or low income.

- (2) The history of the aggregation rule in the United Kingdom reveals how difficult it has been to persuade the authorities to reduce or eliminate the disadvantages of married persons; it is thought that the recommendation of a quotient system would stand very little chance of success and that it would be more advisable to recommend reforms which might have some chance of being acceptable.

1. France, Luxembourg, Germany; it is also available as a very recently (1980) introduced option in Ireland and also in the United States where a number of states operate systems of community property for married persons.

A3. Partial disaggregation of all income up to a specified limit. Originally put forward in 1914, this alternative to aggregation would meet the criticisms of those who consider that complete disaggregation would only benefit a few higher rate taxpayers, but it has a number of disadvantages. First, it would not wholly remove the tax on marriage; next, because the limit proposed is a joint limit, a wife's entitlement to partial disaggregation of her investment income could depend completely on the amount of her husband's earnings and investment income. Again, the proposal does not assist in removing the other adverse effects of aggregation, i.e. the loss of reliefs etc; finally, a system of joint accounting would be required unless husband's accountability was retained : the disadvantages of this are mentioned in A2 (1) above.

A4. A percentage deduction from the tax paid by a married couple. Also proposed in 1914, this was another somewhat desperate attempt to make some inroad into the aggregation rule but it is not considered to be an adequate alternative to complete disaggregation : it would not remove completely the tax on marriage; it would require at least a system of joint accounting; it would be complicated to administer (especially under the PAYE system); and it does not assist with the removal of the other disadvantages of the aggregation rule.

A5. Separate taxation with wife allowance. This is the system adopted in Canada, Australia, New Zealand, Italy, and is optional in Ireland, Germany and the United States of America. It was mentioned by the Radcliffe Commission but not considered. The implications of the "wife

allowance" will be considered later¹ but as far as aggregation is concerned it is thought that this is the best, and only, alternative.

A6. Separate taxation with option to choose quotient system.

This is a mixture of A2 and A5 and is the system adopted in Ireland, West Germany and the United States; it has advantages over the straight quotient system (A2 above) as the spouses are given the right to individual taxation with separate accounting if that is desired with the option of choosing the quotient system if the disadvantages of joint accounting are acceptable. However, although this system could be regarded as an ideal alternative to aggregation it is thought that it would not be acceptable to the authorities for the reasons mentioned in A2 (2) above, namely that it would shift the balance of advantage in favour of married persons, and it is for this reason that it will not be recommended.

A7. Separate taxation of earnings : All investment income added to highest earner's income. Alternatives 7-10 were first proposed in the Meade Report and could be termed the Meade variants. This first Meade variant is in fact the system which is in force in Sweden although in Sweden each spouse enjoys a slice of investment income taxed individually; in Sweden the system operates with separate accounting. The disadvantages of this alternative are that it preserves the tax on marriage and further removes the possibility (albeit anomalous) which exists at present under which a couple where the wife has high earnings and high investment income and the husband has low earnings and low investment income;

1. See Part 4 of this Chapter - The future of the allowances.

can reduce the total tax liability by electing for disaggregation of the wife's earnings. Meade Variant 1 is therefore seen as a regressive alternative to the present system and it will be recalled that it was not considered to be satisfactory even in Sweden.¹

A8. Separate taxation for earnings. Quotient for investment income. This is Meade Variant 2 : the disadvantages of a quotient system for investment income are the same as those for the general quotient system mentioned in A2 above - namely, the necessity for joint accounting and the fact that the system is unlikely to appeal to the authorities as it would create positive advantages for married persons; it would also benefit couples with investment income (statutorily split) as against those with only earned income (no split); finally, it does not deal with the problem of the double set of reliefs.

A9. A married couple progressive scale of one and a half times. Meade Variant 3 is the system adopted, to a limited extent, in the United States of America which operates a quotient system where the joint incomes are aggregated but where the rate bands which are applied are not double those of a single person but somewhere in between. This Variant would benefit couples with one-earner where one spouse has a nil or low income but its disadvantages are that it retains joint accounting; it does not completely remove the tax on marriage for two earner couples and it does not adequately deal with the other effects of aggregation (e.g. reliefs). In the United States of America this system

1. See Chapter 13 page 577.

operates as an alternative to an individual system of taxation and can therefore be chosen in those cases where it is beneficial but it is not compulsory.

A10. Separate taxation of earnings : investment income taxed at $1\frac{1}{2}$ times scale on aggregated amount. This is Meade Variant 4 and is the system adopted in Norway; Norway is a "community property" country and joint accounting is more appropriate under such a system than it would be in the United Kingdom. This alternative would benefit couples where one partner has little or no investment income but it would not remove the tax on marriage for couples where entitlement to investment income is more or less equally divided and it does not deal with the other effects of aggregation.

A11. Joint taxation. Joint taxation is the first of four alternatives proposed in the Green Paper. It would alter the sense of the aggregation rule in section 37 Taxes Act so as to impose a joint liability on husband and wife for tax on the joint income. Apart from the fact that this alternative does nothing to reduce the quantum of tax payable as a result of aggregation, thus perpetuating the tax on marriage, it has the serious disadvantage of removing the privacy at present enjoyed by married men and imposing a new liability on married women who may have little or no income.

A12. Re-wording the aggregation rule. The second alternative proposed by the Green Paper was to re-word the aggregation rule so as to "treat the income of husband and wife as if it were one income"¹ rather than, as at present,

1. Paragraph 44.

to deem the wife's income as part of the husband's income. This alternative is of cosmetic significance only and solves none of the problems of aggregation.

A13. Option for individual taxation. The third alternative proposed by the Green Paper is an option for individual taxation; although, once the option was exercised, separate accounting would result, some exchange of information would be required before the option could be exercised; it would not be possible for one spouse alone to exercise the option; and it is not clear whether the option would remove all the other effects of aggregation; although perhaps a double set of reliefs would become available, the Green Paper does indicate that anti-avoidance measures would be needed to nullify inter-spouse transfers.

A14. Option for equal split of allowances and rate bands. This fourth alternative proposed by the Green Paper is really only a variant on the existing option for separate assessment; although it would, to some extent, simplify the accounting procedures under that option it is still open to the criticism that it does nothing to reduce the adverse effects of aggregation and, once again, spouses would not be able to check whether the Inland Revenue had correctly apportioned the allowances and reliefs.

Conclusion:

Of all the alternatives to aggregation which have been proposed only two are free of disadvantages, namely the quotient system and individual taxation. Although the quotient system is advantageous to married couples, it does require a system of joint accounting (or husband's

accounting) and this could cause difficulties in the United Kingdom; the system also perpetuates a special treatment for married couples and it is the underlying theme of this thesis that, as far as the tax system is concerned, husband and wife should be treated as two individuals; finally there is no certainty that the introduction of a quotient system would deal with the question of the reliefs. In a number of countries where the quotient system is adopted, it is in fact an alternative to individual taxation so married couples cannot lose. However, in view of the difficulties which have been experienced in obtaining equal treatment for married persons it is thought that the quotient system would not be likely to find favour with the authorities and, if it were to be recommended, there might be no reform at all. The conclusion, therefore, is that the only acceptable alternative to the present system is individual taxation.

(4) The abolition of the aggregation rule

As far as the aggregation rule is concerned¹ the adoption of individual taxation in the United Kingdom would be very simple to carry through into legislation as it would only be necessary to repeal sections 37-42 Taxes Act and to make a number of small amendments to the mortgage interest relief and similar provisions. It is considered that the individual basis of taxation is the only basis which provides a complete answer to the six fundamental

1. The subjects of accountability and allowances are dealt with later.

reasons for reform put forward on so many occasions in the past. The six reasons are:-

F1. The tax laws should follow the property laws. The existence of the present aggregation rule is a historical accident : if income tax had been introduced into the United Kingdom after the enactment of the Married Women's Property Act 1882, as happened in Australia, New Zealand and Canada, individual taxation would have been the rule. Even in 1894 the delay in the tax laws catching up with the property laws was considered to be "astonishing". Because there has never been any system of matrimonial community property in the United Kingdom, the otherwise advantageous "quotient system" would not really be appropriate in this country, and the same comment could be made of any system which would require joint accounting.

F2. Reform is demanded by many people. Reform of the present rule, and the introduction of individual taxation, was first demanded in 1894 and has been regularly demanded ever since : although a number of other alternatives have been put forward by learned commentators the fact remains that the taxpaying public is overwhelmingly in favour of individual taxation.¹

F3. The tax laws should be consistent between themselves. When estate duty was introduced the Inland Revenue chose to ignore all the reasons which had previously been put forward in favour of aggregation for income tax purposes and decided to treat husband and wife as separate persons (thus increasing their estate duty liability). Since then, the

1. IFS commentary on responses to the Green Paper.

capital taxes have developed with a number of inconsistencies;¹ it is thought that only with a system of individual taxation can all these inconsistencies be removed.

F4. There should be no penalty on marriage. Almost all those who have expressed an opinion on this subject have been forced to conclude that it is wrong to place a tax penalty on marriage : the removal of such a penalty can only be achieved by the introduction of individual taxation, which is neutral as between husband and wife, or by a quotient system which gives positive benefits to married persons. It is interesting to note that two countries which give married taxpayers an option to choose individual taxation or the quotient system (Ireland and West Germany) both have written constitutions which protect the equality of all citizens and the state of marriage and the family : if the United Kingdom had such a constitution the present tax laws would be repugnant to it. However, the quotient system is not recommended for adoption in the United Kingdom, for the reasons outlined above² and individual taxation is the only remaining system which removes all the tax penalties on marriage.

F5. Husband and wife are two persons and should be taxed as such. It is clear from many of the studies on this subject that the commentators believe that the fact of marriage detracts from the legal personality of the wife : this is not stated openly but it underlies many of the comments made; in particular the concepts of "husband and

1. See Chapter 5.

2. Page 599.

wife", "family" and "household" are frequently confused with many resulting illogicalities. These subconscious attitudes may have been formed by the tax legislation itself but in all other areas of the law the old rule that a wife's personality merged with that of her husband on marriage, has now been completely abandoned.¹

F6. The principle of equality gives the right to separate taxation. If income tax had been introduced in 1982 it would be impossible to justify any system for the taxation of spouses, other than the system of individual taxation.

(5) The termination of marriage

Before concluding this review of the future of the aggregation rule it may be helpful to consider how a system of individual taxation would apply on the termination of marriage and how it compares with systems adopted in overseas jurisdictions.

Under the present law aggregation ceases on the termination of marriage, whether by separation or death, when individual taxation is then applied. The introduction of a system of individual taxation during marriage would ease the transition on its termination and, further, would eliminate many of the inequities which now exist between married couples on the one hand and separated spouses on the other - it would remove the tax incentive to divorce.²

1. Cf *Midland Bank Trust Company v. Green* (1981) 3 ALL E.R. 744 (conspiracy) and *Routhan v Arum District Council* (1981) 3 ALL E.R. 752. (Rates).

2. See Chapter 3.

(6) Overseas jurisdictions

In Chapter 13 the conclusion was reached that it is to the common law jurisdictions that one must look for guidance in considering an appropriate system for the United Kingdom; Australia, New Zealand and Canada have always adopted individual taxation; Ireland has recently adopted individual taxation with the option of a quotient system and the United States of America has an option similar to that of Ireland. The predominating system adopted in the common law countries is, therefore, individual taxation.

(7) Conclusions

One is lead to the conclusion, therefore, that the aggregation rule should be repealed so that husband and wife are treated as separate individuals for all tax purposes; the remaining Parts of this Chapter proceed on the basis that such a reform should be implemented.

3. The Future of the Accountability Rule.

- (1) The present system
- (2) Joint liability
- (3) Individual liability
- (4) Conclusion

If the aggregation rule were abolished by the repeal of sections 37-42 Taxes Act and other consequential amendments, the principle of husband's accountability would automatically be repealed at the same time. It may be useful here to consider whether that would be desirable or whether some alternative rule should be introduced.

There are three possibilities : either to retain the present system, with the option for separate assessment, or to provide for joint liability; or to allow individual accountability to operate.

(1) The present system

The deficiencies of the present system are fully discussed in Chapter 8 and may be summarised as follows:-

- (1) Although the primary liability for making a wife's return rests on the husband, the Inland Revenue also have the additional right to require a wife to make a return, but this does not discharge the husband's responsibility;
- (2) A husband has complete privacy but the wife has none;
- (3) A husband is liable to make a return of his wife's income but has no right to demand the information from her and has no sanction if she refuses to provide it;
- (4) A husband is responsible for paying his wife's tax but has no entitlement to recover it from her;
- (5) A wife's repayments are sent to her husband unless she is taxed under schedule E and the joint income is not liable to higher rate tax;
- (6) A married woman's allowances, expenses and reliefs must be claimed by her husband and she cannot insist that such a claim be made;
- (7) A husband is entitled to his wife's reliefs and allowances, including mortgage interest relief

on interest paid by her on a mortgage on a house solely owned by her; she can only be given the relief with his consent.

An option for separate assessment will solve these problems but creates difficulties of its own : the accounting is extremely complex; the option is not widely known; neither spouse has sufficient information to check that the allocation of reliefs and allowances has been carried out correctly by the Inland Revenue; and the system of allocation of reliefs means that the spouses can guess at each other's income, thus reducing the privacy of the husband without giving complete privacy to the wife.

(2) Joint liability

It is clear that the present system is unsatisfactory and there is no doubt that joint liability and accounting would solve a number of the problems outlined above. However joint liability is open to the two serious objections that it destroys the husband's right to privacy and imposes a new obligation for the husband's tax on the wife, who may have little or no income.

(3) Individual liability

The conclusion is therefore reached that only a system of individual liability adequately meets all the objections made to the present system and to joint liability. Individual liability would also ease the transition at the termination of marriage when a married woman immediately becomes personally liable for her own income

tax affairs. Finally, all the overseas countries which adopt individual taxation also adopt individual liability.

(4) Conclusion

Although aggregation and accountability are separate concepts, and one can exist without the other, nevertheless it is concluded that if the aggregation rule in sections 37-42 Taxes Act is repealed, in order to abolish the principle of aggregation, then the repeal of the principle of husband's accountability should also follow, making husbands and wives individually responsible for their own tax affairs.

4. The Future of the Allowances

- (1) The position on abolition of aggregation
- (2) The position under individual taxation
- (3) The married woman's right to a full personal allowance
- (4) The nil or low income spouse
- (5) Transferred income
- (6) Overseas comparisons
- (7) Support for dependants
- (8) The transferable allowance
- (9) A compromise solution
- (10) The political implications of change
- (11) The cash benefit alternative
- (12) Conclusion

(1) The position on the abolition of aggregation

The future of the allowances does not depend on the future of the aggregation rule, although the concepts are not frequently distinguished. It may therefore be helpful to commence this consideration of the future of the allowances by describing the results of the repeal of the aggregation rule and the effect that would have on the allowances.

The repeal of sections 37-42 Taxes Act would leave unamended the provisions of section 8 Taxes Act; a husband would therefore remain entitled to the higher married man's allowance under section 8(1)(a) and to a further allowance in respect of his wife's earnings under section 8(2). However, a married woman would automatically become an individual in her own right and so she would, in addition, become entitled to her own single personal allowance under section 8(1)(b) for use against either her earned or unearned income. Clearly, this result would be over-advantageous for a married man and consideration would then need to be given to a restructuring of the allowances to accord with the system of individual taxation.

(2) The position under individual taxation

The logic of individual taxation would point towards the desirability of both husband and wife receiving a single person's allowance. This could be achieved by the simple repeal of sections 8(1)(a) and (2) leaving both husband and wife to be taxed as single individuals. The husband would lose the married man's allowance¹ and the wife's earned income allowance and the wife would gain an allowance of her own.

(3) The married woman's right to a full personal allowance

The view has been expressed on a number of occasions that a married woman should not be entitled to

1. The loss of the married man's allowance was strongly recommended by the Meade Committee and by the Equal Opportunities Commission.

use her personal allowance against investment income on the ground that this represents a "state subsidy" for the idle rich. Now this argument ignores two facts; first all men and single women are entitled to use their personal allowance against investment income and, indeed, a married man can use his higher married man's allowance against investment income; there is no justification for refusing a "state subsidy" to idle rich married women while retaining it for idle rich men and single women. If it were proposed to withdraw the personal allowance for all investment income then perhaps the point could be justified but the consideration of such a proposal is outside the scope of this thesis. Secondly, any special treatment of this nature for married women only, immediately creates a penalty on marriage. For these two reasons it is thought that there is no justification for restricting a married woman's personal allowance to earned income.

(4) The nil or low income spouse

It is clear that a system of individual taxation requires that special consideration be given to the case of the nil or low income spouse who is not able to utilise the full personal allowance : it is sometimes thought that the logic of individual taxation would result in such allowance being lost but this conclusion ignores the arrangements which at present exist for transferred income.

(5) Transferred income

All taxpayers who do not enjoy sufficient income

to utilise their personal allowances may take advantage of the deed of covenant procedure and use the balance of their allowance against income transferred to them by another taxpayer : the payer deducts tax at the basic rate on payment and the recipient reclaims tax from the Inland Revenue.¹ There is an argument that this procedure is anomalous² but the fact remains that it is at present available for all taxpayers other than married women and infant children; it is this procedure which, in effect, gives tax relief for maintenance paid on the termination of the marriage. When the aggregation rule is abolished the procedure would automatically become available for married women if the consequential amendments in the "settlement provisions" are repealed. Under this procedure, it is the recipient who is entitled to the allowance and who is entitled to claim a repayment from the Inland Revenue.

Accordingly, if no further legislation were enacted, and if the references to spouses were deleted from the "settlement provisions",³ this procedure would entitle a nil or low earning spouse to utilise the full personal allowance. However, it is appreciated that this particular procedure could give rise to administrative difficulties if used by the 6½M spouses with nil or low incomes; each would have to complete a tax return form and would be entitled to a repayment at the end of the tax year; further, details

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1. For a full description of the procedure see Potter and Monroe, Tax Planning with Precedents.
 2. See B.T.R. 1981 pp. 263, 282 and 284.
 3. Especially sections 445 and 447 Taxes Act.

of the payment would have to appear on the paying spouse's tax return : accordingly, for administrative reasons it may be desirable to look for a solution in another direction but the fact should not be lost sight of that the mere abolition of the aggregation rule and its consequential amendments would make the transferred income procedure available for married women in the same way as it is available for all other taxpayers.

(6) Overseas comparisons

In considering alternative solutions to the way in which a personal allowance can be enjoyed by a nil or low earning spouse it may be helpful to recall the ways in which the matter is dealt with in some overseas countries. The five countries operating the quotient system do not, of course, have any difficulty and all the other countries mentioned in Part III make some allowance for a supported spouse. Of the countries which adopt individual taxation, Australia gives a rebate for any person who contributes towards the maintenance of a spouse, daughter, housekeeper or parent, New Zealand gives a dependent spouse rebate (in practice also allowed for a de facto spouse) which is reduced by reference to the supported spouse's income; and Canada permits one spouse to claim the unused portion of the other spouse's allowance if a joint return is filed.

Of the continental countries, Italy gives a "wife allowance" which is twice the amount of the single allowance, but which is lost if the wife has income in excess of a stated limit; Belgium gives a complicated

system of allowances which are on the whole more advantageous than two single allowances and the Netherlands is the only country to follow the present United Kingdom practice of giving a nil-earner couple less than two single allowances. Of the three Scandinavian countries, Norway gives more than double allowances to a married couple and Sweden and Denmark give double allowances with the right to utilise the other spouse's unused portion.

It is considered that it is to the countries which have a common law jurisdiction, and which now operate individual taxation, to which one should look for guidance for the future of the United Kingdom system and here two distinct possibilities are revealed ; first the allowance given to the supporting spouse, as in Australia and New Zealand, possibly reducing by reference to the supported spouse's income as in New Zealand; or the use by one spouse of the unused portion of the other spouse's allowance if a joint return is filed, as in Canada. Each of these possibilities will now be considered.

(7) Support for dependants

There are a number of precedents in the United Kingdom tax system for an allowance to be made available to taxpayers who support others; the wife allowance was introduced on this basis and this was the basis of the old child allowance and is presently the basis of the additional allowance in respect of children for single parents contained in section 14 Taxes Act; it is also the basis for the housekeeper allowance under section 12 Taxes Act and

for the dependent relative allowance under section 16. A feature of all these allowances is that they are given to the supporting (and not to the supported) taxpayer. None of these allowances amount to a full personal allowance and indeed it is understood that no increase will be made in the housekeeper and dependent relative allowance as they are considered to be anomalous; but the additional allowance in respect of a child, in section 14, is substantial (being the difference between the married man's allowance and the single person's allowance) and is regularly increased in line with the personal allowances. Although this allowance does not regress according to the income enjoyed by the child, such regression was a feature of the old child allowance; Section 10(5) Taxes Act provided that where a child was in receipt of income in his own right in excess of a certain figure the child allowance was reduced by the amount of the excess. It would not, therefore, be difficult to enact a provision for a dependent spouse allowance equal to the full single personal allowance with a provision that the allowance should reduce by reference to the income (earned or unearned) of the supported spouse.

Here it may be noted that if, as in the old child allowance, provision was made for the reduction of the allowance only after income reached a (small) limit, then the supported spouse's right to privacy in respect of small amounts of investment income could be maintained and, to the extent that a pound for pound reduction would be a disincentive for the supported spouse to seek work, such disincentive would be reduced.

If a spouse allowance were enacted on these lines then there would be no advantages to be gained from the use of the deed of covenant procedure which would not then be utilised by married women. Throughout this thesis the point has constantly been made that married women should be treated in exactly the same way as all other taxpayers and it may therefore appear illogical to propose a new allowance for spouses only. Of course, such an allowance could be formulated as a dependent's allowance and made available to all taxpayers who supported other taxpayers with nil or low incomes, or perhaps limited to certain categories of dependent as in Australia. However, such taxpayers can, in any event, utilise the deed of covenant procedure and the 'spouses allowance' is in fact proposed on the basis that if a large number of supported spouses used the deed of covenant procedure, many administrative problems would be created. The 'spouse allowance' does not therefore create a new allowance only for spouses but merely proposes a special procedure for spouses to claim the allowance to which they are, in any event, entitled.

(8) The transferable allowance

The enactment of a spouse allowance on the lines proposed would in practice achieve the same result as the "transferable allowance" proposed in the Green Paper and in use in Canada. However, the transferable allowance has a somewhat different emphasis as its use requires the consent of the supported spouse, whereas the spouse allowance would be claimed solely by the supporting spouse. The

transferable allowance makes it clear that it belongs initially to the supported spouse and in Canada the allowance can only be transferred if the spouses file a joint return.

The principles underlying the transferable allowance are considered to be preferable but ultimately it is the most practical and acceptable system which will be adopted. It is thought that the requirement of a joint return might not be very acceptable in the United Kingdom as it would destroy the husband's right to privacy and would, in any event, represent a departure from the principles of individual taxation.

(9) A compromise solution

A compromise solution therefore might be to provide that the new spouses allowance could only be claimed by the supporting spouse if the supported spouse makes a claim that the allowance should be transferred : this could be done by the submission of a tax return showing a nil or low income and consenting to the use of the unused personal allowance by the supporting spouse. A requirement for married women to submit their own tax returns would have another advantage, namely, to assist in reducing tax evasion. Under the present rules a married woman is at no time obliged¹ (or even permitted) to make a return of her income and is under no legal obligation to declare it to her husband for inclusion in his return : the view has been expressed that very many married women

1. Except where an option for separate assessment is in force.

with low casual earnings completely escape the tax net in this way : if they were required to complete a tax return this position would be regularised. Alternatively, a simple claim would suffice and there is already a precedent for such a procedure in section 36 Finance Act 1976 which provides for the transfer of certain unused allowances and reliefs between the spouses in the first year of marriage.

(10) The political implications of change

Under the reforms proposed the higher married man's allowance would be lost but all married couples (including one-earner couples) would enjoy two single personal allowances. The two-earner couple (or rather, the husband of a two-earner couple) would lose; the one-earner couple would gain. It is thought that it is the loss of the married man's allowance by the husband of a two-earner couple which is contributing to the delay in reforming the present tax system : at present the higher married man's allowance is worth £5 per week to a standard rate taxpayer and politically it may be disadvantageous to reduce take-home pay by this amount : although the failure to enact reform is penalising the one-earner couple, this factor is not so widely appreciated and is therefore a less sensitive issue politically. Although this political difficulty is appreciated, and should not be underestimated in view of the reaction caused on the introduction of child benefit,¹ it is thought that sooner or later the issue

1. See Equal Opportunities Commission Consultative Document "Income Tax and Sex Discrimination" page 44.

will have to be faced and some way found of introducing reform with the minimum of reaction. The Green Paper proposes a system of "phasing" of allowances which could be adopted.¹

(11) The cash benefit alternative

Before leaving the subject of the allowances it may be helpful to explain shortly why the cash benefit alternative to the allowance for a dependant spouse is not favoured. First, it will be clear from what has been said that the present tax system will entitle a married woman to her own personal allowance when aggregation is abolished : it would be anomalous to remove this right from a married woman when it is enjoyed by all other taxpayers. Secondly, the proposed cash benefit is intended to be limited to those with children or other home responsibilities : these will be extremely difficult to define but, in any event, other taxpayers do not have to justify their entitlement to an allowance in this way and there is no reason, therefore, why married women should be obliged to do so. Next, the system of tax allowances and the system of cash benefits are constructed on different principles : a tax allowance is given to all individuals because they have personal identities; cash benefits are given in case of defined need only. Finally, tax allowances are a reduction from taxable income and reduce an individual's tax bill : cash benefits are paid to all persons, even those who do not pay tax, and have no reference to a tax

1. Paragraph 100.

computation.

There may be a case for the payment of a cash benefit to women with home responsibilities, in addition to their personal tax allowance, and this would, of course, benefit those with no taxable income, but such a consideration is outside the scope of a thesis on the tax treatment of the family.

(12) Conclusion

When the aggregation rule is repealed each married woman will become entitled to the single personal allowance in her own right for use against earned or unearned income. It is likely that the married man's allowance and the wife's earned income allowance will then be abolished leaving both husband and wife with a single allowance each. In order to simplify the utilisation of the allowance of a nil or low earning spouse it is suggested that a spouse allowance, equal to the single person's allowance, be provided for a spouse who supports another spouse such allowance to be reduced by reference to the income of the supported spouse. In order to preserve the principle of individual taxation the spouse allowance could be given conditional upon the supported spouse either completing a separate tax return form, showing a nil or low income, and authorising the use of the unused allowance by the supporting spouse or, alternatively, a claim procedure could be introduced, similar to that in section 36 Finance Act 1976, so that the unused allowance of the supported spouse may be transferred.

5. Tax Avoidance

- (1) Prohibitions on covenanting income
- (2) Transfers of income-producing assets
- (3) Overseas comparisons
- (4) The principle of individual taxation
- (5) Position on the termination of marriage
- (6) Conclusions

In many of the studies and criticisms of the present rule statements are made to the effect that, if the aggregation rule were repealed, it would be necessary to enact anti-avoidance provisions. These could take two forms : either a prohibition against covenanting income or a prohibition nullifying the tax effectiveness of transfers of income-producing assets. These will be considered separately.

(1) Prohibitions on covenanting income

There appears to be no justification for nullifying transfers of income between husband and wife when the procedure is available for all other taxpayers (except minor children). If an unmarried man can covenant income to a woman, the same procedure should be available to a married man. However, if the recommendations previously made in this Chapter on the future of the allowances are enacted the covenanting procedure would be superfluous : that procedure is only effective to utilise unused personal allowances and does not save any higher rate tax; if the personal allowances are utilised in the way described no advantages would be gained from covenanting.

(2) Transfers of income-producing assets

Under the new proposed allowance system transfers

of income producing assets would not be necessary in order to utilise the personal allowances but would be advantageous to equalise incomes and save tax when one spouse pays a higher rate of tax than the other. Before considering the justification for nullifying such transfers reference will be made to the treatment adopted in certain overseas countries.

(3) Overseas comparisons

It will be recalled that in five of the countries mentioned¹ a system of statutory income splitting has been adopted : thus, far from prohibiting tax avoidance through inter-spouse transfers, this is, in fact, effected by statute. Three of the countries mentioned² adopt an alternative system of individual taxation. Of the three remaining common law countries, two (Australia and New Zealand) permit bona fide transfers between spouses but give no substantial capital tax exemptions to spouses; Canada, on the other hand, has enacted detailed "attribution rules" on the lines of the settlement provisions in the United Kingdom, but does give spouses substantial exemptions from capital taxes.

From the above it will be seen that income-splitting by means of property transfers is not, of itself, considered to be unjustifiable in those overseas jurisdictions which adopt an individual basis of taxation, the only exception being Canada which has not adopted an individual basis for capital taxes.

1. France, Luxembourg, West Germany, Ireland, U.S.A.

2. West Germany, Ireland, USA.

(4) The principle of individual taxation

It is considered that a consistent application of a system of individual taxation requires that bona fide transfers of income producing assets between spouses should be recognised both for the purposes of income tax and the capital taxes. Where husband and wife are taxed separately such a transfer may effect a saving of income tax but this result would be achieved if the parties were not married and to render the transfer ineffective only for married persons would constitute a tax on marriage. Further, to be effective for income tax purposes, a transfer must genuinely pass the title to property without any reservation to the disponor; such a provision will, in itself, be a deterrent to abuse, especially in view of the current high divorce rate. Finally, any income tax saved as a result of equalisation of assets may be recouped from the capital taxes imposed on the transfer.¹

The alternative procedure, of prohibiting inter-spouse transfers, but retaining substantial capital taxes exemptions, is considered to be less satisfactory for three reasons : first, it does not accord with the principles of individual taxation which treat spouses in the same way as all other persons; secondly, it gives tax advantages to spouses who wish to transfer large amounts of capital to each other while penalising spouses who may be paying high rates of income tax. Finally, it ignores the fact that many spouses may already enjoy an equitable interest in the assets owned by the other spouse, which right would

1. See Part 6 of this Chapter.

become enforceable on divorce or death : a legal transfer of such rights may merely be an acknowledgement of an existing beneficial interest and should, therefore, be recognised as effective if bona fide and genuine.

(5) Position on termination of marriage

Once a marriage has been terminated by separation, bona fide transfers of property between the ex-spouses are fully recognised as effective for income tax purposes and such recognition where the spouses are married will help to reduce the present imbalance of the treatment of married spouses on the one hand and separated spouses on the other.

(6) Conclusion

The view is therefore taken that there is no justification for refusing to recognise as tax effective genuine bona fide transfers of income producing assets between spouses but that such transfers should be chargeable with the usual capital taxes which apply to other taxpayers. The capital taxes will now be discussed.

6. The Capital Taxes

If the recommendations previously mentioned in this Chapter are implemented and fully individual taxation introduced for husband and wife, consideration would have to be given to the capital taxes.

(1) Capital gains tax

Individual taxation would mean that each spouse would enjoy a separate set of reliefs, including the annual exemption and the principal private residence exemption. Capital gains tax would, in theory, become chargeable on disposals between spouses but as most of these would be for no consideration the general exemption under section 79 Finance Act 1980 would apply so as to render the disposal on a no gain no loss basis. The changes would be beneficial for spouses except in the unlikely case where one spouse sold an asset to the other where the gain was not covered by an existing exemption. One small disadvantage of the change would be that the losses of one spouse could no longer be set against the gains of the other.

(2) Capital transfer tax

Under a system of individual taxation each spouse would, as now, enjoy a complete set of exemptions but tax would otherwise be charged on transfers between spouses. However, with the recent reduction of cumulation to ten years, this disadvantage has been considerably reduced.

It would be for consideration whether some special relief should be retained for certain transfers between spouses on death. Australia provides such an exemption for small estates only and New Zealand provides a special exemption for a "Joint Homestead". However, it is thought that, in most cases, spouses will be entitled in any event to a half interest in the matrimonial home, either at law or in equity, and the current exemption limit will be

sufficient in most cases to cover the remaining half. Like other taxpayers, spouses would be entitled to make use of lifetime transfers to take advantage of the lower rates and of the ten year cumulation rule to transfer assets over a period of time. Clearly more capital transfer tax will become payable by spouses but it is thought that this would be acceptable if it were accompanied by a full change to individual taxation for income tax and capital gains purposes.

(3) Conclusion

Under a system of individual taxation spouses should be treated in all respects as other individuals, and this includes the capital taxes. The imposition of capital taxes on inter-spouse transfers would help to compensate for any income tax saving which might result.

7. Children

- (1) Introductory
- (2) Aggregation
- (3) Allowances
- (4) Tax avoidance
- (5) Conclusions

(1) Introductory

In considering the position of children in the family unit for tax purposes one is made aware of the paucity of information and comment. Whereas the tax treatment of husband and wife has been studied on a number of occasions, some in great detail, very little consideration has been given to the position of children.

In very many respects children are already treated

as individuals in the United Kingdom tax system : the extent to which this is satisfactory will be discussed against the background of the three principles of aggregation, allowances and tax avoidance.

(2) Aggregation

Apart from a temporary aggregation of the infant child's investment income between 1968 and 1972, and a recommendation that a child's wealth be aggregated with the parents for the purposes of wealth tax, a proposal to aggregate a child's income with the family would be unlikely to be acceptable in the United Kingdom. Only one of the countries mentioned in Part III¹ continues to aggregate a child's income but credits against tax are also available for each child so, in those cases where a child has little or no income, the provisions would result in a net gain. Italy abolished aggregation in 1974 and Germany abolished it in 1964 after it had been declared unconstitutional. France and Luxembourg both operate the very favourable family quotient system under which, although the child's income is aggregated with that of its parents the existence of the child results in a further division of the total family income before the rate bands are applied.

It is thought that if aggregation did exist in the United Kingdom, then a recommendation should be made for its repeal : children are separate persons in truth and should be treated as such for tax purposes. Even though the advantageous quotient system appears to be initially

1. Belgium.

attractive, it requires taxation of the unit of husband, wife and children and, for the reasons mentioned in Part 2 of this Chapter, the quotient system is not recommended for husband and wife.

(3) Allowances

The only allowances now available for children are those given to single (including separated) parents under section 14 Taxes Act but all children receive child benefit.

Of the overseas countries mentioned, some give child allowances or rebates and others give cash benefits but there appears to be no underlying principle that can be extracted to determine which are most appropriate; benefits are given by Australia, West Germany and the Netherlands and allowances or rebates by New Zealand, Canada, Ireland, Italy and Belgium; France and Luxembourg, of course, obtain the equivalent of allowances through the quotient system.

Of course, child benefits are enjoyed by all parents whether taxpayers or not, whereas the allowances are only of assistance to parents who pay tax and no doubt it must ultimately be a political decision as to which is to be preferred. But in a system of cash benefits, the child allowance for single parents is an anomaly which can result in injustice. If a man and a woman are not married and live together with two children, they can claim two child allowances under section 14; if the man and woman are married then they cannot claim the allowances. This is genuinely a tax on marriage. The single parent's allowance

is equal to the difference between the married man's allowance and the single person's allowance and was enacted to put unmarried mothers in the same tax position as married men. Under the system of individual taxation now proposed the higher married man's allowance will be abolished and it is thought that the additional allowance under section 14 should be abolished at the same time. However, there may be a case for replacing the allowance with an additional benefit for persons having care of a child but it should be borne in mind that both married and unmarried parents have child care responsibilities and any assistance should be extended to all parents.

Whatever may be the merits of benefits as against allowances it is thought that there would be much to be said for the re-introduction of a child allowance and this could amount to the full personal allowance. Underlying this suggestion is the fact that a child who is lucky enough to enjoy income of his own (earned or investment) can claim a full personal allowance but a child who is supported wholly by his parents cannot transfer any of that allowance to his parents. Although children are smaller than adults their needs can exceed those of adults and this is not recognised in the tax system. The view could be taken that a child should be treated like a supported spouse and should be able to transfer the unused portion of his personal allowance to his supporting parents following the procedure outlined earlier in this Chapter.

(4) Tax avoidance

As mentioned in Chapter 4 there are a number of

tax avoidance provisions designed to nullify transfers of income or income producing assets to children. Again, some overseas countries have similar provisions (Australia, Canada, Ireland) and some, on the contrary, achieve statutory income-splitting through the quotient system (France, Luxembourg).

As far as transfers under deed of covenant are concerned it is difficult to see why these should be tax effective for a son or daughter of 18, but not for one of 16 or 17. Deeds of covenant are only effective to save basic rate tax and cannot be used to split income in order to save higher rate tax : accordingly if a child allowance were enacted as mentioned above, the anomalies created by the deed of covenant procedure would be resolved.¹

As far as transfers of income-producing assets are concerned, the settlement provisions nullify these in most cases but it is difficult to see why income or assets transferred to a child under an order of the court are recognised as tax effective to split income whereas such arrangements are prohibited in other circumstances.

The view could be taken that all genuine and bona fide transfers of income and income-producing assets should be regarded as tax-effective in order to recognise the responsibilities and financial obligations imposed on parents by their children and in order to eliminate the anomalies which arise on divorce.

(5) Conclusions

There is little evidence of any demand for the

reform of the tax laws as they affect children. Any proposal to aggregate a child's income with its parents should be resisted : although the quotient system is beneficial it relies on joint taxation of husband and wife as well, which cannot be recommended. The additional allowance for children will probably be repealed with the repeal of the higher married man's allowance, thus removing an injustice to married persons. There is an argument for permitting all children to transfer their personal allowances to their parents, in the way suggested for spouses earlier in this Chapter, so as to recognise the financial obligations and responsibilities of parents, and, for the same reason, the tax avoidance provisions should be repealed, which would also have the effect of removing some of the anomalies which exist which give advantages to divorced parents as against married parents. Children are individuals too, and should be treated as such.

CHAPTER 17

CONCLUSIONS

The objective of this thesis was stated to be to determine a method for taxation of the family unit, bearing in mind changing economic and social conditions. Chapter I examined the rule, originally enacted in 1799 and 1805 that, for income tax purposes, the income of a married woman is deemed to belong to her husband. Chapter 2 considered the statutory exceptions to the rule, enacted in 1914 and 1971, which made some attempt to adapt the original rule to changing social conditions. Chapter 3 described the rules which apply on the beginning and end of marriage and illustrated, by a comparison of married and divorced persons, the anomalies which continue to cause injustice. Chapter 4 traced the development of the distinct income tax rules affecting children and Chapter 5 described the provisions of the capital taxes. Chapter 6 concluded Part I.

Part II considered the studies and criticisms of the existing system differentiating between the distinct concepts of aggregation, accountability and the allowances. The historical treatment revealed a continuing sense of dissatisfaction at the failure to adapt the legislation to the changes in social conditions, in particular to the changes in the proprietary and contractual rights of married women.

Part III examined the tax treatment of the family

unit in 14 different overseas countries. These were arranged into three groups, by reference to the nature of their jurisdiction. The common law countries had all adopted individual taxation whereas joint taxation was almost universal in the civil law and Scandinavian countries, all of which adopted a system of community of matrimonial property : this analysis revealed a continuing development in the laws of matrimonial property and the contractual capacity of married women together with similar developments in income tax law.

Part IV discussed the direction for reform and concluded that, for all cases and in all circumstances, husband and wife should be taxed as separate individuals for all tax purposes. Although there is very little evidence of any desire for the reform of the present tax rules relating to children, the view is also expressed that there is much to be said for treating all children as individuals, too.

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With all my worldly goods I thee endow...
except my tax allowance.

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